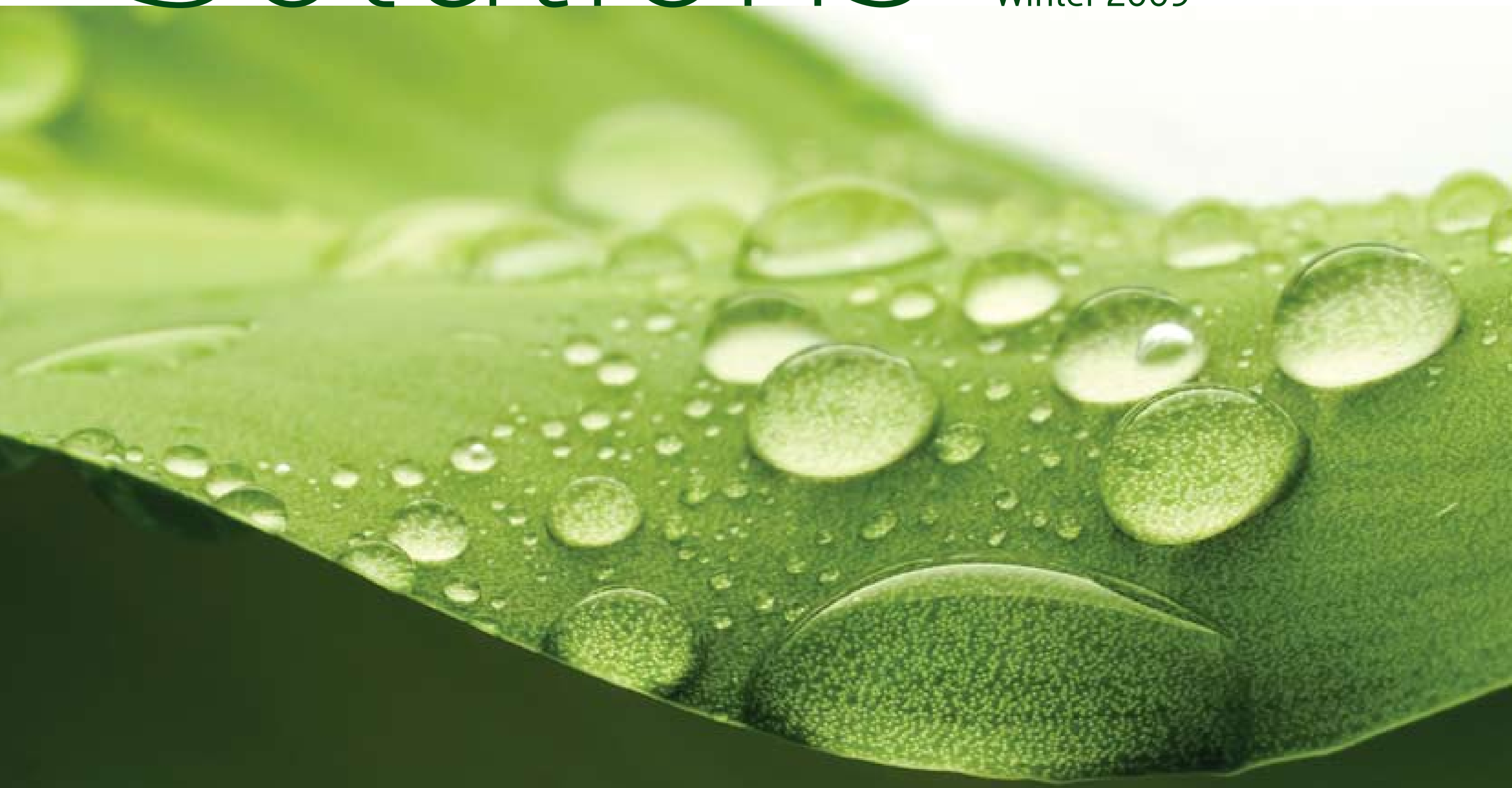
Investment Solutions

Winter 2009



Super: still a smart investment

What's inside:

Snippets

Super reporting

The government has introduced legislation requiring super funds to prominently display long-term returns in member statements. Five and ten-year returns must be highlighted and disclosed at the investment option or sub-plan level in which the member is invested.

Many super funds already report medium and long-term returns. The aim of this compulsory disclosure is to help super funds better communicate their fund's performance over a market cycle (including rising, falling and flat markets) and to ensure uniformity across the industry.

See our article on page 4 which discusses why it's important to focus on long-term super returns.

Compulsory super is turning 20

After nearly 20 years of compulsory super the Government has announced a review of Australia's compulsory superannuation system.

Described as "world leading" Australia's system has some $1.1 trillion under management on behalf of working Australians.

"This landmark process will examine the structure, operation and efficiency of the superannuation system," said Nick Sherry, Minister for Superannuation.

He believes the review, with all parts of the superannuation sector on board, will assist in maintaining community confidence in our world-class system.

Tips to safeguard your financial identity

The Australian Competition and Consumer Commission estimates that identity fraud costs the Australian community in excess of $1 billion annually. Here are some tips to protect your personal information.

Beware the phishers and vishers
Be wary of emails or phone calls that appear to come from your bank – these may be phishing (email) or vishing (phone) scams to get your personal details.

Don't post your personal details online
Fraudsters may scour your profile for personal information which they can use to pass themselves off as you. Never put your personal financial information in an email.

Disable pop-ups
Clicking pop-up messages may allow others to download and install a program on your PC to spy on you and steal your identity.

Change your password often
Use a combination of letters, numbers and punctuation and change passwords frequently.

Safe online banking
When you visit secure sites, make sure you always log out. Avoid using public computers for internet banking. Most banks have PCs in their branches where you can access internet banking securely.

Is the website secure?
If you're asked to provide personal information online, check that the details in the address bar of the browser start with 'https' – the 's' stands for 'secure'.

Don't throw out personal information
Fraudsters may go through your rubbish. Destroy account statements and cards to stop them getting hold of your personal information.

Check your credit report
Make sure your name isn't being used to run up debts. Your credit report contains your personal details and shows credit applications and defaults. You can get a free copy of your credit report from My Credit File (Veda Advantage), Dun and Bradstreet or Tasmanian Collection Service.

Is your car really worth more than you?

Over time, your income is your major asset. You may have car, home and contents insurance, but your life and income is far more valuable.

Having your car stolen or wrecked would be a relatively minor inconvenience. Your insurance may well cover the cost of a hire car until you get your own car fixed. It would be devastating to have your house broken into and your prized possessions stolen. Worse still if your house burnt down and you lost everything.

Difficult as it may be, material possessions can be replaced. This is not always the case for your health.

Protecting against loss of income

If you were to suffer a debilitating sickness or have an accident that left you unable to work, how would you cope? Once your savings run out, how would you cover your mortgage or other loans? What about food and utilities, or medical bills not covered by your private health fund or Medicare?

Income protection insurance helps you manage the unexpected and stay financially stable. You can generally insure up to 75 per cent of your income, which means you shouldn't have to use savings, borrow money, or sell assets to pay off debts and cover day-to-day living expenses.

Life insurance

We were all witness to the devastating Victorian bushfires when hundreds of homes – and lives – were lost. But very few people would personally know someone who has lost their home or their life in this way.

On the other hand, many people know of someone who has been diagnosed with heart disease or cancer. Some are lucky enough to survive, but for others there is no cure.

Have you ever given a thought about how your family would cope if you were to become terminally ill or die unexpectedly? How much money would literally just disappear from your family's weekly budget? On top of the emotional upset, your family would be left with financial headaches.

You can make sure that doesn't happen by taking out adequate cover on your life and that of your partner. You should also make sure your insurance covers you for total and permanent disability and terminal illness so your family is protected if you become permanently incapacitated or suffer a terminal illness.

Deciding how much you need

To work out the right level of cover, you will need to think about your current lifestyle. Add up how much you'd need to pay off all your debts and how much you spend each year on day-to-day living costs. This will give you a reasonable idea of the size of lump-sum payment your family would need to help them through.

You may already have life insurance cover. You may even have a number of insurance policies. If that's the case, you should still check how much cover you actually need. If you are over-insured, you could be paying out more in premiums than you need to – and that money may be of more value to you if you invest it.

Recent statistics

Residential fires in Australia 2008*

The table shows the number of residential fires by state in 2008.

State	Total residential fires
NSW	4,938
VIC	3,252
TAS	412
SA	620
WA	1,559
NT	194
QLD	1,787
ACT	294

Top three causes of death in Australia 2007^

Ischemic heart diseases (which include angina, blocked arteries of the heart and heart attacks) were identified as the underlying cause of 22,729 deaths (16 per cent) of all deaths registered in Australia. Strokes (including haemorrhages, infarctions and blocked arteries of the brain) were the second leading underlying cause of death. Trachea and lung cancer have been the third underlying cause since 1998 and deaths from cancers have increased in number from 6,742 in 1998 to 7,626 in 2007.

* 2009 Duracell National Fire Safety Report.

^ Australian Bureau of Statistics: Causes of Death, Australia, 2007

Why super still makes sense

Many financial experts agree: super is still the most effective way to save for your retirement.

Generally, your super fund will invest via managed funds. You (and other fund members) buy units in the funds and the funds buy shares. If you contribute to your super fund on a regular basis, you'll buy units on a regular basis. When share prices are low (as they currently are), unit prices are low. You'll be buying more units in the fund, which means you should be well placed when the market rebounds.

Case study: personal contributions

Let's compare two work colleagues and their personal super contributions over a 24-month period.

David and Martin have been making personal contributions of $250 a month to their respective super funds to be invested in the same investments. After eight months, they both hold the same number of units. Share prices have been dropping, so Martin decides to stop his additional monthly contributions. When the markets start to recover, Martin starts his extra contributions again.

The table shows the effect on Martin's super balance of the contributions he missed from month eight.

		David		Martin	
Month	Unit price	Total units bought	Total units held	Total units bought	Total units held
8			1224.98		1224.98
9	$1.56	160.26	1385.24	-	1224.98
10	$1.53	163.39	1548.63	-	1224.98
11	$1.49	167.79	1716.42	-	1224.98
12	$1.44	173.61	1890.03	-	1224.98
13	$1.47	170.07	2060.10	-	1224.98
14	$1.51	165.56	2225.66	-	1224.98
15	$1.56	160.26	2385.92	-	1224.98
16	$1.58	158.23	2544.15	-	1224.98
17	$1.61	155.27	2699.42	155.27	1380.25
18	$1.62	154.33	2853.75	154.33	1534.58
19	$1.60	156.25	3010.00	156.25	1690.83
20	$1.64	152.43	3162.43	152.43	1843.26
21	$1.68	148.81	3311.24	148.81	1992.07
22	$1.70	147.06	3458.30	147.06	2139.13
23	$1.73	144.51	3602.81	144.51	2283.64
24	$1.77	141.24	3744.05	141.24	2424.88
Contributions			$6000.00		$4000.00
Total number of units held			3744.05		2424.89
Balance within super at 24 months (number of units x current unit price)			$6626.97		$4292.05

Assumptions: Zero balance at month 0. Contributions net of 15% contributions tax. Does not take into account fees, charges or other taxes.

As you can see, when the prices were at their lowest in the 11th, 12th and 13th month, David's monthly contributions bought more units. If the unit price continues to rise, David's overall balance will be greater because of the additional units he bought at a lower price.

Government Co-contribution

Let the government help you give your super a boost. If your total income is less than $60,342 and you make personal contributions of up to $1,000 to your super, you could be eligible for a Government Co-contribution. Depending on your income, the Government may match your contribution by $1.50 for every $1. That's like getting a 150 per cent return on your investment!

Super facts

A Newspoll survey conducted by the Australian Institute of Superannuation Trustees in March found that 57 per cent of people already making voluntary contributions are planning to continue this year. Around 17 per cent have changed to a more conservative style but only 11 per cent have switched super funds.

Deloitte forecasts that super assets will more than quadruple in the next 20 years and the industry's current assets under management of $1.2 trillion will reach $2 trillion by 2014, $3 trillion by 2018 and $7 trillion by 2028.*

* The Dynamics of the Australian Superannuation System: the next 20 years 2009 – 2028

Smart tax strategies

There are a number of strategies you may benefit from if you take action before the end of this financial year. While it's still uncertain whether we've reached the bottom of the market, we're definitely at a low point so now is a good time to be considering such investments.

Making the most of your bonus

If you know you'll be getting a pay rise or bonus soon, you can arrange with your employer to salary sacrifice the extra money into your super fund. The benefits of this strategy are twofold.

Firstly, you'll be bumping up your super balance. Secondly, you reduce your tax liability. Instead of paying tax at your marginal rate, the amount you salary sacrifice becomes a taxable contribution received by the fund. The contribution (plus any income earned on the investment) is generally taxed at a maximum rate of 15%.

Once you turn 60, pension payments and income from your super fund are paid to you tax-free.

Case study: Bryan

Bryan will be receiving a bonus of $5,000. If he takes it as part of his normal salary, it will be taxed at his marginal tax rate of 40 per cent.

If he then invests this cash for a year and receives interest at 4 per cent, this also becomes part of his taxable income for that year. This is again taxed at Bryan's marginal rate of 40 per cent.

If Bryan salary sacrifices the $5,000 to his super fund, the fund will tax the contribution at only 15 per cent. He directs this to his super fund's cash management account where it earns 4 per cent for the year, which is also taxed at 15 per cent. The table shows Bryan's investment at the end of the year.

Even if the super fund deducts an administration fee of 5 per cent from his super investment, Bryan is still better off to the tune of about $1,000.

	Scenario 1: Bonus taken as salary ($)	Scenario 2: Bonus salary sacrificed to super and taxed by super fund ($)[2]
	5,000[1]	5,000
Tax payable	2,000	750
Net amount invested	3,000	4,250
Interest on investment after 1 year	120	170
Tax on investment	48	25.50
Net investment income	72	144.50
Total net investment after 1 year	3072	4394.50[3]

Assumptions:

[1] Bonus amount is over the 40% threshold for tax.

[2] Bryan has a salary sacrifice agreement with his employer prior to earning or knowing his bonus amount.

[3] Total amount before administration or other fees.

Additional contributions

Personal after-tax (known as 'non-concessional') contributions aren't taxed on entry by your super fund and any earnings on investment are taxed at a maximum rate of 15%. When you access these contributions in the future they are paid to you tax-free.

There is a cap on non-concessional contributions of $150,000 per year. Anything over this attracts tax at 46.5%. Provided you're 64 or under on 1 July in any financial year, you can take advantage of the 'averaging rule' to bring forward two years worth of non-concessional contributions – up to $450,000 over the three-year period.

Top up your spouse's super

If your spouse's income is between $10,800 and $13,800 you can claim a tax rebate of up to $540 by making contributions to your spouse's super. The maximum contribution you can claim as a tax offset reduces by $1 for every $1 extra that your partner earns.

Gearing – prepay interest

Pre-paying some or all of the interest due on your gearing loan for the 2009-2010 financial year in the current financial year can be of benefit if your marginal tax rate is likely to be lower next year.

Time to lock in your home loan?

One of the curly choices you need to make when taking out a mortgage is whether to opt for a variable or a fixed interest rate loan.

There are advantages and disadvantages to each of these options and the choice you make will depend on which type of loan best suits your circumstances. So let's examine the pros and cons.

Variable rate: pros

- You may get a 'honeymoon' rate for the first year, which means you start with a lower repayment.
- If interest rates drop, so does your payment. This frees up money or allows you to pay more off the principal.
- It's generally easier to increase or decrease your monthly repayments if your circumstances change.
- Low or no penalty for paying off the loan early.

Variable rate: cons

- If interest rates go up, so do your payments.
- If rates go too high you may be forced to sell.

Fixed rate: pros

- The interest rate won't change for the fixed rate period even if standard interest rates do.
- The repayment amount won't change so it's easier for you to budget for repayments.

Fixed rate: cons

- If rates go down, you miss out on lower repayments.
- You may have to pay fees to switch from a variable to a fixed-rate loan.
- Fixed rate loans are generally less flexible with sometimes heavy penalties if you pay out early or refinance.

Why the fee to pay out a fixed rate loan?

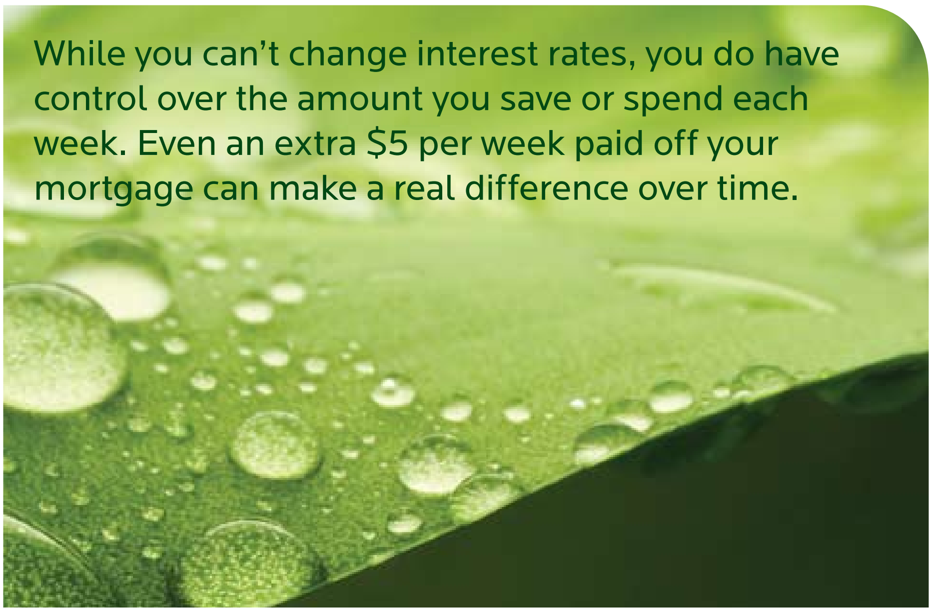
Break fee, economic cost, exit fee, early repayment adjustment, prepayment fee – banks have different names for the same charge. Most lenders will allow you to pay a small amount off your loan each year without charge. But if you go over this amount or pay out the loan, you'll be charged this fee.

When a bank funds a fixed rate loan they borrow money from the wholesale money markets. Their interest rate is locked in at the same time as yours; but the bank doesn't have the option to repay their loan early. So, when you repay yours they still have to pay the interest on their loan.

If the cost of borrowing money on the wholesale market has dropped between when you fixed your rate and when you pay off your loan, the bank has an 'economic cost' to carry until they can repay their loan. They pass this cost on to you as a break fee.

Best of both worlds?

While both fixed and variable-rate mortgages have their benefits, you may be able to split your loan into a fixed and a variable rate component. This allows you to take advantage of the lower variable rate and flexibility for part of your loan and maintain the security of a fixed rate for the other component.



Market outlook
by asset class

This market outlook is provided by the Investment Solutions team, BT Financial Group.

Australian shares

We have a positive outlook for the domestic equity market and anticipate the ASX 200 reaching the 4,000 to 4,500 levels during the second half of 2009 and into early next year. We expect the market to drift towards the 3,500 level once monetary authorities begin the process of policy 'normalisation' and then move higher once global economic and earnings growth accelerate.

International shares

We expect the S&P 500 to reach the 1,000 to 1,100 levels and then drift to around the 750 level during the markets' corrective phase. We are confident that, once global growth gains solid traction, equity markets will move higher. In the near term and on a country-specific basis, we prefer China, emerging Asia and the USA while being neutral on the UK and modestly under-weight Europe and Japan. We would gradually increase allocations towards Japan and Europe later in the year.

Diversified Property

Our fundamental view of the domestic and global real estate listed property market is that valuations are somewhere close to a bottom. However, the second and third quarters of 2009 are likely to be volatile. The combination of uncertainty about lenders' intentions and a heavy reliance on short-term debt could hold prices down. However, REITs are attractive from a relative distribution yield point of view.

International bonds

Global fixed income appears more attractive relative to domestic cash or domestic bonds. Quantitative easing measures should place a 'soft' cap on key global bond yields as this measure is designed to keep bond yields low to encourage other market yields to drift lower, making the cost of borrowing attractive to investors and consumers.

Australian bonds

With very little government or central bank sponsorship and a partially functional credit market, the Australian fixed income market does not look attractive to us in the short to medium term. We expect the 10-year Australian government bond to drift towards the 4.75% to 5.0% level in the near term and then towards 5.5% around mid next year, as the RBA starts to normalise official cash rates.

Alternative assets

We favour macro and managed futures funds, while being cautious on hedge funds that are subject to industry controls and/or regulation. Funds that employ relative-value strategies (such as credit long/short, equity long/short, fixed income arbitrage, convertible arbitrage or multi strategies with sound risk controls) are more likely to generate alpha relative to most directional strategies, as most asset classes are likely to continue to be extremely volatile in the foreseeable future.

Commodities

We are positive on commodities. China is at the most commodity-intensive stage of urbanisation and has moved ahead to secure long-term supplies of crucial commodities, either by taking a direct stake in commodity-producing companies or entering into bilateral trade agreements that ensure a steady supply.

Currencies

We expect both the Australian and New Zealand dollars to fare well under a weak US dollar scenario. It is estimated the Australian dollar's fair value is around 0.8300. We expect the Australian dollar to remain strong against the US dollar, British pound, Euro and Japanese yen. It should target 0.7300 to 0.7500 against the US dollar later this year and possibly move higher during early 2010.

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