

# The state of investing in 2021

Finder Report

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## The state of investing in 2021

Compared to the rest of the world, Australia fared relatively well through the pandemic. Though Covid-19 led to lockdowns, unemployment and a general incitement of fear and uncertainty, Australia has suffered far less than most nations and with the exception of several minor outbreaks the virus has been largely eliminated and the country open for business. There is evidence that a successful vaccine rollout could drive economic recovery this year if it allows domestic borders to remain open and businesses to operate at a competitive capacity. If this occurs there is hope Australia may see significant economic growth in 2021; there is an opportunity for consumers to take advantage of this growth by investing in non-cash assets.

Households have accumulated an extra \$113 billion in savings over the course of 2020 according to the Australian Prudential Regulation Authority <sup>1</sup>, and in June the household savings rate peaked at 22%, thanks to government stimulus measures and lockdowns minimising discretionary spending <sup>2</sup>. But with interest rates at a record low, savings accounts have become less attractive for Australians to stockpile their wealth. Instead, households are increasingly looking to shares and property for higher relative gains.

This report will delve into the investment outlook for 2021 across share trading, the property market, micro-investing, and superannuation.



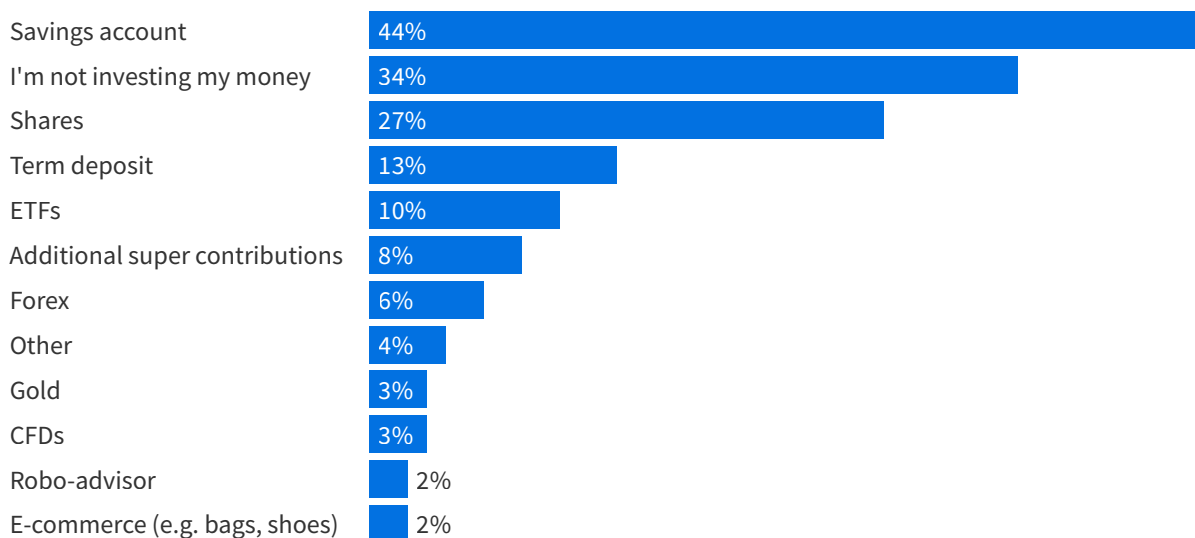
# The low cash rate has driven a shift towards investing

In November of last year, the RBA cut the cash rate to a historical low of 0.10%<sup>3</sup>. There is general consensus that interest rates will remain low and steady, with 37 out of 40 economists in Finder's RBA Cash Rate Survey predicting no change until at least December 2022<sup>4</sup>. At the time of writing, the most competitive rate on a savings account is 3.0%, offered by Westpac to 18 to 29 year-olds<sup>5</sup>, but this is contingent on meeting a range of criteria. The highest standard variable rate is 0.35%, offered by Citibank<sup>6</sup>. Interest rates have in fact been trending downwards for decades<sup>7</sup>, but these historical lows have been exacerbated by the recession.

Australians have been taught the savings account is the holy mecca of the money world, while the stock market is perceived to be risky and volatile. And it's true: cash is likely a safer asset than shares or property in the short term. But in the long run, the stock market tends to outperform cash assets, and with savings accounts currently offering negligible returns this is truer than ever.

Compared to other nations, Australians are quite conservative when it comes to investing their money. In November, a Finder survey found just over one in four Australians (27%) invest in shares<sup>8</sup>. This may seem significant, but this figure is actually modest when compared against other countries: in the U.S., 35% of Americans own stocks outside of their retirement fund<sup>9</sup>, while 33% of Brits own shares<sup>10</sup>. However Covid-19 may have been a push in the right direction for some, with a Finder survey revealing 13% of Australians started investing in shares during the pandemic<sup>11</sup>. With interest rates forecasted to remain low for some time, more Australians would be doing themselves a favour by looking beyond cash.

## How Australians are choosing to invest their money



Source: Finder Consumer Sentiment Tracker, November 2020

## Share markets will remain volatile in the near-term

The stock market proved unpredictable in 2020, and if there's one thing investors should keep in mind in 2021, it is to expect the unexpected. Between February and March the ASX plunged by 33%, reaching its lowest trough since 2016<sup>12</sup>. In theory a crash provides a golden opportunity to enter the market and buy undervalued stocks. But the beginning of the recession - combined with the uncertainty of the pandemic - sparked investor fear, and many scrambled to sell their shares as quickly as possible. Research from Fidelity Investments shows nearly one in five investors (18%) sold all of their stocks between February and May, and a third of investors over the age of 65 (33%) sold all their stocks<sup>13</sup>. While the data is based on American investors, there is no reason to believe Australian investors behaved differently.

### Performance of ASX 200



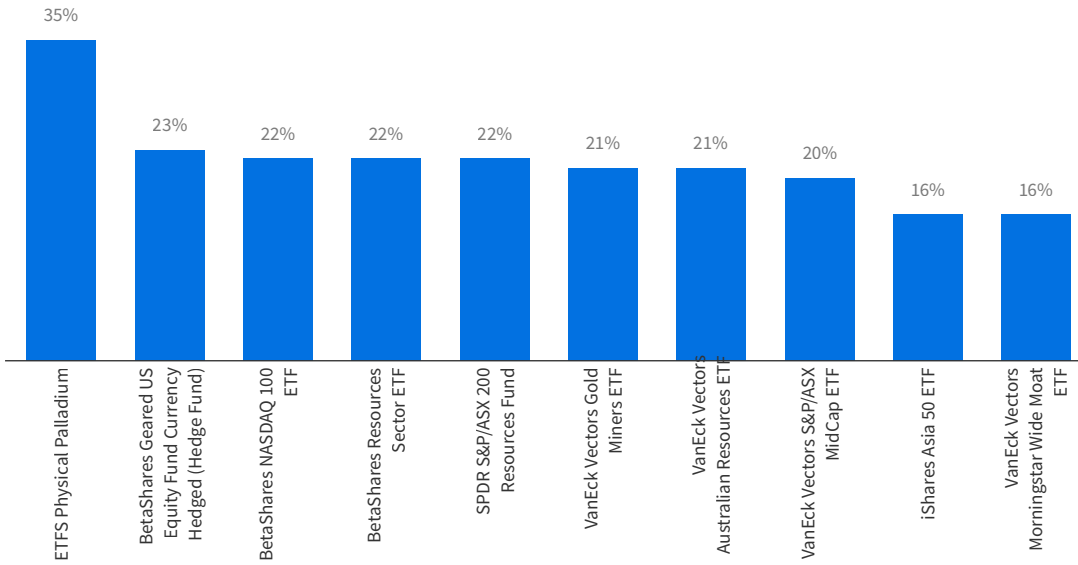
Source: ASX

However some sectors have fared better than others in the past year. The pandemic has prompted remarkable growth in the technology sector, from education technology and telehealth to ecommerce platforms and digital payment methods. As an indicator of the exponential growth of the technology sector in 2020, the Perpetual Global Innovation Share Fund, which invests in disruptive stocks, saw 54% year-on-year growth in January<sup>14</sup>. As economic recovery looms however, Finder predicts growth in technology stocks may slow as investors turn to the banking, energy and travel sectors.

While the stock market is steadily returning to its pre-Covid growth trajectory, global recovery hinges somewhat on the success of upcoming vaccine rollouts. The reduction of restrictions and resumption of international travel is expected to reignite the economy beyond the technology sector, but the assumption the vaccine will be the magic pill for the global recession is naive. According to Russell Investments' Composite Contrarian Indicator, investor optimism is nearing pre-pandemic levels<sup>15</sup>, which makes markets particularly vulnerable to bad news. With ongoing uncertainty around Covid-19 and global politics, share markets are likely to remain volatile in the short term.

Nevertheless, near-zero interest rates make the share market one of the best investment options for 2021. For the more risk-averse, indexed exchange-traded funds (ETFs) are diversified funds that follow the same growth trajectory as the index it tracks (e.g. ASX 200). In general, these sector-neutral ETFs are less risky because they give investors a buffer when one area of the economy suffers.

### Top performing ETFs over the past five years

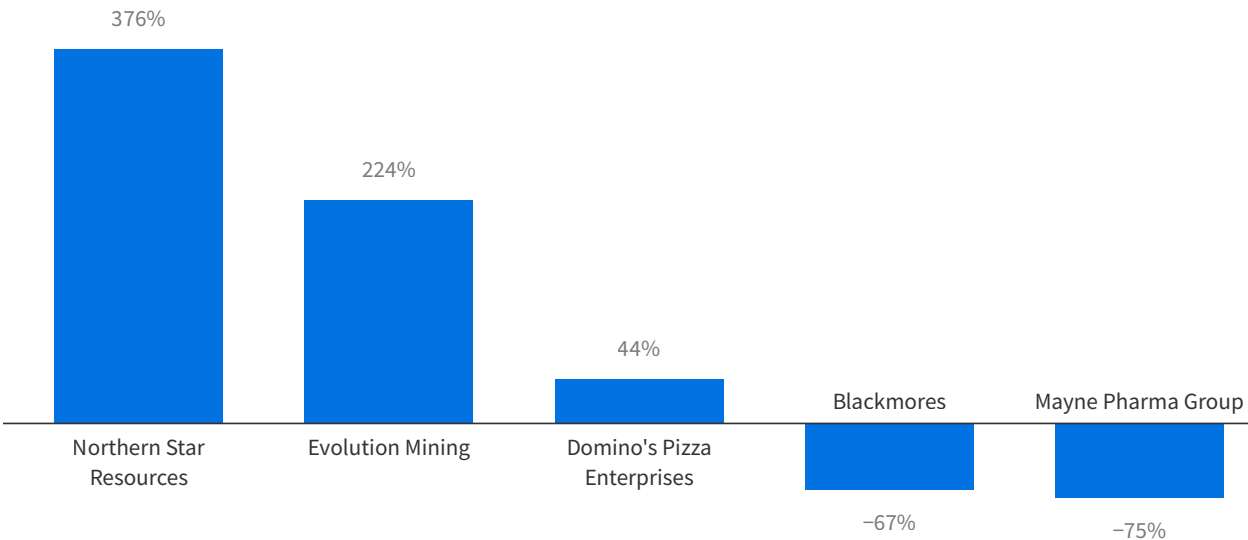


Source: ASX, period ending 31 December 2020

### Putting all your eggs in one basket is a risky game

In contrast to indexed funds, which tend to perform at the same rate as its index, the figure below shows just how risky it can be to bet on a single stock, even when a company is performing well. The chart shows the five-year growth of five of the top performing stocks of 2015<sup>16</sup>. Of these stocks, two have seen tremendous growth over the past five years (Northern Star and Evolution Mining), one has seen strong growth (Domino's Pizza), and two have declined (Blackmore's and Mayne Pharma Group)<sup>17</sup>. Those who had invested in either of the mining and resources companies five years ago would have fared well: a \$1,000 investment in Northern Star Resources in 2015 would have grown to \$3,760 by now. In contrast, the same investment in Mayne Pharma Group would have left you with just \$250. The analysis emphasises the importance of asset diversification for long-term returns, and just how tricky it can be to predict the "winners" ahead of time.

### Five-year performance of selected top performing stocks of 2015 (2016-2021)

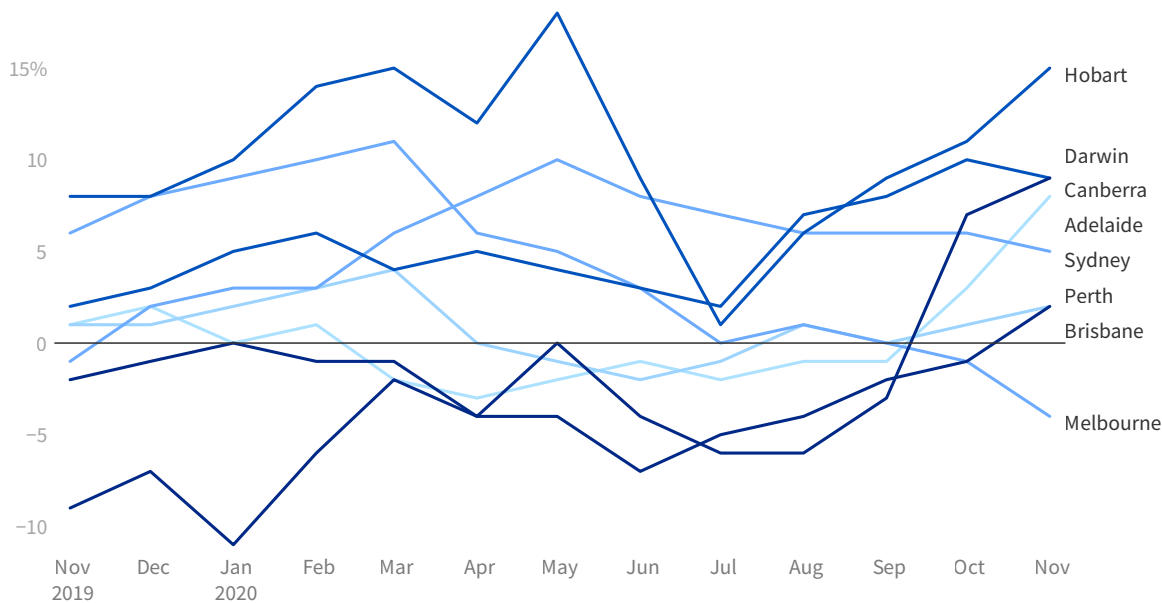


Source: ASX, period from January 2016 to January 2021

## The property market is looking hopeful...

Property has proven to be incredibly resilient to the pandemic. While many predicted the market would plunge to record lows in 2020, the effect has actually been the opposite. Data from CoreLogic shows that while prices faltered slightly in the initial shock, all major cities except Melbourne achieved positive year-on-year growth in October. The smaller capital cities have seen the largest gains, with Hobart reporting a 14.6% year-on-year increase, followed by Darwin (8.9%) and Canberra (8.7%)<sup>18</sup>.

### Year-on-year change in property prices (houses and units)



Source: CoreLogic Capital Cities House Prices, October 2020

Meanwhile, plunging interest rates have made it cheaper than ever to borrow money for a mortgage. According to Finder's Consumer Sentiment survey in August, more than a third of Australians (34%) believe the pandemic has made property ownership more achievable for first time buyers<sup>19</sup>. With the average variable owner occupier discounted rate now sitting at 3.65%<sup>20</sup>, it's no wonder buyers are scrambling to get their hands on some land. New ABS data shows owner occupier home loans reached a record \$18.2 billion in December, with 26% growth over the previous year<sup>21</sup>. In all capital cities the number of sales in October was up year-on-year, with Brisbane leading the way with 69% year-on-year growth. Demand in the Melbourne market is showing signs of recovery, with the number of sales up 357% between September and October<sup>22</sup>.

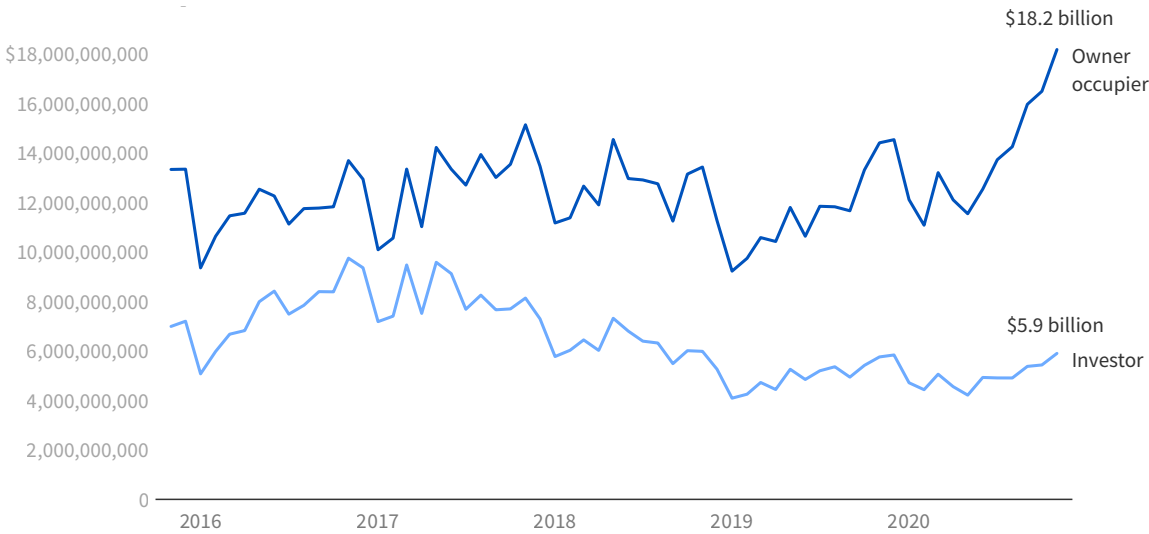
The fall in interest rates has also caused a surge in homeowners refinancing their home loans to get a better deal on their mortgage. The average variable discounted home loan interest rate is 3.65%<sup>23</sup>, and according to the ABS the average Australian refinances a \$443,858 loan<sup>24</sup>. For a borrower with 30 years left on their home loan, by reducing their rate by 0.5% they could save \$44,298 over the lifetime of their mortgage. Lenders are highly competitive at the moment, but with little scope to drop interest rates further, some are offering cashback options between \$2,000 and \$4,000<sup>25</sup>.

### ... but investors aren't buying it

The state of property is looking a little gloomier for the investor market however. While investor home loans grew 2.5% year-on-year to a total of \$5.9 billion in November, ABS data shows the portion of home loans taken out by investors has dropped to a record-low 25%<sup>26</sup>.

The pandemic has had a notable impact on the rental market, with the influx of immigrants and students putting a halt on demand. Meanwhile, the supply of long-term rental properties has increased as short-term lessors suffered from the lack of tourism and sought to find long-term tenants instead. Government policies were introduced to limit evictions of tenants who were suffering due to the pandemic, and landlords were encouraged to cooperate with tenants to negotiate lower rents. All of these factors, plus forecasts from the Department of Treasury that Australia's population in June will be 1.5% lower than pre-Covid projections<sup>27</sup>, have contributed to a less profitable investor market.

## Owner occupier and investor home loan commitments

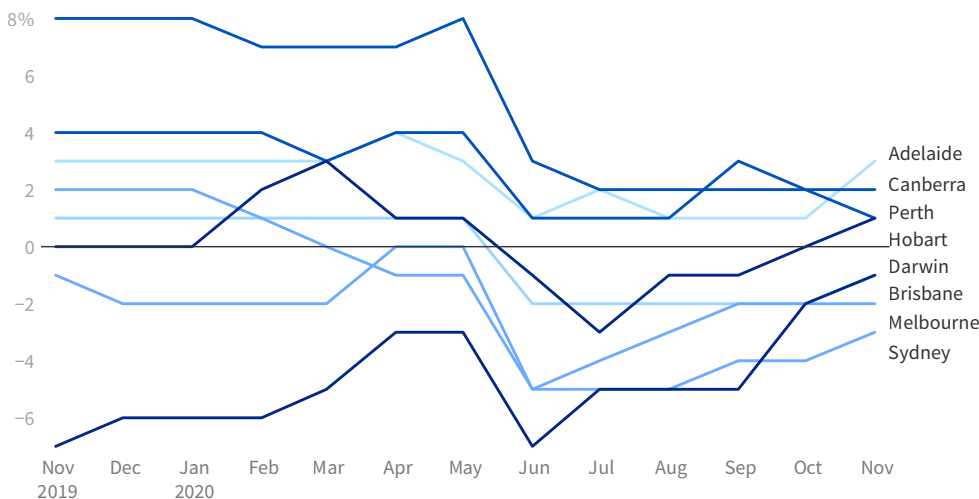


Source: ABS Home Loans, November 2020

Approximately 60% of investors are in a net rental loss<sup>28</sup>, and following the recession this figure is likely to be even higher. With less than a third of investment property owners (29%) owning more than one property, the majority of investors have not reached an adequate portfolio scale to turn a profit<sup>29</sup>.

Other long-term trends driving down investor returns include mortgage rate premiums for rental investors and high levels of construction over the past year which have driven down rental prices by increasing market supply<sup>30</sup>. While the construction sector faltered at the beginning of the pandemic, construction picked up in the second half of 2020, and now accounts for 20% of all home loans according to ABS<sup>31</sup>.

## Year-on-year change in rental prices (houses and units)



Source: CoreLogic Capital Cities House Prices, October 2020

Data from CoreLogic shows median asking rent has been down year-on-year in the larger capital cities for the most part of 2020, but Hobart, Adelaide and Canberra have seen growth. For the most part, the smaller cities were less impacted by falling demand from students and immigrants. While it may be too early to tell, the increase in remote working may contribute to a shift away from metropolitan centres and towards Australia's smaller cities and regional areas. In Sydney and Melbourne, net metropolitan populations declined by 14,000 and 10,000 respectively<sup>32</sup> in the first half of 2020. In these cities, median rents have fallen in the inner suburbs, while the outer suburbs have seen growth. Victoria's Southern Grampians, for example, saw 31% year-on-year growth in September<sup>33</sup>. If this trend continues, investors may have to reconsider the long-term profitability of inner city locations.

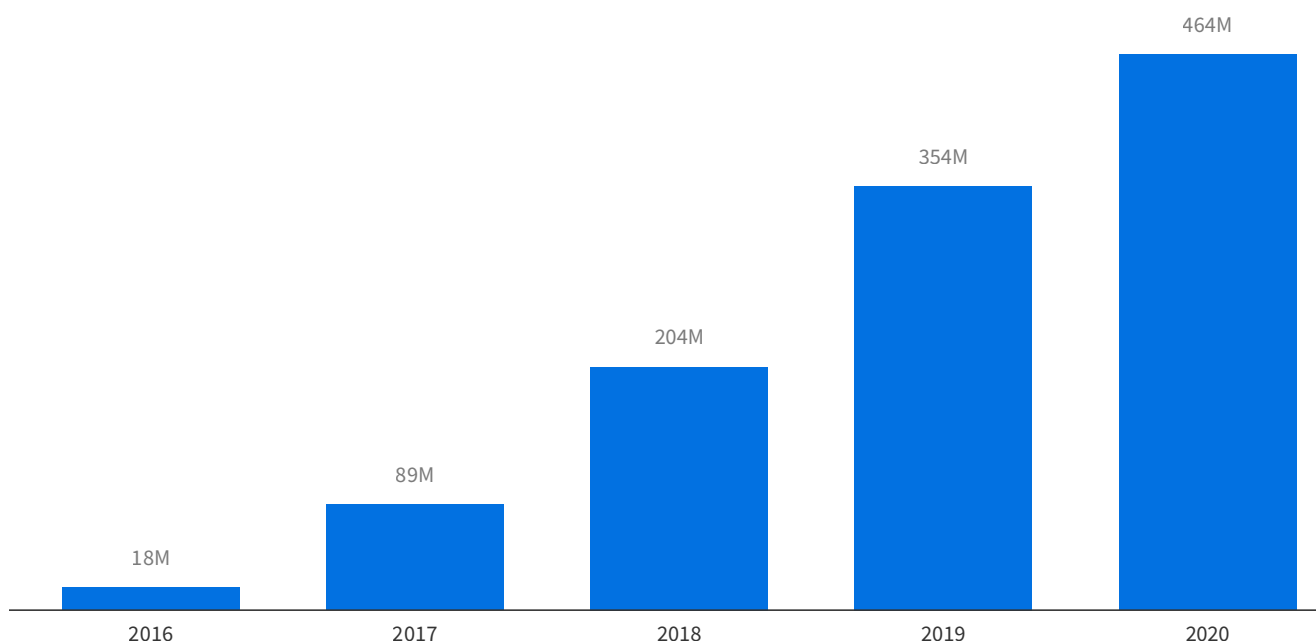


## Micro-investing and robo-advice platforms will continue to prosper

Micro-investing involves consistently investing small amounts of money over a long period of time. This allows small-scale investors to enter the share market without large amounts of cash. Apps such as Raiz Invest and Spaceship Voyager have seen an immense growth of this market, particularly among younger generations who may lack sufficient savings to enter the traditional share market. Micro-investors can choose to invest small amounts periodically, rather than a large sum of money at once. Many apps also allow consumers to round-up their spending into their investment account. For example, a coffee costing \$3.50 is rounded up to \$4, with the extra 50 cents put into the investment account.

This form of investing has become popular amongst younger generations, simply because they have less money to spare. Millennials are worse off than their parents when it comes to student debt, property ownership and are now bearing the brunt of the economic recession. For the generation that has been criticised for choosing smashed avocado over superannuation, micro-investment apps help to reignite a culture of savings without making consumers feel like they are missing out on anything. Between 2016 and 2020 Raiz Invest (previously Acorns) grew by a factor of 24, now holding \$464 million in investor assets<sup>34</sup>. If Raiz can be used as a proxy for the micro-investing market, there is evidently a major market opportunity.

### Raiz Invest: Total assets under management



Source: Raiz Invest annual reports 2016-2020

The proliferation of digital investment platforms has also made financial management more accessible to a population that is increasingly addicted to screens. According to Google insights, smartphone users have an average of 2.5 finance apps downloaded on their phone<sup>35</sup>, and nearly three-quarters of users (73%) regularly use an app to manage their finances<sup>36</sup>. As consumers increasingly turn to their phones for financial advice, the market for investment robo-advisors is flourishing.

Like traditional financial planners, robo-advisors provide tailored financial advice, but at a fraction of the cost. The platform uses a mix of algorithms and background analysis to customise an investor's portfolio, and then continuously re-balances the portfolio to ensure alignment with the investor's financial goals. KPMG has predicted that robo-advisors manage around USD\$2.2 trillion worth of assets, and the market is rapidly growing.

## Australians are switching up their super

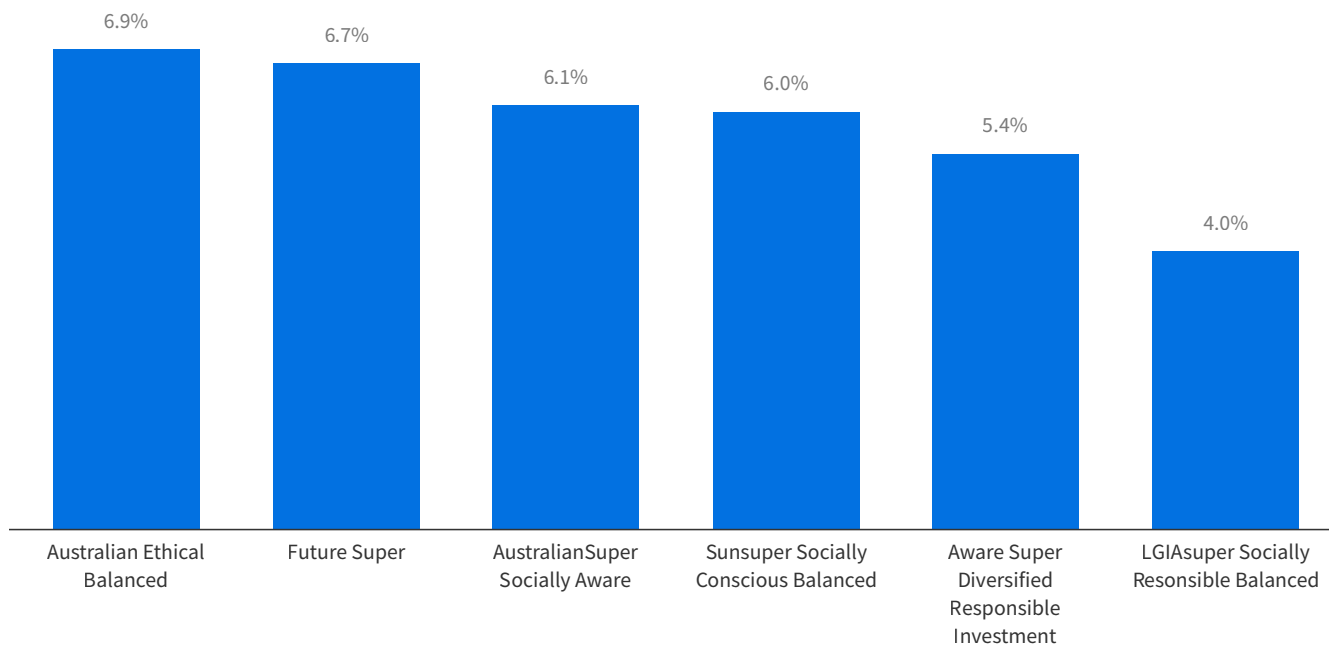
The stock market crash instigated a flurry of panic for superannuation holders who worried they would lose their life savings. In April, Finder revealed 12% of Australians were considering changing their super fund in light of market volatility<sup>37</sup>. However the market has largely recovered its losses and most diversified funds are no worse off than they were a year ago. In fact, now is the perfect time for Australians to increase their superannuation contributions as economic recovery will support fund growth. As of November, around 8% of Australians invest in additional super contributions.

The government recognises this opportunity too: as of July the super guarantee is set to increase from 9.5% to 10%. For the average Australian with a \$89,123 salary<sup>38</sup>, this adds up to an extra \$8,912 entering their super account per year. This will make income-earners better off, but only if their superannuation is paid on top of their base salary. For those on a bundled salary package, take-home pay will decrease slightly.

Australians are also developing a growing interest in ethical investing. A Finder survey found nearly a third (29%) of Australians would consider switching super funds if their provider was investing in industries they deem unethical, and for Gen Z this grows to 45%<sup>39</sup>. Younger Australians in particular are becoming increasingly concerned with the state of the planet and are willing to boycott investing in industries that are misaligned with their values.

But it's not just about the ethics. A report from the Responsible Investment Association Australasia found 62% of Australians believe ethical super funds perform better in the long term<sup>40</sup>, a stark increase from 29% in 2017. And they aren't necessarily wrong: Australian Ethical, for instance, has achieved a five-year annualised growth rate of 6.88% on its balanced fund, well outperforming the industry average of 5.9%<sup>41</sup>.

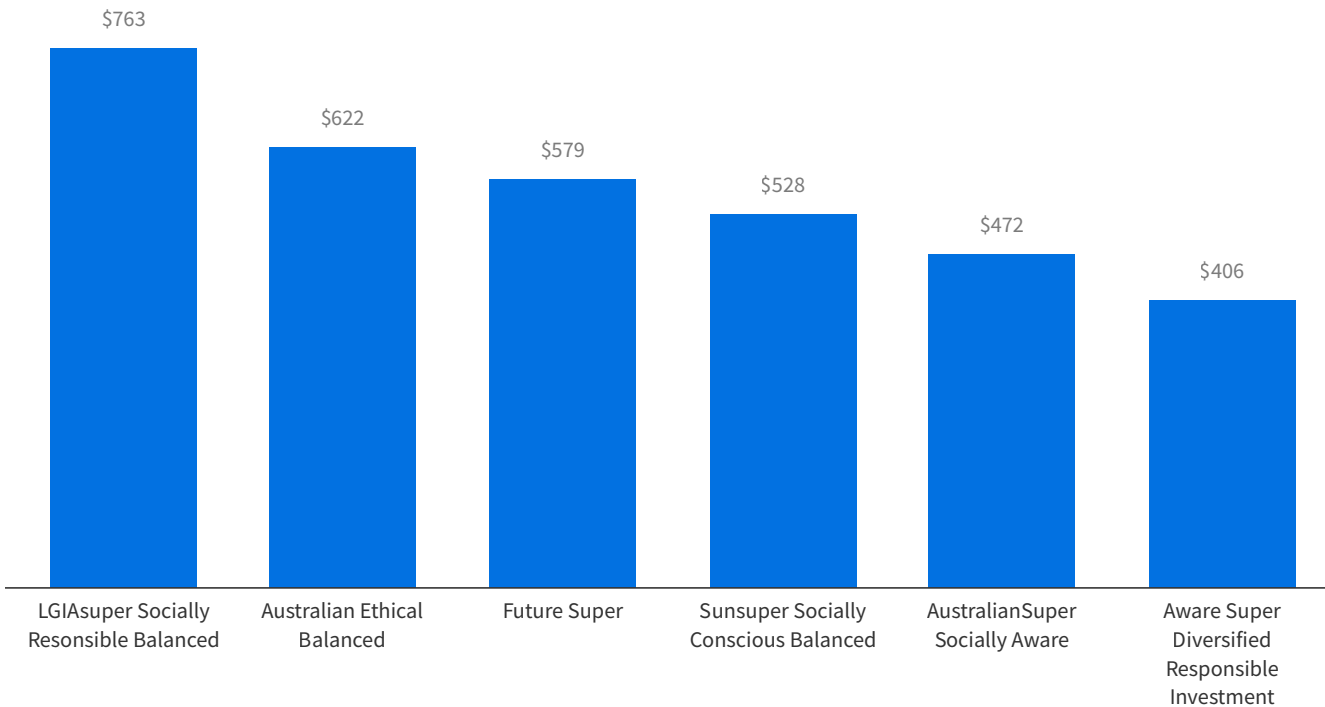
### Five-year performance of selected ethical super funds



Source: Most recently available annual reports for the providers mentioned

However not all ethical funds are outperformers, and Australians should also be wary of management fees. A report by the Productivity Commission found a 0.5% increase in management fees can cost the typical full-time worker \$100,000 by the time they reach retirement<sup>42</sup>. As a general recommendation, fees should make up less than 1% of the account balance - or \$500 on a \$50,000 balance. Fees for a number of ethical funds exceed this figure, so consumers will need to weigh up the long-term performance of the fund and the importance of ethical investing against this cost.

## Management fees for selected ethical super funds on a \$50,000 balance



Source: Finder research and most recently available annual reports for the providers mentioned

## The bottom line



With the cash rate expected to remain unchanged for the next few years, the best places to keep your money depend on your goals and appetite for risk. The share market remains a reliable long-term investment when assets are appropriately diversified, but investors should expect price volatility to continue in the short-term. While property remains a good investment for owner occupiers in the long-term, investment property is unlikely to see significant growth in the near-term as rental prices remain subdued. The low and steady cash rate also makes now the ideal time to pay off any remaining debts.

With the proliferation of fintech platforms such as robo-advisors and micro-investing apps, the investing landscape is becoming increasingly accessible to younger and less wealthy demographics. Instead of needing thousands of dollars to get started, consumers can start with their spare change. Over time this could contribute to a more equitable distribution of wealth as lower-income earners generate exponentially more money than if they hadn't invested at all.

Some will maintain that 2021 is the year of the bitcoin, while others will insist on investing in high-growth startups. However financial advisors agree that trying to 'beat the market' is not a sustainable strategy, especially for inexperienced investors. Understand your financial goals and timelines and invest accordingly. And if you're a young investor in it for the long haul, don't let one economic recession break your sweat - there will be plenty more where that came from.

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