Your Wealth Bulletin

July 2007

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Hi,

The end of the financial year has now passed. The usual frantic rush for tax planning was exascerbated this year with the changes to superannuation.

As we have commented upon over the last few months, there really isn't too much to worry about for those that aren't retiring in the next 1-2 years or who don't have a 'lumpy asset' such as commercial property that needs to be transferred across.

In fact, if you've got a lazy $1.8 million needing a home in superannuation, then it can still be transferred over to your super fund, it will simply take 3 years and 1 day to do so.

Your Wealth Bulletin this month discusses:-

- Property within Superannuation
- Historical Equity Premia

For our Asgard investors, please note that many funds are now 'ex-dividend' over the past 24 hours. Therefore, your portfolio value may drop until the dividends are distributed, which is expected to be the end of July.

Asgard advises that the drop this year has been higher than usual. Please note that this is only temporary until the dividends are placed into your portfolio. Therefore, the fall in value does not represent your funds actually dropping in value.

Property in Super

The times are a changin'

Breaking news this week has been that the Federal Government has tabled legislation that will allow super funds to invest into instalment warrants by introducing a new exemption to the prohibition of borrowing.

There are a few rules for which the Trustees must adhere to, but in summary, common structures such as instalment warrants for shares are fine.

Typically, these instalment warrants are similar to the Telstra 3 type share, whereby you pay some for the first tranche, then another amount for the 2nd tranche.

The financier, typically a bank, will charge interest on the 2nd tranche amount until it's paid. The only recourse the investor (in this case the SMSF) has will be the underlying asset itself, nothing more.

These warrants will typically allow 50-90% leverage and have been available to investors for sometime in the ASX marketplace.

We now expect to see a proliferation of similar structured finance arrangements for other assets. There have already been two brought to market, the first is for residential property, the second for commercial property.

Both facilities offer SMSF's the opportunity to buy into property with as little as 20-30% of the property value. They offer the rest of the finance on a non-recourse basis. So generally, if the SMSF defaults on the loan, then the financier may only sell the asset and if it's worth less than their finance amount, they typically cannot pursue the SMSF for the outstanding amount.

This means that the interest rate may be slightly higher than residential rates, eg. approx. 9%. Nevertheless, the opportunity it brings for superannuation funds to gain access to an asset class with substantial leverage offers an interesting opportunity for investors.

Furthermore, for those with commercial properties within their SMSF, particularly those that have home mortgage debts, there is an opportunity whereby you may be able to access equity from the SMSF commercial property and extinguish your non-deductible home mortgage debt.

If you would like to know more about these opportunities, or just SMSF strategies in general, please feel welcome to email or call me directly on 9525 0777.

Historical Equity Premia

What markets do you for you....

Last week, we were very fortunate to attend an educational conference in Sydney with leading academic professors in attendance. These included Professor George Constantinides of Chicago University and Noble Prize winner, Professor Myron Scholes.

They presented some very interesting academic research and gave advisers an insight into their current work and where they are heading.

Professor Constantinides took the time to review the historical premium of equity markets. Without going into the complexities of the research, it was interesting to see the very long term realised returns that are available to investors that have a philosophy of 'capturing market returns' rather than trying to outperform the market.

From 1871 to 2006, a $1 US investment into One Year Bonds would result in a balance of $556.24. After inflation is taken into account, this is equal to $4.02. So for all that time, you may be able to buy a can of Coke and a Mars bar.

However, from 1871 to 2006, a $1 US investment into the S&P index would result in $123,224. After inflation, it is equivalent to $7,637.

What this means is that there is obviously a premium available for investors to invest in the stockmarket rather than bonds.

For investors, while you may not be investing for 135 years, it does highlight the fact that while bonds may typically be considered 'low risk', they are in fact 'high risk' when inflation is taken into account as you are struggling to outpace inflation over the long term.

The Professor then went on to examine the realised annual equity premium from 1926 to 2006. The sample mean S&P return for the US was 11.93%. The sample mean interest rate of one year bonds was 4.61%.

Therefore, the historical equity premium above that of bonds is 7.32% per annum.

In essence, this 7.32% annualised return is the investors reward for taking the risk of investment into the US equity market rather than placing their money into bonds.

For Australia, the 1900 to 2006, the adjusted mean equity premium for Australia was 8.1%. A very high figure when compared to one year bond mean rates of 0.8 and emphasises the importance of having equities in your portfolio to maximise potential returns.

The study also highlights the mean return of approximately 12% per annum over the past 80 years from the US S&P index.

For investors, this represents a doubling of investment capital every 6 years and further illustrates our philosophy of utilising the maximum potential of investors capital to expose themselves to the market rather than stockpicking or market timing so as to attempt to outperform the market.

If you have any queries about this month's newsletter or would like to discuss your financial situation in more detail, please feel free to email or call our office on (02) 9525-0777. If you would like to forward this email to a friend, click on the forward email link below.

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