Newsletter: Spring 2007

STUART + CARLYON

Financial advisers for your lifetime goals

A long beautiful sunset

One of the interesting sessions we attended at a recent Portfolio Construction conference in Sydney concerned longevity. David Williams, an expert on longevity pointed out how in NZ, the average life expectancy for a new born male is age 80 and for a female: 84 years. But if you get past the risks of infancy and teenage driving, and you reach age 50 then you are more likely to live much longer: 92 for males and 96 for females.

David then made another unexpected point: clients of financial advisers will probably live even longer than even this average. It's not that we have a secret anti ageing potion, but clients who wish to get financially sorted also tend to invest in their health. Expect a telegram from the Queen, we say.

But don't be surprised if we ask you: "what do you think your life expectancy is?" At age 50 you are basically only half way. Will your finances make the distance? In fact a session considered changing retirement attitudes and behaviours and asked this same question.

Beth Segers from US-based Putnam Investments shared research findings about retirees. They found that 25 per cent of "retirees" are not retired at all and have gone back to work. Meanwhile 50 per cent are helping their ageing parents either financially or physically. About a third are paying their children's rent or providing their accommodation or living expenses. The most sobering statistic was that 60 per cent of US people over age 65 still have a mortgage on their home and on average this will be paid off by age 77.

In this regard how we look after our own health, and how we plan our working lives becomes crucial. The NZ 2006 Census showed that 45% of men aged 65 to 69 were in fulltime or part-time work and 20% of men aged 70 to 74. If we opt for working longer, we would want work to be satisfying and engaging and at our own pace; not get too burnt out too fast. We may choose to have different careers or work engagements.

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How we plan our finances becomes more relevant if we are living longer. Allocation of our current income becomes more of an issue: to provide for the future but not at the expense of enjoying life today. Appropriate investment strategies have to be adopted to ensure the purchasing power of our savings is maintained. The ways we create wealth may change over time. Our views on risk may need modifying; should we take on more risk to get better returns? Are we too underinsured? Should income protection insurance be extended beyond age 60 or 65?

Everyone's situation will be different but we believe in tailored financial planning for the future in order to match an individual's goals with the most appropriate strategies – to try to get it as accurate as possible so you don't risk not having enough down the track.

Support Plunket

Our sofas were never the same again. Do you remember the campaign by ANZ where we hunted for 5 cent pieces before these were withdrawn from circulation? Kiwis scrounged some 14 million five cent pieces or $700,000 for Plunket.

This year ANZ are behind the Plunket Appeal on 13-21 October. And they have an offer: open an ANZ Youth Account in October and set up a regular monthly automatic payment of at least $25 for your child, and they'll give you a book about how to teach your child about money. Guess which book: Start Talking Cents: Teach Your Children & Teens To Manage Money by Susanna Stuart.

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Housing market

High mortgage interest rates are finally kicking-in. The number of houses sold hit a six year low in September and prices are softening. This is not so bad if you are selling your house and buying another to live in, but if you are buying for investment then property may not be the one-way bet that it appeared to be a couple of years ago.

> "For home owners, average salaries have not kept pace with the huge mortgages required to buy a home in Auckland"

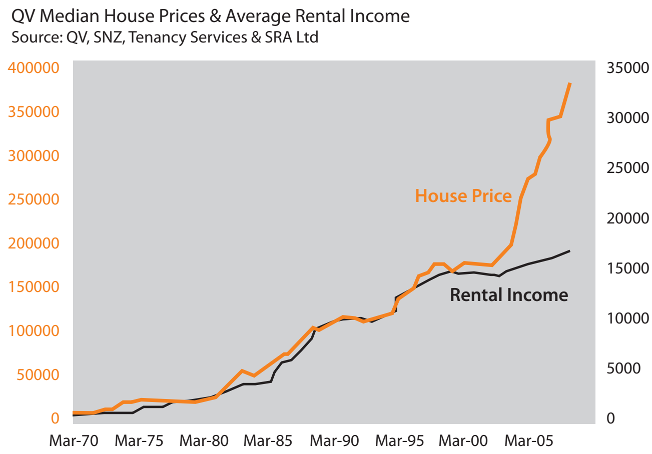
Don't forget, the big driver behind the housing market over the past 10 years has been immigration, but recent figures suggest that migrant numbers have slowed significantly.

At Stuart + Carlyon, we believe in looking at the future prospects for investments including rental property. Just because house prices have doubled in the past six years, doesn't mean you can expect the same again. Right now the economic fundamentals for both owner-occupiers and investors are severely out of kilter.

For home owners, average salaries have not kept pace with the huge mortgages required to buy a home in Auckland – so even two income families are struggling. Either salaries must double over the next few years (unlikely) or house prices need to stop rising for a while.

For landlords, rents have barely increased and thus rental yields have almost halved. Remember when landlords used to buy houses for the income they generated? Right through the 1990s, purchase yields were over 8% and with the ensuing capital gains, significant wealth has been accumulated. But with house prices doubling and rental yields now at 4% we should expect that house prices must level off for some time to restore equilibrium.

NZ House Price Appreciation



ING September 2007 Roadshow

The high mortgage interest costs mean residential rental property sums no longer compute compared to alternatives. For example, bank deposits and listed property trusts at 8.5% are more appealing than 4% rental returns with little prospect of immediate capital gain.

With Auckland now ranking the 5th most expensive city in the world to buy a house, we suggest caution for investors considering the residential market.

Credit Squeeze – and risk exposure

The timing was unfortunate. While we were at the Sydney conference calmly listening to the session on the exponential growth of the Indian economy we were aware that outside the lecture hall a "correction" was happening. The Australian share market had plunged, and the Kiwi dollar had fallen out of bed. Next day the front page headlines of the Sydney Morning Herald summed it all up: "A correction we had to have" and "Seismic shift hits home".

Low interest credit has been so freely available in much of the world and some assets were artificially priced - due to the staggering take-over deals involving private equity and huge amounts of debt. Some US investors who had misunderstood risk decided to get out.

> "All credit involves risk and therefore there is always a possibility of loss."

In New Zealand, finance company, Bridgecorp, is testimony to the bad risk/return equations on offer and negative sentiment has hit the whole finance company sector.

All credit involves risk and therefore there is always a possibility of loss. That's why we rely not only on our experience (Bridgecorp's Petricevic had a 20 year history of poor risk) but also, always, on independent assessment from credit rating agencies. We continue to recommend nothing below A rated debt securities issued by substantial corporations.

An A rating simply means the average risk of default is lower. We have never used unrated finance companies not only because of higher risk but also the complete lack of liquidity. Corporate and bank bonds we use are listed, have higher disclosure rules, are valued daily and able to be sold at any time. Although the market value may fluctuate, investors who hold to maturity receive their purchase interest rate but if they need money early they can sell.

Our current strategy

Credit concerns in the UK and US will continue to cause global share market and currency volatility. Caution is required. However, with growth in the rest of the world continuing at a faster pace than in NZ, clients with new money should buy offshore shares on any dips. Any strength in the NZ dollar is a bonus. Current portfolios have made good returns from shares and we will re-weight as necessary into NZ cash and bonds to capture gains and reduce risk.