Your Wealth Bulletin

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Hi,

Welcome to the March issue of your wealth bulletin.

Quote of the month

To pursue your passion and never achieve it is far better than never having a passion and living with regret forever*(Keith Abraham)*

Federal Government Second Stimulus Package

What's in it for me?

The Federal Government second stimulus package that has gone through legislation comprised of the following elements:

- one-off cash payments for eligible families, individual workers, students, drought affected farmers and others
- a temporary investment tax break for small and general businesses buying eligible assets
- free ceiling insulation (capped at $1,600 per house over 3 years) for around 2.7 million Australian homes - available from 1 July 2009 until 31 December 2011 to all Australian owner occupiers who currently don't have ceiling insulation uninsulated owner occupied properties
- building or upgrading a building in every one of Australia's 9,540 schools
- building more than 20,000 new social and defence homes
- significant increased funding for local community infrastructure and local road projects

One-off cash bonuses The bonuses included:

- Tax bonus for working Australians
- Single income family bonus
- Farmers hardship bonus
- Back to school bonus

- Training and learning bonus

Bonus payments will not be taxable and will not be counted as income for social security means test purposes.

For the bonus tax payment, your taxable income has to be under $100,000 in the 2007-2008 financial year to qualify. If under $80,000 income, then a $900 bonus payment will be provided. From $80-90,000 then a $600 bonus payment applies while for $90,000 to $100,000 a $250 payment applies.

On 3 February 2009 the Government announced small business and general business tax breaks. However, legislation has not yet been introduced to give effect to this measure.

Small business tax break Small businesses will be eligible for an additional 30% bonus tax deduction for eligible assets. The assets must:

- cost $1,000 or more;
- be acquired or start to hold under a contract or start to construct between 13 December 2008 and 30 June 2009
- be installed ready for use by 30 June 2010.

In addition, a small business can claim a 10% bonus tax deduction on eligible assets that are acquired, started to be held under a contract, or construction is commenced during the period from 1 July 2009 to 31 December 2009. The asset must be and installed ready for use by 31 December 2010.

General business tax break Businesses that do not qualify as small businesses will be able to claim bonus deductions for eligible assets if the assets costing $10,000 or more and meet the other criteria outlined above.

Example - 30% bonus deduction A small business purchases a commercial wood fire oven for $15,000 on 1 February 2009. It is installed and ready for use on 20 March 2009. The business can claim a bonus tax deduction of $4,500 (30%) for the financial year 2008-09

It should be noted that if the installation of the oven was delayed and the oven was installed and ready for use on say 20 July 2009, the business will be able to claim the bonus tax deduction in the 2009-10 financial year, i.e. the deduction is available in the financial year it is first held ready for use.

Expected Return In A Bad Economy

Comments from Professors Fama & French

Finding some directions or opinion on where the markets are headed in times like these is always easy. It seems everywhere you look, a self- proclaimed expert will provide you with their exclusive 'tip' on where we will be in 12 months time.

While it makes for entertaining reading, we typically adhere to academic philosophy in that it's impossible to predict what markets are going to do, and when they are going to do it. They are totally random.

The leading academics for this area of economic study is Professors Eugene Fama and Ken French.

If you google their names, or review academic archives on University libraries, you'll probably find that they have one, if not the, most cited references in the world.

So when these guys offer an opinion of markets, it's generally worth paying attention. Which brings me to their recent column, Expected Returns In A Bad Economy from the 11th March.

Their thoughts on market returns were as follows:

"The market has declined sharply in response to rough times and forecasts of future rough times. The decline in market prices combines two effects: (i) lower current and expected future profits, and (ii) higher discount rates for the expected future profits.

The discount rate, in turn, has increased because uncertainty about future profits (in other words, risk) has increased and, apparently, because investors have become more risk averse. Higher discount rates for expected profits translate into higher expected stock returns.

In short, the two of us believe that the expected return on stocks is currently high.

But beware: the high expected return is compensation for the risks associated with different possible outcomes. If the quite pessimistic assessments of future economic performance built into current market prices turn out to be right (which is our best single guess), realized returns will be high.

In other words, we will get the currently high expected return if the market's pessimistic expectations of future economic performance are realized.

On the positive side, there is a substantial chance that the current assessments of future economic performance built into market prices turn out to be too pessimistic. If so, realized returns will be even higher than expected.

But there is also a substantial chance that the current quite pessimistic assessments of economic performance built into market prices turn out to be too optimistic. In that case realized returns will be low, perhaps quite low.

This is always the general nature of the risks in stock market investing. The story is more poignant at the moment because risk is so high."

This is an interesting commentary. My simplest interpretation is that we don't know what will happen short term, but the risk premium in equities over cash is quite high. For the risk premium to return to its historical average, then significant returns must be experienced at some point in time to return us to the average.

Expected Returns In A Bad Economy

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