more4life
FINANCIAL SERVICES

Newsletter

Summer 2008

Welcome

As many of you see your investment portfolios falling, jobs in the economy under threat and more uncertainty ahead, it's no wonder the 'holiday season' may lack some lustre. I personally would like to thank you for continuing to support our business throughout this unprecedented period. No client has left our firm as a result of this global financial crisis, but I know it has been tough for you. I acknowledge your commitment to your long term investment goals, and the trust you have placed in our firm to help you achieve those goals.

You are probably aware that we have recently commenced monthly lunch time client economic briefings. These have been held at the board rooms of leading fund mangers and investment houses and so far clients have heard from Chris Caton at BT and Jonathon Payne at HFA. These events have proven to be very successful and as a result we plan to hold monthly client briefings throughout 2009. We will inform you of when and where the next client briefing will be held, however there are limited places so we encourage you to speak up and register your interest early. These events allow you to ask the 'tough questions' across any topic of concern - from investment markets to Sydney house prices.

I was also fortunate recently to be invited to be a main platform speaker at the Society of Independent Financial Advisers held in New Zealand. Talking to many other financial planners there, it became very apparent that all clients (not just mine) are deeply concerned about their investments and the future. With this in mind, I have included an article about how best to 'Beat the Bear Market' and come out on top which is something everyone should be aware of. We think it's still important to remind investors that locking their money up in fixed interest accounts may sound attractive right now, but many not be an ideal longer term solution. Aside from the risk of missing the share market recovery (when it happens), there is the hidden risk of inflation to be reckoned with so we have included an article explaining this too. We also address the benefits of structuring your insurance through superannuation, and finally we look at the ASIC 'Pie In The Sky' awards for the world's most outrageous scams. Whilst most people are too smart to be fooled by a Nigerian businessman giving millions of dollars away to complete strangers, some cons are far less obvious.

We hope you enjoy our Summer Newsletter. Please be advised our office will close on December 19th will reopen January 12th 2009. If you need to contact us during that time, you can call 0407 468 712.

Have a safe and happy holiday season and I look forward to speaking with you in the New Year or before.

Kind Regards

James Walker Powell

How to eat the bear

Good News Follows Bad

"Well, dude, sometimes you eat the bear, sometimes the bear eats you"

– The Big Lebovski (movie, 1998)

Forbes Magazine, one of the world's best known business publications, recently suggested that the best way to survive a bear market was to behave as if you were being confronted by a real live bear instead of a stock market drop*.

Rule one, they advised, is to stand your ground, because running at the first sight of an angry bear draws attention to you and makes the situation worse. It's hard to outrun a bear anyway. Bears weigh up to 1000 kg, climb trees and can outrun a horse. Furthermore, when a bear attacks, running or fighting back is likely to antagonize the bear and make the situation worse.

Similarly, if you run away from the bear market by immediately shifting to less risky asset classes such as cash or fixed interest, you run the risk of locking in losses and not being around to participate in any recovery that could occur after the attack.

Consider this: In the 25 years since 1982, the ASX has recorded a January – December calendar year loss only seven times and in every one of those years, there was a substantial recovery in the following year. For example, in 1982, the market dropped 13.86% but in 1983 the return was plus 66.81%. In 1984 the market dropped 2.24% but in 1985 it achieved 44.07% . A fall of 17.51 in 1990 was followed by growth of 34.26 in 1991, and so on.

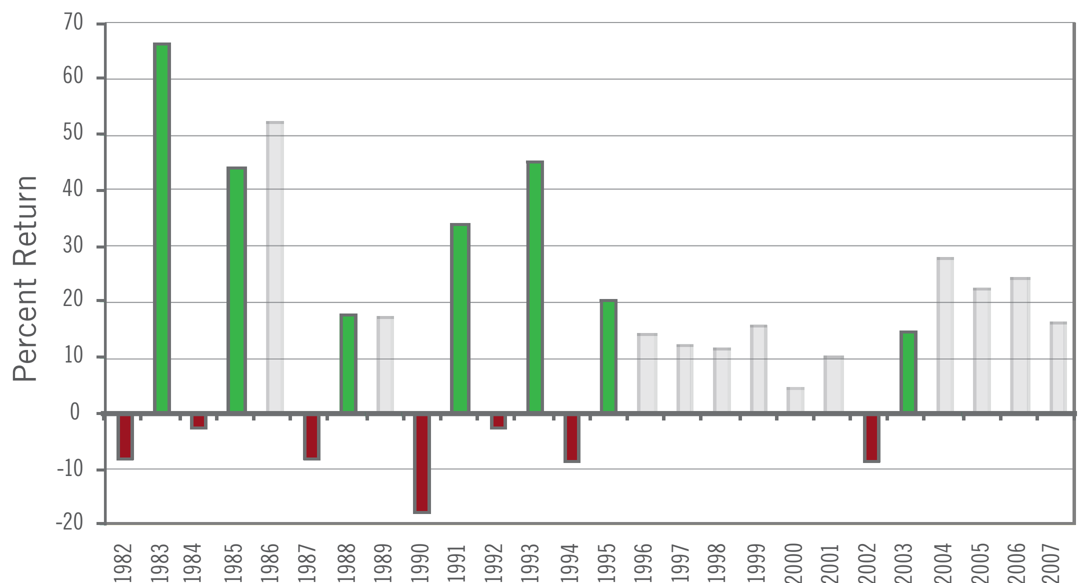
This pattern teaches us that the pendulum can swing back in a short space of time. If you are out of the market when the pendulum swings the other way, you lose your best chance of making good your losses.

Another survival tactic is to shift your share investment emphasis from capital growth to dividends until conditions improve. There are two ways to make money out of shares – one is through an increase in the share price and the other is the annual dividend, often fully or almost fully franked if it's an Australian company and therefore tax advantaged.

In a bear market, it pays to focus on the element of your portfolio that can continue to work for you, and that is the income side. Dividends are often a significant proportion of your total return, and they can continue to produce a return year in year out assuming you have a diversified blue chip share portfolio. So until the bear market has subsided, focus on the fact you can still be earning a dividend return and wait patiently for prices to rebound.

And finally, as Forbes points out, if you love the great outdoors you wouldn't spend the rest of your life huddled indoors following an unpleasant encounter with a bear. Instead, you would learn from the experience and be patient until the bear moves on. For share investors that means remember the basics, like spreading your risk and maintaining a long term focus.

*Forbes.com March 2008



Calendar Year Returns - Australian Share Market 1982 - 2007

Source: Datastream 2008

Stash your cash?

Inflation – the guaranteed way to erode your wealth

Imagine if the prices of bread, bananas, eggs and petrol increased by 1000% in a year?

You'd be paying $4,000 for a loaf of bread, $5,000 for a dozen eggs, $2000 for a kilo of bananas and $2,290 a litre for petrol.

You would have to take a supermarket trolley to the shops just to carry your cash! And now imagine how you would cope if you were a school teacher or a sales executive and your salary had not increased 1,000 times to cover the new costs?

This may sound far fetched, but it's exactly what has been happening to the poor people of Robert Mugabe's Zimbabwe, where inflation runs at 1000% a year. It also happened in Germany in the early 1920s, when prices famously increased by more than thirty thousand percent in one month! [1]

Inflation on this scale, called hyperinflation, usually has a very simple cause – faced with an economy in ruins, the government simply prints more money. This currency pays the army and the public service bills, but with no real assets to back the money, it loses all value and becomes worthless paper. A dollar is suddenly and literally not worth a cent and prices rise accordingly.

However, it would be a mistake to think inflation is only a problem for third world countries with bankrupt economies. Inflation, best described as a decline in the real value of money or a loss of purchasing power, is present in every free market economy, even in relatively good times. Think about it - prices tend to go up, not down and when they go up, the purchasing power of the dollars in your pocket decreases. Only a totalitarian government that freezes prices artificially can keep inflation close to zero.

In Australia, our Reserve Bank has a stated policy of adjusting interest rates in order to restrict inflation to between 2% – 3% a year. That's as low as it is likely to get in a free market economy, but lately it has been creeping up. In June last year, the official inflation rate was 2.9%, but by June 2008 it had crept up to 4.5% boosted by huge increases in the price of petrol.[2] The price of crude oil has thankfully dropped since then, but so has the value of our dollar which has offset the lower prices.

The global financial crisis has put a firm dent in Australia's inflation rate lately, and economists are now tipping inflation to fall back into the Reserve Bank's target band by late 2009. Other countries are not so lucky. They have been more seriously affected by the financial crisis and fear a more severe economic slow down causing deflation. Deflation occurs when prices fall in an economy across the board.

Let's be clear, inflation will still be an issue for Australians over the next 20 years. Inflation is the main reason why fixed interest investments have never been too popular with sophisticated investors who understand its effect.

If you invest $100 for 12 months in a fixed deposit account at 10% per annum, you are guaranteed to receive $110 back at the end of that year, right? Well no, not quite. If the inflation rate rose to 5% per annum, the buying power of your hundred dollars worth of capital would be worth $95 in a year's time and your $10 interest would be worth around $9.50. In other words, inflation has stolen around $5.50 from you.

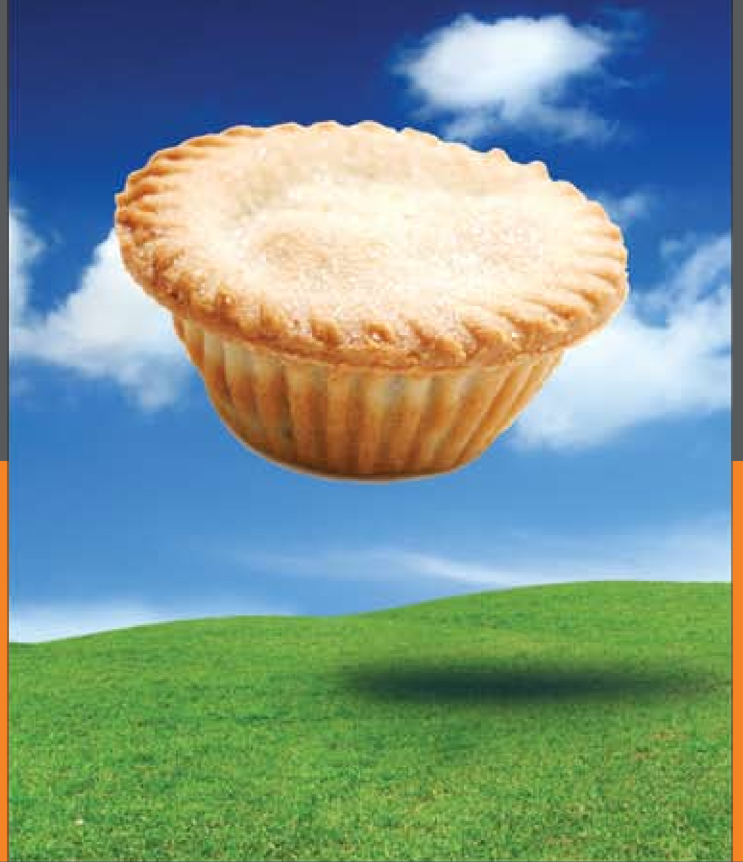
In reality, assuming an interest rate of around 7% p.a. and inflation of 4.5% the value of your money is actually only increasing by around 2.5% per annum after inflation has taken its toll. On top of that, these earnings are likely to be taxed!

This is precisely why long term investors prefer the share market. Despite the volatility of share investments, they have the potential to increase in value over time, as well as the benefit of earning tax-free or tax advantaged franked dividends. We cannot forecast the future, but historically, share investments over any 10 year period have exceeded the rate of inflation by a handsome margin.[3]

This may be cold comfort at the current time, but it is nevertheless one of the truths of investing. Bank fixed deposits may be a more secure place to stash cash, but they can be a poor way to protect your capital against the eroding effects of inflation.

1. Globe Asia August 2008
2. www.rateinflation.com/inflation-rate/
3. Datastream 2008

Pie in the sky financial schemes still devastate far too many people.



Sky high returns are just pie in the sky

Pie in the sky

Scammers use sophisticated props and hard sell techniques to trap even financially experienced people. Just imagine receiving an email from a distinguished but very ill gentleman, confined to his bed in a North African village. He attaches numerous photos to his email which clearly convey just how sick he is now, and also how wealthy he was as a healthy man.

He says he has specially selected you, as a fellow distinguished citizen in Australia (the country he loves and has visited many times), to help him arrange the dissolution of his $4 million fortune to the Australian charity of your choice. He is incredibly generous and offers you half of the fortune for your trouble.

He gives you legitimate passwords and contact details for the security company in London that is holding the fortune. You contact them to fact find and realise they are genuine. You can indeed collect the fortune, subject to a mere $14,000 in outstanding fees. You pay the $14,000 in outstanding fees and are told you will be sent the money in 5 business days. You make follow up enquiries thinking there must be a logical reason for the delay after 7 days. The phone number you were provided is disconnected. After 2 weeks, you realise you have been scammed and will never see the $4 million, or your hard earned $14,000.

This is just one of a number of financial scams that has been targeted at Australians. ASIC's Pie In The Sky (PITS) is awarded each year for the most outrageous financial scheme that's just too good to be true. The serious purpose behind these awards is to warn people about the vast array of financial scams going around.

Perhaps you've heard about the fabulous Mercorella investment scheme – offering 36% per year just for starters, with up to 72% if you refer a friend?

Or don't forget Dr Paul Mbizala's offer to split $35 million with lucky old you, if he could transfer the funds into your account due to an uprising in his country.

In an attempt to alert investors to the prevalence of scams, ASIC came up with some April Fool investment scams just to see whether anyone would respond. They were flooded with calls from people wanting to invest in Blue Bottle Farms, Geeps (a cross between goats and sheep) and Land and Air Space Packages in which you charged rent from planes flying over your house.

Although we do laugh at such outrageous scams, ASIC's Executive Director of Consumer Protection, Mr Greg Tanzer, is quick to point out the sobering message of the awards: "Pie in the sky financial schemes still devastate far too many people. Always deal with licensed Australian financial providers, because that way your rights are protected if something goes wrong".

The ASIC 2007 "Pie in the Sky" scam winner was the Ponzi scheme, operated by Giuseppe Mercorella from South Australia. Offering between 3% and 6% per month, Mr Mercorella's illegal scheme received $216.9 million from investors who ultimately lost $76 million. Mr Mercorella is now serving a five year jail term on ASIC charges.

So what's our advice regarding unlicensed investment promoters? If something sounds too good to be true, it probably is. To see all the nominations for "best scams", visit the ASIC consumer website: www.fido.gov.au

Protect yourself now via your super

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Cash flow concerns prevent many people taking up insurance

It's amazing really, we always remember to insure our home and contents and cars, but many of us forget to insure the most valuable asset we have – ourselves. How long would your family be able to keep paying the mortgage if you died, or lost your income through illness or accident?

Proper estate planning is the process of identifying real threats to you and your family and managing them with proper planning. It involves arranging your financial affairs while you are alive so that when you die, your assets pass to the people you want to receive them, in the way you intend. As part of that process, insurance is often extremely important. What would you live on if your savings were eroded by huge medical bills? How would the school fees and the grocery bills be paid if you couldn't work for a period of months, or even years? It's easy to see why we need different types of personal insurance such as Death, Total and Permanent Disablement and Income Protection insurance but they are NOT simple products to buy. There are many different policies from many different insurance companies and the conditions and benefits vary substantially. It's critically important to choose the right policy for your needs as part of your overall plan.

Here are just three of the vital questions you need to ask:

1. How much money do I need to live on if I can't work because of accident or illness?

Income Protection insurance allows you to insure 75% of your income in the event you can't work due to sickness or accident. It can be used to cover all your normal bills or anything else for that matter. In fact, the benefits can be paid to you each year until age 65 whilst you are unable to work. While Income Protection may be 100% tax deductible, cash flow concerns prevent many people taking up this vital insurance. The good news is the government has recently changed the legislation to allow Income Protection insurance to be acquired through your superannuation fund. This means you can protect yourself with this insurance cover without it affecting your hip pocket. Instead, the premiums get paid from your super fund.

2. What lump sum do I need to eliminate debt on death or disability?

If you're like most people, you've used debt to finance a range of lifestyle purchases, including the family home. If you die or become disabled, loan repayments are still required and, consequently, most people want their lifestyle debts cleared as a bare minimum in the event of their death or disablement. Taking out insurance for death and/or total and permanent disablement will ensure you receive a lump sum to repay all your family's debts. Death and Total and Permanent Disablement insurance is generally not tax deductible if the policy is purchased in individual names. However, if you purchase the insurance through your superannuation fund, it becomes tax deductible to the superannuation fund, and it doesn't affect your day to day cash flow.

3. How do I maintain the family's lifestyle?

You need to ensure you have enough insurance to clear your debts, but your family will still need to meet ongoing expenses. That's why you should take out Death and Total and Permanent Disablement insurance for an amount higher than just your existing debt. With our help, you can determine what your ongoing expenses will be after a tragic event such as death or disablement, and how long you'd like your family to be financially supported.

Remember, superannuation is a tax effective vehicle to purchase personal insurance such as Death, Total and Permanent Disablement and Income Protection and it may not have any effect on your day to day cash flow. Because these are complex products with different features offering different premiums and benefits, it's important you find the right policy to fit your individual circumstances. Please don't hesitate to call us if you would like to discuss your insurance requirements.

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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