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News & Views

2010

The past year has certainly been an interesting 12 months. Australia is well known for its droughts and flooding rains and the last year has been no exception. First it was El Nino, then it was La Nina. Throw in a GFC (Global Financial Crisis), just to make things more interesting, and you've got some very uncertain times to say the least.

Australia managed to survive the GFC in much better shape than its major counterparts on the back of our resources boom, and as a result of good financial management by our recent Governments. However, even since this newsletter started to take shape the economic forecasts have changed following the financial problems in Europe and the slowing of growth in China. In our initial commentary there was talk of a mining boom on the back of China's developing economy and its need for raw materials. The Australian economy is so closely aligned to the Chinese economy, so when China is booming we follow suit and so it goes in reverse when China starts to slow. In a very short space of time we've gone from what some predicted to be one of Australia's biggest mining booms to a more uncertain outlook as China's demand for materials, after the global financial crisis, starts to wane and the world markets are again nervous about international banking institutions.

So, here comes Goldilocks - "Not too hot, not too cold". That is the recipe that the Reserve Bank governor Glenn Stevens has been trying to cook up in relation to official interest rates. April saw the RBA's fifth rate hike in seven months. The Goldilocks scenario of getting it "just right" was the RBA's attempt at keeping Australia's economy on an even keel in the face of the expected mining boom while restraining the rest of the economy. They certainly couldn't have guessed though that the government would respond to the Henry Review by slugging the mining industry with its proposed resources super profits tax, or that sovereign debt risk would become a real issue for European countries like Greece, Spain, Portugal and Italy. Not only has this added to the woes of the mining sector, but also the global banking institutions, that presently fund approximately half the loans in the Australian banking system. The weakness in Australia's banking system is that our bank loans are not all covered by local savings, but use borrowed funds from abroad and these institutions apply a 'risk margin' which will have the flow on effect of raising our real interest rates. However, our interest rates currently still represent low rates historically.

From an agricultural perspective most of the country has experienced its best season in years with most land holders heaving a sigh of relief at the prospect of good production outcomes, and the now easing Aussie dollar is more favorable.

Sadly, not everyone will benefit from our current economic position but with some sound financial decision-making there are always opportunities for smart investors.

It is impossible to predict the movement of sharemarkets on a short term basis as investors' emotions affect their decisions. However, over the longer term, the fundamentals are easier to understand. The value of shares in profitable companies will rise, and conversely the value of non profitable companies will fall. The sharemarket is a leading indicator of the economy. The market will rise long before any sign of recovery occurs in the economy and similarly a drop in the market will precede an economic downturn.

As always, the critical decision is identifying the timeframe for your investments. For funds needed in 1-2 years, investing in anything other than interest- bearing funds should be considered speculative. For funds not needed for 5 years or so, investment in growth assets like good quality property and Australian and International shares may be appropriate, so long as you understand that volatility will occur in relation to both income return and value, along the way. The secret is being able to ride out these periods and not having to sell investments in a down market.

The past month of May shows just how news events can cause short term volatility in world sharemarkets, and how these events can't always be foreseen. We witnessed volcanic eruptions in Iceland which caused international travel disruptions (again), a major oil spill for the US, a European debt crisis, the ensuing crisis for the Euro currency, an Australian dollar tumble(especially in relation to the US dollar) a Wall Street Trading error triggering a 1000 point crash on their sharemarket, China's tightening of their economy, North Korea talking war (again), a change of government in the UK, riots in Greece and Thailand, the release of the Henry Tax review here in Australia and the announcement of the Resources Super Profit Tax. All in the space of a month - we certainly do live in interesting times.

In Australia, since 1950, the average bear market fall has been 33%, and it has taken an average 41 months for the market to reach a new high. The average gain of the ensuing bull market has been 132%. The percentage fall in our market to March 2009 was 55%, and over the past 15 months, we have seen a return of approximately 36%. If history is repeated, there will still be substantial gains to come. The question is when?

Personal Risk Insurance

The Global Financial Crisis has reminded us that our personal wealth can be affected by unforeseen global events and similarly, personal events such as accident, injury or in extreme cases death can rock our financial situation and that of our loved ones.

Insurance should play a significant role in our lives and it is important to ensure you protect what you have acquired - both in terms of physical assets and the ability to continue to earn an income to both maintain your lifestyle and service any debt. A good financial plan should provide protection against:

- *Death;*
- *Temporary and Permanent Disablement;*
- *A Traumatic event (e.g. stroke, heart attack, cancer); and*
- *Loss of income.*

Your partner may contribute significantly to such duties as childcare and home maintenance, therefore it is equally important to ensure they are insured against death, disablement or traumatic events, even if they are not earning an income. In the event of their death, disability or serious illness, the cost of hiring professionals to provide these services could be considerable. It may also be expensive to provide care for your family should one of them become disabled.

It is also important to have your insurance reviewed on a regular basis to ensure that you are not under insured or over insured either.

With the end of the financial year fast approaching, now is an appropriate time to think about income protection insurance. Income protection premiums are usually tax deductible, which means a more positive outlook on your tax return. Income protection insurance can replace up to 75% of your income. This benefit will help you with your ongoing living costs and allow you to continue to meet your financial obligations, in the event that you are unable to work through illness or accident.

Kennas Financial Services is able to arrange personal insurance cover for you and also compare your existing cover with newer, more modern products now offered. We can appraise all available cover on the market and select the cover that we consider best for you.

Call Brent Giles, one of our qualified financial planners, if you wish to have a no obligation insurance appraisal.

Superannuation

Superannuation continues to have significant taxation concessions attached, and with the sharemarket currently suffering a downturn, it may be an opportune time to invest in share-related investments within superannuation if you are at least 5 - 10 years from retiring. Alternatively, you may prefer to have your superannuation investments entirely in capital guaranteed investments, or something in between, in a balanced fund. All investment options are available and we can advise on the option that best suits your risk profile and time frame.

Some of the taxation advantages attached to superannuation are:-

- *Possible tax deductions of up to $50,000 if you are over 50, and up to $25,000 if less than 50 years of age.*
- *Only 15% p.a. maximum tax on earnings within the fund.*
- *No income tax payable by the fund once a pension is being paid.*
- *Tax fee lump sums and pensions for people aged 60 years and over.*

To find out more about superannuation and the potential tax savings you can make before 30th June 2010, contact one of our advisers for more information.

Superannuation co-contribution

The superannuation co-contribution is a government measure to boost superannuation savings. If you are a low or middle income earner, you may be able to receive the superannuation co-contribution from the government by making eligible personal superannuation contributions to your fund. The maximum amount of co-contribution is $1,000, and will be received if you contribute $1,000 to superannuation, and your income is below $31,920.
The co-contribution:

- *Will be paid by the Government into a superannuation fund or retirement savings account (RSA) – it can only be accessed when other preserved amounts can be accessed*
- *is not included as income in your tax return*
- *will not be subject to tax when paid to the fund or RSA provider*
- *will not be taxed when received as a benefit.*

Superannuation contributions for a Spouse

Another Government incentive available is an 18% taxation offset allowed to a taxpayer, on superannuation contributions of up to $3,000 for a low income spouse. The full offset is available where the spouse's income is less than $10,800 and cuts out all together at $13,800.

Estate Planning

Estate planning refers to the process of ensuring that your assets are dealt with according to your wishes should you die, or become unable to act for yourself.

Do you have a current Will? Have you appointed an Enduring Power of Attorney? Have you considered an Advanced Health Directive so your loved ones are aware of your wishes in the event of you being seriously unwell?

These are all important legal documents that should be drawn up by your solicitor, in conjunction with us as your accountant or financial planner. Additionally, they should be revised at least every 3 years, or at any time a major change occurs in your personal or financial situation. These may include:

- *marriage*
- *divorce*
- *birth of a child*
- *establishment of family trusts or companies*
- *retirement.*

If your Will was made a long time ago, whilst your main beneficiaries may still apply, it may be appropriate for you to consider the use of a testamentary trust. This particularly applies if your beneficiaries may now or in the future be subject to family law or bankruptcy proceedings, or you consider they may need some assistance with financial management.

In the case of the elderly, it may be appropriate to consider if your estate should be left to your spouse, or whether there may be advantages in having some or all of your assets directed to your children. If your spouse is likely to enter an aged care facility on your death, it may be advantageous for him/her to have fewer assets.

Our financial advisers can assist you with information in relation to all aspects of estate planning.

2010 Federal Budget and the Henry Tax Review

The 2010 Federal Budget and selected items from the Henry Tax Review included several proposals that may affect your future financial plans. We take a brief look at some of the primary proposals that could affect you.

2010 Federal Budget

. The temporary super co-contribution reduction to $1,000 will be made permanent and the co-contribution income eligibility thresholds will be frozen for the next two financial years. The maximum super co-contribution payable reduces by 3.333 cents per dollar of income over $31,920 p.a. and phases out altogether when your income reaches $61,920 p.a.

. Confirmation that the low income tax offset will increase from $1,350 to $1,500 for the 2010/11 year.

. 50% discount on the tax assessment of up to $1,000 of interest earned on eligible investments from 1 July 2011, resulting in an annual tax saving of up to $232.50.

. Optional standard work-related expenses tax deduction of $500 for the 2012/13 financial year, increasing to $1,000 for subsequent financial years.

. Increase in the medical expenses tax offset threshold from $1,500 to $2,000 from 1 July 2010, indexing annually.

Henry Tax Review

. Gradual increase in the current 9% Superannuation Guarantee (SG) rate commencing on 1 July 2013, peaking at 12% in the 2019/20 financial year.

. Increasing the cut off eligibility age for the SG from 70 to 75 effective from 1 July 2013.

. Government low income earners superannuation contribution of up to $500 for eligible individuals with adjusted taxable income of less than $37,000, effective from 1 July 2012.

. Retaining indefinitely the $50,000 cap on concessional superannuation contributions for people aged 50 or over from 1 July 2012, with superannuation balances below $500,000.

. Reduction of the company tax rate to 29% in 2013/14 and 28% in 2014/15. For small businesses, the company tax rate reduces to 28% from 2012/13.

The proposed increase in the superannuation guarantee and the retainment of the higher concessional contribution cap for eligible persons over age 50 could have a significant influence on your retirement planning strategies.

Many of the proposals may also have a significant impact on your personal cash flow budgeting and on your investment decisions.

To help you optimise on these changes, please contact us to discuss how these budget changes affect your personal situation.

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