eureka
report

Riding Out a Recession

Theo Marinis provides some advice on how to stay in the saddle when a recession looms.

By Theo Marinis

11 Jul 2023

"If you hear the sound of hooves, it is smarter to expect horses than zebras."

This advice, often given to trainee doctors, is essentially a reminder to rely on your training and experience, rather than jumping to colourful conclusions.

Australia is facing two or more quarters of negative growth due to the blunt instrument of interest rate rises. That's why we should expect a recession, soon. I hear the hooves of the market coming at us at full canter (and, by the way, happy new financial year).

On the Edge

Every economist from the big four banks now predicts a further two interest rate rises before easing – and this is a massive pull on the economic reins, increasing the annual cost to average home borrowers of almost $20,000 pa. Unfortunately, there are borrowers on the edge who face being pushed over economically (which provides an opportunity for those who are cashed up, but that is another story).

The problem with reducing consumption by increasing the cost of borrowing is that 100 per cent of the real pain falls on just 25 per cent of the population. As a solution, it is inequitable. A far fairer approach would be a GST increase of 10 per cent, with compensation built in for those below the minimum wage. This strategy would reverse the pain percentage and spread it across all consumption. Unfortunately, it is politically unpalatable and therefore politically impossible.

For Eureka readers the question remains: What should I do?

The smart thing might be to do nothing, but importantly, don't panic. That advice, however, is not always as straightforward as it seems.

Be Conservative

You can, however, prepare – with a full audit of your financial situation and your approach to investing. Make sure you are not exposed to margin loans or betting on the markets and adopt a sensible financial posture. Get conservative advice promptly – and act on it.

Long term wealth is grown by 'staying in the saddle' and riding out the bumps. In fact, downturns and recessions can be a very effective way to grow wealth by continuing to buy discounted assets, if you can afford it.

There are two and a half groups of investors: those in the wealth accumulation stage, those in drawdown phase, and a small group in transition to retirement while continuing to earn an income from employment. A recession will have the impact the RBA desires, but it causes widespread pain for those who lose jobs and then can't pay mortgages. For those in employment, our capitalist system provides great opportunities at such times.

Part of my approach for those in the drawdown phase is to recommend an investment buffer in cash of around two years' income. Yes, this buffer underperforms against the stock market, but it provides a shock absorber for investors. It means you don't have to sell assets at discounted prices to be able to eat.

Going Slow

Many people over the age of 50 will be more comfortable with a conservative investment profile that allows them to continue to accumulate wealth and ride out the shocks. As regular readers will know, I am a disciple of journalist Edna Carew's philosophy of "getting rich slowly and staying rich".

I also advise investors to plan for a return of around 5 per cent per annum. The norm is around 6 per cent – 7 per cent, but the 2 per cent gap also helps considerably to buffer the downtimes.

Obviously, the majority of investors in wealth drawdown phase will be retired, and many will be alarmed when they hear the 'hooves' of recession. They should ignore the fear merchants who will proclaim (as they always do) that retirees don't have enough time for markets to recover. If they have good advice, a conservative approach and are well educated in the vagaries of the investment markets, they should not be alarmed.

Patience

They will understand that economic cycles can be brutal, that humans can make rash over-reactions (or panic, as I believe the RBA has done) and that after the economic pain ahead of us, there will be plenty of joy as well. When they ride out the bumpy next year or so, maybe they can, perhaps, afford an African safari to see the zebras in situ.

Recessions are not the end of the world; just as high inflation doesn't mean the end of investing. They are both part of a normal cycle of boom and bust that should not spook anyone unless they are exposed to get-rich-quick schemes.

History tells us the stock market is the best way to transfer wealth from the greedy to the patient.

Theo Marinis is Managing Director of Marinis Financial Group.

Disclaimer: Performance data quoted represents past performance and does not guarantee future results. The information in this article is general information only.It is not intended as financial advice and should not be relied upon as such. The information is not, nor is intended to be comprehensive or a substitute for professional advice on specific circumstances. Before making any decision in respect to a financial product, you should seek advice from an appropriately qualified professional on whether the information is appropriate for your particularneeds, financial situation and investment objectives. The information provided is correct at the time of its creation and may not be up to date; please contact Marinis Financial Group for the most up to date information.

Proudly

INVESTSMART

Financial Strategies (SA) Pty Ltd trading as Marinis Financial Group
T 08 8130 5130 | F 08 8331 9161 | A 49 Beulah Road, NORWOOD SA 5067
E admin@marinisgroup.com.au | W marinisgroup.com.au
ABN 54 083 005 930 5067 | AFSL No: 326403

Reproduced with the permission of InvestSMART

https://www.eurekareport.com.au/investment-news/riding-out-a-recession/152689?v=556031

Disclaimer:

Performance data quoted represents past performance and does not guarantee future results.

The information in this article is general information only. It is not intended as financial advice and should not be relied upon as such. The information is not, nor is intended to be comprehensive or a substitute for professional advice on specific circumstances. Before making any decision in respect to a financial product, you should seek advice from an appropriately qualified professional on whether the information is appropriate for your particular needs, financial situation and investment objectives.

The information provided is correct at the time of its creation and may not be up to date; please contact Marinis Financial Group for the most up to date information.