

Why we should rethink our old ideas on risk and ageing

As clients become older, financial advisers generally recommend that they take less investment risk. This is partly driven by considerations of what recommendations advisers would make for their own parents.

It is also driven by fear that the financial regulator could find fault with advisers' processes if they recommended risky investments.

Are they doing the elderly more harm than good, however, by recommending only cash or fixed-interest options?

Is this simplistic advice a convenient way of avoiding the prospect of stressed elderly clients worrying about the stock market roller coaster?

I am not recommending a sea change in approach. I wonder, though, if advisers are treating pensioners condescendingly.

Are advisers overlooking the need to revise their thinking in line with changed circumstances? By assuming that elderly clients will become too stressed about investment risk or cease to be intelligent in their sixties, are we removing appropriate investments in these changing times?

This may be deemed to be heresy by many of my peers. Of course, the rationale for moving to less risky, less volatile assets as one gets older is understandable.

As people edge towards retirement, their ability to earn their way out of a stock market fall diminishes considerably, as does their

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ability to outlive the long-term effects of any market decline.

Traditionally, this was achieved by locking in guaranteed rates from government bonds. Returns in the past were far more attractive than they are now.

The conservative approach was also the sensible one. Why wouldn't one lock into high interest rates if one had the option, especially if inflation was likely to fall?

The major difference between now and, say, 30 years ago is that longer life expectancy has extended the need for income and, in some cases, capital. Interest rates are also far lower than in the past.

People have fewer expenses as their lifestyles slow down and their mortgages are paid off. The cost of healthcare, though, increases dramatically.

The problem has not been helped by the effective closure of the fair-deal scheme for nursing home care. For those unable to get government financial support, the burden may be untenable.

The average cost of nursing home care is €1,200 a week or €62,400 per annum. Over four years the bill is €249,600 — a

massive sum.

If the fair-deal scheme remains closed, people will have to find these funds from their own resources.

There is no doubt that returns are correlated with risk, and that equities are more risky and volatile than bonds. As long as your time horizon is 10 years or longer, though, the risks decrease, especially if you have a broad-based diversified portfolio.

Even over the past 10 years, with all the market crashes and uncertainty, returns on equities were essentially flat. And that is a bad period.

Just because somebody is 60 or 65 it doesn't mean that they need to go to cash immediately, even if they are risk-averse.

The higher cost of long-term care means that they need to focus on returns rather than minimising risk.

Some level of investment risk could still be considered, provided it is spread broadly over a wide range of assets.

The traditional option of buying Irish government bonds is no longer safe. It would be a brave adviser who recommended a large holding of such bonds.

Equities require far more

growth to justify investing now because valuations are stretched. Time in markets, though, usually produces results. Even moderate exposures to equities can make substantial differences to portfolios relative to cash-only holdings.

Of course, conservatism is necessary for those who are naturally risk-averse, irrespective of their age. But they ignore at their peril the investment returns needed to maintain their portfolios.

Riskless investors face a difficult dilemma with risk-free returns being so low.

Probably the best solution is to undertake adequate saving and reasoned investing from a young age.

Whatever your age, investment planning should start with your net financial worth before balancing expected investment returns with expected income and capital needs.

This is as applicable to a 65-year-old as it is to a 25-year-old. Risk tolerance rather than just risk propensity is also a key consideration in relation to the range of possible investment returns.

The automated old-age/low-risk approach needs to be revisited by many investment advisers to reflect not only the different personal circumstances of their elderly clients, but also the changed economic environment we now live in.

Anything else may do such clients a disservice.

Eamon Porter is the principal of Aspire Wealth Management based in Malahide, Co Dublin, a financial planning and wealth-mentoring firm