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TABLE TALK: In investing, accept some downs to get the ups

Key take-aways

- Enlist the help of a financial adviser through all stages of your investing life – they can guide you to better outcomes.
- Be sure you consistently have enough exposure to growth assets to beat inflation and take advantage of compounding; don't de-risk at retirement because you likely still have 20 years to live.
- Despite the high volatility in markets, it is best to hold onto your investments so as not to miss out on any recovery. Don't try to time the market; accept its ups and downs.

Question:

Financial markets have been so volatile in the past few years (even in the US and Europe), isn't there a way to avoid the downs and still be able to capture the ups? I only have about 10 years before I retire, and I need the upside.

Answer:

Over the past three years, investors have experienced quite a tumultuous time in global and domestic markets. Markets had very little runway to recover from the pandemic-induced market shocks. Last year, volatility was elevated due to heightened uncertainty, fanned by stubbornly high inflation and rising interest rates, subdued growth prospects and geopolitical tensions. Market expectations point towards a continuation of these investment themes driving markets in 2023 and beyond.

When looking at the market reaction to different events over the years, including the COVID-19 market crash and Russia-Ukraine war, among others, you can see that there is no way to predict how and when the market will move. Volatility is a natural part of investing in growth assets, but continued volatility can be uncomfortable, even for the most astute investor. However, volatility can work in your favour, too, as it provides opportunities to buy assets at relatively reduced prices. At certain times, it's best to do nothing, allow the volatility to play out and the reward could greatly benefit you in the long run.

Typical investor behaviour during periods of sharp market declines is a knee-jerk response to switch away from equity to the "safety" of cash to avoid losses. But when the markets recover, those who disinvested miss out on the upside because they're sitting on the side lines. By the time they get back into the market, they've missed the opportunity.

The graph highlights the missed opportunity when comparing the returns of South African (SA) equity (using the FTSE/JSE All Share Index as a proxy) to SA cash (using the SteFI Composite as a proxy) over a 10-year period to December 2022, which was a particularly challenging period for SA equities. Investors who switched out of equities in favour of cash during this period would have missed out. Trying to time the market by attempting to predict when markets will recover could mean missing the potential upside and locking in losses.

During the most recent three-year period, the graph highlights how the market corrections offered enormous opportunity for those who remained invested through the ups and downs.

Some considerations as you approach retirement

First, **re-evaluate your retirement goals**. What is your preferred retirement age/date? How much will you actually need to retire in comfort? Have you established a retirement lifestyle budget? You can use the M&G Retirement Calculator to assist you with this.

Second, **assess where you are in your retirement savings journey**. What have you accumulated thus far? It's never too late to make the necessary

changes to put you on a more appropriate path towards your retirement goals. After all, this is likely to be the period in your career when your salary and savings are at their highest. These years are important to bolster your savings, offering the greatest opportunity to reinvest and then allowing the effect of compounding to really solidify your retirement pot. Most people consider reaching retirement as the end of the retirement savings journey, but importantly, the time horizon for retirement savings should be viewed as extending beyond your retirement date.

Third, **close the retirement savings gap**. Is there a gap between your retirement goals and what you've accumulated so far? If so, to close the gap, some options could be to increase your retirement contributions, and/or increase your allocation to growth assets (equity and property). Having suitable exposure to growth assets to generate inflation-beating returns becomes critical in ensuring you have adequate retirement capital to cover your retirement years. Inflation poses a very real risk to retirement savings, in that it erodes the value thereof over time.

This underscores the importance of aiming for inflation-beating returns over the full duration of your retirement savings journey: both in pre-retirement and in post-retirement. De-risking (reducing your portfolio exposure to equity and property) without careful consideration at this point can erode the long-term growth potential of your accumulated retirement pot. In fact, de-risking is one of the biggest pitfalls faced by retirees. Many investors de-risk at retirement in an attempt to reduce the volatility associated with higher-risk assets, only to expose themselves to inflation risk, in that their returns do not keep pace with inflation.

For example, a retiree whose pre-retirement portfolio was invested in a balanced fund that targeted a return of CPI+6% decides to de-risk their portfolio at retirement and go into a conservative portfolio that targets CPI+3%. In addition, the retiree takes an income drawdown of 5%. By design, this will result in their portfolio going backwards in real terms, and ultimately significantly increase the chance that they'll run out of money before they die.

Keep in mind that safeguarding your retirement pot against undue risk is important, too, but avoiding risk could result in returns that do not keep up

with inflation. Targeting inflation-beating returns well into retirement can also help to combat longevity risk, which refers to the risk that you may outlive your retirement savings. Life expectancy has increased over the years, which in turn means that you may have to save more for the additional years during retirement. This dynamic has placed more pressure on retirees to seek ways to bolster their retirement savings.

Finally, **ongoing retirement planning is key.** Partnering with a financial adviser during your entire retirement savings journey is critical, as they can help you draft a retirement plan and suggest additional ways to help keep you on track to reach your retirement goals. They're also best placed to guide you through challenging market periods and, importantly, help you identify the various risks you'll face, help you prioritise which of these are most important to resolve, and then put an appropriate plan in place for you to navigate through them. If your accumulated savings is lagging, they can determine whether you should include more growth assets in your portfolio, since you still have 10 years left in your investment horizon, during which the risks of losses will be reduced. A financial adviser's importance is elevated when you reach retirement, as they're able to help you make the most appropriate decisions at this time -- you'll likely get the best outcomes if you have this relationship in place early on.

Remain focused and stay on track

Spend time focusing on your holistic retirement planning rather than trying to time the market. At M&G Investments, we consistently monitor the market for opportunities that arise during the various market cycles, making tactical asset allocation calls and stock-picking to the benefit of our client portfolios.

Remember that sticking to a carefully crafted long-term financial plan with suitably diversified asset exposure is the most likely avenue to help you achieve your desired investment outcome over time, regardless of market movements. Staying consistent in your approach will reap rewards in the end. For long-term investments, such as retirement savings, this approach is even more relevant.

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