Are they truly clueless about investing?

By Chan Fook Leong

By Vince Koh

THE declaration "I don't know how to invest" is soon followed by another: "All my money is in the bank." Every so often, we come across these utterances from the public, of all ages. If our memory serves us right, we tend to hear them more from the millennials and Gen Zs.

As finance professionals, we try to offer helpful solutions and point them in the right direction: "You can access financial literacy portals, they are freely available" or "Sign up for educational courses, many are complimentary." But are millennials and Gen Zs truly clueless, or do they have deeper concerns? After some probing with friends over coffee, we uncover more insights.

Losses sound scary

Finance professionals usually have a ready stock of replies to a wide array of queries on investments. But before dishing them out to millennials and Gen Zs, we suggest taking some time to listen closely to their concerns, especially those who might not have had much exposure to finance concepts.

One of their foremost concerns, apparently, is fear of losses from investments, especially hefty losses. This is a legitimate concern, as it can be very painful to watch your nine to five sweat and toil go up in smoke during a market crash. Recently many of them witnessed first hand how the S&P 500 lost nearly 34 per cent of its value from its February 2020 high to its March 23, 2020 low at the height of the Covid-19 pandemic.

Misconceptions, knowledge gaps

Someone they know may also have suffered losses, or shared with them about their sub-par investment returns. Other concerns include whether financial advisers were attempting to sell them products which were not suitable for the sake of generating commissions.

While some concerns are genuine, others appear to arise from misconceptions and gaps in knowledge. These can often be addressed with answers from our professional tool kit.

Affirming that investors can suffer losses does help. It signals to millennials and Gen Zs that they are heard.

Financial advisers can explain to them the role of diversification and the importance of asset allocation, investment horizons and financial goals. With these strategies, the fear and stress associated with rollercoaster rides can be avoided for the "clueless" millennials and Gen Zs. When global markets tanked in March 2020, investors' first instinct was to offload lock, stock and barrel quickly. During the mad stampede out of markets, it takes courage and conviction for one to stay invested.

But had you taken a contrarian approach in March 2020, you could have reaped handsome rewards, indeed. The S&P 500 has surged by roughly 90 per cent since to 4,400 this year. Its recovery has been spearheaded by a technology wave and investors' rotation to value sectors.

Diversified global asset allocations

Putting all eggs into the S&P 500 – which comprises the 500 biggest firms listed in the US – would have meant losses in March 2020. If some eggs, however, had been placed in a global investment grade bond fund for example, the losses would have been cushioned by bond gains, as funds exiting equities rotated to safer havens such as bonds. Besides the US, investors can achieve geographical diversification by investing into other regions such as Asia and Europe. This creates a global diversified portfolio which can weather volatility.

For a start, investors can allocate their funds equally into global equities and global bonds. This investment allocation will create a global balanced portfolio, allowing investors to reduce volatility while participating in gains in equity markets. Investors can adjust the allocation of equities and bonds according to their risk appetite.

Dollar-cost averaging

Investing does not always have to involve huge sums of money. As the Chinese saying goes: "A journey of a thousand miles starts with a single step."

Investors can invest a fixed amount, say S$100, in an asset such as a S&P 500 exchange traded fund at regular intervals over a period of time. When the value of the fund rises, the S$100 will buy fewer fund units per dollar. Conversely, when its value drops, the S$100 will get you more units. In the long run, investors reduce the average cost of their investment in the fund and they get to build up wealth in a steady, gradual manner.

Anecdotal evidence suggests that millennials and Gen Zs do not invest due to a lack of compelling reasons. Accumulating funds for a HDB flat deposit, children's education or retirement seem decades away. But time is precisely the issue here, as a long runway is needed for most people to accumulate sizeable funds. ILLUSTRATION: PIXABAY

> To spur millennials and Gen-Zs into giving serious thought to early financial planning, professionals may have to turn to something outside their traditional tool kit – which is a little psychology or behavioural finance.

Danger of overlooking compounding

Anecdotal evidence also suggests that millennials and Gen Zs do not invest due to a lack of compelling reasons. They may be accumulating funds for a Housing Development Board (HDB) flat deposit, children's education, or retirement seems decades away. At present, they may be preoccupied with building their careers or travelling the world. But time is precisely the issue here, as a long runway is needed for most people to accumulate sizeable funds.

With core inflation averaging 1.6 per cent in Singapore from 1990 to 2021, prices of goods and services have been rising every year. This effectively erodes the purchasing power of your funds in the bank.

It does not help that with the pandemic, the 2020 Mercer CFA Institute Global Pension Index report on retirement systems has given a bleaker assessment of retirement adequacy. The report pointed out four factors that will reduce future retirement benefits: reduced contributions to retirement schemes, reduced investment returns, lesser future government support, and earlier access to retirement benefits.

To spur millennials and Gen Zs into giving serious thought to early financial planning, professionals may have to turn to something outside their traditional tool kit – which is a little psychology or behavioural finance.

Fear of missing out

Property marketers have been known to tap buyers' fear of missing out (FOMO) at property launches, by touting "the last few units". FOMO may be applied to the millennials and Gen Zs as well. Albert Einstein reputedly said that "compound interest is the eighth wonder of the world".

If we were to invest S$10,000 today in an asset that returns 0.05 per cent per annum over 20 years, the return at the end of the 20 years will amount to S$10,100.48.

If we invest the same sum in an asset that yields 5 per cent per annum, the return balloons to S$26,532.98 in the 20th year. Perhaps the substantial gap in the accumulated wealth over the long run may provide a sufficient FOMO reason for millennials and Gen Zs to take action early.

Early birds get the worms

An OCBC poll in 2019 found that one in three Singaporeans did not invest. Most of the respondents were also financially unprepared for retirement. We may think this predominantly applies to Gen Xs and the baby boomers.

The truth is, retirement adequacy has deteriorated for most as a result of the coronavirus pandemic. Hence, there is a need for money to work harder now. Starting sooner rather than later will allow the eighth wonder of the world to work its magic.

Chan Fook Leong, CFA, is executive director, advocacy, CFA Society Singapore. Vince Koh is CFP, ChFC, CLU, Phillip Securities (a member of the Securities Association of Singapore).