SUMMER 11

finance forum

your quarterly financial newsletter from Strategic Planning Partners

welcome to the Summer edition

2011 has been quite a year for financial markets both overseas and here in Australia, with a remarkable, although not unheard of, period of volatility in investment markets.

While the media headlines appear focused on negativity in the European and American markets, closer to home the outlook is brighter.

The population continues to grow rapidly, requiring the need for housing and consumer goods and therefore the economy. The resources boom that has been Australia's buffer over the past five years continues to provide support.

Few people can resist the pricing war that is currently being fought out between retail giants and this will only continue through the Christmas period and the end of year sales.

As individuals we have little control over what goes on across the major investment markets. You can however control your own financial plan by engaging with your adviser to map out the strategy that's right for you.

In the meantime we would like to wish you a very merry Christmas and a happy new year.

2011 in review

by Paul Clitheroe

What a year it's been. Four years on from the global financial crisis, and we're still dealing with its aftermath.

Europe is wracked by debt problems, the US economy remains sluggish and despite the best efforts of governments around the world, the global outlook continues to be uncertain.

There are some bright spots though. Many emerging economies especially those of Asia, are experiencing strong growth. Australia is benefitting from global demand for coal and iron ore, and a massive pipeline of investment is poised to expand our resource output. Households have made a return to saving and we have become a lot more cautious about taking on debt. Nonetheless, for investors the two-speed global economy is dishing up plenty of conflicting signals.

Despite the health of our economy, the Australian sharemarket has been caught up in the wave of volatility that has rocked global stock markets. As I write in mid-November, the S&P ASX 200, which measures the performance of our largest 200 listed companies (by market capitalisation), is down by 6.35 per cent for the year. Yet the same index rose 6.9 per cent over the last quarter.

The housing market experienced a slowdown in 2011 but research group RP Data believes it could be turning the corner. Median values rose in September in a number of cities including Brisbane and Adelaide, and the November rate cut is likely to give buyers the confidence and financial means to return to the market.

focus on you

In uncertain times like the present it's important for investors to choose a clear path. One of the best ways to do this is by tuning out from the day to day dramas on world markets, and focus on your personal long-term financial plan.

Stashing the bulk of your wealth into term deposits for instance, as many Australians have done this year, may seem like a sensible option today. But over time it will cost you dearly in lost capital growth and fully taxed returns.

By contrast, the shares of many leading Australian companies are now priced well below their value of a few years ago. Yet many are paying excellent (tax-friendly) dividends and have solid foundations for a bright future. Remember too, opportunities aren't limited to Australia. Adding some global stocks to your portfolio provides valuable diversification.

celebrate sensibly

The upcoming holiday season is a time to relax, celebrate and prepare for 2012. At this busy time of year it's easy to let money matters take a back seat to festivities, but it's worth sticking to your normal financial routine. Aim to pay a bit extra off your home loan each month – an easy way to do this is to maintain your repayments at the pre-November rate cut level. Where possible, continue to grow your investments through dollar cost averaging and use the balance of your bank account, not your credit card limit, to shape your Christmas spending.

My best wishes for a safe and merry festive season.

Paul Clitheroe is a founding director of financial planning firm ipac, Chairman of the Australian Government Financial Literacy Board and chief commentator for *Money Magazine*.

understanding today's investment environment

This was a year when sharemarkets were volatile as investors became increasingly concerned about developments in Europe. Here we answer common questions about the current investment environment.

investment markets are very volatile - why is that?

Investors are reacting with heightened sensitivity to political developments in Europe and are largely ignoring the strength of underlying company profits, which do not change markedly from day to day. What's changing rapidly is investor sentiment. And at the moment, the potential for bad news about the Euro is the dominant influence on sentiment.

It's worth remembering that bouts of volatility have always been part of the investment landscape.

In the last two decades we have survived a banking crisis in Australia as well as the technology bubble and its subsequent bursting. History shows that share prices of quality investments do recover; it is the timing of the recovery that is hard to predict.

what is happening in Europe?

The situation in Europe is very fluid. There are significant concerns about how the Government debt crisis will be managed and what this means for economic growth in Europe. A recession in Europe is likely but its intensity is hard to forecast. The concerns have been magnified by the complex challenges faced by policymakers to develop and implement a co-ordinated and effective response.

While the debt concerns were initially focused on smaller countries, like Greece and Portugal, we have seen these worries spread to larger nations such as Italy. European leaders have agreed in principle to measures to stabilise the situation. And parliamentary changes in Italy, Spain and Greece are signs that the political will to drive necessary change is strengthening.

The issues in Europe are complex and we should continue to expect the news flow, both positive and negative, to drive investor sentiment in the near term. European policymakers are very aware of the risk of a disorderly outcome for the debt crisis and seem to be making meaningful progress and are acting more collectively to meet the challenges.

why isn't the Australian sharemarket doing better?

The Australian economy remains well-positioned with low unemployment and good underlying company fundamentals, even though activity in some sectors is quite subdued. Australia's exposure to the fast-growing Asian economies underpins our economy. While these should be positive influences on the Australian sharemarket, they have been overshadowed by events in the US and Europe.

Some investors fear that a significant slowdown in the US and Europe would reduce demand for exports from Asia which would reduce demand for our raw materials. There is however another aspect to the story. Ongoing growth and expansion in Asian economies continues to drive demand for Australia's raw materials. Domestic demand remains high and bodes well for the future of Australian exports.

In addition, over time, the increased national income arising from the resources boom will be recycled from the mining sector into other sectors of the economy such as housing construction, retail and financial services. This will support a wider sense of well-being and consumer confidence. With this as the backdrop, and based on current valuations, the outlook for the Australian sharemarket is quite positive on a medium-term horizon.

how is the situation in the US?

The US Federal Reserve continues to believe that US economic growth can maintain a moderate pace over the medium term. They are committed to support the economy with very low interest rates

for quite some time because high unemployment rates and weak housing prices continue to have a negative impact on consumer sentiment.

The political environment is also proving to be an impediment to business confidence. Large companies in the US are in very good shape and looking to invest and employ people to take advantage of growth opportunities in emerging economies. However they are hanging back waiting for the politicians to lay out policies to reinvigorate the US economy over the short term while addressing concerns regarding their debt position over the longer term.

can shares perform in this environment?

There are two important factors that investors should consider. The first is that the sharemarket is forward-looking. Investors are well aware of the current risks and share prices already reflect the negative outlook. So a further downwards adjustment in the market would only be driven by severe deterioration in that outlook. While this possibility can't be totally ignored, a protracted economic downturn is not the base case.

Secondly, and most importantly, companies are generally in great shape, with high earnings, healthy balance sheets and lean, productive operations. The long term prospects for Australian companies like BHP and Commonwealth Bank of Australia (CBA) are strong. Their prospects have not deteriorated over the past four months even though their share prices have declined.

It is sentiment, not the quality of the business, that has changed.

The same is true globally with Nestle, GE, Apple and Wal-Mart among a host of companies that continue to do well.

The performance of these and similar companies is what will drive sharemarkets over the medium term. As share prices are currently low relative to fundamentals there is a good case for shares to produce above-average returns over the medium term even in an environment where growth in the US and Europe is below average.

why wouldn't I just move my money to term deposits?

Depending on your personal circumstances, it may well make sense to have some of your money invested in term deposits. It is understandable that investors would want a level of certainty around a portion of their capital to meet shorter-term living expenses.

However, if you are investing to produce an income stream for retirement then term deposits are unlikely to be the best way to meet this need. This is particularly the case at present when, for example, the shares of all of the big four banks in Australia have a higher dividend yield than you can obtain from them though a term deposit.

Take the Commonwealth Bank of Australia (CBA) as an example. Including the benefit of franking credits its dividend yield at 7 November was 9.3 per cent, contrast that to the bank's 12 month term deposit rate of 5.3 per cent. CBA shares offer an extra 4 per cent in annual income. In addition, shares offer the potential for capital growth over the medium term while term deposits do not.

how can investors respond?

Investors who stick with their investment strategy will be well-placed when the focus of investors returns to the underlying strength of companies. History shows that when sentiment turns positive after a period of pessimism, the lion's share of the gains in the market is made in the early days of the recovery. Investors who stick with their plan will automatically participate in this upswing.

remaining calm this Christmas

As singer Andy Williams once said, 'it's the most wonderful time of the year', and for most people Christmas time is exactly that.

For some however it can also be a stressful and hectic period, at a time when you should be winding down with those close to you and looking forward to the year ahead.

So that you can properly enjoy the holidays we've come up with a few tips to help you remain calm and enjoy a relaxing Christmas.

don't break the bank

Despite the bombardment of negativity within the media regarding consumer spending, retailers are very clever and they will be battling hard to part you of your hard earned cash through sales campaigns.

We all know that we're susceptible to the emotional baggage that comes with giving our loved ones the gifts they want but during these volatile times it's hard to know just how much you should spend!

Consider establishing present limits that won't cause you to fall out of sync with your budget. Let's face it a thoughtful gift is generally more cherished than far higher priced items. An expensive gift however really will be the gift that keeps on giving by growing interest on your credit card!

just say 'no'

It's the season of good will so why wouldn't you want to make your friends/family happy? It's actually easier said than done. Whatever your plans this Christmas make sure that you prioritise the items that enable you to best relax and say no to anything that might cause stress or complications.

think of others

Tap into your deeper values this season. As hard as it is to remember during times of crisis it's true to say that there is always someone worse off than you.

Gifts are always a nice gesture to say you're thinking about someone, but it doesn't necessarily have to come in the form of a new pair of jeans, a computer or a TV.

Why not consider rallying the family together to spend a couple of hours in a homeless shelter or a soup kitchen? Or you could 'adopt' a family friend or acquaintance and invite them to your own family gathering? The feeling of helping someone less fortunate than you is sometimes just as warm as receiving a gift.

abandoning healthy eating habits

Mince pies, Christmas cake, chips and dips are all reasons we enjoy Christmas. Food and alcohol are arguably at the centre of many Christmas celebrations – and why shouldn't you let your hair down a little, it's been a long year!

If you've been following a diet throughout the year it's probably worth thinking about keeping your food consumption within moderation. If you're one of these people who take care but remember that Christmas only comes round once a year. Treat yourself accordingly!

plan ahead

You don't have to be a meticulous event organiser to bring everyone together this Christmas. Why not talk to your family and work out who will be the host and where your get-together will take place.

You can even organise a 'bring your own' item of food buffet where all your guests choose an item of food to contribute to your overall dinner. If you're having a BBQ this makes it easy! Whatever you decide to do give yourself plenty of time. Spare time = less stress.

above all be realistic

Remember to speak to your financial adviser if you're feeling the squeeze this Christmas. Your adviser can run through your options to determine the best solutions for you and your family.

holiday office closure

As previously advised in a letter to all of our clients, our office will be closed from 5pm Friday 16th December and will be reopening at 8.30am Tuesday 3rd January 2012. We are closing a week earlier this year in order to carry out some much needed renovation work in our client meeting rooms and back office. We wish all our clients a safe and wonderful Christmas and we look forward to seeing everyone in the new year!