Strategy 2
Growth assets can make your money work harder

When investing for long-term goals, you should consider putting some of your money in growth assets such as shares.

What are the benefits?

By using this strategy, you could:

- Protect the purchasing power of your investment, and
- Receive a tax-effective income that grows over time.

How does the strategy work?

After a period of sharemarket decline, investing in a term deposit may seem appealing. But there are some downsides of term deposits too.
For example:

- They do not provide any capital growth to prevent the purchasing power of your money being eroded by inflation,
- Interest rates can fluctuate considerably over time, depending on the Government's objectives and economic conditions, and
- Every dollar of interest earned is taxable at your marginal rate.

As a result, term deposits may not generate the returns you need to achieve your long-term goals, such as educating your children or funding your retirement.

With shares, on the other hand:

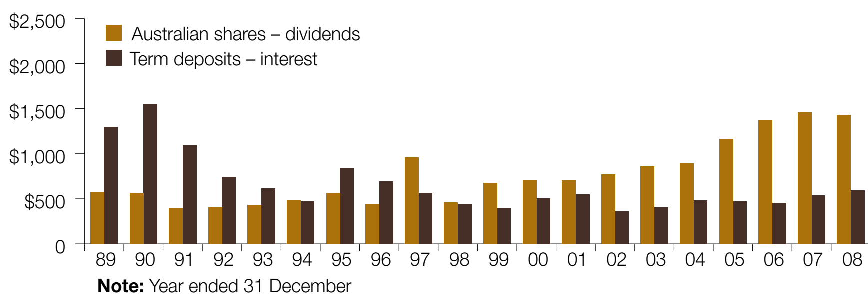
- Your capital has the potential to grow in value over the long term and outpace inflation,
- Your dividend income can increase substantially over time, as share prices rise, and
- The imputation credits that often come with dividends from Australian shares can be used to reduce your tax bill (see FAQs on page 26).

While shares can be volatile over the short term, they have a very important role to play in a long-term investment strategy.

Case study

Jack and Vanessa each had $10,000 to invest 20 years ago. Jack decided it was important to protect his capital, so he put the money in a term deposit. After seeking advice, Vanessa invested her money in an Australian share fund via a unit trust. Both used the after-tax income from their investments to meet their financial commitments each year. The chart below compares the income they received over this period.

Income from an investment of $10,000 made in December 1988

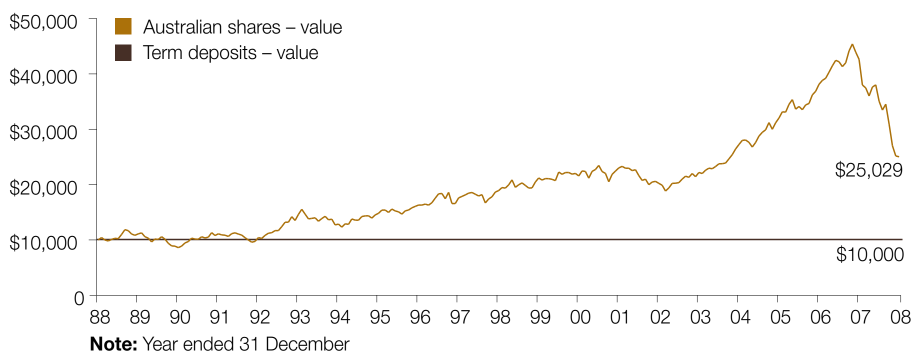


Note: Year ended 31 December

Clearly Vanessa made the right move. Initially, her share fund paid less income than the term deposit but as her capital grew in value, so did her dividend income. By contrast, Jack's term deposit paid interest at the prevailing rates, based on the original capital value only.

The next graph shows the value of their investments over this period (up to the end of 2008). As you can see, even after one of the worst sharemarket downturns in history, Vanessa would still have come out well ahead by making a long-term investment in the Australian sharemarket.

Capital growth from an investment of $10,000 made in December 1988



Note: Year ended 31 December

Vanessa's strategy of investing in shares would also have come out ahead if they had both re-invested the income to compound their returns (see Strategy 1). In this scenario, Vanessa's and Jack's investments would have been worth $57,213 and $34,998 respectively.

Tips and traps

- To access greater opportunities and reduced investment risk, you should consider investing in shares through a unit trust (see page 2).
- Should you need to sell all or part of your investment, the resulting capital gain may be eligible for concessional tax treatment. Provided the asset has been held for at least 12 months, only 50% of the capital gain is taxable. You could also reduce (or eliminate) Capital Gains Tax by using capital losses (see Strategy 9) or deferring the asset sale until a new financial year (see Strategy 10).
- Property investments can also provide a growing income stream and long-term capital growth. Investing in property via a unit trust can provide additional benefits including diversification, lower costs and easier access to your capital, when compared to investing directly.

Assumptions for Income and Capital Growth graphs: Returns are based on the S&P/ASX 200 Index (prior to April 2000 – All Ordinaries Index) and the RBA Term Deposit Rate (1yr $10,000). This example does not take into account the impact of fees or taxes on distributed income and capital gains. This example is based on historical performance and is not indicative of future performance. Future performance is not guaranteed and is dependent upon economic conditions, investment management and future taxation.