Newsletter: Autumn 2007

STUART + CARLYON

Financial advisers for your lifetime goals

How money keeps the social fabric intact.

Ah romance! The romantic view is that marriages and family life will survive anything – for richer or poorer.

Without taking anything away from the notion that family bonds are chiefly driven by a sense of love and commitment a Ministry of Social Development study, presented in early April at a Social Policy Conference in Wellington, showed that a healthy economy is easing relationship strains.

Our own experience as advisers backs up these observations. Over the years we've encountered many families who have been under really big emotional pressures – and these have spilled over from financial problems, many of which were preventable.

In some cases the pressure has arisen because some financial basics were simply overlooked that left the couple open to life's risks. In other cases big rash financial decisions have led to marriage strain. It would be a resilient marriage that survives the debacle of borrowing to the hilt to buy what turns out to be a leaky home.

Our advice: make sure simple things like life and income protection insurance are in place. Always do your homework before making big decisions. Parents should also impart financial education to help their children develop sound money skills.

But money doesn't just help glue families together. The economy affects the social fabric.

Joakim Palme, a keynote speaker at the MSD conference has been the director of the Institute for Futures Studies since November 2002. He is also a professor at the Swedish Institute for Social Research, Stockholm University.

In Europe, he told delegates, the Scandinavian countries are the best performers in combining inequality reductions with high employment rates and excellent growth records. As he points out; a disparity in incomes (for example gender disparity) can undo the social benefit of wealth per se. So from his point of view society needs to have an economic framework that manages the balancing act of improving incentives, human resources, social services and employment opportunities.

“Our advice: make sure simple things like life and income protection insurance are in place. Always do your homework before making big decisions.”

He made an interesting point about the aging of our societies and how social and economic policies are being considered. In his view the discussion has been unduly focused on pension reforms and savings to ensure future living standards for the elderly.

Instead, he argues, we should focus more on how social policy interacts with education, fertility and other fundamental determinants of the future tax base. In order to design social policies that are sustainable for the future, we need to put our children and youth first.

That will be an interesting thought to bear in mind as we enter the next election cycle.

Currency capers

What a great time to travel overseas. At the time of writing, the Kiwi dollar can buy US70 - 72c and we may well see it hang around at the current levels given a number of concerns in the US about sub prime mortgages, and their weakish economy.

Unfortunately our own dollar's relative strength isn't due to booming activity on our home turf. Actually it is due as much as anything to debt. Despite the increase in interest rates, household debt in New Zealand has continued to rise. The Reserve Bank has hinted at further hikes to discourage local borrowing and this will fuel more demand for Kiwi dollars from overseas. This works for cash-rich local investors also. The recent bank on-call and short term deposit interest rates of 7.5% to 8% are hard to beat. However, the outlook for global growth remains good and overseas is still the place to be. A

155 Parnell Road, PO Box 137-154, Parnell, Auckland 1151, New Zealand Phone: 64 9 307 2331 Fax: 64 9 307 2330 www.stuartcarlyon.co.nz

well diversified portfolio is however the best way to deal with the ups and downs of the markets.

For local investors, the relatively low US dollar provides us with reasonable entry prices – so new investments offshore remain attractive – though this is definitely a poor time to cash up offshore investments as the sinking US dollar will devalue the returns earned by any holdings in your overseas portfolio.

Looking for neglected stocks; investing in future trends

Have you ever been to a fruit market at the end of the day? You've got dollars in your hand but the bananas are black, the apples are bruised – the grapes have seen better days. What do you buy?

The same situation occurs occasionally in the world's sharemarkets. It's looking a tad over-ripe out there. That's why it is always refreshing to hear from investment managers who have crystal-clear reasons for investing where they do. We recently attended an investment update by Platinum Asset Management Ltd. Their Platinum International Fund is included in our client portfolios mainly because they do not follow the herd and instead invest in future trends.

Some of the more interesting companies they invest in include:

- Bombardier: a Canadian company constructing trains with lower emissions. There is huge potential in selling to Europe.
- Singapore Airlines: because they continue to be innovative and have no debt. They are well positioned to tap into China and India as these markets continue to grow into financial powerhouses.
- And while minerals and metals are the hot sectors for many investors, Platinum is directing more attention to the unloved sector - paper and pulp. They see recycled paper is at a saturation point and demand for virgin pulp will increase.

Given the global share markets have been on a roll, it's a comfort to know that Platinum will only invest in stocks that are under valued and have – when they see it necessary – the courage to simply accumulate cash until they find the right companies. That's a rare quality in a profession where too many investment managers feel compelled to back the "best of a bad bunch" rather than simply let the market correct itself. If Platinum walked into our fruit market they'd have the sense to hold onto their dollars and come back tomorrow.

Tax talk

On 18 December the Taxation Bill relating to offshore investments was passed. With the introduction of this new tax regime, it is fair to say that things have become a lot more complex.

From 1 April 2007 investors who hold investments outside of NZ will be taxed using a "Fair Dividend Rate" (FDR) of 5% of the opening market value each year. If the total return (that is market movements and dividends) is over 5%, the excess is tax free. If the total return (including a loss) is less than 5%, tax is payable on the lower amount. If a loss occurs investors will not be taxed in that year but the loss is not deductible.

A concession is given for individuals (but not family trusts) holding offshore equity investments with an aggregate cost of up to $50,000. They will be taxed on the dividends only.

For family trusts and individuals, Australian resident companies listed on the Australian Stock Exchange – All Ords Index - are exempt from the regime but this does not include so-called stapled securities such as Westfield and Australian listed property trusts. All shares listed elsewhere are taxable under FDR and this includes UK, USA, Australian unlisted unit trusts, and UK listed investment trusts.

- In a nutshell investors should maximise their return by seeking out investments that pay interest or dividends in excess of 5%. Don't let your perfectly natural tax-aversion rule your portfolio. Sound, profitable investments are still the order of the day and investment expertise and prudent fiduciary practices are just as important.
- Right now you have an opportunity. Purchases made after 1 April 2007 will not be taxed for the first year of the new regime - so we advise you to make the most of this taxation window.

"In a nutshell investors should maximise their return by seeking out investments that pay interest or dividends in excess of 5%. Don't let your perfectly natural tax-aversion rule your portfolio."

Clients on our Investment Management Service will have received an assessment of their tax positions and where we have found that more tax is liable we have been able to neutralise the position by combining certain investments. In view of the complicated legislation, Aegis our custodian is working to program client reports in a manner that will help you comply with the new tax regime.