



Personal Wealth



Summer 2011

A Quarterly Newsletter for

Lifespan Clients

The European Rollercoaster Previous Quarter

Equity markets had big rallies in October due to the over optimism for a workable Greek bailout package. There was an agreement for private holders of Greek debt to write off 50% of the face value of this debt, essentially a default in everything but name. Australian equities rose over 7% while the Australian dollar rose 9% against the US dollar.

In Australia the Reserve Bank (RBA) lowered the official cash rate by 0.25% to 4.50% on Melbourne Cup Day. The September quarter inflation number (CPI) came in lower than expected at 0.6% to post an annual rate of 3.5%. The core CPI which is the preferred measure of the RBA came in at 2.5%, in the middle of the RBA's 2-3% target range.

US Growth for the September quarter was stronger than expected with GDP rising a 2.5% annual rate. Global growth forecasts for 2012 were lowered by the International Monetary Fund (IMF) and many other economists. The IMF downgraded global economic growth in 2011 and 2012 to 4% (formerly 4.3% and 4.5% respectively) - Chart 1. This is down from 5% in 2010. The Chinese inflation rate fell to 5.5% last month, well down from the recent high of 6.5%.

The prime ministers of both Greece and Italy agreed to resign amid the turmoil caused by their debt problems. Markets sold off again as Italian 10 year bond yields traded over 7%. When highly indebted governments have to borrow new money at 7%, the interest pay-

ments are considered to be unsustainable. At that point, those governments seek a bailout which usually requires harsh conditions such as major cuts to spending on public services, welfare and so on.

Economic Backdrop

The sell-off in global equity markets this year has been driven by concerns about slowing global growth and the European sovereign debt crisis, first Greece and now Italy. Italy is the third largest economy in Europe and has a \$2.6 trillion dollar debt and a debt to GDP ratio of over 120%. If Italy has to borrow at 7% (or higher) as this debt rolls over then something has to give as this is unsustainable. The size of this economy means that a solution will be far more difficult than for Greece. Italy's debt exceeds that of Greece, Spain, Portugal and Ireland combined. It is

also the world's third-largest bond market and eighth-biggest economy. The Italian situation is likely to be a major driver of market sentiment going forward.

Against this, the US and China have provided some comparatively good news recently. Markets have been worried about high Chinese inflation and how fast that economy will grow as they seek to lower the inflation rate. However, inflation now seems on a downward trend. While policymakers still have inflation as a top priority, there is some scope for policies to be more pro-growth next year.

There was a lot of concern last quarter that the US economy was about to enter a double-dip recession. This is not the case with recent data pointing to an economy growing at about 2%. However this is still not fast enough to lower the unemployment rate which remains at 9.0%. There is also the potential for mar-

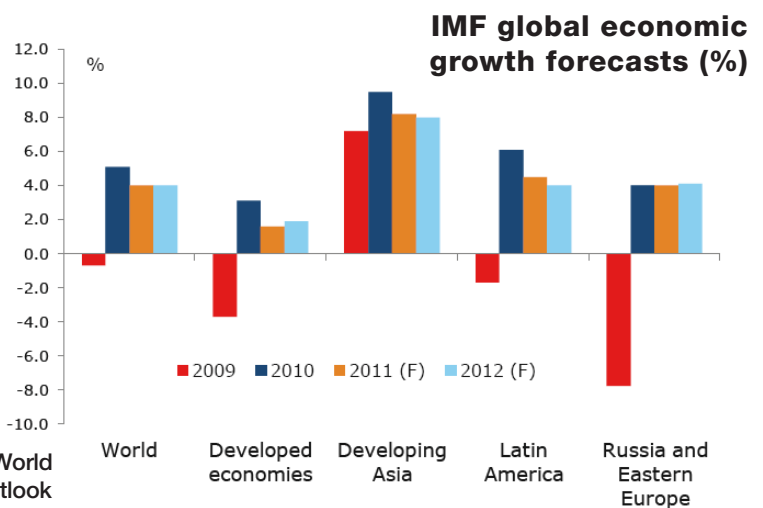


Chart 1
Source: IMF World Economic Outlook September 2011.



ket volatility arising from the debt reduction super committee and a President who is looking for election issues rather than solving problems.

In Australia, the good inflation data enabled the RBA to cut interest rates by 0.25%. The accompanying statement suggested the RBA now sees monetary policy as being a fairly neutral influence on the economy. We should note that we still have some of the highest interest rates of developed countries. We do not believe we will see too many more rate cuts given the strength of the mining sector. However this small cut should be of help to the subdued consumer sector.

Outlook Investment

Increasing global risk aversion more so than the underlying fundamentals have been the dominant influence on markets lately. The biggest exception to this is obviously in Europe where austerity programs will dramatically slow growth in the region. A number of the economies will probably have recession next year and European growth will likely be under 1%. If we can see some progress

or resolution on European debt issues, particularly in Italy then equity markets will rally significantly.

An illustration of risk aversion causing a fall in equity prices is in Australian equities. The equity market fell more than 20% from its April peak, causing the one year forward PE (price earnings ratio) to fall from about 12 times to about 9.5 times, a drop in the PE multiple of over 20%. During this period, earnings estimates were only reduced by about 5%. We believe that the Australian equity market is trading at less than 11.5 times PE which is about 20% below its long term average (UBS).

As in our last newsletter, the projected dividend yield at over 5% for 2012 is higher than both the cash rate and the Australian government 10 year bond rate. The estimated US equity market dividend yield is also higher than the US 10 year bond yield of about 2.0%. Global equities and emerging market equities are also trading well below their long average PE ratios and Price to Book Value ratio (a common valuation measure).

The bottom line is that equities are attractively valued from a long term perspective but in the short and medium term performance will be determined by risk aversion or sentiment. Investors who can ride out the volatility should be rewarded eventually. And remember that in a flat market where inflation is not an issue that the dividend yield of a market will contribute greatly to the total return.

The opposite is the case for bonds as a flight to safety has led to a big rally in quality sovereign bonds, i.e. yields have fallen and prices have gone up. The Australian 10 year bond is yielding 4.2% while the US 10 year just 2.0%. From a long term valuation perspective we prefer "cheaper" equities versus "expensive" fixed interest. However we expect a great deal of volatility, especially out of Europe for a while.

Investors should be looking to add to accumulate risk assets such as equities on pullbacks in the market. How cautious you are obviously depends on your investment timeframe. The best strategy for investors is to use dollar cost averaging as much as possible.

Chart 2.
Investment Returns to October 31, 2011 (% p.a.)

Asset Class	1 month	3 month	1 year	3 years	5 years
Australian Shares	7.25	-1.25	-3.65	6.94	-0.18
Global Shares	1.23	-3.87	-7.31	-4.70	-6.58
Listed Property	3.8	2.21	-2.25	-1.67	-12.79
Fixed Interest	-0.57	2.32	8.42	6.90	6.96
AUD / USD	9.2	-3.4	8.2	17.2	6.5

Source: Mercer

Carbon Tax Compensation Measures

On the 8 of November 2011 a number of Bills which form the Carbon Tax package were passed in Parliament. The measures include a tax (Carbon Tax) on Australia's largest polluters and measures to compensate individuals to offset the increase in the cost of living.

The carbon tax will be fixed at \$23 a ton for 3 years starting 1 July 2012 to move to an emission trading scheme (ETS)

where prices will be set by the market.

The Government has put together compensation measures to help households adjust to the carbon tax impact. The Household Assistance Package is aimed at helping pensioners and low to middle income households. Compensation measures that affect tax payers and social security beneficiaries are summarised as follows.

Tax Payers

As shown in **table A** commencing 1 July 2012 the tax free threshold will triple from \$6,000 to \$18,201 with the first marginal tax rate increasing from 15% to 19% and from 30.00% to 32.50% for the second marginal tax rate. From 1 July 2015 the tax free threshold will then increase to \$19,401 and the 30% marginal tax rate will increase to 33%. These new adjustments will ensure that people earning less than \$80,000 per annum qualify for



a tax cut. According to the Government around 60% of all taxpayers will get a tax cut of at least \$300 from 1 July 2012.

In conjunction with these changes, the Low Income Tax Offset (LITO) will be reduced to a maximum of \$445 and to \$300 from 1 July 2015 from the current maximum of \$1,500.

The rate at which the LITO reduces will change from the current 4% on income above \$30,000 to 1.5% on income above \$37,000 and to 1% from 1 July 2015 on income above \$37,000 as shown in the **table B**.

These new measures will result in people earning up to \$20,542 from 1 July 2012 and earning up to \$20,979 from 1 July 2015 paying no income tax, resulting in an increase of \$4,542 and \$4,979 over the current \$16,000 threshold.

Table C compares the current tax position and net income with the new tax free threshold and tax rate commencing in the 2012/13 financial year for different individual's income. Please note that these calculations exclude the Medicare levy.

Social Security Beneficiaries Pensioners

Age pensioners, including part-rate pensioners and Self-funded retirees who hold the Commonwealth Senior Health Card, will receive assistance under the Clean Energy Supplement as follows:

Under the Clean Energy Supplement a single person will receive an annual amount of \$338 and \$510 for a couple combined (\$255 to each member). These payments represent an increase of 1.7% in the maximum rate of pension and will be paid fortnightly (quarterly for Self-funded retirees) from March 2013 and are in addition to the existing Pension Supplement.

To help with the increase cost of living from 1 July 2012 a one off lump sum payment will be made under the Clean Energy Advance in May/June 2012. A one off payment of \$250 will be paid to a single person and a payment of \$190

Table A

Current		From 1 July 2012		From 1 July 2015	
Threshold	Tax Rate	Threshold	Tax Rate	Threshold	Tax Rate
\$6,000	15.00%	\$18,201	19.00%	\$19,401	19.00%
\$37,001	30.00%	\$37,001	32.50%	\$37,001	33.00%
\$80,001	37.00%	\$80,001	37.00%	\$80,001	37.00%
\$180,001	45.00%	\$180,001	45.00%	\$180,001	45.00%

Table B

Date	Maximum Offset	Taper Rate
Current	\$1,500	4.00% on income over \$30,000
From 1 July 2012	\$445	1.50% on income over \$37,000
From 1 July 2015	\$300	1.00% on income over \$37,000

Table C

Tax Year	Taxable Income	Tax	Low Income Tax Offset	Net Income Tax Payable	Net Income	Difference in Net Income
	\$	\$	\$	\$	\$	\$
2011/12	20,000	2,100	(1,500)	600	19,400	
2012/13	20,000	342	(445)	0	20,000	600
2011/12	25,000	2,850	(1,500)	1,350	23,650	
2012/13	25,000	1,292	(445)	847	24,153	503
2011/12	30,000	3,600	(1,500)	2,100	27,900	
2012/13	30,000	2,242	(445)	1,797	28,203	303
2011/12	40,000	5,550	(1,100)	4,450	35,550	
2012/13	40,000	4,547	(400)	4,147	35,853	303
2011/12	50,000	8,550	(700)	7,850	42,150	
2012/13	50,000	7,797	(250)	7,547	42,453	303
2011/12	60,000	11,550	(300)	11,250	48,750	
2012/13	60,000	11,047	(100)	10,947	49,053	303
2011/12	70,000	14,550	0	14,550	55,450	
2012/13	70,000	14,297	0	14,297	55,703	253
2011/12	80,000	17,550	0	17,550	62,450	
2012/13	80,000	17,547	0	17,547	62,453	3

for each member of a couple (\$380 combined). These upfront payments equal nine months of the Clean Energy Supplement.

Families, Carers & Disability Support Pensioners

- ▶ Families receiving the Family Tax Benefit Part A will get up to an extra \$110 per child and eligible families will get up to an extra \$69 in Family Tax Benefit Part B.
- ▶ Parenting Payment recipients will receive up to \$289 per annum.
- ▶ Allowance beneficiaries will get up to \$218 extra per year for singles, \$234 per year for single parents and \$390 per year for couples combined.

- ▶ Student payments recipients will receive \$177 for single with higher payments if they have dependent children.
- ▶ Carers and people with disability will receive assistance through their Carer Payment or Disability Support Pension.
- ▶ From 1 July 2012 people who hold a relevant concession card and rely on essential medical equipment will be able to claim an annual amount of \$140 under the Essential Medical Equipment Payment. This payment is in addition to other assistance and the claimant must be either using the medical equipment or be the carer of the person using the equipment.



▶ People in receipt of the Disability Support Pension or the Carer Payment will see their pension payment increase up to \$338 for singles and \$255 for each member of a couple. As with the Age pension beneficiaries they will receive a lump sum advance payment in May/ June 2012 to cover the first 9 months

to March 2013 from which time they will receive their assistance payment fortnightly.

▶ The people in the above situation are also eligible for the tax cuts on top of the increase in their Centrelink benefits if relevant to their situation.

For more information on the Government Clean Energy Future refer to the following link <http://www.cleanenergyfuture.gov.au/>

Featured Service

Australian Unity has extended their Health Fund membership offer of a second month free until the end of February 2012 to Lifespan clients.

Australian Unity is a national healthcare, financial services and retirement living organisation providing services to 560,000 Australians. The company has some 280,000 members nationwide, including more than 10,000 members who have been with them for more than 50 years.

Australian Unity believes that good health cover is so much more than just providing clients with excellent hospital and extras cover. It also means giving you the help and support you need to be healthy all the time.

Australian Unity Health Fund Benefits exclusively available to Australian Unity members include a range of services, innovative support tools and rewards to assist you to enjoy a healthier, happier future.

- 1. You'll also get over \$450 in additional benefits for losing weight, quitting smoking and getting a GP health check.
- 2. Free access to Wellplan Online, our comprehensive personalised health and

wellness service that gives you the tools and information to help you be the healthiest you can be.

- 3. Extras cover means you can keep your teeth in good health with regular check-ups. Our No Gap Dental Network provides selected preventative dental services at no out-of-pocket cost to you.
- 4. Wellplan Rewards offers great savings on a range of health and lifestyle products and services.
- 5. Fantastic financial benefits include a 4% discount when you pay your membership by direct debit. You'll also be eligible for a 10% discount on Australian Unity Home & Contents Insurance, Travel Insurance, and Car Insurance.
- 6. If you're single and earning over \$80,000, or your combined family income is over \$160,000p/a, and you take out hospital cover, it'll help reduce your tax.
- 7. Make extra savings by excluding pregnancy cover, you can always include it later if you plan to have a baby.
- 8. Already got kids? Well, until they're 23 or 25 if they're studying or doing



Join before ~~February 29/2012~~
~~November 30~~
and get your
second month
free.
Plus you
can claim
immediately
on many extras. Find out more

an apprenticeship, they can be covered under the family membership, at no extra cost.

- 9. Get others to join Australian Unity hospital cover and we say thanks with a \$100 gift voucher every time someone you've referred joins.
- 10. Because there's no two month general waiting period, you can claim immediately on many of the benefits we offer.

Subject to conditions

To find out more about this service contact your adviser.



SEASONS GREETINGS
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