bravium

Newsletter

Summer 2010

Welcome

A warm welcome to the Summer newsletter, and some stimulating additions to your holiday reading.

Australians are thinking about holiday plans now, and the current strength of the Australian dollar makes travel to the US and Europe more affordable. In our article on exchange rates, we take a closer look at the pluses and minuses of currency fluctuations, what the future might hold, and how both business and investors manage currency risk.

We also take a closer look at the income options available to the over 55s, with a focus on how transition to retirement pensions contribute to your financial future.

And to set you up for the New Year, we look at the vexed issue of time — how to use it productively rather than lose it.

We hope you and your families have an enjoyable and relaxing time over the Christmas break and if you are going away that you travel safely.

Kind Regards,

Scott Farmer

Latest news

As the year draws to a close, it has become even clearer that the Australian economy is fit and healthy in comparison to much of the developed world. When the Reserve Bank (RBA) raised interest rates in November, the banks' out-of-cycle hikes stirred public resentment but took pressure off the need for future official rises. As employment comes closer to full capacity and pressures emerge in wage rates, the RBA will be watching for signs of inflation.

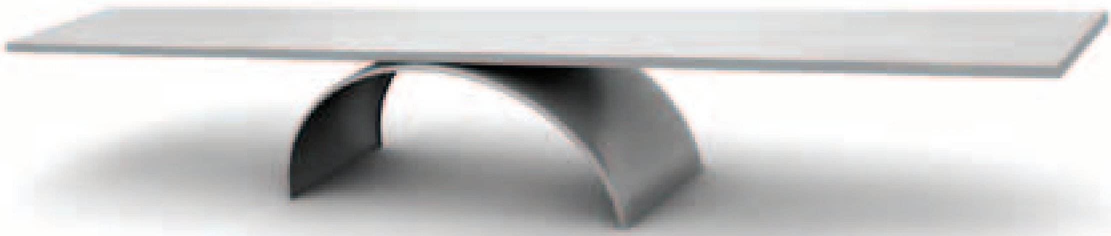
House prices have settled in most states, while construction figures are down in the September quarter but up over the past year. Nationally, the resource states are providing strong impetus to the 2011 outlook. October's labour figures showed a rise in participation rates and annual employment growth of 3.4 per cent, the strongest since January 2007. Consumer confidence levels remain well above the long-term average, suggesting a solid Christmas season for retailers.

However, overseas news remains downbeat at best. In the US, the Federal Reserve began a risky second round of "quantitative easing" or QE2 to kick-start the sluggish local economy.

Nervousness returned to Europe with the spotlight on Irish debt levels, while closer to home our market is watching cautiously to see how the Chinese government deals with inflation and currency issues. In southern skies the sun is definitely out, but there are still dark clouds around.

GOING DOLLAR FOR DOLLAR

Is parity with the US now business as usual?



When the Australian dollar (AU$) achieved parity and then topped the value of the greenback (US$) in October and November 2010 there was much excitement in the media.

It took the AU$ nearly 30 years to hit parity and the hype made it seem a breakthrough had occurred. But what does it really mean? If you are planning to take the kids to Disneyland, it is certainly good news. But if you are selling Australian holidays to tourists from the USA, it's bad news.

Currency fluctuations produce winners and losers because currency values are relative; "parity" means "equal with" because currencies come in pairs — US$ versus AU$, AU$ versus Euro, and so on. It is their relative values which are important, and these are influenced by local and global issues.

Getting parity into perspective

The AU$ and the Canadian dollar are both rising against the US$. That highlights that there are multiple causes of currency fluctuations: in this case, the current strength of two well-managed, resource-based economies versus the weakness of the US economy.

Right now the US is certainly in a tight spot. The economy is struggling to go forward and unemployment remains high. The US Federal Reserve recently decided to inject more cash into the economy by buying its own government bonds, but this is an inflationary strategy that carries an element of risk. Another possible outcome is that the AU$ will fall in value against the US$. Early indications are that this is happening, at least in the short term.

A new era - or back to normal?

The key question is whether the AU$ will remain one-for-one with the US$ in the longer term. The Australian Reserve Bank thinks our dollar will be at or above parity for the next three years. Other commentators believe that the US Federal Reserve's tactic of increasing the money flow will lead the AU$ down to the US$0.90 cent mark within a year.

One Australian economist, Dr Shane Oliver, believes that the AU$ will be around parity for a decade or more because of the underlying strength of the local economy and our trading position. He argues that, as the graph shows, this was the case for 82 years between 1900 and 1982, and suggests that it was the last 28 years that were abnormal.

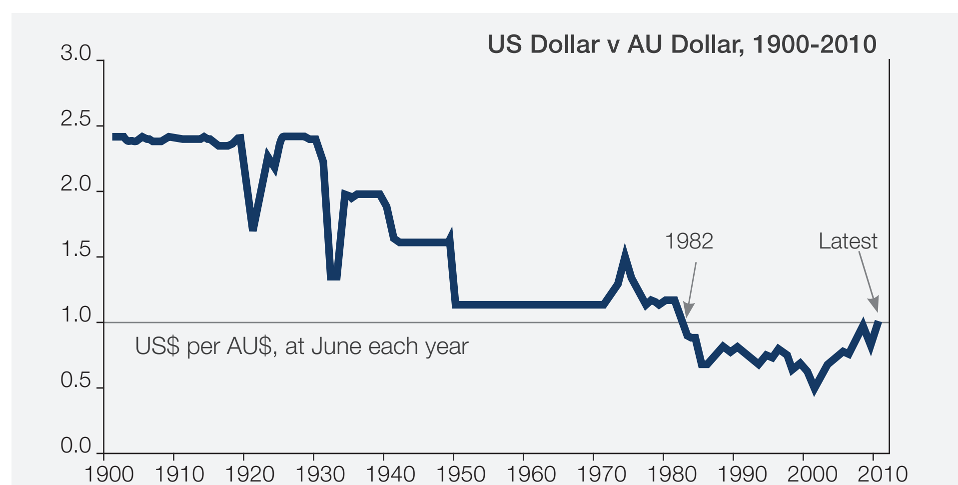
Where to next?

Predictions can't be made but some trends seem clear. The Australian economy is relatively strong and likely to remain that way while there is solid demand for our resources from China, India and other developing economies in Asia. Globally, investors compare our economy with those of major developed nations and see it as strong and well-managed, with stable inflation and interest rates. With currencies, it is relative strength and performance which are important, and if these factors remain stable, they will support a stronger AU$.

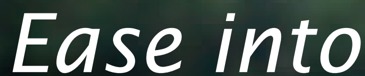
When dealing with currency, both companies and investors have to consider risk. Do they opt, like BHP Billiton for example, not to hedge currencies or commodity prices but manage risk carefully while remaining open to price movements? Or do they side with Rio Tinto, and take hedged positions? One size does not fit all, no more than any one currency is the investor's perfect answer.

This is an important and often complex issue affecting investment decisions, so we encourage you to contact us and discuss any concerns.

If the pundits are correct and parity becomes standard fare, chances are you'll be able to take the family to Disneyland this coming year — and line up again in a few years' time.



Source: Thomson Financial, AMP Capital Investors



RETIREMENT

the modern way

Just as Australians have taken to self-managed super funds, so they have taken to super pensions. Only they are not waiting until they are 65 as their parents had to, but they are starting pensions when they turn 55 or 60.

With the flexibility of a non-commutable account-based pension (NCAP), they can make real choices about how much they work, while at the same time building up their superannuation accounts and getting the benefit of significant tax advantages. Many have embraced their new-found flexibility. This strategy works for individuals remaining in their current job, cutting back their hours or stopping work to spend more time with the grandkids and golf clubs.

How does an NCAP work?

Once you have enjoyed your 55th birthday celebrations, you can elect to convert all or some of your super to an NCAP and nominate a minimum pension amount you will draw down each year. That level is determined by your age: for example, 4 per cent if you're under 65 (except that it is 2 per cent until 30 June 2011 to allow funds to recover some ground after the GFC). There are penalties if you don't take the minimum, but you can also re-contribute as part of your super strategy.

There are quite a few rules to observe but there is a lot of flexibility at the same time — provided you follow the rules! (Just remember that the rules are there because you receive tax advantages whenever your money goes into your super account.)

You can continue to work full or part time while receiving income from your NCAP, and keep tipping money back in, up to the contribution limits. This reduces your taxable income, lets you put more aside, and can allow you to maintain your disposable income level all at once. If you only have a small amount in super or were hit hard by the GFC, it also gives you a chance to catch up towards the end of your working life.

Case study – Jenny's story

Jenny is a 55 year old professional person, and plans to retire at 65. She earns $110,000 per year, and already has $485,000 in super. She wants to maintain her current income level while building her super account balance.

To achieve these objectives, Jenny commences an NCAP while salary sacrificing a larger pre-tax portion of her income into super; this is taxed at 15 per cent, not at her marginal rate.

The NCAP's tax advantages reduce Jenny's personal income tax; the investment earnings and growth on her pension account are tax free; plus, her NCAP income is taxed at a concessional rate. Using this strategy, Jenny can salary sacrifice and will boost her superannuation by around $68,000 when she turns 65.[1]

Getting started

When you look closely at Jenny's story you can see it is made up of a number of components that sit alongside the NCAP, especially salary sacrificing and making contributions within available limits. Minimising the pension payment and maximising the salary sacrifice component will deliver the gains she is looking for. And when Jenny turns 60 the rules change again, and she may need to revisit her strategy.

Linking an NCAP with other super strategies brings a series of tax breaks into play, most of them involved with putting money into super and taking it out again, which may sound simple but must be done by the book. And you must know what your annual contribution limits are, both concessional and non-concessional.

While more and more Australians are taking this early pension path, there is no simple "off-the-shelf" option. Liquidity issues, risk management, and the needs and broader investment strategies of individual clients are just some of the considerations. If you do want to know more about this strategy and the benefits it can bring you, please be sure to contact us.

1 Assumptions: The projections in this strategy are based on various assumptions, including, but not limited to: selected pension payment = $32,133 in year 1; salary sacrifice = $40,100 in year 1; no change in take-home pay before/after strategy; no change in risk profile; estimated investment return (Growth portfolio) = 6.4% pa (super), 7.3% pa (pension); all investment earnings figures are after tax and after fees; no change in Super Guarantee contributions, i.e. 9% of $110,000; administration fees and charges are not included. Note that taxable pension income from an NCAP qualifies for a 15 per cent tax offset if aged 55–59. The payment is tax free if over age 60. Note that taxable pension income from an NCAP qualifies for a 15 per cent tax offset if aged 55–59. The payment is tax free if over age 60.

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THE TIME *of* YOUR LIFE

BUT ARE YOU MAKING THE MOST OF IT?

If you knew you only had 6 months to live, would you choose to spend your time differently? A study by Charlie Breeding, a life coach from Dale Carnegie Training addressed this question. It's probably no surprise respondents chose spending more quality time with family and friends (and mending frayed relationships) ahead of work commitments. The study provides an interesting conclusion – why not live like you only have 6 months left, irrespective of your health?

Many people argue they don't have enough time in the day to achieve much other than the bare essentials of daily life. Would getting out of bed at 5.00 am each day to "save" time or "make" time help? Would you achieve more? Or would you just feel tired and under pressure after the first week of disciplined early mornings?

Time's building blocks

There are a few time basics we shouldn't overlook as we grapple with these questions. First, we all have the same time available, the same 24 hours in every day. The second point is that if you have too much to do, too many places to go, people to see, things to read, then there is usually one cause — yes, it is you. Most of us make our own choices and decisions about what we do in each 24 hour day. We are the ones that make ourselves busy.

Time's myths

To help us sort out a way forward, Breeding lists what he calls some "myth-conceptions":

- If you speed up, and keep active, you get more done. Wrong; *acting without thinking first gets little done.*
- If you want something done right, do it yourself. Not so; *you need to prioritise rather than attempt everything.*
- If you delay until the deadline looms, you will be more productive. No; *you will not have time to deliver your best.*
- If you're asked, should you help others? Yes; *but be aware that solving other people's problems won't help with your own – so be selective in your help.*

Planning — never a waste of time

If every day is made up of the same amount of time for each one of us, then it is how we use it that makes the difference. That is why it helps to have a list of priorities, in our minds or written down. Sixty seconds a day spent firming up and ordering your priorities will save you hours wasted on inessentials and help you achieve more of the things that really matter.

Your time balance sheet

The Melbourne Institute of Applied Economic and Social Research found that close to one in four (23 per cent) employees are working at least 50 hours a week. Many of these employees are trapped by the lure of promotion and more dollars, and find they cannot reduce their hours even if they desperately want time out.

Trapped in what the study calls the work-and-spend cycle, people seek higher incomes and, as a result, find themselves putting in more hours to buy more expensive goods and often incur more debt which perpetuates the need for more work – and less time to do other things.

Getting off the treadmill or at least turning down the treadmill's speed dial might not only free the need for extra debt and extra spending, but it can have an amazing effect on attitudes towards both work and time.

More time means more opportunity to focus on what matters most to you.

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.

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