INVESTMENT SOLUTIONS

EDITION 05 | Summer 2013

Welcome

Investment Solutions

Summer 2013

Which comes first – saving or investing? In this edition we take a look at the principles of saving and how to get the balance right between saving and investing to establish a solid financial foundation.

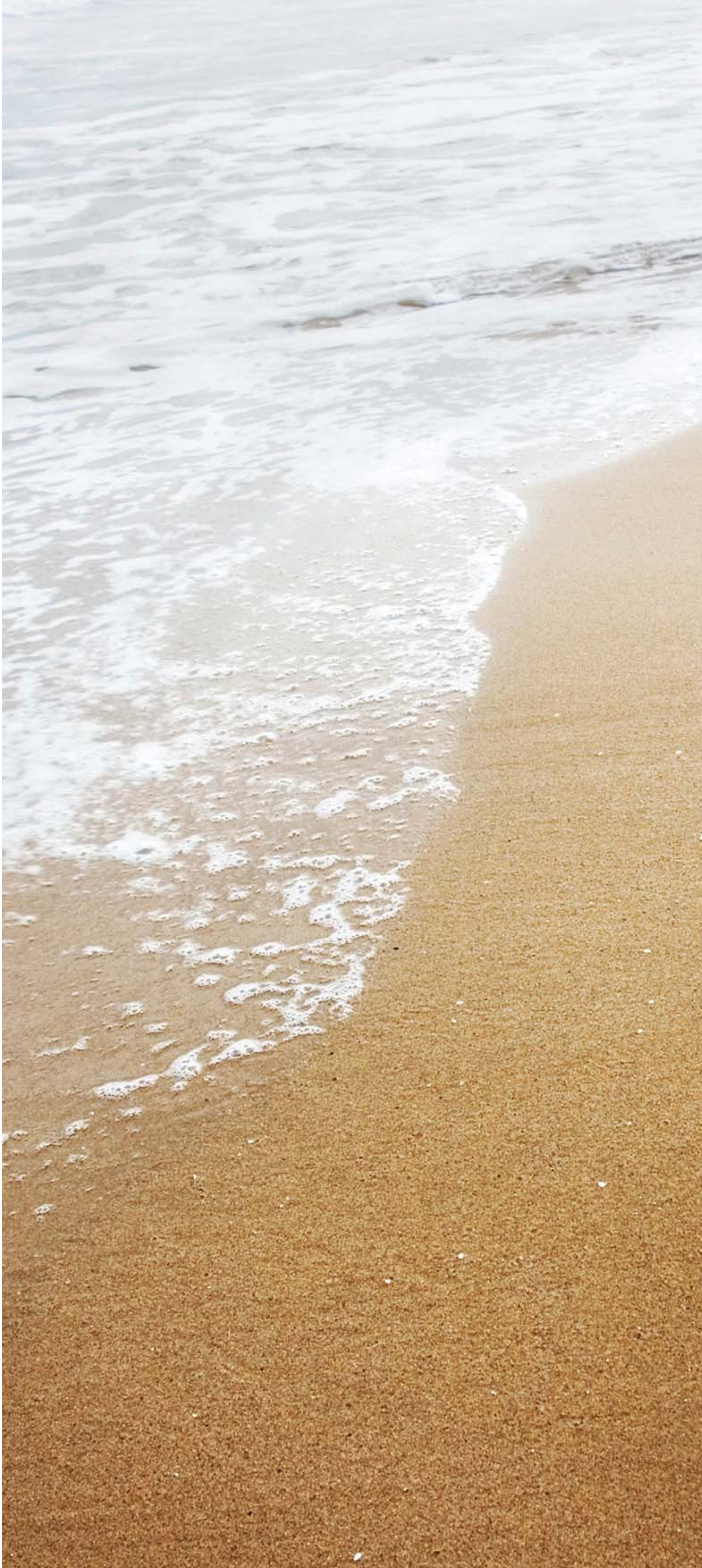
We also use the end of year as an optimum time to consider how to best stick to your financial plan for the new year, providing you with a short yet valuable 'how-to' guide.

Our regular Market Update provides a wrap up of the global and local markets for 2013 and considers what's to come in 2014.

Finally, we recognise the important role of grandparents in our community and take a look at how those who are providing financial assistance to their grandkids can structure their generosity in the most financially effective way.

Until next time – happy reading.

onePlan Financial Planning
Louise Scifleet 02 6372 0716
invest@oneplanfp.com.au
www.oneplanfp.com.au



Market Update

As we head into the back end of the year, now is the time to reflect on the financial markets events that shaped 2013 and what may be in store for 2014.

Global Overview

When we look at performance of many asset classes year-to-date, over the last twelve months we have witnessed a strong rebound in equities with a number of equity markets (i.e. US S&P 500) reaching all time highs, while locally, the S&P/ASX 200 Index also reached five year highs. At the other end of the spectrum, the more defensive asset classes such as fixed income have struggled to deliver the same level of performance seen in previous years, with bond yields moving higher throughout the year.

Much of this rotational shift from lower to higher risk asset classes has been off the back of central banks maintaining high levels of liquidity in financial markets, resulting in interest rates remaining at historic lows. At the same time, we've witnessed a steady (albeit unremarkable) improvement in the global economy, with the US leading the way. Additionally, Europe (and the UK) continues to show signs of stabilisation. And in Asia, policy announcements particularly from both the Japanese and Chinese governments have focused on much needed reform as a key ingredient for capturing future growth opportunities.

However, while there are genuinely positive signs for the global economy, risks are still prevalent. The improvement in economic activity has not to date resulted in significant jobs growth, particularly in Europe, where the unemployment rate remains at all time highs (12.2%). In the US, while the jobless rate has steadily improved, it remains above the preferred 'target' of 6.5% set by the US Federal Reserve. To this end, the ongoing liquidity program of the Federal Reserve (known as quantitative easing) is likely to continue well into 2014. While the Federal Reserve may 'taper' from the current level of $US85bn per month, we expect that stimulus measure will remain in place, and that cash rates globally will be lower for longer. While in Asia the slowdown through 2013 has highlighted the need for governments to remain proactive in adopting a broader economic and social policy framework.

At Home

Against this backdrop, the Australian economy has continued to meander. After a period of political gridlock we now have a new coalition government. However, many of the core issues that have been a hindrance to the economy in recent years still remain. Principally, questions abound around how the economy can transition from a mining and resources boom to an environment where labour productivity has slowed and the impact of a high Australian dollar has reduced the competitiveness of export and manufacturing sectors. Furthermore, the continued rise in the unemployment rate – forecast to reach 6% plus in 2014 – also has the ability to drag on growth.

One bright spot is the positive turnaround in residential house prices. The historic low interest rates (with official cash rates at 2.50%) have provided the perfect backdrop in recent periods for a recovery in housing. Capital city home values have increased 7.9% y/y, with a rise of 8.2% CYTD. Nevertheless growth has been mixed with much of the rally fuelled by a large rise in property values across Sydney and Melbourne.

Looking Forward

So against this backdrop what are some of the opportunities and risks to consider as we head into 2014? The global economy, while not out of the woods yet, is expected to improve through 2014. This may provide a continued positive backdrop for equities over bonds. As a result, central banks may pull back from current levels of quantitative easing. Cash rates appear set to remain lower for longer both domestically and globally. And the domestic economy may slow further from current levels as the peak of the mining boom subsides and the economy transitions to a new normal. Therefore, the challenge for 2014 will be to maintain a disciplined and selective approach to investing with a focus on managing downside risk.

Which comes first – saving or investing?

As a nation, both our level of savings, as well as our level of investment, are higher than many other developed countries'[1]. But over the last five years there has been a shift in the relationship between how much we save and how much we invest. So what does this say about how we should approach saving and investing in the future to make the most of our dollars?

According to the Reserve Bank of Australia (RBA), the amount we save as a nation started to increase from the mid-2000s, after a period during which the amount we saved started to fall.[1] Accordingly, from 2000 to 2010 the ratio of national net saving to GDP rose by three percentage points, from 4.9% to 7.9%.[2]

Interestingly, and although it might seem counterintuitive, saving and investing are not mutually exclusive. Just because we're now saving more than in the past doesn't mean we're investing less. In fact, the RBA has also noted our high levels of household, as well as corporate, savings have allowed Australia to fund substantial investment in the mining sector.

So how do you get the balance right between saving and investing to establish a firm financial foundation? First, let's take a look at the principles of saving.

The key is to consistently set funds aside beyond what is needed to pay for bills, groceries, school fees and other payments.

To do this, it's important to understand the true cost of these commitments.

Once you know how much you need to set aside to pay for your ongoing expenses, you can work out how much you have left available to save. A rule of thumb is to aim to save 10% to 15% of your after-tax income.

This is often more difficult at certain stages of your life – for instance when you start a family. When this happens you might find you don't save as much as during other stages of your life. Don't be too concerned – the idea is to develop a habit of saving throughout your whole life, rather than be too focused on the specifics of the amount.

So what's an effective way to save? One of the most beneficial strategies is salary sacrificing into superannuation. This may allow you to make a tax-effective contribution to superannuation, subject to certain thresholds.

It's a way of increasing your nest egg, while also reducing the tax you pay.

Another saving strategy is paying your mortgage through an offset account. This allows you to use your savings account balance to reduce the amount you owe on your loan, which could lower the interest you pay on your mortgage.

These are just two ways you can help increase your savings. There are lots of other initiatives you can also put in place to help build up the value of your investments over time.

The idea is to work with your financial adviser to put together a comprehensive financial plan that incorporates the right savings and investment strategies to help you achieve your goals, taking account of your individual circumstances and life stage so you can make the most effective use of your financial resources.

Sources

[1] Bishop, James & Cassidy, Natasha 'Trends in National Saving and Investment', RBA, 2012

[2] 'Measure of Australia's Progress', Australian Bureau of Statistics (ABS), 2010

Sticking to your financial plan: a how-to guide

"The best laid plans of mice and men often go awry." – *Robert Burns*

Poet Robert Burns understood more than most that life often gets in the way of our good intentions when he wrote this line in 1786.

Sometimes life events such as the birth of children, unexpected expenses and career changes can make it tough to stick to your plans.

One plan of particular importance regardless of your life events is your financial plan. This living document helps you map out your income against the investment milestones you would like to achieve to help you reach and maintain your desired lifestyle.

So what's the best way to steer a true course for your financial future?

Markets

It's the nature of financial markets to rise and fall. For instance, over the past five years the All Ordinaries index has risen from 3111 points in early March 2009 to around 5228 points in early October 2013.

As markets transition through these peaks and troughs it's easy for investors to consider changing the strategies they have put in place to help them achieve their goals. For instance, during a market rally it can be tempting to walk away from a disciplined dollar cost averaging strategy and suddenly make a substantial investment in the market.

But a good financial plan should take market volatility into account. So no matter how equities perform day-to-day, you can ride through the market's ups and downs to help reach your goals.

Personal circumstances

It's not just market fluctuations that can make it tempting to divert from a financial plan. According to the latest labour market statistics, more than 200,000 people lost their job between February 2012 and February 2013, as a result of a retrenchment or because their employer went out of business[1].

A major event such as a job loss can prompt us to question whether our long-term financial plan is still suitable.

However, a good financial plan should be flexible enough to adjust to changing circumstances, no matter whether you are retrenched, get married, have your first child or change your career.

The key message is not to allow major events to place your goals at risk. In fact, a significant life event is often when the true value of a financial plan reveals itself.

If something important happens in your life, it's a good idea to talk to your financial adviser about the best way to manage your finances and at the same time stick to your financial goals.

Source – [1.] Labour Mobility, Australian Bureau of Statistics (ABS), February 2013

What are some ways to get disciplined about achieving your financial goals?

1. **Set a small number of big goals that mean something to you –** Select your three most important goals and think about how it would feel to realise those goals. Talk about your goals with you financial adviser and the best way to achieve them.
2. **Break down your goals into manageable pieces –** Work with your financial adviser to construct a journey of small steps to reach your big goals.
3. **Frequently review your plan –** Remind yourself of the goals you committed to and the small steps you agreed to take.

Above all, remember a financial plan is a living document. It's an idea to see your financial adviser every six months or every year to review your goals and assess your performance against them, to help you steer a positive course for your financial future.

Getting it right for the grandkids

Grandparents really are the jewels in the crown of our community. Having raised their own children, many are now helping raise their grandchildren. This often extends to providing financial support to the grandkids. If you're in this situation, how can you make sure your generosity is as financially effective as possible?

If you're a grandparent, there's a big chance you're involved in the upbringing of your grandchildren. According to recent research, one in ten of those over the age of 65 in New South Wales look after their grandchildren full-time on an unpaid basis, with this figure reaching 20 per cent in some areas of the state.[1] And that's just the figures for NSW.

But we don't just rely on grandparents for hands-on help – many families also count on them to provide financial support. At the moment, there are no formal statistics about the monetary support grandparents give their grandchildren, and also their own kids. But anecdotal evidence from the financial advice community suggests grandparents are helping out their grandkids with, for instance, money for their first car or funds for a deposit on their first property. Some are even contributing to their grandkids' mortgages.

Given the increasing financial reliance of families on older generations, a growing number of people are looking for help to find out the best way to use their money to help their grandchildren.

If you're helping out the grandkids financially, it's a great idea to talk to a financial adviser about how to take advantage of incentives such as the First Home Savers Account, or how to employ clever strategies like using investment income to help pay down a family member's mortgage. Your adviser can also help navigate the financial system so the whole family realises the highest benefit possible from your generosity.

Considering the right questions

If you're helping out younger generations financially, one of the most important considerations is making sure the right money ends up in the right hands at the right time. But this will mean different things for different people, depending on their unique circumstances.

It's very important to consider the goals you are trying to achieve by helping out the family. That's why it can make sense to work with a good financial adviser, who may spend a great deal of time asking questions, listening and probing to uncover what you want to achieve by helping out your family.

This assists the adviser to design the right strategies to help you achieve your goals. For instance, let's say you want to help your grandchildren with their first home. Things your financial adviser may consider with you include:

- whether you want to help pay for the deposit and/or repayments.
- whether you want to invest this money now or at retirement, or include it in your legacy.
- how much money is available after you have provided for your own retirement.
- whether your grandchildren are financially dependent on you.

The answers to these questions may lead down very different structural tracks such as family discretionary trusts, testamentary trusts or gifting to maximise tax efficiency, and to make sure you don't trigger any adverse consequences. Whichever form it may take, your financial adviser can help you structure your generosity in a way that suits you and your circumstances.

[1] 'Grandparent Carers', Council on the Ageing NSW (COTA), 2013

Six key issues for grandparents

There are numerous factors your adviser may look at when working out the best strategy for you and your family. But here's a checklist of six of the major issues you may need to consider if you want to help out your grandchildren:

Age and income of the grandchildren

Investment income for minors can be taxed at penalty rates. Whereas, for people over the age of eighteen, investment income up to $20,542 may be tax free. This can be a particularly important consideration if you'd like to help contribute to education costs.

Centrelink benefits

If you receive a pension or part-pension from Centrelink you may only be able to gift up to $30,000 every five years, to a maximum of $10,000 per year, without adversely affecting your entitlements.

The right team of experts

The role of a financial adviser is often to project manage a team of experts. So it's an idea to ask your adviser if he or she has a network of other specialists such as lawyers to ensure you are receiving holistic advice.

Relationship risks

Although it's hard to do so, it's worth thinking about the risks associated with potential relationship breakdowns in the family, such as sibling rivalry and divorce of any family members. This could mean a gift for a grandchild ends up as an asset to be fought over in the courts. It might be worth talking to your adviser about the appropriateness of testamentary trusts or drip feeding financial assistance rather than gifting lump sums.

"Pay yourself first"

It's easy to fall into the trap of being too generous and not properly considering your own living and lifestyle needs in retirement before deciding how you will help out your family. So make sure your own financial future is secure before committing to help out your family.

Manage family risk

Families are often called on for help in the event of illness and injury of a child or grandchild. So you may want to consider talking to your family about how you can help to pay for your insurance premiums to help protect your grandchildren, depending on what is appropriate to suit your and your family's situation.

As you can see, there are a multitude of elements to consider when helping out your family financially, and your financial adviser is well placed to help you make the most of this.