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## MARKET UPDATE

An unprecedented global effort to inject trillions of stimulus dollars into the global economy and into the global financial system by governments and central banks has, to this point, done the trick. From the depths reached in March, the Australian stock market has risen by around 45%. Fear has subsided and we have seen the return of some optimism, although at the time of writing this update, we are seeing some increased volatility and caution returning to the markets. In January the Australian share market was down 6.1% and February was not fairing any better. The US market fared slightly better with falls of about 3.7%.

In 2010 the market has had plenty to pause and think about. We were just pondering the potential impact of a slowdown in China, when the Obama administration shook the US financial system by announcing its intention to legislate more stringent regulations on the banks. No surprises there! Whilst still digesting this, we are now being confronted with a potential sovereign debt default in Greece which has forced the whole of the EU to come to the party with a rescue package.

It seems the global credit crisis has gained another scalp and we can expect more to surface in the coming year. This will make markets nervous for a while as they assess the impact of these events.

Since the market low in March 2009 we have watched the markets claw their way back through a flood of good, bad and indifferent economic events. 2010 will see some powerful forces working to influence markets in opposing directions, which forces prevail is open for debate.

### Some tailwinds for markets and the economy in 2010

#### Interest Rates

Interest rates around the world remain at or near record lows. This could encourage speculation and investment activity and may provide a real economic boost in the short term making investing in stocks more appealing as interest rates reinforce low returns on cash. We suspect rising rates globally may be an issue for the second part of 2010 or into 2011 but rates are accommodative currently.



#### Government Stimulus

China spent nearly 25% of GDP (national income) stimulating their economy (and Australia's in a roundabout way). We believe the global stimulus packages have almost finished helping stock markets rise, but the momentum generated, in some economies, may continue to spur on stock market growth through 2010.

#### Asian development

Urbanisation and population growth in Asia provides an ongoing stimulus to resource rich countries such as Australia. China and India should continue to buy all of the coal, iron ore, uranium and gold we can produce for some time to come. The nature of Asian development means that many parts of Asia are still in the industrialisation phase (industrial economies feed on resources). Given the need for job growth for political stability in China, stimulus driven construction projects that rely heavily on our resources should continue.

#### Some headwinds for markets in 2010 and beyond

##### Tax rises for countries in debt

Developed countries have borrowed huge amounts and governments are spending much more than they earn. Governments will be forced to raise taxes to repay the debt incurred to fund the bailout and stimulus packages. This is likely to impact negatively on company profits at some point, which in turn will reduce dividend returns to investors.

##### Debt outstanding

Consumer and government debt particularly in developed countries is huge, relative to income levels. Australia is no different, with our rapidly inflating house prices, consumer and housing debt has grown to very high levels. As consumers repay debt, rather than continuing to spend, this can impact many sectors of the stock market and the economy. The irony of the bailouts that occurred in countries with persistent deficits (borrowing to spend) is that the problem of 'too much debt' is being solved by even more borrowing, but this time by governments.

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### Inflation on the horizon?

High inflation can put upward pressure on interest rates and hurt some types of stocks. The US and UK, governments and central banks 'quantitative easing' programs ('printing money') has attempted to stabilise their financial systems, and boost confidence. The positive effect to date has been quite minimal with the UK only recording a 0.3% increase in growth in the 4th quarter of 2009.

The longer term implications of this program however is that the newly printed money eventually seeps into the economy putting upward pressure on prices, food and energy leading to very high rates of inflation. The inflation of



energy cost could be a serious problem for developing countries such as China.

### Summary

We do not know whether the positives will outweigh the negatives in 2010. We suspect we have a few more nasty surprises in store. Whilst interest and inflation rates are low we don't believe that leaving all of one's money in cash at the bank is a good idea given the way currencies can depreciate and inflation can pick up at short notice.

Diversification is the key to getting through 2010 as the risks both positive and negative are evenly poised. Should Kevin Rudd over stimulate our economy, or should China run out of steam Australia's apparent immunity to the crisis will be severely tested. If not, we could continue to enjoy economic stability and a continued market recovery which is the envy of the world.

## Business Planning for the Unthinkable - Part 2

### Asset Protection

Whenever a business owner is asked what the most important assets of their business are, in most cases the response is related to the physical assets. These are highly valuable, but it's usually the intellectual capital and personal exertion provided by the key people in their organisation (the business owners and associates) that makes the physical assets generate profit.

What would be the impact if you should lose a key person, temporarily or permanently, from your business? The death, disablement or long term illness of a key person can result in financial loss and demands more disastrous than the loss or damage of a physical asset.

How would your business run if your business partner couldn't come into work for 12 months and the personal guarantees they have made for the business debt comes into question by creditors?

Some of the common implications of the above scenario include:

1. Trouble meeting debt payments as the void left by the key person's absence, dramatically reduces the revenues of the business.
2. Creditors of the business may come calling on the personal guarantees or assets.
3. Your business partner may want to have personal assets, held as security for business loans, released.
4. You may need to increase debt facilities to assist with the restructuring of the business.

### Identify the Risks

Sometimes determining the level of business risk in relation to the loss of a key person is difficult.

Some simple questions that can help identify the risks and potential losses include:

- Who does the business' success and profits depend on?
- On their death or disablement, could the business meet its loan repayments and creditor commitments?



- Would the key person want their personal assets, held as security on business loans, released?
- Would you want to avoid selling or encumbering business and personal assets?
- Would you want to, or be able to, borrow more money?
- If you had to quantify the amount of cash the business would require to repay debts, release personally secured assets and provide additional cash for business management, how much would you need?

### The Solution

Asset protection is a form of business risk management insurance which will ensure your business has enough cash to address the issues you have identified from the above questions should your business partner die or be disabled.

In the event of a claim, the proceeds of the insurance are paid directly to the business (not the key person). The business is then able to immediately free itself from liabilities, re-secure personally guaranteed loans and implement strategies to protect revenues.

It is important to note that as the insurance is to protect assets (not revenue), to pay down debts, it is not a tax deductible expense to the business.

Asset protection requires the collaborative expertise of you and your business associates, your accountant and your financial adviser to ensure that the level of cover is appropriate and that the insurance policies are correctly established to meet the business needs.

*Without Asset Protection in place, you may find that the death or disablement of a key business partner may well signal significant creditor and cash flow problems for the business, during a time when you are trying to steady a business which has just lost a key leader.*

## Investing for Education

These days employers place significant value on education and training and with all the additional technology and technical occupations that are being created, education and training will continue to be important. Providing the best opportunities for children, or grand children, is often considered a priority for parents. The decision between public and private education can often come down to costs and is normally a decision addressed just prior to the child commencing studies or training. For many, the funding of education will usually come out of the family income paid as the fees fall due. This can place substantial strain on a family's after tax cash flow or alternatively may result in parents having to forego their preferred option of schooling or training.

The alternative to funding education from a family's after tax income is to establish a plan early, whilst the child is still young, so that the power of long term investing and savings can work in your favour. By commencing an investment plan early and continuing to regularly save, the costs can be spread over ten or more years and you can benefit from the compounding effect on investment returns.

Private schooling is often used as a benchmark for costs as they are often the dearest form of education for children. Some school fees are in the tens of thousands a year and often increase by as much 8 to 10% per year (on average).

To illustrate this cost lets look at a child turning two this year. They will commence high school at age 12 and finish at age 17, the school fees at the desired school are currently \$7,000 per year. Assuming school fees increase by 8% per year the fees in the first year will cost the parents over \$15,000. The total fees for six years high school will be approximately \$111,000, which excludes uniforms, books and school trips. The parents currently have a disposable income, after tax and living expenses, of \$2,900 per month.



Our couple decided to commence a regular savings plan starting with \$2,000 plus \$200 per month invested into a portfolio expected to return, net of costs, 7% per annum (3% income and 4% growth) for the 16 years until their child finishes high school. Each year they increase the monthly amount by 9.2%, (from \$200 per month in year 1 to \$219 per month year 2) and all pre-tax income is reinvested.

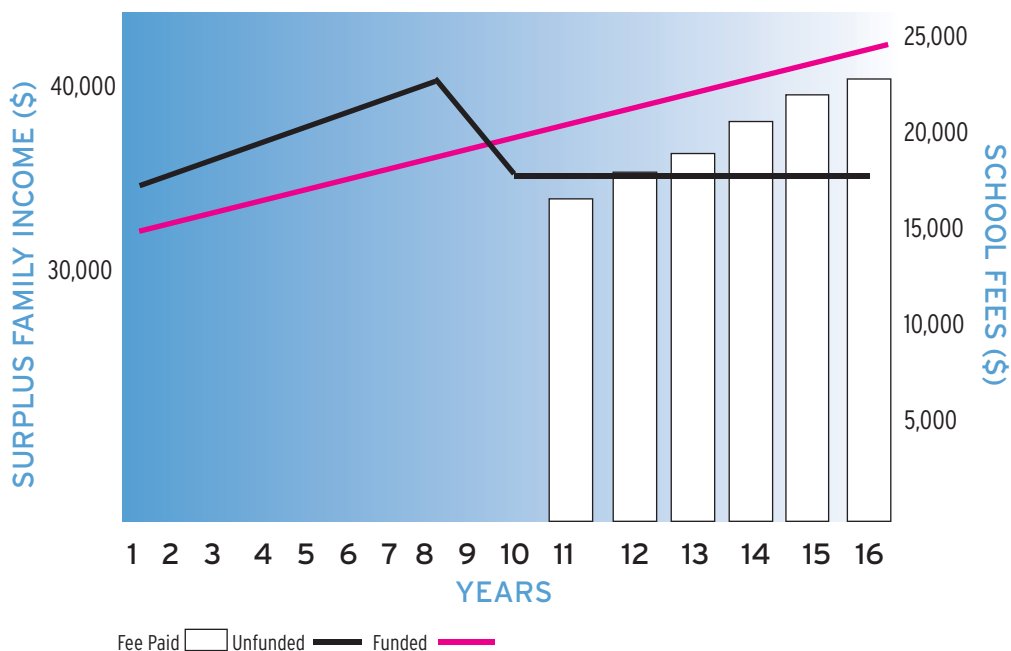
At the commencement of the first year of high school the couple accumulated over \$52,000 in the investment which, along with their regular savings, helped them meet the school fees over the next 7 years. The long term investment allowed them to spread the cost of education over 16 years and reduced the total cost by about \$30,000, a significant saving.

The chart below illustrates the scenario for our couple. It compares the effect on their family's surplus income of funding or not funding their child's education.

Some points to consider about investing for a child's education include:

- The school fees you expect to incur and when they will commence. This will determine the expected investment value you require at the time your child, or grandchild, starts their education.
- The type of assets you wish to invest in i.e. shares, property, cash. This will relate to your attitude to investment risk.
- What level of access you require from the investment prior to your child commencing education or training.
- Who will own the investment, as income, and realised capital gains, may be taxable.

### FUNDING EDUCATION



## Enduring issues for everyone

So you've made a Will and taken out life insurance to provide for your family in case the unthinkable happens. But what if instead of dying you became mentally incapacitated? Who could you trust to make financial, medical and lifestyle decisions on your behalf? And how can you make sure they'll have the power to do so unchallenged?

Consider the following:

Sarah and Jason, both 32, had been married for just over a year when he suffered a serious brain injury in a car crash. Although their relationship was well established they still had some separate finances at the time of the accident, his TPD and income protection plans were still to be paid to his personal bank account.

Although Jason was well organised, he hadn't found the time to appoint an enduring power of attorney to handle his financial affairs. That meant neither Sarah nor any of his family were legally able to administer his finances or access his bank account. Sarah sought legal advice and then decided to lodge an application. Whilst waiting for the Commissioner to approve the appointment Sarah had to meet mortgage payments and other bills from her own savings and income, whilst also trying to care for Jason. To get by she had to borrow money from her retired parents. This all just added to the stress during a very traumatic time in both Sarah and Jason's lives.

All this could have been avoided had Jason and Sarah both taken the time to appoint an enduring power of attorney to handle their financial affairs in this situation.

### Why appoint an Enduring Power of Attorney?

An enduring power of attorney is a document whereby one person (the principal) authorises another (the attorney) to act on his or her behalf, generally in relation to financial and property decisions. In some states, this can also extend to medical and lifestyle issues. An enduring power of attorney (EPA) enables someone to immediately step in and make financial decisions needed to ensure that a person's incapacity doesn't adversely affect them or their family's financial position. In Sarah and Jason's case, an EPA for Jason appointing Sarah would have allowed her to access his personal savings, which may include lump sum and income based insurance benefits, to meet expenses, repay loans and to ensure that long term plans could be put in place for their financial future. Once in place an EPA only needs to be presented to the financial institution undertaking the requests, no application to courts is required.



### What limitations does an Enduring Power of Attorney have?

An appointed Attorney (i.e. Sarah) must at all times act in the best interests of the principal (i.e. Jason) and can be prosecuted for not doing so. A principal can make or revoke an enduring power of attorney at any time provided they have the mental capacity. The easiest way to revoke a power is to tear up all copies. It's also a good idea to send a signed letter to all financial institutions informing them that the relevant power of attorney is revoked and asking for all copies to be posted back.

An enduring power of attorney can come into effect from the date signed or specified in the document, or when a particular event occurs (such as when the principal loses legal capacity to act for themselves).

Be aware that legislation differs from state to state. In NSW and WA, an enduring power of attorney is not permitted to make decisions in relation to medical treatment, that's not the case in Victoria, SA, the ACT and Queensland. In NSW and WA, where a more extensive medical and lifestyle enduring power of attorney is not available, it's important to also appoint an Enduring Guardian in the event of the appointor's incapacity.

Source: Alena Miles, Technical Analyst, Zurich

## OUR OFFICES

### Perth

Level 2  
8 St Georges Terrace  
Perth WA 6000  
P: 08 9261 9200

### Sydney

Level 12  
60 Castlereagh St  
Sydney NSW 2000  
P: 02 9233 8933

### Melbourne

Level 8, Rialto South Tower  
525 Collins St  
Melbourne VIC 3000  
P: 03 9286 1800

### Canberra

Level 1, 103-105  
Northbourne Ave  
Canberra ACT 2601  
P: 02 6247 5988

### Adelaide

Level 4  
191 Pulteney St  
Adelaide SA 5000  
P: 08 8232 3000

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