Members’ Investment Choice

Members’ Investment Choice provides an opportunity for you to choose from three investment portfolios, depending on which is best suited to your own individual needs and circumstances. The Trustees recognise that members are in different financial positions, have different retirement savings requirements and have different tolerances for investment risks. Therefore, the Trustees offer the following three portfolios that you can choose from.

The **Growth** portfolio is for when your prime objective is to maximise your long-term returns. This is for when you are willing to accept some risk of losses and fluctuations in your account balance in the short term.

The **Conservative** portfolio is for when you are planning to withdraw (some of) your savings soon (say, within the next three years) either for your retirement or perhaps for purchasing your first home. This is for when you wish to minimise the risk of losses in the short term.

The **Balanced** portfolio sits in between the Growth and Conservative portfolios and, thus, represents an intermediate point which ‘balances’ risk and return. This may be appropriate for when you are approaching retirement and wish to forego the prospect of higher returns to reduce the risks of losses.

Case study

The following table sets out characteristics for someone earning $90,000, who contributes at 7% (matched by their employer) for 30 years.

	Average return (% per annum)	Expected savings balance (at age 65)	Weekly retirement income (age 65 to 90)
Growth	4.20%	$610,000	$580
Balanced	3.43%	$537,000	$510
Conservative	1.63%	$403,000	$380

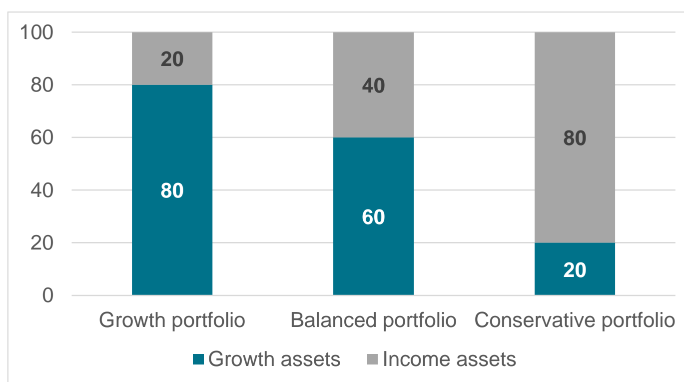
If invested in the Growth portfolio, the average return is expected to be 4.20% per annum, which translates into an estimated balance at age 65 of $610,000. By contrast, the Balanced portfolio is expected to earn a lower return (but be more stable and less risky year to year) and accumulate to $537,000. The Conservative portfolio has the lowest expected savings balance.

The savings balance can support a weekly income in the retirement years. The more one has saved, the more they can draw over the period from age 65 to 90. For someone who has invested in the Growth portfolio throughout, the expected retirement income that can be supported is $580 per week. This drops to $510 per week for the Balanced portfolio.

Over the long term, the choice of portfolio makes a big difference to the amount of savings one can expect to have and what lifestyle can be supported in their retirement. This is not without risk, though. In the appendix (page 3 onwards) more detail is given, including for different case studies.

What is a portfolio?

A portfolio is a basket of investments like shares, bonds and cash that you buy with your savings. The three portfolios differ depending on the split between growth assets (shares) and income assets (bonds and cash). The target percentage splits between growth assets and income assets of the three portfolios are:



Growth assets (shares) are expected to give higher returns, but these returns fluctuate more than the returns of income assets (bonds and cash). Hence portfolios with more growth assets are the expected to give higher returns but be more volatile than portfolios with more income assets.

All the portfolios are expected to have periods of negative returns, although these will usually be more frequent and more severe for the portfolios with more growth assets. All the portfolios have risks and returns tend to be volatile in the short term.

Two simple questions to help you choose your portfolio

1. **How soon do you expect to access the money in your portfolio?**
   a. In 7 years or more: you're likely to prefer the **Growth** portfolio.
   b. In 4 to 6 years: you're likely to prefer the **Balanced** portfolio.
   c. Within the next 3 years: you're likely to prefer the **Conservative** portfolio.

   If you don't intend to defer your benefits when you retire, your retirement date is no longer so relevant in considering the timeframe of your investments. Instead, you should consider adopting a longer investment period extending into your retirement.
2. **What's most important to you as you save and invest?**
   a. 'Likely high growth over the long term, even if that means big ups and downs in some years.' You're likely to prefer the **Growth** portfolio.
   b. 'Middle-of-the-road long-term results, with some ups and downs in my account balance.' You're likely to prefer the **Balanced** portfolio.
   c. 'Low long-term returns, but with minimal ups and downs along the way.' You're likely to prefer the **Conservative** portfolio.

MARITIME RETIREMENT SCHEME
Securing your future

Appendices: More detail

The main factors which you should consider in making your investment choice are:

- the timeframe for your investment – if you are 25 to 35 years old your timeframe should generally be 30 to 40 years, at age 45 to 55 your timeframe is likely to be 10 to 20 years and even at age 55 to 60 your timeframe is likely to be 5 to 10 years.
- the expected returns of the three portfolios - depending on your timeframe, the cumulative returns of the Growth portfolio are expected to be significantly higher than the cumulative returns of the Balanced portfolio (and the expectation is that there will be an even greater differences between the cumulative returns of the Balanced and Conservative portfolios)
- your willingness to accept some risk of a market downturn, especially as you approach retirement which could cause losses without you having time for your account balance to recover before you retire and withdraw your savings
    - if your timeframe is 20 years or more there is only a very small risk of the Growth portfolio not outperforming the Balanced portfolio (and the expectation is that, over this period, the Growth portfolio will significantly outperform the Balanced portfolio).
    - if your timeframe is 5 to 10 years there is a risk of the Growth portfolio underperforming the Balanced portfolio although the risk of any underperformance being significant (more than 5% to 10%) is small and, again, the Growth portfolio is expected to outperform the Balanced portfolio in most circumstances.
    - if your timeframe is less than 5 to 10 years, the risk of a market downturn without time for your account balance to recover increases while the scope for the Growth portfolio to outperform the Balanced portfolio (and similarly the scope for the Balanced portfolio to outperform the Conservative portfolio) reduces.

You should consider your willingness to accept fluctuations in your account balance while you are saving. Unless losses occur at the end of your savings period, they will not have a significant effect on your overall cumulative returns or the overall risk from market downturns. It is best if you aren't concerned with short-term volatility since your main concerns should be returns and risks over the full period of saving for your retirement.

Members' financial circumstances differ, and members don't all have the same tolerance for risk. As a guideline, the Trustees suggest, in general:

- until the age of 55 to 60, members should be invested in the Growth portfolio
- at age 55 to 60, members should consider switching to the Balanced portfolio
- members who intend to defer their benefits should remain in the Balanced portfolio until retirement and then progressively (but slowly) switch to the Conservative portfolio during retirement
- members who intend to withdraw their benefits when they retire should consider switching to the Conservative portfolio a few years before retirement.

Following these guidelines, as a default arrangement, new members are enrolled in the Growth portfolio* and are then switched to the Balanced portfolio at age 60. Of course, at any time members can switch to a portfolio of their choice.

* Provided they are aged under 60 at the time of joining. If a member joins the Scheme aged 60 or over, they are instead placed into the Balanced portfolio.

How much difference could this choice make to your Retirement Savings?

The earnings rates (after tax at 28%, costs, and allowing for inflation) of the three portfolios over the long-term are on average expected to be:

	Return (% per annum)
Growth portfolio	4.20%
Balanced portfolio	3.43%
Conservative portfolio	1.63%

Applying these earnings rates, the following table sets out expected account balances after 5, 10, 20 and 30 years of contributions, for members earning $90,000 and $100,000 before tax who contribute 7% with matching employer contributions:

	Annual gross earnings					
Time horizon	$90,000			$100,000		
	Growth	Balanced	Conservative	Growth	Balanced	Conservative
20 years	$320,000	$295,000	$246,000	$355,000	$328,000	$274,000
30 years	$610,000	$537,000	$403,000	$678,000	$597,000	$448,000

These estimates show that your choice between the Growth and the Balanced portfolios could make a difference to your account balance after 20 years of $27,000, and between the Balanced and the Conservative portfolios could make a further difference of $54,000. The differences are even greater if you expect to contribute for, say, 30 years.

Over the long term, your choice of investment portfolio is likely to make a substantial difference to the balance in your account at retirement. Especially if you expect to be saving for a long time for retirement without needing to access your savings, a riskier portfolio may be your better choice.

How much difference could this choice make to your retirement income?

If you contribute to the Fund for 20 or 30 years, the resulting account balances would support the following monthly payments for 15, 20, 25 and 30 years (e.g., from age 65 to ages 80, 85, 90 and 95).

Your portfolio:	Growth portfolio		Balanced portfolio		Conservative portfolio	
Invested for…	20 years	30 years	20 years	30 years	20 years	30 years
A savings balance of	$320,000	$610,000	$295,000	$537,000	$246,000	$403,000
Will support weekly income of						
Age 65 to 80	$470	$890	$430	$780	$360	$590
Age 65 to 85	$360	$690	$330	$610	$280	$460
Age 65 to 90	$300	$580	$280	$510	$230	$380
Age 65 to 95	$260	$500	$240	$440	$200	$330

The estimated future balance is taken from the previous table for the $90,000 salary level. The weekly income projections assume you are invested in the Conservative portfolio during the retirement years.

As you can see, your retirement income can vary widely depending on which portfolio you choose, how long you invest for, and how long you depend on the income.

Here's the opportunity your choice presents

Investing always brings more or less risk with it. It's why we receive returns: for taking more or less risk with our money.

If you can tolerate the ups and downs in value in the short term (those years when your balance will fall), taking on more risk is worth it in the long term. This is because you are likely to be rewarded for taking on that extra risk with a better return.

So if you have decades to go before you expect to use your invested money, the Growth portfolio is likely to be the better choice, as it's expected to generate higher returns than the Balanced or Conservative portfolios over the long term – despite its large swings in the short term.

Choosing the Conservative portfolio over the long term has an 'opportunity cost' that comes with it – you miss out on the opportunity for higher returns, which are typically tens of thousands of dollars difference in your retirement. If you are too conservative with your choice, your savings may end up too little to provide for your desired future lifestyle.

Short term ups and downs in your account balance don't matter as much as what your balance will be when you need it. As you get closer to using your money, it's generally advisable to move to a more conservative setting to reduce your chance of a loss and make sure your money will be there for you.

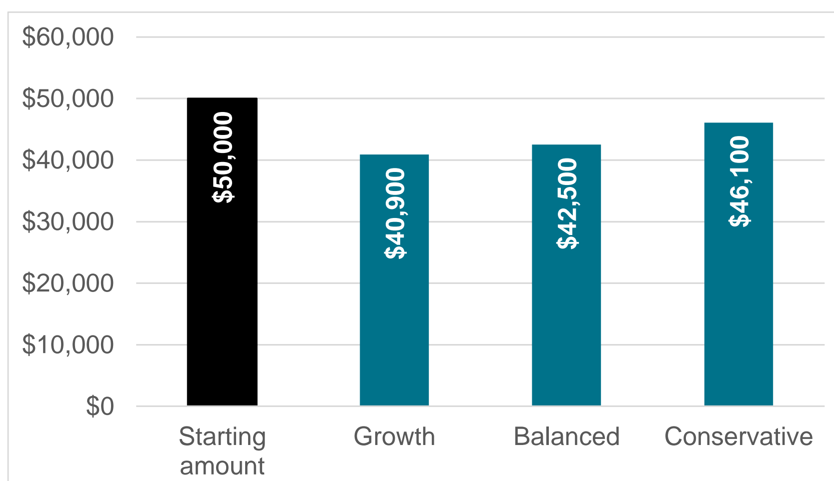
How certain are these expected returns?

To give you an idea of how the level of risk between the three portfolios varies, we can take a look statistically at how much you could stand to lose. Since the future is uncertain, these figures are calibrated to estimate the "worst year in 20 years". That is, if you picked a 20 year period in history and found the worst single year within it.

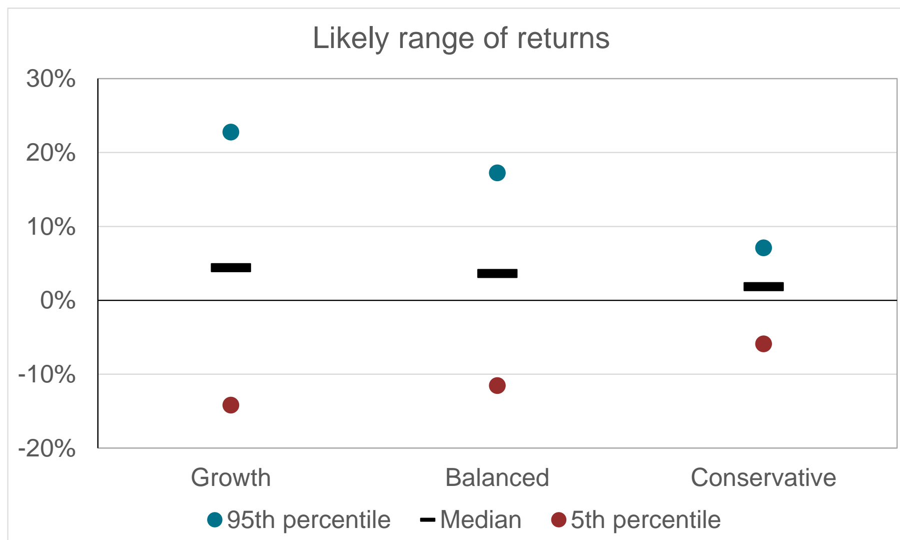
The amount varies depending on your portfolio.

- **Growth** – you could see a loss of 18%. Or $1,800 for every $10,000 you have invested.
- **Balanced** – you could see a loss of 15%. Or $1,500 for every $10,000 you have invested.
- **Conservative** you could see a loss of 8%. Or $800 for every $10,000 you have invested.

The following chart shows how this would look for a savings balance of $50,000. The Growth portfolio drops to $40,900, while the Conservative portfolio falls to $46,100.



Another way to look at the risks is to look at the range of annual returns you might experience in each of the three portfolios. The more risk you take on, the more ups and downs you are likely to experience. The following chart shows the likely range of returns (the range the annual return is predicted to lie within 90% of the time).



- **Growth** –you could see returns range from as low as -14.2% to as high as 22.8%.
- **Balanced** – you could see returns range from -11.6% to 17.2%.
- **Conservative** – in the Conservative portfolio, your returns could range -5.9% to 7.1%.

Yet another question you can ask is: how often might I expect a loss? Here's how the three portfolios differ, statistically speaking:

- **Growth** – you will see a loss 1 year in every 3 years.
- **Balanced** – you will see a loss 1 year in every 5 years.
- **Conservative** – you will see a loss 1 year in every 20 years.

As you can see, while the Growth portfolio is expected to earn the highest returns, these returns are likely to be the most volatile and come with the most risk of loss in any particular year. The Conservative portfolio is expected to earn the lowest returns, but these returns are likely to have the least ups and downs.

Overall, this means that if you invest in the Growth portfolio your account balance will be more uncertain, but there is a likelihood it will give you better returns over the long term. If you invest in the Conservative portfolio, your returns are likely to be less at risk.

Although forecasts remain uncertain…

Statistical modelling on which the above assessments of returns and risks are based are not very good at predicting the extreme risks in real-world financial markets. So while the above assessments give a sense of the expected differences in the magnitude of the losses for each portfolio, you should not be surprised to see bigger losses in the real world.

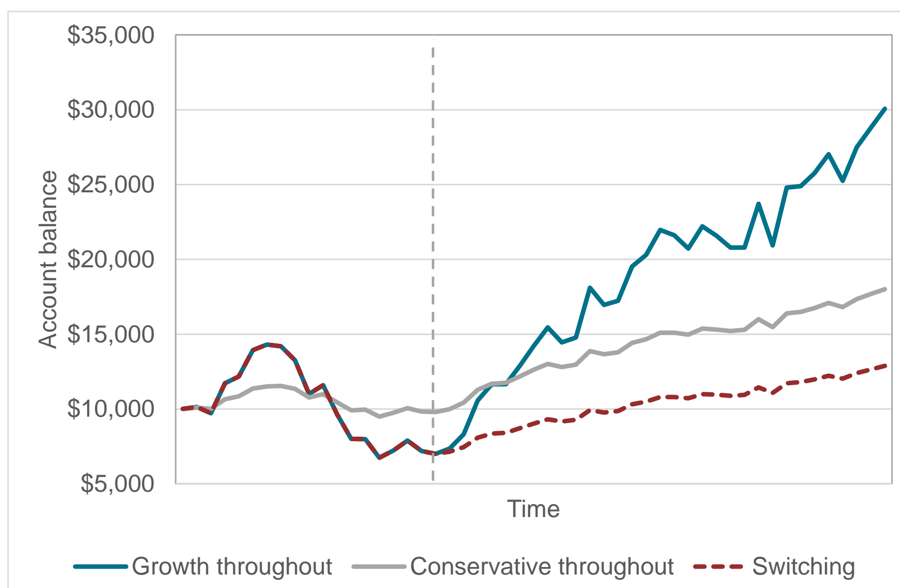
Here's how to certainly lose money

That said, there is one sure way to lose money that is to be avoided. If, during a market downturn, you see your balance falling and suddenly switch to a lower-risk portfolio, you lock-in your losses. You effectively remove any chance you have to recoup what you lost when markets recover as they always eventually do.

Recoveries can take a while or be quite quick, and timing them is near impossible. That is, if you wait to try 'jump back in', you are likely to miss out on good returns.

So for example, if you are in the Growth portfolio, see your balance fall, and suddenly switch to the Balanced or Conservative portfolios, or you are in the Balanced portfolio and switch to the Conservative portfolio, you cement your losses and will find it quite difficult to make them up.

The following chart illustrates this for a hypothetical example. Here, we begin at $10,000 in the Growth portfolio and consider the impact of switching at the vertical dashed line.



After a short period of good returns, markets crash and the Growth portfolio halves in value from almost $15,000 to $7,000. In comparison, the Conservative portfolio is still around $10,000, having not fallen as far (nor had it risen as far).

If at this point, one were to switch from the Growth to the Conservative portfolio, they would 'lock in' their losses. The Growth portfolio goes on to recover strongly, while the switcher only receives the lower (and more stable) Conservative portfolio returns.

In fact, in this example one would have been better off being in the Conservative portfolio throughout! This shows the perils of switching at the wrong time.

No one should lose sleep over their investments. If you don't think you can tolerate market volatility because you do not like seeing your account balance go up and down, you should consider investing in a lower-risk portfolio and accepting the likelihood of lower long-term returns.

How to change your portfolio settings

When you join the Scheme you will be initially enrolled in the Growth portfolio as the default option unless you specifically select another option (or unless you are aged 60 or over, where the default option is the Balanced portfolio). Thereafter, you may change your choice of investment option at any time by completing an *Investment Switch Form* which is available from the Administrator. You can choose to switch between portfolios at any time. Switches are processed on the first day of the month following receipt of the completed form.

If you never make a portfolio selection (i.e., have been enrolled in the Growth portfolio since joining), after you reach the age of 60 you will be moved to the Balanced portfolio – unless you make an investment switch application before this date.

You may, if you wish, split your account balances and your future contributions between any two, or even all three of the portfolios. The same splits will apply to your member and employer account balances, and similarly, the same splits will apply to your own contributions and to your employer contributions.

If you are close to retirement, you may wish consider switching to a lower-risk portfolio, particularly if your intention is to withdraw your benefits when you retire. You should take into account however that, when you retire, you will still need to invest your retirement savings. Assuming you expect to have a normal life expectancy, the timeframe for your savings after retirement could still be 20 years or so.