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QUARTERLY INSIGHT

InterPrac Financial Planning Newsletter Spring 2018

Spring is the time when sports mad junkies get their fix

It is the start of the football finals, and racing carnival

Questions like will Winx win another Cox plate, will another European rider take away the Melbourne Cup, will Richmond take out the AFL premiership again, and will it be a Melbourne, NSW or Queensland team that wins the NRL in 2018.

Spring is also the time from a financial planning point of view where we encourage clients to undertake a spring clean and review plans to see if they are still on track or need tweaking.

In this edition you will find a number of articles on Superannuation, alternative ways to pay for Life Insurance, and an article on the magic of the number 72 (see page 3) and financial abuse.

If nothing more we hope the newsletter gets you thinking about us, and prompts you to consider making a time for a review meeting.

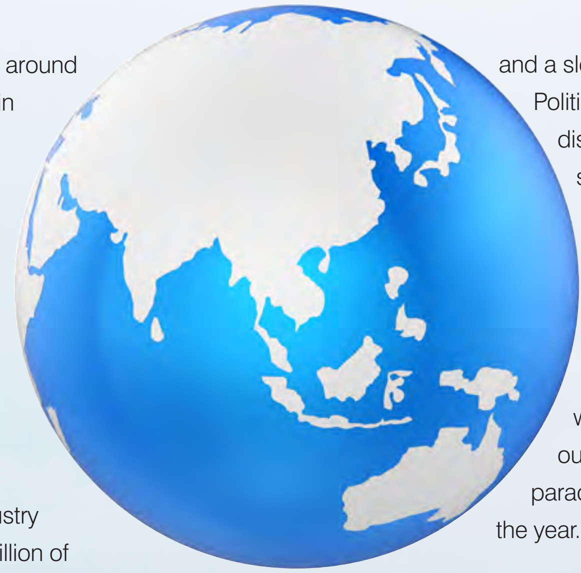
I urge you to call our office to discuss any article or any matter relating to your own personal circumstances.

We are here to help, and as an example if you would like to arrange a review of any of your finance needs, I can introduce you to assistance with home loans, investment loans, construction loans, tax debt finance, car loans or any business equipment finance.

I hope you enjoy Spring, and the next time when you are working out how much your investments may be worth over time, you can use the rule of 72 to help with your calculations.

Economic Outlook – Asia/Pacific

For all the noise that has arisen out of this region, we remain constructive on its outlook. Looking past the political turmoil (trade tensions, the U.S.-North Korea summit, Japanese Prime Minister Abe's cronyism scandal), our assessment is that the fundamentals remain intact. Economic growth looks resilient at mid-year after having decelerated in the first half of 2018, and corporate earnings expectations are in an upgrade cycle for many countries in the region.



Let's start with China, where concerns around debt and the potential for escalations in the rhetoric around trade negotiations have placed pressure on the equity markets. But looking past the news headlines, we see an economy that continues to be on a good footing. Private investment is growing, and it is likely that we will see an increase in Chinese government spending to further boost activity and confidence. The inclusion of China A-shares in the MSCI indices, according to some industry analysts, will draw an estimated $20 billion of foreign capital into Chinese equities through this year.

Developing Asian economies have managed to weather the storm of rising U.S. interest rates and a rising U.S. dollar much better than their counterparts in Latin America and Eastern Europe. India and Indonesia have each raised interest rates, which we view as a combination of defending the currency and acknowledging economic activity. Overall, the elevated level of trade within the region, combined with our constructive outlook for China, leaves us with a positive outlook for developing Asia.

Moving across to Australasia, we continue to expect Australia to outperform New Zealand. Economic growth in the former is solid, underpinned by public investment, external trade and buoyant business confidence. Looking at corporate performance, we see the potential for positive earnings revisions, particularly in mining and resource companies. We view the weaker-than-expected labour market as temporary and expect to see a rebound in the second half of 2018. This should support the Australian consumer, who has been cautious given high levels of debt and muted wage increases. In New Zealand, in contrast, weak business confidence and a slowing housing market remain headwinds. Political uncertainty in New Zealand has dissipated following the release of a fairly sensible budget from the new Labour-party government; however, uncertainty lingers in several key policy areas.

Both the Australian and New Zealand currencies have been pushed down by the negative rate differential, which we highlighted in our previous quarterly outlook report. We reiterate our view that this paradigm is unlikely to reverse over the rest of the year.

Japan continues to offer one piece of positive data for every piece of negative data. On the positive side, we have seen very strong earnings growth, the first signs of decent wage growth, a strong labour market and robust business confidence. On the other hand, weak consumer confidence has translated into poor retail spending and household consumption; while rising oil prices are not great for a country that imports nearly all its oil. We expect consumer confidence to rebound as higher wages flow through to household balance sheets, but further increases in the oil price will be a drag and overall upside for the economy is limited from here. The support from the Bank of Japan should remain for some time, as we do not expect any change in policy for this year, at the very least.

The key risk to the Asia-Pacific region, in our view, continues to be the implications of trade rhetoric escalating into action, which likely would most impact China. Our view remains that the threats of tariffs are primarily negotiating gambits, and that we are unlikely to see trade barriers being permanently erected. Further rise in the U.S. dollar (which is not our base case) would also be a risk to the region.

The Rule of 72

Why 72 is The Answer to The Ultimate Question of Life, The Universe and Everything (not 42 as Douglas Adams would have you believe!).

A family business is a journey - challenging, rewarding and often unpredictable. Should you decide to sell the business - often a daunting decision - careful planning and skilled execution are required to ensure a successful outcome.

A recent survey of ultra-high net wealth individuals, highlighted the opinion that a lack of strategic planning for the family was the greatest destroyer of wealth. Perhaps the hardest decision for any family business owner is when, or if, to sell the family business. Selling a family business is like no other sale. It requires an approach which addresses both the family's issues and the business' issues as one, with the two often closely intertwined. It needs extensive preparation and great judgement, with timing and stakeholder management often critical.

Most owners have strong family and emotional ties to the business - part of their family heritage and their collective identity. They may also wish to achieve specific outcomes for wider stakeholders, including highly valued staff and long-standing customers. The challenge is even greater when family members are actively involved in the company. Some family members may take a purely commercial view, whilst others believe the business should be handed down to their children and grandchildren and be part of their livelihood and collective identity.

The business is often the most valuable family asset, so the sale should not be considered in isolation from the wider interests and future intentions of the family. The use of proceeds and future careers of family members are important considerations in the long-term success of the family.

What is so great about the number 72?

Let me explain what makes 72 The Answer. Using an example, if you invested $10,000 that earned you 10% per annum, how much would that investment be worth after 7 years? You may expect the answer to be $17,000, as 10% return on $10,000 for each of 7 years would be $7,000. However, the answer is actually $19,487.17 to be exact. This is because your investment earns interest on the interest each year, in jargon speak, compound interest. What this means is, at the end of the first year, you would have $10,000 plus $1,000 of return, and at the end of the second year, you would have 10% on this $11,000 (rather than just on the initial $10,000). Each year this happens, the greater the effect on your long-term returns. Of course, if you spend the 10% return each year, you will still have $10,000 at the end of 7 years.

What about the number 72? How does that fit in? The number 72 allows you quickly and easily work out how much investments may be worth over time. It works like this - if you divide 72 by the interest rate, this will estimate how long it takes to double your investment. Using the example above, 72 divided by 10(%) equals 7.2. So your initial investment doubles from $10,000 to $20,000 after 7.2 years. This sounds pretty good, but it gets better as this doubling effect continues. After 14.4 years, you would have $40,000, then $80,000 after 21.5 years, $160,000 after 28.8 years, and $320,000 after 36 years. So in this example, your $10,000 investment would increase to $360,000 after 36 years. Pretty cool, isn't it?

Another great way to use this method is to work out the effect of inflation on your investments. Let's say you have 24 years left before you retire, and you think you will need $1 million in today's money to retire on. If you had one million dollars and put it under your mattress for "safekeeping", that one million dollars would buy more today than it would in 24 years' time because of the impact of inflation. If we estimate that inflation is 3% per annum, then 72 divided by 3(%) to gives us an answer of 24(years).

This means that having $1 million today is the same as having $2 million in 24 years' time, because of the impact of inflation. Considering inflation then, the $360,000 after 36 years in the first example is actually closer to $125,000 in today's dollars. This is still pretty good, but does prove that the earlier you start saving, the better off you will be.

Is there a better way to pay insurance?

Superannuation changes introduced in 2017 have opened new opportunities whereby employees can use their superannuation to fund their insurance needs.

These changes saw the timely abolition of the 10% rule. Under that rule employees were prevented from making additional deductible personal contributions – even though those deductions did not breach concessional contribution caps.

Effective from the start of the past financial year should an employer's compulsory superannuation contribution fall below an employee's concessional cap then the employee can make a deductible personal contribution to their fund and have the fund pay their insurance premium – providing of course that the payable premium keeps the additional contribution below their cap.

This results in a number of key benefits for the employee: -

First of all, it can substantially reduce the net cost of insurance. Many types of insurance are not deductible for tax purposes and, based on personal circumstances, some definitely should be held outside super. By holding insurance within a superannuation fund and paying the premiums by use of deductible personal contributions we can achieve a better net result. To illustrate this assuming an employee earns $100,000 p.a. and would be paying 39% (37% plus 2% Medicare) on income above $90,001. On a pre-tax scenario the employee would need to earn $8,197 to fund an annual premium of $5,000. By funding through superannuation the actual cost of insurance is reduced to $5,000 per annum.

Secondly it can go a long way to prevent erosion of retirement savings.

One of the major issues we see when funding premiums through superannuation is the negative impact it may have on a member's balance and resulting erosion of their final entitlement. This significant dilution of member benefits can be avoided by empowering the employee to top up their super.

What about contribution Tax one may ask.

There remains a lot of confusion regarding the imposition of the 15% Contributions tax. While the personal contribution is included as assessable income in the hands of the super fund this is offset by the tax offset for the insurance premium being paid effectively reducing the contributions tax to zero.

But a word of caution - seek the advice and guidance from your financial planner before setting any strategy into place.

It is assumed that all personal contributions into a superannuation fund are non-concessional contributions. The member must issue a "notice of intention" to claim a tax deduction to the trustee of the superannuation fund. Failure to do so will negate the opportunity to claim the tax benefit.

Holding insurance within your superannuation fund is not always appropriate nor the best way and professional advice should always be sought prior to any decision. Seek an appointment with your financial adviser to discuss this and other strategies.

Our thanks go to David Glen and TAL Life Ltd.

FIVE FINANCE TIPS

Get in shape this financial year

As a new financial year begins, there's no better time to take a step back and review your finances. In this article, Russell Investments' experts share five tips to get you in great shape this financial year.

1) ORGANISE YOUR TAX

Make a resolution to begin this financial year with a decent filing system so you don't end up with bags of unfiled receipts next 30 June.

Whether you manage all your receipts digitally or in a shoebox, separate out any paperwork relating to income and expenses. Set up folders for each main category (e.g. travel, insurance, rent) so as soon as you get a receipt, you can put it in the right spot.

2) REVIEW YOUR FINANCIAL COMMITMENTS

Consider evaluating the big-ticket items you're spending money on to make sure they're right for you. Does your mobile phone plan reflect your usage? Does your health insurance cover your needs?

It can also pay to review your existing utility policies or loan rates. Shop around for a better deal, or try calling your current provider and asking them to do better.

3) SET UP A BUDGET

Once you've got your bills worked out, take a look at your other spending habits and see if there's any room for improvement.

When setting up a budget, the trick is to include absolutely everything—from car registrations to takeaway coffees. You'll get a picture of where your money is going, and you'll probably be amazed at how quickly little luxuries can add up. There are a number of websites and apps that can help with this—check out this budget planner [1].

4) SELL WHAT YOU DON'T NEED

Jump onboard the trend of getting rid of the excess 'stuff" you just don't need or use anymore. Do you really need an extra toaster or three tennis racquets?

Clear out what you don't need, and then sell it online or have a garage sale. You could make some extra pocket money as well as reclaiming precious space in your home.

5) GET YOUR SUPER SORTED

Do you still have multiple super accounts from your old jobs? You're probably paying fees on all of those accounts—and those duplicate fees could cost you thousands by the time you retire.

Talk with your adviser about combining your accounts. If you're not sure whether you have any lost super hanging around, your adviser can help with that, too. It may only take a few minutes to simplify your super.

If you're in line for a pay rise or a bonus, consider boosting your super with before or after tax contributions. Extra cash tends to get absorbed into our daily living expenses. But if you set up an automatic deduction, you'll never even miss it, and will benefit from it at retirement.

[1] https://www.moneysmart.gov.au/tools-and-resources/calculators-and-apps/budget-planner

SUPERANNUATION: is it time to review your investments?

You may be missing out or taking unnecessary risks if you take a set-and-forget strategy to your super

A lot can happen between the time you start your first job and the time you retire. From building a career, buying a home and raising a family to dealing with setbacks such as redundancy or divorce, life doesn't stand still and neither should your investments.

In all likelihood, the investment choice you made at age 25 may no longer be appropriate at age 45 or 55. Or you may not have made an active choice, opting for your fund's default option instead.

In most cases, the default option is a 'balanced' portfolio of growth and conservative assets. The mix of investments is chosen by the fund manager to suit the average fund member who might be anywhere from 18 to 65 years of age.

The problem with this approach is that we all have a slightly different appetite for risk and different financial circumstances. What's more, these things are not set in stone but can and do change as you progress through life.

Check the menu

To make sure your super suits your current needs, start by checking how your money is invested and then compare this with what else is on the fund's menu.

All super funds have a range of investment options for you to choose from. These vary according to the kinds of assets they hold. Your choice will depend on the amount of risk you are willing to take and the return you can expect to make in the long run.

Most funds these days offer an a la carte menu of single asset options such as Australian shares, international shares, sustainable shares, property and fixed interest, which you can mix and match to suit.

Alternatively, you can choose from a selection of ready-mixed options to suit different risk profiles. Different funds use different labels, but according to ASIC's MoneySmart website there are four broad categories [1]:

Growth options typically hold around 85% of their funds in shares and property with the balance in cash and fixed-interest investments. High growth options can have up to 100% in shares and property. Average returns are higher over the long term – typically several percentage points above inflation - but the ride may be bumpier along the way. Losses tend to be higher in bad years and you can expect a loss in four or five years out of every 20.

Conservative options have around 70% in low growth, low risk cash and fixed interest with the balance in shares and property. Average returns are lower than growth options over time but there is less risk of loss in any year.

Cash invests in short-term deposits with Australian institutions which offer relatively low, stable returns and no risk of loss. The risk is that returns won't keep pace with inflation.

Balanced or default, option may hold anywhere between 60 and 75% of its investments in shares and property with the rest in cash, bonds and fixed interest. Average returns over the long run will be a little less than the growth option but higher than conservative and cash options.

The balanced option is designed to suit most of the people most of the time, with above average returns for below average risk. But there are other ways to manage risk while maximising returns over the course of your life.

[1] Super investment options, MoneySmart, www.moneysmart.gov.au/superannuation-and-retirement/how-super-works/super-investment-options

A matter of time

The thing to remember about risk in investment, as in life, is that time often heals all wounds. If you have 20 or 30 years left to work and save, you may consider taking a little more risk than someone with less than 10 years till retirement. That's because you have more time to recover from the swings and roundabouts of global investment markets.

Time can also eat away at your savings if you invest too conservatively. That's because inflation reduces the buying power of money over time. So, those with at least 10 years to retirement may consider keeping a substantial portion of their retirement savings in a growth or balanced option.

The argument for reducing your investment risk grows stronger as you near retirement and have less time to recover from a market downturn. Even so, people entering retirement nowadays may still have up to 30 years to plan for. Depending on your appetite for risk, it may be appropriate to keep some money in growth assets to avoid depleting your capital too quickly.

Just because super is a long-term investment, it doesn't mean it should be filed away in a drawer until you retire. Given that many of tomorrow's retirees can look forward to living well into their 90s, the reward for taking an active interest in your super is that your savings are more likely to last the distance.

Thanks to Colonial First State Investments Limited

Lessons from the market

Every market cycle – bull or bear – provides opportunities for investors to improve their process for investing. The best thing to do is learn from past events and apply those lessons to your future investment strategies and circumstances. Here are the top five lessons you can use to help navigate towards your future desired outcomes.

Lesson 1: Keep your cool

This is the most important learning from recent times. Through market cycles, it's easy for investors to react emotionally–through overconfidence in rising markets or, equally, reacting with fear in falling markets.

We know that the best way to reach your financial goals is to remain cool and stick to your long-term investment strategies. History has shown us that markets tend to recover just as quickly as they fall.

Lesson 2: Stay invested

While short-term market falls are hard to ignore, it's essential to stay invested. In fact, long-term investment discipline is more important than ever especially in a market crisis. We know that markets move in cycles, and that historically each bear market has been followed by a bull market. Therefore, if you remove your investment during a down market, you won't benefit when the market rebounds.

Successful investors understand the importance of sticking to the plan. Those who have built a robust investment strategy, with appropriate diversification, and successfully navigated many market gyrations along the way, keep the 'plan' front of mind in the midst of market volatility and emotional ups and downs.

Lesson 3: Diversification still works

Without the knowledge of which asset classes or sectors will outperform, the key is to diversify. Trying to pick the best-performing asset class of the year is very risky, considering that one year's best performing asset class can just as easily end up as the next year's worst performer.

We believe that a sound, well-diversified portfolio with a long-term focus will help reduce volatility and provide steady, consistent returns over the years.

Lesson 4: Investing in the markets is the primary way to meet retirement and financial goals

The markets can be tough on your nerves, but despite this, it's important to discount short-term market performance when considering your longer-term financial objectives. Investing is still the most prudent approach to beat inflation and help realise your long- term financial objectives.

Lesson 5: Markets are cyclical. Whatever goes down will likely come back up again

Markets follow cycles of ups and downs. What we don't know is their timing or duration.

The global share market experienced strong gains in 2009 following the downturn which commenced in late 2007 and more recently, some global markets (such as US shares) have reached historic highs. The point is that markets typically recover.

Different asset classes – like shares, bonds and property securities – carry various levels of risk and return. Investing in a single asset class is risky when you consider no one asset class consistently outperforms on a regular basis.

Strategically diversify your portfolio across asset classes, investment strategies, managers and styles. This approach aims to reduce risk and can help you weather different seasons of the market, no matter which asset, strategy or style is in favour at any given time. Blending complementary asset classes, strategies, styles and managers can also help provide more consistent returns through various market environments.

Lesson 6: Partner with a professional adviser to choose strategies aligned with your personal goals

Start each day this week with a daily planning session.

Investing is personal. It's so important to make sure that your strategies are well suited to your goals, life stage, risk tolerance and other specific factors that matter to you. For example, a retiree invested solely in Australian shares in 2008 (-38.9%) [1] probably felt the pain of investments that were too risky for his life stage and real-life risk tolerance. A professional financial adviser can help you design a plan based on your personal needs—and stay on track over time.

What we've learned

With recent market volatility, investors may consider making changes to their investment strategy and perhaps exiting markets altogether. However, years of lows and highs – such as 2008 and 2009 – help to demonstrate what we think are the key principles of investing:

Diversify - it's essential to have a well-diversified portfolio to help lessen the impact of market downturns.

Stay invested - don't miss your opportunity for financial gains when the market recovers. You have to be in it to win it.

Concentrate on the long term - short-term market returns shouldn't concern the long-term investor.

Don't try to time the markets, or pick next year's winner - no one knows when markets will peak and trough, and which asset class will outperform. Consider working with a professional financial adviser to help choose investments aligned with your personal goals.

[1] Past performance is not a reliable indicator of future performance. S&P/ASX 300 Accumulation Index.

A Tale of Abuse

This is a story that was recently published in a financial planning industry magazine and is typical, unfortunately of the type of problems that are often referred to a financial planner for assistance.

Tanya was an investigative journalist back in the day and has run her own businesses. When she met and fell in love with the man who would become her husband, she was quite well off. She had a successful business, property and cash in the bank.

At the end of the relationship, there was nothing left in her own name. All had been transferred into a company and trust of which he was the director and signatory of. She remained just a shareholder, so all decisions could be made without consultation.

The belittling had by then been going on for years. She was told she was bad with money, and obviously, she thought it was true.

Everything she had was no more. All her decisions were wrong. He was right. The emotional abuse was there too, alive and well.

Friends and family hardly recognised the frail shell that eventually did leave the relationship, the one she'd been told that she'd never be brave enough to do. The relationship by then was 12 years old and Tanya had wanted out for the last six.

Her health was broken; she had a stroke and a series of seizures brought on by the stress and she was financially at ground zero and emotionally bankrupt. But she had a good reason to soldier on - her daughter.

Onlookers may make comments like 'She should have gotten out earlier.' 'Why would you stay with a guy like that?' 'What was keeping her there?' 'Why did it take so long?' And I guess unless we're there ourselves, we'll never really, truly know.

So, to ask the question everybody seems to want the answer to... why did you stay?

"It was the frog in the pot scenario. If you throw a frog into boiling water it jumps out, but if you put it in warm water and slowly turn up the heat it will be boiled alive before it even knows it," Tanya said.

"I was isolated by the time I realised I needed to get out, cut off from my family and my friends, I felt there was no out. But then one day, I realised I couldn't risk being a bad role model for my daughter any longer. I wanted her to know that she could get out, should the cycle repeat, and that she could have an amazing life in doing so."

One day Tanya's husband gave her an ultimatum: stop "playing around with the media" and get a job in a supermarket.

"When my daughter heard this, she burst into tears and said 'that's not you mummy'," Tanya recounted.

"In that moment I realised I'd failed her and we had to go."

And how did you finally manage to get out?

"I started putting $20 per week onto a grocery card so that we'd have funds to last us for food once we'd gone. I managed to have three months saved when we left and had squirrelled things away with a close friend," she said.

"The timing had to be right too. It's not an easy thing. If I had advice for anyone looking to move on from an emotionally and financially abusive relationship is that if possible, put aside whatever you can to tide you over for when you're out. That may not work for everyone, but it sure made a huge difference to me."

It took a lot of time and the rebuilding is ongoing, of Tanya's health and finances. She's used all of her experience in media and small business to build a success business today and her personal and business growth continues.

The role of a financial adviser

As a financial adviser, it is rare to come across a client that is being financially abused. But it does happen.

Some signs we see is the closure of accounts or paperwork going missing; often the client becomes agitated and confused about the state of their affairs.

Sometimes the abuse can escalate to fraud and lead to police prosecution if the Power of Attorney is not acting in the best interests of those they're acting on behalf of. This is already widespread and rarely reported due to shame and embarrassment.

We believe clients should always be advised to nominate two people to jointly act as Power of Attorney - if two are signing, it's harder for one to go rogue.

For younger people, unfortunately women are more often the victim of financial abuse, particularly if they are in a relationship with a controlling partner.

Deleting friends and family from their phone contacts; limiting or refusing them contact with loved ones; taking earnings; doling out limited spending money; requiring receipts and not allowing the purchase of personal items like shoes and clothing or discretionary items like hair, nails, grooming and so on are all red flags.

It's an unfortunate reality, but financial abuse - in all forms - is on the rise.

Advisers can have an important role to play in combating financial abuse and advice practices do look to report where they are concerned

Clients who know others that you feel may need help, can look to refer those parties to a planner and we may be able to be the rock that your friends need to right any wrongs.

Disclaimer: *Please note that these are recollections and a story from a magazine but is typical of what is happening, possibly right under your nose with a friend.*

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