

Sujet: Hypothèse de rendement sur placements dans les planifications de retraite / Assumptions about investment returns in retirement planning.

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Today's Most Important Client Conversation

Posted By [Dan Richards, ClientInsights.ca](#) On April 14, 2010 @ 8:15 am In [Dan Richards](#) | [No Comments](#)

Of all the assumptions that go into retirement plans, none has a bigger impact than the expected return on a client's portfolio.

Media coverage about the returns investors can expect is not generally helpful in bringing clarity to this question. Often the media features attention-seeking apocalyptic voices of doom. And in part it's because when the media talks about a return forecast, they often fail to clarify whether that return is before or after inflation and whether it's for equities only or for a balanced portfolio.

Framing a client conversation

Given the importance of the decision on the expected return on investments, this is one of the most important conversations you can have with your clients.

You could start by reminding clients that over the very long term, stocks have averaged a pre-inflation return of about 10% a year – even after the market turmoil of 2008. Then acknowledge that in the last while, many credible industry voices have suggested that it would be over-optimistic to expect this kind of return going forward

When it comes to your return assumptions, there are obvious costs to being too bullish – overly rosy assumptions can result in complacency and ultimately disappointment as people fail to save enough and fall short of their goals as a result.

But there's a price to being too conservative as well, as overly pessimistic assumptions can lead to undue stress and to investors making bad financial choices. After all, if you think you're only going to get low single digit returns on stocks, why not just buy GICs?

[Access Dan Richards' compendium of articles at ClientInsights.ca](#) ^[1]

Three key decisions

To think intelligently about expected returns, you need to talk to your clients about three things.

First, shift their thinking to after inflation or real returns instead of the nominal, pre-inflation returns so commonly used. This way, you'll focus on spending power – what really counts in retirement. Indeed this is what sophisticated pension plans and high net worth investors focus on.

Second, you have to help clients extend their timeframe. The shorter their timeframe, the more dispersion they'll experience on returns – pick one year as your time horizon and you could experience swings of 50% in either direction.

Even five and ten year periods subject you to substantial swings in returns on stocks, especially if your clients do what many investors do – and set their expectations based on what happened in the last three to five years.

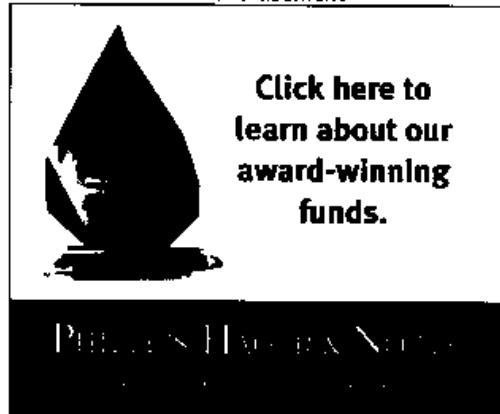
The only way to bring stability to investors' expected returns is to follow pension funds and high net worth investors – and look out fifteen or twenty years. That may seem an unduly long timeframe to some clients, but in fact that's the minimum horizon that most Canadians need to think about. Even if your clients are a 65 year old couple, half the time one of them will live to age 90. And one in ten couples will see the last survivor reach age 98 – a thirty-three time horizon.

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Looking inside average returns

The third key decision for investors is to look beyond averages.

Recently, I sat down with Michael Nairne and his team at Tacita Capital to look at data on stock market returns in the U. S. going back to 1926.

In the 85 years since then, after inflation returns have averaged 6.6%. The big difficulty with an average number is how often you'll be below it. Given the hardships imposed from underperforming a return assumption, when selecting the forecast return for the equity component of their portfolio you need to help clients look beyond the average return to the distribution of returns that got to that average -that will tell them how badly they might fall short based on historical precedent.

Since 1926, there have been 65 twenty-year periods. If we list the real returns during those 65 periods from highest to lowest - and look at how often those returns happened, here's what you end up with.

Annual return after inflation in 65 20-year periods - 1926 to 2009:

Return return	% of the time this return	Number of times this
13.3% year periods	1%	1 out of 65 20-
12.7% 65	5%	3 out of
11.9% 65	10%	7 out of
10.8% 65	20%	13 out of
9.3% 54	33%	22 out of
8.5% 65	50%	33 out of
5.0% 65	67%	42 out of

3.3% 65	"	80%	52 out of
2.2% 65	"	90%	59 out of
1.8% 65	"	95%	62 out of
0.8% 65	"	100%	65 out of

Picking the right number

In recommending the expected return for the stock component of clients' investments, you could pick the after inflation return that's half way down the list - that would give you a return of 8.5%. Despite this, given the price of falling short of the return assumption, few advisors would suggest assuming the historical median of an 8.5% real return on stocks.

For most investors, assuming a real return on equities of 3% to 5% will likely make sense; 5% was achieved two thirds of the time, 3% was exceeded 80% of the time.

To put these numbers in perspective, the CPP Investment Board assumes a real return of 4.2% for a portfolio with a 60% stock weighting, reflecting equity returns of 5% or more. And a recent article in the Financial Analyst's Journal forecast a real return of 4% for U.S. stocks.

Finally, for clients who want to be really cautious, you could pick 2%; 1.8% was delivered 95% of the time, in 62 out of 65 twenty year periods.

Of note, the worst after inflation returns all occurred during the high inflation years in the 1970s. As a result, your recommendation on the return assumption for the stock component of clients' savings will be heavily influenced by your concern about a return to inflation.

Picking the return assumption to recommend for equities will vary with your own and your clients' attitude towards risk - there clearly is no one right number.

However, by focusing on after inflation returns, taking a long term view and digging deep into the range of historical experience, you can help clients end up with a realistic number that strikes the right balance between undue optimism and extreme pessimism.

To read the full column in Investment Executive, click here:

*Now utilisons dans nos
planification : inflation 2 1/2%
recommand 2 1/2%*

*5%
TOTAL*