The Count Report

Rise as the dollar falls

SMSF: How and why to diversify

Teaching kids the secrets of success

AUTUMN 2015 | ISSUE NO. 119

Count

Welcome

A message from the CEO

Welcome to the Autumn edition of The Count Report.

It's been interesting to observe the performance of the Australian dollar over the last decade or so. There's been a fair amount of bouncing around but the current trend is down.

In our feature article 'Rise as the dollar falls', we look at what this means for your investments and what it can teach us about risk.

This month, we also look at what needs to be considered before getting your asset allocation right inside or outside an SMSF, and how it's a fantastic exercise in developing a broader investment discipline.

And in 'Teaching kids the secrets of success', we share some tips to help your children and grandchildren become wealthy and wise at an early age.

I hope you enjoy reading this edition of The Count Report. Along with your Count Financial Adviser we look forward to helping you reach your financial and lifestyle goals in 2015.

Regards,

David Lane
Count Financial Chief Executive Officer

"It's been interesting to observe the performance of the Australian dollar over the last decade or so."

David Lane

Teaching kids the secrets of success

In an increasingly digital world the concept of money can be foreign to children. Here are some tips to help your kids and grandkids become wealthy and wise.

When our generations were young we would often find ourselves standing next to mum or dad at the corner store, watching them count out notes and coins as they paid for the bread and milk. This was a valuable lesson to us in the purpose of money, in its value and meaning.

Fast forward to today and few corner stores exist. When our children see us pay for anything at the shopping centre it is with a piece of plastic, and soon it will be with our mobile phones. Counting change is foreign to many children. Even the school canteen, has become about internet orders and credit card payments.

It is now more important than ever to consciously teach children about money, finances, cost, saving, spending, interest and budgeting.

MONEY DOESN'T GROW ON TREES

Many children believe parents have an endless supply of money, that it is an unlimited resource. Until they are told that money must be earned, and that it must be saved, that basic misconception will continue.

Budgeting can be discussed with children in relation to your own costs, such as weekly grocery bills and phone bills etc, or in terms of something they wish for, like a new soccer ball. Sit down with them, write up a budget and work out how long it might take them to save their pocket money each week before they can afford that item.

This, of course, brings up the topic of pocket money, a powerful way to teach children the value of cash. Whether it is payment for completing chores or reward for using good manners and behaving well, children learn very quickly that money must be earned. They may soon learn that they can save for their new scooter more quickly if they earn extra by helping walk the dog each morning.

A good idea is to keep their pocket money in two different piggy banks, one for spending and one for saving. This works well with the budgeting idea as they see each piggy bank serving its purpose.

SPEND AS WELL AS SAVE

Spending is an important part of the process, so don't make children save endlessly without reward. In a child's life the reward must arrive more quickly, before they become bored with the process.

Make money fun through play, whether it is via games (shopping in the lounge room, catching a dining-chair bus etc), a website, an app or a board game such as Monopoly. It is widely believed, in fact, that Monopoly is a version of an earlier board game called The Landlord's Game. Said to be the brainchild of Quaker and social activist Elizabeth Magie, The Landlord's Game was created in the early 1900s in order to demonstrate to its players the fact that rent and taxes made landlords rich and tenants poor. It's as good a lesson now as it was then.

Finally, ensure the children have their own bank accounts. Discuss the statements with them each time they arrive in the mail, praising them for saving and imagining what they could buy with their wealth. Everything about childhood should be enjoyable, including the thrill of saving.

Quick Checklist:

- Speak to your children about how you earn money.
- Work with them to develop a simple budget to save for something they want.
- Figure out a pocket money system so they can earn and save their own money.
- Spend some of the money they have saved on something they want, but when they're choosing be sure to differentiate between wants and needs.
- Ensure children have their own bank accounts.

Rise as the dollar falls

The Australian dollar has done its fair share of bouncing around during the last five to ten years, and its current trend is down. What does this mean for our investments? And what can it teach us about risk?

A recent research study comparing the strength of the Australian dollar with the prices Australian businesses charge for their goods and services revealed a fascinating pattern caused by the dollar's turbulent travels over the last few years.

The *Business Expectations Survey* released by Dun & Bradstreet in January 2015 shows that our weakening currency appears to be contributing to higher input costs for Australian businesses. These higher costs are being reflected in the prices their customers are paying. So, as the Australian dollar drops against the US dollar, the majority of Australian firms expect to increase their prices.

This indicates potential future issues for firms that compete locally with operators from other territories. If Australian businesses have to lift their prices thanks to a falling dollar, it makes them less competitive in the market.

DOLLAR'S DROP IMPACTS BUSINESS

Such pressure most strongly affects those businesses that rely on imported goods and services. In the *Business Expectations Survey*, a not-inconsiderable 21% of businesses surveyed said the Australian dollar's value is the issue that will influence their operations the most, while 23% expected a positive impact from the dollar's current levels and 25% expected a negative impact.

Pricing of goods and services is just one of many effects of the changing value of the Australian dollar in an increasingly global business environment. Another was identified in an article from The Australian newspaper in early January, titled 'Australian dollar fall helps offset plunging commodity prices'. The tumbling Australian dollar was actually timely for the domestic economy, the article claimed, as it partly made up for the steep downturn in commodity prices (iron ore and crude oil prices, the article says, fell by 50% last year and coal fell by 28%) and helped to mitigate a potential spike in inflation.

Interestingly, the dollar's rise and fall does not only flag specific issues that individual investors need to watch out for in terms of asset classes and industries, it also brings into focus questions about risk and return. After all, if a high dollar offers a certain industry, category or asset class less perceived risk, then surely a low dollar has the opposite effect.

HOW TO ANALYSE YOUR RISK PROFILE

Even before considering the changes in risk patterns caused by a fluctuating dollar, investors should develop a detailed understanding of their own risk profile. This is not a set-and-forget exercise that only needs to be carried out once. Risk appetites and profiles constantly change throughout an individual's different life stages.

So what questions need to be asked to come to an understanding of your own risk profile?

First of all, in finding a definitive answer investors should seek professional advice from their financial adviser. But in order to develop a better understanding on your own, begin with questions around stage of life.

How many years do you have left in the market before retirement, or are you retired already? Do you have time to ride out the various ups and downs of the money markets? Are you investing for the short or long term?

Stage of life questions will also answer other risk-based queries around whether you have dependents, what types of expenses you see in your future (school fees, international travel etc), what income you make now and what your future earning potential may be, and whether you foresee any breaks in your career.

WHAT IS YOUR INVESTING EXPERIENCE?

The types and levels of investing you have done before, the investments you saw your parents become involved with, and the results of your past investments all influence your level of comfort with particular asset classes and levels of risk.

For instance, if you dove headlong into US shares a month before the GFC struck, then you may understandably be a little shy about dipping your toe into that pool again. And if your parents invested successfully in property then you are likely to have greater comfort with property as a result.

Today's investment decisions should not be driven by yesterday's results or experiences, but many of the world's most respected financial experts, including Warren Buffett and Peter Lynch, argue that it pays to invest in what you know.

The trick in analysing your risk profile is to recognise which past experiences are pertinent and useful, and which are simply emotional memories that deserve to be erased or reset.

ARE YOU COMFORTABLE ON A ROLLER COASTER?

One of the great benefits of property ownership is that it is very difficult to check the value of a piece of real estate on a daily basis. If you could, you might find that you are regularly surprised and concerned.

How comfortable are you with the ups and downs that are so visible on the share market, for instance? Are you willing to witness your investment shrinking in value over the short term in exchange for the potential to make greater gains over the long term? Or would you prefer to always see growth, albeit at a possibly slower rate?

There is no right or wrong when it comes to levels of risk aversion. There is no better or worse option. There is only your unique and personal take based on your current situation.

WHAT ARE YOUR GOALS?

Finally, what are your retirement goals, or your other reasons for investing? Are you hoping for a retirement that is currently beyond your means, or something more simple? How much will you need on an annual basis to make your desired lifestyle a reality?

And don't forget shorter-term plans and expenses, whether it be a house, an overseas trip, a car or private school education for the children. They all have an effect on your choice of investment and the levels of risk that come with it.

WHAT HAS IT ALL GOT TO DO WITH THE AUSTRALIAN DOLLAR?

The rise or fall of the Australian dollar, or its rate of movement in general, puts various investment options into new categories in terms of risk and return (see breakout box). It is important that these changes are recognised and understood by individual investors so they can ensure their portfolio is following its intended strategic path.

With such dramatic changes in the value of the dollar in recent months, and as you move into new life stages and therefore change risk profiles, consider discussing with your financial planner/ personal financial adviser whether you need to re-balance your portfolio.

Winners and losers

Most businesses can find both positives and negatives from the Australian dollar falling against foreign currencies. Banks, for instance, may benefit when they raise money from international markets but might also suffer thanks to a lower number of offshore investors. Manufacturers that export product can sell at a more competitive rate but may face higher costs for the resources required in the production process.

Here is some food for thought:

- Potential to benefit from a low Australian dollar
- US shares that are not hedged back to the Australian dollar
- Australian businesses with major US operations
- Exporters
- General retailers
- Tourism
- Agriculture export
- Resources
- Universities and other educational institutions that attract international student interest

Potential to benefit from a high Australian dollar

- Importers
- Retailers specialising in imported goods
- Retailers specialising in white goods and electronics
- Businesses and assets that generate Australian domestic income only
- Australian real estate firms
- Property investors (low interest rates)

How and why to diversify

Knowing exactly what needs to be considered before getting your asset allocation right inside (or outside!) an SMSF is not just a smart move in terms of obeying strict SMSF regulations. It is also a fantastic exercise in developing a broader investment discipline.

No matter your age, gender, risk profile, objective or income, for every investor there is a single golden rule – diversify. It is a truth universally acknowledged that a diversified investment portfolio is likely a safer one as it will potentially weather storms in a more balanced fashion than a portfolio that is heavy with one specific asset or asset class.

Members of self-managed super funds (SMSFs) are required by regulation to consider the diversification of their Fund's portfolio. The law insists that SMSF members put in place an investment strategy that considers diversification (among other factors) and review it on a regular basis. Then members must ensure their Fund's asset mix matches their investment strategy document.

But what should this consideration involve before such¬ a document is written? How does an SMSF member, or anybody with an interest in the responsible and reasoned diversification of their portfolio, ensure they are asking the right questions of their own risk appetites and resulting asset class percentages?

FIGURE OUT YOUR PERFECT ASSET MIX

Each SMSF member or investor will have different reasons for diversifying. For some it will be for greater chances of balancing risk and return in turbulent markets. For others it will be to take advantage of opportunities in various geographical locations. Some will diversify because of the varying time requirements of particular asset classes, holding some asset classes for longer than others and constantly re-balancing.

How do you figure out your own risk profile? Seek professional assistance for an in-depth analysis, but it has a great deal to do with your stage of life, and therefore how much time you can afford to wait out the various ups and downs of the market. It also involves other considerations. How much do you have to invest and how regularly? How do you feel about seeing your portfolio fluctuating in value? What are your individual tax circumstances?

ESSENTIAL SMSF CONSIDERATIONS

Regulations specific to SMSFs outline the fact that you must show consideration to five essential points before writing your investment strategy. These are:

1. Consider the risk and likely return from the fund's investments taking into account the member's needs and circumstances
2. Consider the solvency of your fund. In other words, can it afford to pay benefits to members when required, and pay its own bills such as auditing, accounting and legal?
3. Analyse the role and level of diversification in your fund. What is its purpose? What are the risks if there is inadequate diversification?
4. Analyse the level of liquidity of the fund's assets, and the role and purpose of this liquidity.
5. Is there insurance for members within the fund? You must be able to prove that you have at least considered whether the fund should hold insurance for SMSF members.

WHAT ASSET CLASSES CAN I CONSIDER?

In the world of Australian SMSFs, cash and shares are the front runners, with both typically making up over 30% each of an average fund's total assets.[1] Property, including commercial and residential, takes third place with an average of less than 20% of each fund's value.

There are several other asset classes that can be considered for ownership within SMSFs, and it is a good idea to seek professional advice on exactly what is and is not allowed. Listed property trusts, foreign property and managed funds tend to be accepted. Art works, precious metals and vintage cars etc may also be allowed, but professional advice should be sought before purchase. More complicated financial vehicles such as warrants and derivatives also require special advice.

Interestingly, in certain situations if you currently own your business's commercial property then the SMSF can buy the property from you under a Limited Recourse Borrowing Arrangement at market value, then you rent it back from the fund. This may mean lower tax on rental income and eventual capital gains tax on sale, compared with holding the property outside super.

DON'T FALL FOUL OF LAWS

There are many very specific rules and regulations for assets held within an SMSF. For instance, if an investment benefits you at all now, instead of after retirement, then it is unlikely to be allowed in your SMSF. Please seek professional advice as penalties can be serious. Don't just assume you can make your holiday house a part of your SMSF.

Examples where you may breach superannuation investment rules include:

- Expensive artworks that are held as an investment inside your SMSF cannot be kept hanging on your walls at home but instead must be stored in a reputable art storage facility and must also be insured.
- Staying in an investment property, or allowing friends or relatives to stay in the property, is also a big no-no if that property is held within an SMSF.
- Market value must be paid for everything held within an SMSF, meaning all transactions must occur at arm's length. You can't make a purchase from a family member at mate's rates. If it is difficult to avoid such a clash, please seek professional advice.

1 http://www.superguide.com.au/comparing-super-funds/smsf-investment-diy-super-asset-types

Facts & figures

According to a report titled 'Usage of Payments Systems' by the Australian Bankers' Association

In the last **5 years**

Cheques **Halved**

Eftpos **Doubled**

A research series by Roy Morgan

shows that, as of **August 2014**, customer satisfaction with their banks is at a record level of

82.3%

Lows were recorded during **2001** when the figure dipped below

60%[2]

81% of Australians have a home broadband connection

5.5 million Australians regularly access the web via a tablet rather than a desktop or laptop computer[3]

77% of **Australian internet users** aged 18 and over use the web for **banking or paying bills** says the ACMA Communications Report 2013/14, compared to **61%** in the UK

69% use the web for **social networking**

64% for **buying and selling** **23%** for **gaming**[3]

$246 billion

the estimated revenue from **online sales of goods and services** during 2012/13 (ACMA Communications Report 2013/14)

According to the Centre of Excellence in **Population Ageing Research**

400,000 Australians are **aged over 85**

28,000 Australians are **aged over 95**

3,000 Australians are **100 or over**[4]

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2 Roy Morgan Research Consumer Banking Satisfaction Report

3 The Australian Communications and Media Authority (ACMA) Communications Report 2013/14.

4 ARC Centre of Excellence in Population Ageing Research.

CONTACT YOUR COUNT ADVISER AT:

Looking after your financial life