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Winter Newsletter

Economic update

It seems the end of the economic downturn is in sight, with the economy edging back in the black by 2010 – this was the positive message of a surprisingly mild annual budget that was heavy on short term infrastructure stimulus and light on short term cut backs. The immediate budget winners were pensioners. The biggest losers were the top 2% of income earners (earning $150,000 plus per year) who face restrictions on both private health subsidies and tax minimisation strategies such as hobby farms. The biggest long term change was the extension of the pension eligibility age from 65 to 67 by 2023, starting in 2017.

On a positive note, the Australian Reserve Bank and the Treasury Department both predict the recession will be relatively mild and short for Australia, with China, our major trading partner, already showing signs of early recovery. The RBA also forecasts fairly stable interest and inflation rates for the foreseeable future. Australia's biggest short term problem will be a spike in unemployment, which is estimated to reach 8.5% in 2010.[1]

And what of Australian share prices? No radical about turns yet, but there has been some life in the market in recent weeks. Many analysts have pointed out that deep recessions often result in steep recoveries within 12 months – the famous V-curve. Others favour a slow but steady upward trend as economic conditions improve.[2] Who is right? Time will tell.

1. www.abc.com.au Tony Eastley
2. www.fmd.com.au/downloads/Olivers%20Insights

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General Advice Warning: This advice may not be suitable to you because it contains general advice that has not been tailored to your personal circumstances. Please seek personal financial advice prior to acting on this information. **Investment Performance:** Past performance is not a reliable guide to future returns as future returns may differ from and be more or less volatile than past returns.

Is SUPER not so super anymore?

"Favourable tax concessions are still applicable".

It's not surprising some investors are hesitant to be reminded of their super balance after the onset of the global financial crisis.

After all, the value of just about everybody's super fund investment has shrunk. Further jolting people's faith in super has been the recent Federal Budget announcement halving the available tax deduction for super contributions from July 1st 2009. So the big question now is, "has super become a poor investment choice"?

The truth about superannuation is that it can never be a bad investment because it is not an investment at all. A superannuation fund is an investment vehicle offering attractive government tax concessions to encourage you to save for and fund your own retirement. Remember, these concessions still apply even after the Federal Budget. The most significant change, applying from 1 July 2009 if passed in the Senate, will impose a $25,000 limit to tax deductible superannuation contributions if you are under age 50. For those over age 50, a temporary limit of $50,000 will apply until 2012.

Obviously, having given you a major tax concession to save for your old age, the government has to put rules in place to prevent you accessing it before you retire.[1] This means that super (or a large part of it) is generally seen as a long term venture even for retirees. To put this into perspective, a retired couple aged 65 years today, still have an average life expectancy of 19.45 years, meaning their money needs to last at least that long with some margin for error.

This is why most professional fund managers invest a large proportion of superannuation funds in the asset class proven to have outperformed others over the long term – shares.[2] Over the last 125 years, through wars and depressions, the average return on Australian shares has been an impressive 11.2% per annum.[3]

Painfully for all of us who have superannuation money in the share market, the falls of the last 18 months have taken a big bite out of our retirement savings. As a result, many investors are looking for an alternative that is safer than shares, one that will also help them recover the value they have lost. And there's the rub. What investment other than shares has the potential to keep on growing your nest egg to make good the losses you have already suffered, and in many cases also pay you a tax effective income stream via dividends?

Do you think something as safe and solid as a bar of gold would do it? Gold has increased in value by 300% in 50 years (from around $300 an ounce in the 1960s to $900+ today), but this only represents compound interest of 6% pa. This is around half of the historical return on shares – and who knows what the gold price will be in 10, 20 or 30 years time.[4]

And what about that classic safe investment, fixed interest deposits? While our banking system is pretty safe by world standards, fixed interest investment is very unlikely to ever recreate the wealth you have recently lost unless you have a very long time to invest. Even by harnessing the magic multiplying power of compound interest, capital invested at 5% pa today would take 15 years to double in value. Shares have historically doubled at more than twice this rate, because they offer dividend income and capital growth.[5]

Not surprisingly, almost every financial writer and investment specialist in Australia agrees on one thing: What the share market has taken away, the share market is most likely to replace over time and exceed. It is just a matter of when. Remember, superannuation is a concessionally taxed investment vehicle, not an investment, and what you do within that vehicle is the key.

1. Superannuation can be accessed from age 55 (if conditions of release are satisfied) or alternatively reaching age 65. 2. Diversification is always an important consideration. You should seek advice before choosing an asset allocation for your investments. The average superannuation 'default' fund allocates between 60%-70% of funds to growth based assets. 3. Perennial – Economic and Market Outlook February 2009. 4. Datastream 5. Datastream.

Poorly constructed wills can lead to unintended consequences.

Will power – how to get it and how to lose it.

Most of us are too involved in the business of living to worry too much about what might happen to our assets after we're gone. But the more you own, and the more complex family life can become as a result of second marriages, de facto relationships and blended families, the more important it is to take estate planning seriously and leave a valid and watertight will behind you.

Poorly constructed wills, often the result of "do-it-yourself" will kits, can lead to unintended consequences, adding an extra burden on families already dealing with grief, or forcing heirs to pay a much higher tax bill than might have been the case.

Drawing up a will is particularly important when you get married or remarry. This is because under Australian law a marriage revokes any existing will - but divorce does not. Many people are unaware of this rule and, as a result, an estate can be left to an ex-spouse by accident, leaving a second spouse and family penniless.

Case Study

David and Mary both 48 years old are on their second marriage, both having had children from their first marriages. David came into the marriage with substantial assets including several investment properties. When David dies, he wants to provide for Mary, and also ensure that his children from his first marriage receive a part of his estate.

David and Mary don't seek professional advice and instead complete a "do-it-yourself" will kit leaving each other their estate on the understanding that both David and Mary's children will share equally in the estate, once the surviving spouse dies.

Shortly after, David tragically dies in a car accident. During the emotional time that follows David's death, Mary turns to David's old friend Richard for comfort. This causes a rift between David's children and Mary. Sadly, Mary then dies 2 years later from cancer.

Unfortunately for David's children, Mary has remade her will in the intervening period and has left all her assets, including the substantial assets left to her by David, to her own children. David's children receive nothing!

How could David have ensured his estate would be distributed according to his wishes? In drawing up his will, David could have created a life interest in his estate.

A life interest would give Mary the use of all his assets within the estate only until she dies. Once Mary dies, those assets would revert to the 'remaindermen' – in this case BOTH David and Mary's children.

The use of life interests is common for farming properties, second marriages and providing for disabled children. In the case of a disabled child, a family may wish to leave assets to provide for the disabled child during his or her lifetime, and then pass those assets to the other children upon the death of the disabled child.

If you have worked hard all your life to build up assets, you owe it to yourself to make sure they are passed on exactly as you wish them to be. Professional advice is important as there are many estate planning strategies including the use of testamentary trusts that can assist you in protecting your estate.

Call our office to discuss your specific estate planning requirements and we'll point you in the right direction.

How committed are you?

Staying motivated is like staying married - you have to work at it!

Beginning a new personal project is a lot like falling in love. Like a relationship, a project has both ups and downs – sometimes you feel very passionate and enthusiastic, and at other times you don't.

Think back on the last bright idea you had – perhaps you were going to start a blog site to lift awareness of your business, join a gym to improve your fitness, create and stick to a budget, or even start writing a book?

Sadly, while many of us enthusiastically commit to these personal projects, very few of us stick with them. American statistics show that 80% of new gym members drop out after the first 8 weeks and more than 25% of blogs are abandoned after the first post.

Why is it so hard sometimes to sustain initial motivation and enthusiasm and carry a new project through to a successful conclusion? Starting a new project has many similarities to falling in love.

When we first fall in love, we are totally obsessed with our new partner, can't bear to be separated from the new love of our life, and think about them constantly.

Similarly, many of us are completely obsessed with a new project when we first begin it and spend every waking moment thinking about it or working on it.

For people falling in love, this is an important first step in the pair bonding process, but of course one simply can't live at that level of heightened emotions for the rest of one's life. So what happens then? Successful long term relationships require more than attraction and enthusiasm to keep the flame burning. They are grounded in commitment as well - that is why they survive the inevitable ups and downs.

By the same token, if you can establish a long term commitment to your personal project and keep reminding yourself of its importance to you, it has a much higher chance of success especially if you are sensible enough to realise from the start that any worthwhile project is likely to cause changes and make extra demands on your life and leisure time.

A useful way of maintaining motivation is to record the enthusiasm you felt for the project when you first started it.

Make detailed notes right at the beginning of a project, accurately recording your hopes and dreams and describing the importance of the project to you and what you hope to achieve. Refer to these notes at least once a month to remind yourself that your project is important to you and worth committing to.

Tell your friends, family and co-workers about your project. It's more likely you'll go that extra mile when you've said something publicly - it helps to make you accountable. Focus on the small achievements and ensure you celebrate the small successes.

In other words, next time don't just get excited about a bright idea - marry it!

A thought from Charles Kingsley 1819-1875...

'We act as though comfort and luxury are the chief requirements of life, when all we need to make us happy is something to be enthusiatic about'.