fluid financial planning
SECURING YOUR FUTURE

Autumn 2014

The economic outlook for Australia for the coming year is very much a mixed bag. Our property prices and our share prices remain high. Recently share prices moved up when key company earnings in particular BHP Billiton's higher than expected interim profit were unveiled. At the same time Qantas has announced job losses of 5000 and the last remaining car manufacturer Toyota announced plans to stop manufacturing in Australia. It is expected future job losses in the auto industry will involve thousands of both white collar and blue collar workers and uncertainty surrounds the flow on effects to the Australian auto parts industry.

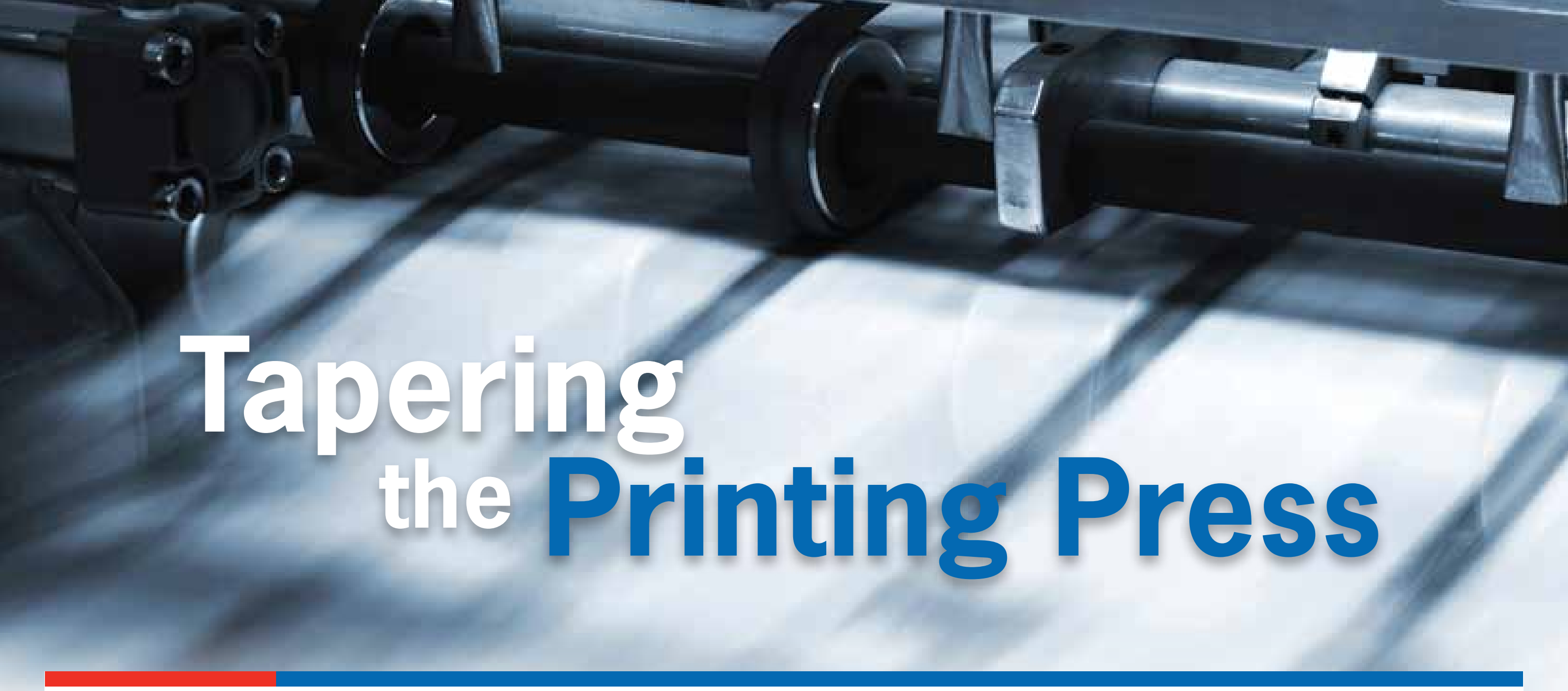
The broader picture however is still basically positive. The Reserve Bank has forecast Australia's economy to grow by 2.75% in 2013-14 and by more than 3% in the following 2-3 years. However higher unemployment and the slowest wage growth in decades suggest that less of the benefits of our prosperity now flow through to workers.

The picture overseas is just as, if not, more confused than in Australia. The issue which will have the most impact is what the United States Federal Reserve decides to do with its ongoing economic stimulus program. The uncertainty surrounding the policy changes in the United States has lead the IMF to urge the major economies to act cautiously in response to increasing financial volatility in emerging markets along with the onset of deflation in Europe.

Fluid Financial

Suite 4a, Level 1, 5 Ridge St
North Sydney NSW 2060

P 02 9922 4448
F 02 8072 1386
E peter@fluidfinancialplanning.com.au
W www.fluidfinancialplanning.com.au



Tapering the Printing Press

A funny thing happened while everyone was winding down for the Christmas break. The US Federal Reserve began winding back the biggest economic stimulus program in history. This news may have failed to excite Australians in barbecue mode, but the effects were soon felt from Boston to Buenos Aires and Brisbane.

Federal Reserve chairman, Ben Bernanke, announced in December the US$85 billion a month stimulus program known as quantitative easing would be wound back – or tapered – by US$10 billion a month. If all goes to plan it may be shelved completely by the end of 2014. Ben Bernanke has since been replaced by Janet Yellen who helped develop the strategy and is unlikely to change course.

What is quantitative easing

Quantitative easing refers to the US central bank's policy of "printing money"* to buy government bonds and mortgage-backed securities. The aim was to pump money into the moribund economy and stimulate growth in the wake of the global financial crisis (GFC). The effect was to keep interest rates low while depressing the US dollar to make US exports more attractive.

The first round of quantitative easing began in December 2008 and finished in June 2010. A second round (QEII) followed from November 2010 to June 2011 while the third and final round began in September 2012. Each injection of stimulus inflated the Australian dollar against the greenback.

Normally central banks use interest rates as their primary tool to manipulate the economy. Cutting rates tends to promote economic growth by encouraging households and businesses to borrow; lifting rates subdues an over-heated economy.

If rates are cut too aggressively there is a risk prices of goods and services will rise sharply, causing a spike in inflation. But after the GFC, Americans were so focused on reducing debt they could not be tempted to borrow, even when rates were cut to zero.

Hyperinflation in Germany

Critics of a stimulus strategy based on money printing argue that it results in inflation or, in extreme cases, hyperinflation.

The best-known example of hyperinflation occurred in Germany between the wars. When it lost World War I, the German government was ordered to pay crippling war reparations, so it printed more money. Industrial and farm production collapsed, leading to a shortage of goods. And because there was so much cash in circulation and so few goods, prices spiralled out of control.

In December 1922 one US dollar was worth 2,000 marks; by August 1923 it stood at more than one million marks. Not surprisingly, many Germans preferred to be paid in bread and sausages.

After the taper

Although the worst fears about quantitative easing were unfounded, it is difficult to say what would have happened if it had not been introduced. What is not in doubt is the Federal Reserve would not be tapering if it did not believe the US economy was on the mend.

Ironically, the removal of monetary stimulus in the US should stimulate growth elsewhere, including Australia, although not without some hiccups along the way. When the taper was announced, investors fled emerging nations for the perceived safety of the United States. South Africa, Turkey, Brazil and India were forced to raise interest rates to support their currencies, while Argentina devalued its peso.

The news is more positive for Australia. As US interest rates and the dollar gradually rise to more normal levels, the Aussie dollar should continue to fall. This will make our exports more competitive and strengthen the non-mining sectors of our economy.

If you would like to discuss any of these issues in light of your investments, don't hesitate to contact us.

* ie injecting a specific quantity of funds into the financial system each month

SUPER CHOICES

Australians merrily take out car insurance without a second thought but are more reluctant when it comes to protecting their family and lifestyle. It's not surprising then, that we are seriously underinsured.

So, what are the different types of insurance that should be considered?

- Life insurance – provides a lump sum to your family or nominated beneficiaries should you die.
- Total and permanent disablement insurance (TPD) – provides a lump sum if you are permanently unable to work again.
- Trauma insurance – provides a lump sum upon diagnosis of a critical illness such as cancer, stroke or heart attack.
- Income protection insurance – provides ongoing income (up to 85 per cent of your employment related income, including superannuation) if you can't work due to illness or injury.

Are you underinsured?

It's not uncommon to underestimate the amount of money families require when insurance payouts become relevant. According to a recent report by actuaries Rice Warner, Australian families claiming a life insurance payout will on average only receive 42 per cent of the funds they require. The figures are even lower for TPD and Income protection cover. Can you believe existing TPD cover is only sufficient for about 14 per cent of the population and Income protection is marginally higher at 16 per cent.[1]

What are the odds

It's easy to be complacent when things are going well but it is important to ensure you are protected for the future.

– There is more than a 60% chance of being disabled for more than one month during your working life and a 1 in 3 chance of being disabled for more than 3 months.[2]

– There are 60,000 strokes each year (an average of one every 10 minutes).[3]

– Around 108,000 new cases of cancer are diagnosed each year, (more than the capacity of the MCG) and there are 109 cancer related deaths every day.[4]

Using superannuation to pay

In reality, insurance cover can be more affordable than you think, especially as you may be able to pay for some of the cover through your superannuation fund. This means cash flow concerns shouldn't be a reason to remain underinsured.

The way you fund your insurance can be complex, with many issues to consider. For example, premiums on income protection insurance are tax deductible. So if you are on a high marginal tax rate, you might be better off holding this type of insurance outside your super.

While TPD is often held inside superannuation, specific advice must be sought regarding whether you choose "any" or "own" occupation.

Although a lump sum will always be paid if you successfully make a claim, being able to access it prior to age 55 can be an issue.

Providing protection for your family is the cornerstone of a wealth creation plan. Implementing the right risk strategy is paramount.

CASE STUDY

Andrew, 40, is married with a young family, a $700,000 mortgage and earning $120,000 a year. He is well aware that if something were to happen to him, his wife Laura would face serious financial problems, so he sought financial advice. He had all sorts of questions. For instance, should he choose "own" or "any" occupation in his TPD policy, how would he access an insurance payout if it were in super and what kind of impact would having his insurance in super have on his overall savings?

With school fees, a mortgage and generally tight finances, Andrew could see it would suit him to split the policies with half in super and half outside. That way he could enjoy some added cash flow while still knowing his family would be covered. So he took life and TPD ("any" occupation) insurance with cover of $1.2 million apiece through his super fund paying level premiums and, trauma ($250,000) and income protection ($8000 a month) insurance outside the super environment, paying stepped premiums. And by bundling his products he could also enjoy lower premiums.

Please note: This case study is illustrative and the information contained in

1 Rice Warner Media Release 02/12/13 'Proper adequacy in life insurance means looking beyond rising premiums'

2 "Interim Report of the Disability Committee," Institute of Actuaries of Australia 2000

3 Australia's Health 2010, Australian Institute of Health and Welfare, December 2010

4 Cancer in Australia, an overview, Australian Institute of Health and Welfare, December 2010

Date-onomics

... AN ECONOMIST'S VIEW OF THE DATING GAME

If online dating prospects sound too good to be true, then just like any other investment, they probably are.

The parallels between online dating and investing go well beyond the too-good-to-be-true maxim, as was discovered by Stanford University professor and economist Paul Oyer when he found himself in the online dating scene after 20 years' marriage.

The more dates he went on, the more he recognised similar principles at play in the two arenas which led to his book Everything I Ever Needed to Know About Economics I learned from Online Dating.

Given that 51 per cent of Australians have looked for love online, one could conclude that many know a lot more about investing and the economy than they realise.

Time in not "timing"

When it comes to investing, it is argued that time in the market brings better results than trying to time your entry and exit. The longer you are in the market, the more you smooth out the cyclical movements, minimising the impact of sudden peaks and troughs. The argument goes that if you missed the best 10 days on the market over the last 10 years your returns could fall into negative territory.

In much the same way, the longer you persevere with the online dating game, the more likely you are to finally find Mr or Ms Right. Patience, both in love and investment, is a virtue.

Online romances are akin to panning for gold. You have to sift through the sediment to find the nuggets and on occasion even they will be fool's gold! All that can take time.

Diversification

One of the golden rules of investment is to diversify. That way, when one asset class is suffering a down cycle, your other investments can pick up the slack.

Similarly, don't just focus on one dating site, but upload your profile to several to spread your chances of finding a partner by playing to a larger audience.

Thick markets

If you invest in a company that only has a small number of shareholders, then you will be faced with a thin market that can prove problematic when you want to sell. Thin markets also can lead to higher price volatility. It's much the same when it comes to love - thick markets are the better option as the more people who populate each dating site, the greater your chances of finding the perfect match.

Too good to be true

It's tempting for everybody to post a glowing profile on a website. After all, you hardly want to highlight your negative attributes. But if you will fudge the truth, then so will others. As a result it's important to execute due diligence on any potential partner.

It's much the same with hearing a good tip about an unknown stock. You are hardly going to sink your hard-earned cash into an investment without checking with us about the validity of the tip.

Painting a good picture is what Oyer refers to as cheap talk and it is prevalent both in the world of internet dating and across society and the economy in general. Everybody expects it to happen. In fact, if you were to be honest and admit to carrying a few pounds, then potential partners would assume you were seriously overweight as they expect you to be understating your negatives.

Similarly in the world of investment you may see brokers who underwrite an IPO* talk up the stock more than an independent broker. But, as with the dating sites, the audience expects this.

Applying good business principles to the online dating game can go a long way to finding your Mr or Mrs Right. At least that is what Professor Oyer has found – and it worked for him!

* Initial Public Offering