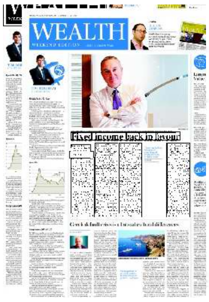

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Fixed income back in favour

Boomers planning to retire want to cut investment risks

BEN POWER

JON Lechte says the looming retirement of baby boomers, as well as recent sharemarket volatility, has triggered a surge in demand in Australia for more stable forms of income.

The executive director of markets at fixed-income broker FIIG Securities says sharp falls in equities and flat to falling property prices have caused investors to take a closer look at fixed income as a class.

It includes instruments such as term deposits, government and corporate bonds and hybrid securities

Lechte says the strong interest in fixed income, which is leading the firm to sign up 250 clients a month without any advertising, is driven by both short-term and macro factors. The major macro factor is the retirement of baby boomers.

"It's like a tide coming in," he says. "The first of them born in the late 40s turn 65 this year."

Lechte says boomers typically already have property — with many wealthy individuals having made their money out of property — and they already hold and understand shares. "What they don't understand is fixed income," he says.

But retirees, and those planning to retire, are clamouring to reduce the proportion of risky assets in their portfolio.

Lechte says a rough rule of thumb is the percentage of a portfolio allocated to fixed income is equivalent to age; so a 70-year-old would have 70 per cent invested in fixed income.

"I don't think many people look at it that way, but it's often how it develops," he said.

The other massive factor driving interest in fixed income is recent falls in equity markets. Lechte says those moving into retirement, and who have funds set aside, don't want so see their portfolios drop 10 per cent in a short period. "People are looking for a greater percentage of investable funds in stable returning assets."

FIIG was launched in 1999 to meet this expected retail demand for fixed-income products from retiring baby boomers. But Lechte says despite the growing demand, the fixed income sector market in Australia is relatively small, whereas 63 fixed income brokers service the London market alone.

One reason for lack of interest in fixed income is the superior performance of equities since the 1980s, but many investors are now questioning the likely performance of equities for the next 20 years.

Another issue has been access to direct bond holdings. FIIG found that many investors wanted to buy bonds but could not because the minimum investment threshold was too high in the past. The firm then decided to make access to direct bond holdings easier for retail investors and reduced the minimum investment to $50,000.

Lechte says there are hundreds of bonds available, although the vast bulk are government bonds which are low risk but low yielding.

Corporate bonds are riskier than government bonds but higher yielding. However, Lechte says investors should remember that all bonds rank ahead of equity and are therefore less risky than an equity holding in the same corporate name.

Lechte says bonds issued by the federal government yield about 4 per cent, while senior debt in leading Australian companies and banks yield about 6 per cent. Subordinated debt from banks earns 7 to 8 per cent.

Lechte says unlisted hybrids issued by highly rated banks earn close to 9 per cent.

"They're the lowest-ranking bond, but at the end of the day they're still issued by household names," he says.

There are also bonds issued by brand names such as Axa, Swiss Re and GE, companies well-known to investors even though they are not Australian.

Lechte says European bonds are very volatile at the moment, but earn yields are as high as 12 per cent. "People need to understand what they're doing when they're buying those things," he says, adding they may sensibly make up about 5 per cent of a fixed-income portfolio.

About 20 to 25 per cent of FIIG's sales are inflation-linked securities. "There is good demand for that thing," Lechte says. "One of the biggest concerns talking to people about funds for retirement is will they run out of money (longevity risk). They (retirees) might have set aside the right amount of money, but if the value of money declines due to inflation, they have got a problem."

Relative to shares and property, investors lack an understanding of fixed income due to their apparent complexity. But Lechte says it is actually the most simple investment.

"It's more simple than buying shares," he says.

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AARON FRANCIS

Jon Lechte of fixed-income brokerage FIIG Securities says his products are simple for investors to understand and more stable than stocks

'People are looking for a greater percentage of investable funds in stable assets'

JON LECHTE
FIIG SECURITIES DIRECTOR