Profile's Corner

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Issue 16

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PROFILE
FINANCIAL SERVICES

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PROFILE UPDATE

Welcome to Volume 16 of our quarterly client newsletter. In this section, we update you on what's happening at Profile.

This year's **Federal Budget** contained a number of proposed changes that are likely to affect Profile clients and their families. Just some of the headline measures include tightening up eligibility for and slowing indexation of many welfare payments, and the introduction of a 2% levy on high income earners.

Our usual warning that these changes are not yet legislated is even more important this year. To implement these measures the government must gain the support of at least six of the (record) 18 crossbench senators, which may not be an easy feat!

Please see our separate paper on the potential implications for clients' financial situations, and make sure you contact your planner if you have any questions or concerns.

Soon we will be sending out information to all our clients about participating in our next **Client Satisfaction Survey**. We regularly ask all clients to let us know what we do well, where we can improve, and what you most value when it comes to the services we provide you.

The results really are important to us! They are reviewed by our board, and included in staff performance assessment, and in the past we have made a number of changes to our business based on this feedback – launching new products and services, changing our staffing structure, and re-engineering our review processes and communications. So please be assured that the time you spend letting us know what you think will be worthwhile.

This year, the survey will look a little different. This is because we are changing to a provider who works with many firms in our industry (Beddoes Institute), so we can start tracking how we compare with other leading Australian financial planning practices. You will also have the option to let us know who provided the comments this time (you will still have the option to remain anonymous if you wish).

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INVESTMENT UPDATE

By Dr Bart Dowling, Investment Strategist, Select Investment Partners

Period returns to 31 March 2014 (%)

ASSET CLASS*	1 MTH	3 MTHS	1 YR
Australian shares	0.2	2.0	13.0
International shares ($A)	-3.1	-2.0	35.0
Fixed interest	0.0	1.5	3.3
Cash	0.2	0.6	2.8
Gold ($US)	-3.2	6.5	-19.7

This quarter our investment article comes from Bart Dowling at our Asset consultant Select Investment Partners. Bart has written for us before – this time his article is on the very topical issue of demographics and what the long-term trends might mean for the Australian economy. We reviewed a longer version of this paper at our March investment committee meeting – if you would like to see the full copy, please contact your financial planner.

There are too many people in the world. Every time I drive to the airport I'm reminded of this fact. Traffic snarls, long queues at the check-in, crowded planes, even the frequent flyer lounge isn't what it used to be... I was far more comfortable when Australia's population was only 13 million. Back then you could get a decent car park at the beach – in some cases you even had the entire beach to yourself!

So much for my rant, I'm sounding decidedly old! Still, there is an upside. A country's economic growth potential is a combination of its population growth and productivity – quite simply, the more people there are in an economy and the more they produce, the higher a nation's output. So rapid population growth goes hand-in-hand with a greater level of economic well-being - at least in an absolute sense.

Asset prices too are affected by this demographic change. More people implies more demand for assets to meet our saving / drawdown needs. Further, the average age of this ever growing population has an impact on asset demand.

Demographic change – Australia in a world context

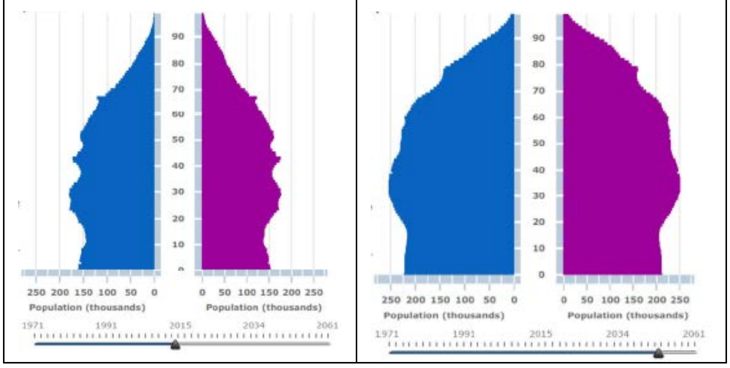
The message from demographic change is quite simple – in the future there will be a lot more of us and, on average, we will be older (at least in the developed world). The world's population is set to grow 20% between 2010 and 2030. That's a lot of people. Indeed, more people were born during the 1990s than during the entire history of human existence prior to the industrial revolution.

Population is set to expand particularly rapidly in the 20-29 to 60-64 age cohorts (Source: The Economist).

In Australia too, the news is of both a growing population and an aging one. Australia's population is expected to double by 2050, and in terms of composition, the population pyramids reveal the all too familiar 'mid-life bulge' pattern:

I used to be a lot thinner when I was young – Australia's population pyramid both now and 2050

2014	2050



Source: Australian Bureau of Statistics

So there's going to be a lot more people about and they are, on average, likely to be a lot older. But apart from a growing market for walkers, hip replacement surgeons and incontinence nappies, are there any investment implications flowing from this? It is to this topic that we now turn.

How demographic change affects asset prices

Most academic studies in this area focus on the rising 'age dependency ratio' in the developed world for modelling population impacts on asset prices. This simply reflects the proportion of individuals pre (0-15) & post (65+) retirement, relative to the working age population (15 - 65 year olds). The hypothesis is that as people head toward retirement they will progress from the 'growth / accumulation phase' of their life to the 'income phase' regarding their investment preferences.

This captures the aging population impact in a relative sense but not its absolute sense: because even though in the future there are a lot more people in the 'mid-life' cohorts, there are a lot more people in the younger cohorts as well. So in an *absolute* sense the demand for **all** assets is set to rise.

So much for the scare-mongering that an ageing of the developed world's baby-boomers will trigger a crash in global equity markets. More people simply implies more demand for assets overall, albeit in with a slight preference for income producing assets in a relative sense.

So what does all this mean for Australian investors?

The ageing of the world's population is likely to put significant strains on the health systems of the developed world and, through this, strains upon the developed world's public finances.

In Australia we are already witnessing this unfortunate fact of life in action - with all the banter surrounding the May Budget highlighting that the Commonwealth government is struggling to provide a future health spend consistent with the public's expectations.

So the ageing of the world's population likely implies a greater issuance of sovereign bonds as the developed world's public finances feel the strain. The investment implications are that there is only one way for sovereign bond yields to go – especially from today's levels – and that is up.

In fact we may have already witnessed the low point in developed world bond yields for the remainder of this century. So putting your money into a sovereign bond fund that is duration exposed to very long term yields (for instance 30year US Treasury's at 2 - 3%) is fraught with risk. This is an important point as quite often investors flock to this asset class with the idea that they are *avoiding* risk – rather than increasing the prospect of significant capital losses.

As for equities, the outlook is not so bleak. More people overall implies greater demand for all assets – with perhaps a slight tilt toward income producing assets. So both growth-oriented equities and income-orientated equities are likely to be beneficiaries of the upcoming population explosion. Specifically, from a valuation perspective, emerging market ("EM") equities look set to become huge beneficiaries because after all, that's where much of the growth is.

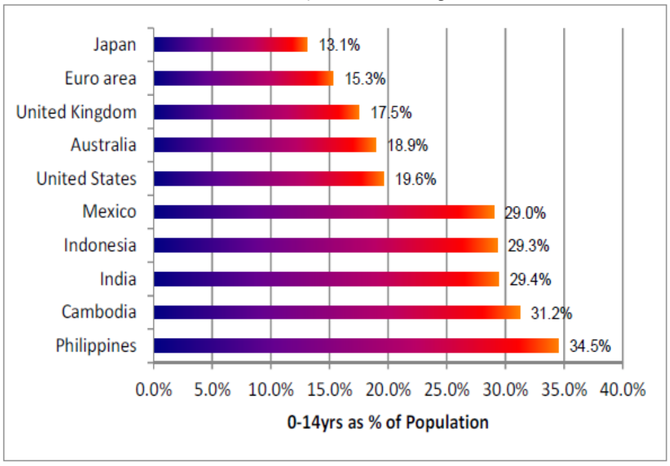
If as stated earlier a nation's economic growth potential is a combination of population growth and productivity growth, in both respects EM has an advantage over the developed world. For starters, EM has a faster growing young population than the developed world.

Take for instance the chart below which highlights the proportion of 0-14yr olds as a percentage of total population in some EM economies versus developed nations. Over the next 10 years these individuals will enter the workforce, giving in some cases (at the very least) a 10% GDP advantage to the emerging economies.

And it is not just from a population sense that EM has an advantage. Most of the EM world is (by definition) yet to hit the upper limits of the world's production possibilities frontier. This implies significant productivity advances are still ahead for these economies.

So EM is set to reap a huge productivity dividend in the coming decades, giving them a significant economic growth advantage relative to the older / more technologically mature Western economies.

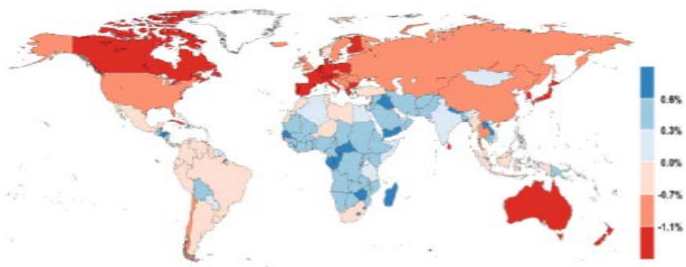
The benefits of being young and vibrant – EM economies stand to benefit from 0-14yrs entering the workforce



Source: IMF

The chart below from Nomura shows a nice summary of this relative economic growth advantage, which highlights where they see the economic growth upside (blue) / downside (red) over coming years. There's not much blue in the developed world.

Economic growth favours the young – EM growth advantage



Source: Nomura

Now that I've covered both the broad asset and country allocation calls, what about the sector specifics? Here agriculture and health care come immediately to mind as direct beneficiaries of the aging / growing population. I like one and I don't like the other.

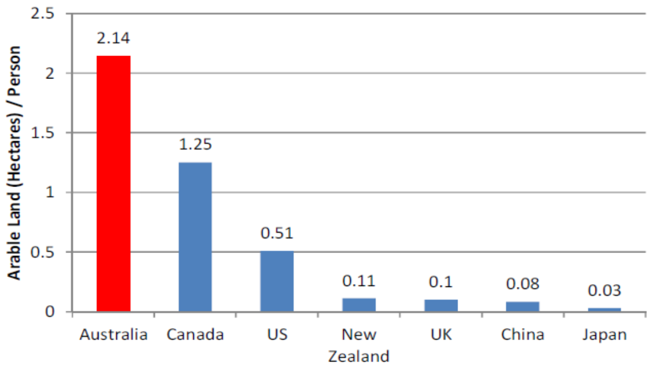
Let's start with the one I don't like – health care. Sure it seems plausible that the health care sector will benefit in some way from the world's ageing population, but what concerns me about this sector is the political angle. Public sector finances are challenged by the strain of the ageing of the developed world's population.

While the developed world's health care systems are likely to be major beneficiaries from a volume basis, I worry about government intervention distorting the price effects. Making a call on the outcome of government policy is always difficult, so for my money this is a sector that is relegated into the 'too hard' basket.

A far easier call is agriculture. I like agriculture for a number of reasons but primarily it comes down to the simple premise of supply versus demand. Unless there is another massive boom in agricultural productivity – possibly through using GM technology – then population growth is outstripping the world's finite arable land by a substantive margin. Just as we may have already witnessed the low point in developed world bond yields for the remainder of this century, we may also be approaching a turning point in the sense that agricultural commodity producers are ceasing to become 'price-takers'.

What are the implications of this? It appears Australia is well placed. As the chart below testifies, Australia has a massive comparative advantage in terms of arable land and this, combined with the fact that we are geographically very close to a lion's share of the world's fastest growing consumers (notably in Asia) stands us in good stead.

Australia's massive comparative advantage – arable land



Source: World Bank

So to summarise, the investment ideas flowing from the upcoming population boom along with its associated aging are as follows:

- Avoid developed world bonds – especially at these levels as the only way for interest rates is up;
- Equities: EM looks appealing for a long term 'buy and hold' strategy;
- Sectors: agriculture is the pick.

And we had all better get used to living in a much more crowded house in the future!

SUPER REFORM

By Kurt Ohlsen, Senior Financial Planner

Way back in May 2009, the government commissioned a review into the governance, efficiency, structure and operation of the Australian superannuation system, led by Jeremy Cooper (the eponymous Cooper Review.)

Then in late 2010 we saw the 'Stronger Super" reforms…. And now, only five years after the process started, we have two of the announced reforms; *Super Stream* and *My Super,* starting to affect some of our clients.

It's been a while…..

Super Stream

If you have a Self-Managed Super Fund (SMSF) that receives employer contributions, Super Stream will require you (as trustee) to ensure that the fund has an Electronic Service Address (ESA) by 1 July 2014. This is different to an email address. The change is to allow for more streamlined sending and reporting of superannuation payments, which must be electronic from this date.

To obtain an ESA is relatively quick and easy. You will just need your fund's ABN and 5 minutes on the internet to apply. Once you have registered, you will be provided details to give your employer. These should be provided to your employer by **31 May 2014** for employers with over 20 employees. (Smaller employers have an extra year to comply).

You may have already received letters from the Australian Tax Office warning of the compliance requirement, or you might have received instructions from your fund's accountant on how to register. If you haven't yet received any advice from your accountant on this, it may be worth giving them a call to ensure things are on track for the deadline.

MySuper is a new type of superannuation account, which will replace what is currently known as default superannuation accounts. They are a cost-effective super product with very simple features, regardless of who provides them.

They have:

- a single investment option,
- a minimum level of insurance cover (life and TPD),
- an easily comparable fee structure, with a short prescribed list of allowable fee types,
- restrictions on how advice is provided and paid for, and
- rules governing fund governance and transparency.

The Cooper Review has questioned previous assumptions that most superannuation members make rational and informed decisions about their superannuation. This is probably a fair enough point, when you consider that of the almost 12 million Australians who currently hold a superannuation account, 80% have their compulsory superannuation contributions paid into the default. Although it's possible this could have been a rational choice based on a comprehensive assessment of the available options – realistically it is probably driven more by apathy, or choice paralysis -failing to make a choice at all.

The MySuper reforms simply aim to make sure that when someone doesn't make a choice, they will end up in a low-fee product that is unlikely to get them into too much trouble.

Since 1 January 2014, employers have been directing super guarantee contributions for employees who have not selected a fund to an authorised MySuper product. Nearly all current default fund providers also offer a MySuper product, so the change has been reasonably easy to implement for employers.

For employees, those using a default superannuation account may have already received correspondence from their fund asking whether they want to opt-out of their existing balance being transferred to a MySuper account. Generally the Fund is required to give members 90 days' notice before automatically transferring your balance if they have not heard from you. Funds have until mid-2017 to complete this process, however, so depending on the funds' timetable members might not hear anything for a while yet.

What's next?
The next battleground looks to be around which products can be the default funds in the various Modern Awards. An expert panel of the Fair Work Commission is set to review the current default funds; however the validity of that process is being challenged by the Financial Services Council (FSC) which mostly represents the large banks and other financial institutions. The default super space is currently dominated by unions and associated industry super funds. At stake is a very substantial amount of money – total employer contributions made to super in the 2012/13 financial year were $77.5 billion! [1] – so we expect sparks to be flying here for some time to come.....

As always if you would like to discuss how the changes affect your personal situation please contact your Profile financial planner.

[1] Source: APRA Annual Statistics, June 2013

END OF FINANCIAL YEAR CHECKLIST

By Scott Ungaro, Associate Financial Planner

30 June is fast approaching! Below we suggest a few ways to beat the rush, maximise your benefits and ensure you can still enjoy the year-end sales....

Transactors beware!
One of the first things to note is 30 June falls on a Monday this year, so consider Friday 27 June your cut off. It is unlikely that any funds transferred after 4pm on Friday will make it to your accounts in time.

Contributions
Maximising your super contribution limits is a great way to save for retirement in a tax-effective way

Concessional (before-tax) contributions
In this financial year (2013/14), your concessional contribution limit depends on your age. If you are 59 years or older on 30 June 2013, you can contribute up to $35,000 as concessional contributions to super. For everyone else, the maximum is $25,000.

It's a tax effective way to contribute to your retirement, because these contributions are taxed at 15% instead of your normal marginal tax rate.

It's very important to check your employer contributions on normal pay and bonuses, salary sacrifice and premiums for insurance in super as they may all be included in the limit. Remember, some employers only pay quarterly so if your contributions look low for the year, ensure first that there isn't another large contribution due to come in. This is important because if you exceed the concessional contributions cap for the year, you may be required to pay significant extra tax.

Non-concessional (after-tax) contributions
Non-concessional contributions are initially taxed at your personal tax rate, but while in super, investment earnings are only taxed at 15%, which drops to 0% once you are over age 60 – still a pretty good tax deal, and particularly attractive for the over-55s.

This financial year the maximum remains $150,000 per person. If you are approaching 65, ensure you discuss your contribution timing strategy with your planner as you may be able to take advantage of a $450,000 bring forward provision.

Co-contribution (Government matching up to $500)
Your eligibility for the co-contribution is largely determined by your income. For those earning less than $48,516 you do qualify for a partial co-contribution, while those earning less than $33,516 can earn up to $500. Remember you must make a personal contribution of $1,000 or more to receive the benefit which will be automatically calculated and paid to you after filing your income tax return. Remember, even if you don't qualify then chances are someone in your family may – a low-income spouse, a child in a first job etc.

Spouse contribution
If your spouse has income of less than $13,800 then you should consider making a spouse contribution. You may be able to claim an 18% tax offset on super contributions of up to $3,000 you make on behalf of your non-working or low-income-earning spouse.

Minimum pension drawings
For those with SMSFs, make sure you have drawn your minimum pension payments before 30 June in order to avoid a breach. For pensioners under the age of 65, you must withdraw 4% of your super balance as at 1 July 2013.

For those aged 65-74, the minimum pension payment is 5% of your super balance as at 1 July 2013. Please make sure to speak to your financial planner if you are unsure whether you have met your minimums.

If you are in a public offer fund, such as Macquarie Wrap, the Trustee of the fund automatically calculates your minimum pension amount and pays this to your nominated account.

Medical expenses tax offset
Depending on your family status and income you may be eligible to claim a tax offset for the net medical expenses you have incurred over the threshold. You may want to consider bringing forward any large medical expenses and having them in this financial year which will allow you to maximise the tax offset.

The table below illustrates your potential entitlement:

Family status	Income ("ATI") threshold	What can I claim?
Single (single at 30 June 2013 and no dependent children)	$84,000 or less	20% of net medical expenses over $2,120
	above $84,000	10% of net medical expenses over $5,000
Family (with a spouse at 30 June 2013, or dependent children at any time during the year, or both)	$168,000* or less	20% of net medical expenses over $2,120
	above $168,000*	10% of net medical expenses over $5,000

** plus $1,500 for each dependent child after the first.*

CLIENT PROFILE – DORSET SUTTON

By Phillip Win, Senior Financial Planner

Dorset Sutton likes to describe himself as an "URS" (Unemployable Retired Senior) – which couldn't be further from the truth!

Dorset likes to relate how he failed his first year at University of NSW after struggling with accounting. Despite this inauspicious start he went on to graduate in Commerce/Marketing (earning the Marketing Medal along the way). As he walked out of Uni on his very last day, he noticed a small ad on the board that Colgate Palmolive were looking for marketing trainees. "Hallelujah!" he thought, applied immediately, and to his great surprise was hired by a boss, who became his career mentor for over 30 yrs.

This mentor was the kind of visionary boss who was not afraid to give people space and opportunity. An early opportunity he gave Dorset was the chance to take 12 months off to travel the world after only 18 months with the company – holding the job open for when Dorset returned.

Coincidentally, another early important relationship was with another long-term Profile client, Laurie Stokoe, who early on sent Dorset to the 'wild west' of sales to learn the art of negotiation and customer interaction. To this day Laurie and Dorset still meet in Manly for coffee/lunch catch ups, and a few laughs over the state of life.

An important lesson learned through this, says Dorset, was to focus on being the best in what you are passionate about, and openly embrace a career/life mentor which he says have both stood him in great stead over the years.

Says Dorset, "Colgate Palmolive opened the doors wide for great experiences, best-in-class marketing training, and ultimately a wonderful career which took me all over the world. New York for global / big picture exposure, then 17 years working all over Asia in marketing and general management assignments."

In Asia came Dorset's most important opportunity of all: he met his beautiful wife Jenny in Kuala Lumpur, Malaysia where she was working with Colgate's Advertising Agency as a TV producer on the Colgate Palmolive account. "Jenny and our daughter Charmaine joined me as we travelled as a global family with all its challenges and life-lasting rewards."

Dorset says that working for a great international marketing company taught him the value of working hard, not expecting to be better than you are worth, and most importantly the value of being flexible, open minded and willing to take on new challenges in foreign parts of the world - while still maintaining work-life balance and having fun!

One unexpected assignment took the family to Topeka, Kansas to be responsible for CP's pet nutrition division. Topeka is a small, old mid-west town, not easy to spot on the map. It was certainly an entirely different product line (specialty pet and veterinary nutrition diets for dogs and cats) and culture and characters quite different from our experiences in Asia!

An important lesson learned from this experience was to be humble at any stage in life when you're thrown into the fire, and need to rely on others to learn an entirely new business. "We were so grateful the Stokoes came to visit us once when we really needed old friends to lean on!", says Dorset. Jenny will never forget watching a beagle on the treadmill in Hills Technology Centre where animal nutrition diets were measured for effectiveness: energy, weight loss etc!

Above all else, 34+ yrs with Colgate Palmolive, of which 28 years were living overseas, demonstrated the enduring power of true partnership.

Says Dorset, "Working for a company you really believe in, and gaining the rewards from a company which believes in you, creates unique and interesting opportunities, and means you never once have to rethink tenure or trust. This strong sense of partnership and trust has now extended to our partnership with Profile for 10 yrs now, and our Danish investment banker for 14 years."

Perhaps the biggest challenge in the Sutton family's collective lives came upon retiring from Colgate. Settling back into Sydney after a very long time living away, making new friends, finding new interests and challenges, and becoming Joe Citizen again after having been Joe Corporate for such a long period. With the benefit of time and patience, new opportunities have come along for Dorset.

One challenge he is very much enjoying is being on the Strategic Leadership Team for the "Good for Manly" Community Association (now a political party within local government).

This is a group which is fighting hard to ensure that Manly can grow in a way which protects its natural beauty and focuses on environmental responsibility, while retaining and enhancing a strong village culture. Dorset is also Chairman of Manly Library Board of Trustees, through which role he has become involved in helping to build the literacy resources within Manly Community.

Dorset says, "My lesson learned in the last few years is that you don't have to be a "big shot" after you retire. There are so many rewarding, small, local activities to engage in, and "salt of the earth" friends to enjoy. To this day I continue mentoring/coaching, something I did my entire career with people of all ages and backgrounds - helping them find that passion they may have that, if sparked, can redirect a whole life in a positive direction. One mentoring tip I try to pass on is to encourage belief in one's values, and to live those values every day - something I garnered from family and a great company to have spent my career with."

Dorset's hobbies today include ocean swimming, harbour kayaking, buddies social golf, travelling (as his married daughter now lives in Columbus, Ohio), and maintaining strong networks with great friends met over the years all over the world.

And when all else fails, hopping on the Manly Ferry, meeting a buddy at Circular Quay, while his Ferry captain waits to return him to Manly. As a "Super Senior" this is the best $2.50 you could ever spend, says Dorset (of course, add $3.00 for a great coffee!).

I can certainly attest that Dorset is truly living his "3H Vision":

- Health
- Happiness
- Harmony

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