

Profile's Corner

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PROFILE
FINANCIAL SERVICES



PROFILE UPDATE



GENERAL ADVICE WARNING

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**Asset class returns referred to in this publication are based on the following indices: Australian shares: S&P/ASX 300 Accumulation Index. International shares: MSCI ex Aust (AUD) Index. Fixed interest: UBS Warburg Composite All Maturities Index. Cash: UBS Warburg bank bill Index. Gold: Spot Gold Bullion (USD).*

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

Recently we asked clients to participate in our first-ever **Client Satisfaction Survey**. We wanted to get a gauge of how effectively we were meeting the needs of our clients, and what we could do to improve the services we offer. We were also keen to understand how we compared with other similar financial planning firms, so we used an external company (Woolcott Research) which has run these surveys for several similar firms. We have been very happy with the results of the survey:

- Over one third of our clients completed the survey (more than three times the average participation rate).
- Our overall satisfaction score (of 8.6 out of 10) was well above the average score of 8, and the second-highest of all financial planning firms.
- We scored well above average on effectiveness of all forms of communication.
- Commenting on the aspects of our service they most valued, clients said that our advice was well-tailored to their specific circumstances, well-researched and was explained in a way that was easy to understand. Clients also felt our advice was honest and frank.

We also had several good suggestions from clients on things we could do more of, such as:

- Some clients would like to receive more frequent unscheduled contact / phone calls from Profile.
- We have clients who access their portfolios frequently online using Xplan, and would like to see more frequent updates of this platform.
- Some clients working full-time thought it would be handy if Profile offered some appointment times on a Saturday.

Many of our clients have recently changed their financial planner, due to the retirement of our founder Garry Ohlsen, and are looking forward to getting to know their new planner better. We are working through the detailed survey results and we will keep you posted on changes that we make as a result.

In the meantime, if you have specific comments or suggestions you would like to make, please don't hesitate to contact your planner, or our CEO Sarah Abood, on (02) 9683 6422. And congratulations to Karin Konyari, who was randomly drawn by Woolcott Research as the lucky winner of the \$500 travel voucher prize!

We are happy to welcome a new staff member to the team – **Sharon Cruikshank** has joined us as receptionist, replacing **Marilyn Campton** who unfortunately needed to move to the Central Coast for family reasons. Sharon joins us after 18 years at State Super Financial Services in various roles, including receptionist and Client Services Officer.

INVESTMENT UPDATE

By Jai Parrab, Head of Investment Research

As conditions in Europe deteriorated in early May this year, fear and uncertainty about the global economic outlook crept back into markets, setting the stage for another round of panic selling and market volatility. In the first section of my article I look at global economic conditions and the investment outlook. In the second section I take a detailed look at an asset class that's been garnering a lot of support lately – Term Deposits.

Period returns to 30 September 2011 (%)

ASSET CLASS*	1 MTH	3 MTHS	1 YR
Australian shares	-6.13	-11.58	-8.56
International shares	+0.94	-7.98	-4.54
Fixed interest	+0.90	+4.63	+9.04
Cash	+0.39	+1.24	+5.02
Gold	-11.05	+8.24	+24.12

When you look at the big picture, it's hard to argue with the view that the world is going through a very difficult period, which is likely to remain entrenched for some years to come. The excesses of the past, inflated by high levels of borrowing, overpaid Wall Street bankers and indiscriminate spending on the part of the consumer, must now be repaid. In late 2008, we stared the collapse of the global banking system straight in the face. Had it not been for concerted policy action taken by national governments, things may well have been much worse.

Today we find ourselves in what some see as a similar predicament - although now the issues are more around solvency (balance sheets) than liquidity (access to capital). Another difference today is that instead of strong political action being taken to provide markets with reassurance, we are seeing politicians jettison concerns about market sentiment as they speak to their own constituencies rather than to global economic welfare. At least in some countries, political survival has become more important than the common good.

In early August, congress in the US played chicken with markets as it waited until the last minute of the last hour to pass a motion to raise the US debt ceiling. Concerns about the politicking around this event led the Standard & Poors credit rating agency to downgrade US sovereign debt for the first time in seventy years. As unemployment in the US remains stubbornly high (at 9.1%), republicans and democrats continue to prepare for the presidential elections in November 2012 by hurling accusations - rather than coming up with plans to find jobs for the eight million people who lost them during the crisis.

In Europe, it is every man - and nation - for themselves. Germany (and to some extent France and Scandinavia) holds the key to alleviate market concerns, if they can convince the world that they will do whatever is required to prevent debt contagion into core European countries and their banking systems. However, political will is questionable - words are being bandied around, but actions are thin on the ground. That said, in one of the most anticipated parliamentary votes of the year, the German Bundestag convincingly passed the expansion of the European Financial Stability Fund (the EFSF). If it had been rejected, it could have cost Angela Merkel her chancellorship. Despite this, the EFSF is still far from being a done deal. Although at time of writing, the Slovak parliament had passed the bill (after an initial rejection had led to the fall of the previous government!), and there are still more hurdles to jump.

With the US possibly on the precipice of a double-dip recession, and European governments and banks scrambling for cohesion and capital, how can financial stability be maintained? Well, according to markets at least, it probably cannot! It is not very hard to make a case for a very bleak economic outlook. But from my point of view, the world is merely transitioning and while this period will be hard, longer-term prospects are much rosier. There are two important factors to bear in mind at present. The first is the ongoing growth and development being witnessed across Asia and the emerging markets. The second is that on the other side of this financial turmoil is the prospect of a global economy with a stronger base and more productive and efficient assets (people, businesses and technology).

Despite Asia's vulnerabilities to the West and looming inflationary pressure, it will nonetheless almost certainly remain the fastest-growing region in the years to 2016. That Asia will continue its strong rate of expansion is attributable to two factors. The first is that Asia's economic fundamentals are still in good shape. Levels of debt (both government and private) are low compared with the West, and most Asian banks were resistant to the effects of the global financial crisis.

The second important factor is the emergence of China as an independent engine of regional growth. This trend is likely to continue as its middle class grows and the economy moves towards a more balanced model, with private consumption accounting for a greater share of demand. Moreover, rising wages in China are beginning to prompt companies to seek alternative low-cost production bases, to the benefit of Asia's other low-wage countries. So far, Bangladesh and Vietnam have been the main beneficiaries of this trend.

There are still concerns that China is about to suffer a "hard landing" in its economy. These are centered on the property market, where activity has been excessive since the government rolled out stimulus measures in 2008. However, I do not believe that we will see a repeat of 2009, when a collapse in global trade sent many Asian economies into recession. Of course the risk still remains and policymakers are likely to be more cautious in taking steps to cool domestic demand as a result.

In the face of Western turmoil offset by Asian growth, markets remain skeptical – they continue to demand a significant risk premium and are likely to remain volatile. It is difficult to see the debt problems of Europe being solved in the short or medium term, or the US launching into the next growth cycle until some significant deleveraging takes place, but this does not mean we should run for the hills. Corporations – both in America and globally – are in strong shape, with high levels of cash on balance sheets, low levels of debt, easy access to credit and lean operations underpinning high free cash flow levels. Quality companies and assets will come through this crisis stronger and better than before. As markets continue to discount all assets indiscriminately, our dynamic, opportunistic and active risk management approach remains key to delivering consistent returns in this market.

Feature – Term Deposits

With market volatility remaining elevated, and continuing uncertainty about the global economic outlook, we are increasingly discussing term deposits with clients. We also hold some term deposits in our model portfolios.

Term deposits can be a useful investment tool in that they provide certainty of nominal return (interest payments) over a given time period, and certainty of capital at maturity (based on the financial integrity of the offering institution). In this section, I outline the key points I consider as Portfolio Manager, when deciding whether to use term deposits in our model portfolios.

Portfolio objective

The first question to consider with any investment is the purpose. I ask myself, am I considering a term deposit to "park" cash for the short-term, or to hold for the medium or long term because of attractive nominal rates? Term deposits generally offer only limited diversification benefits in a portfolio. This is because when markets are falling, they will hold their value, but they will not increase in value like some bonds (which become more valuable as forward interest rates fall). Therefore they act primarily as a capital preservation tool, rather than as a portfolio diversification tool.

Relative interest rates

Every time you make an investment, you should look at relative value. This involves comparing the return you can get on a similar instrument of equal credit quality (for term deposits, the relevant comparisons are with cash and fixed interest). For example, when I am looking to invest in a six-month, twelve-month or three-year term deposit, I first look at where government bonds, and similarly rated bank bonds, are trading in the market. Term deposits should offer a higher rate, as you should receive an illiquidity premium. This is because you must hold a term deposit to maturity, and you should be compensated for having to "lock up" your cash. Bonds, however, can usually be sold day to day, meaning they are more liquid, and therefore people will generally accept a slightly lower rate to hold them.

Future expected interest rates

Every time you make an investment, it's important to have an exit strategy. When it comes to term deposits, this means looking at what reinvestment strategies are potentially available at maturity. There are three primary risks to consider here:

1. If market interest rates are expected to be lower when your term deposit matures, then you will be rolling over into a lower return investment;
2. If market interest rates climb higher while you are invested in the term deposit, you are missing out on potentially higher rates on offer over that timeframe; and
3. If you are using a term deposit to park your cash due to market volatility, by the time the term deposit matures, markets may already have run – meaning you will be buying in at much higher prices than were on offer during the term your money was locked up.

Drivers of term deposit rates

Term deposit rates on offer are driven by three main factors:

1. The current central bank cash rate and forward interest rate curve;
2. Bank demand for capital (which can be a function of new regulations, credit spreads in wholesale funding markets and/or increased lending growth); and
3. Investor demand, which is primarily a function of investor sentiment.

You might remember that during late 2008, banks were offering very attractive “special rates” because of distress in wholesale funding markets. At the moment, however, term deposit rates are falling since investor demand is high, credit growth is low, and forward interest rate curves are pricing in rate cuts (at time of writing).

Expected inflation

The final consideration is to calculate what the real return will be, as opposed to the nominal return (or interest rate) being offered. To work this out, you need to have a view about inflation. If the term deposit is offering you a rate of 5.5%, and inflation is expected to be 2.5%, then your “real” rate of return is 3.0%. However if the inflation rate is expected to creep higher to say 3.5%, then your “real” rate of return over time could be as low as 2.5%. This is a real 1.0% cut to your personal spending capacity, even though the term deposit rate has not changed.

In summary, there are a number of considerations that go into the decision to use a term deposit, beyond fear of market volatility and a desire for certainty. Term deposits should be analysed rigorously just as any other potential investment. At times it will make a great deal of sense to use them – at others, the disadvantages (particularly lack of liquidity) may outweigh the benefits.

Exchange Traded Funds explained

By Isabelle Zhang, Financial Planner

Exchange Traded Funds (ETFs) are an investment type that’s experiencing huge growth in Australia – according to the ASX, the market capitalisation of ETFs increased almost 40% in the year to April 2011. The largest single ETF in Australia – the SPDR S&P/ASX200 fund – had over \$US 2.4 billion invested as at mid August this year.

What is an ETF?

An ETF is a portfolio of securities (such as shares, bonds or commodities) that is traded on the Stock Exchange in a similar way to a share. ETFs are usually designed to replicate the performance of a selected index (such as the S&P/ASX200 – an index of the top 200 stocks by market capitalisation on the Australian sharemarket).

There are two broad types of ETF: standard ETFs (which hold actual assets such as shares or commodities) and synthetic ETFs. Synthetic ETFs replicate their chosen index using derivatives (often an instrument called a swap). They are ‘synthetic’ in the sense that the ETF does not confer ownership in a hard asset, merely part ownership in a financial derivative.

What are the benefits of ETFs?

One of the main reasons ETFs are becoming more popular is their low cost. Compared to an actively managed fund, where you could pay typically from 1% to over 2% of the net asset value (NAV) as a management fee, ETFs are generally a much cheaper option, at around 0.2% - 0.3% of NAV.

Another feature of ETFs is that they are valued throughout the day, unlike managed funds which are valued less frequently – often daily or weekly, and sometimes monthly or even quarterly. For example, on 9th August this year the S&P ASX200 traded in a range of over 6% on the day – although it closed just 1% up from the opening. Using an ETF would allow an investor to trade this volatility, a feature which is not available in managed funds.

With more ETF products entering the market, it is becoming easier to access a broad range of different market indexes to diversify asset allocation within an investment portfolio. Investors can now use ETFs to invest in international indexes as well as Australian indexes and market sub-sectors, as well as commodities. For example, investors may want exposure to gold bullion within their portfolio. If it is believed that the price of gold is likely to rise, they can purchase an ETF Gold Bullion Index without having to physically purchase gold on the market, store it, insure it and so on.

What are the potential pitfalls of ETFs?

Despite their additional costs and less frequent valuation, actively managed funds may actually be a better choice in volatile markets, as active fund managers have the ability to outperform the market. Because ETFs are passively managed, they simply track a particular market index. ETFs will not outperform in up markets, nor can they protect you from or minimize the impact of falling markets – they will simply follow the trend.

Although ETFs are generally cheaper than managed funds this isn’t always the case. There are a number of cheap managed funds available, and investors should also check additional fees (such as buy/sell spreads and other transaction costs) as well, which can be high with some ETFs.

If you are using an ETF to access international markets, pricing can be a problem if the market isn't open when you are transacting – you may end up paying too much. In addition, changes in currency can have a substantial effect on your investment returns.

Some ETFs use a practice called 'securities lending' in which they lend out some of their underlying securities to another investor, for a fee. This introduces an additional potential risk, as the securities may not be returned by the borrower.

Investors also take on additional risks by using synthetic ETFs – such as the risk that the counterparty to the derivative instrument might fail.

How does Profile use ETFs?

We are currently using ETFs in our model portfolios in two main ways:

1. We use an ETF that tracks the performance of the top 200 shares in the ASX, for a small portion of our Australian equities exposure (most is with active fund managers). As markets are highly volatile at present, this investment allows us to move very quickly and cheaply for clients if we want to change our weighting to Australian shares overall, taking advantage of any substantial price moves within a day.
2. We use ETFs to manage our gold exposure. These products enable us to benefit from defensive holdings in gold bullion without the problems of physically storing gold.

In light of the strong recent expansion of the ETF market and the complexity of products available to the retail investors, ASIC recently published some information to assist consumers to understand the different types of ETFs.

You can find it at:

[www.moneysmart.gov.au/investing/complex-investments/exchange-traded-funds-\(ETFs\)](http://www.moneysmart.gov.au/investing/complex-investments/exchange-traded-funds-(ETFs))

If you have any questions about ETFs, please contact your Profile financial adviser.

CLIENT PROFILE – SOKA GAKKAI INTERNATIONAL AUSTRALIA

By Phillip Win

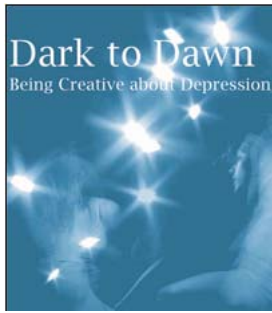


In this edition, we thought that as all the clients we have featured so far have been individuals, it might be interesting to profile one of our corporate clients.

Organisations which are entrusted with member's funds or donations have a strong need for sound financial advice. We asked Greg Johns, General Director of Soka Gakkai International Australia (SGIA), to explain some background on the organisation, and how SGIA became a client of Profile.

Soka Gakkai literally means "Society for the creation of value". The organisation originated in Japan in the 1930s, with the aim of promoting peace, a culture of nonviolence and sustainability, and education. Its aims are grounded in Buddhist philosophy, and centered on a belief in the unlimited potential of every individual and the importance of a lifelong pursuit of self-awareness, wisdom and development. It is now represented in 192 countries and has representation at the United Nations as a Non-Government Organisation (NGO).

The Australian organisation was founded in May 1964 by SGI International President and UN Peace Award recipient Dr Daisaku Ikeda. It now has over 4,000 members nationally, of which 1,500 are located in Sydney. Members usually meet in small groups, however, they also draw around 500 members to larger meetings at their Homebush centre once a month. SGIA has recently purchased new premises in Melbourne to accommodate its rapidly growing member base.



SGIA are very active in the community, and engage in multi-faith community groups to promote understanding and peace. They also host initiatives combatting depression, in conjunction with Beyond Blue, such as talks, art exhibitions and community engagement. Their aim is to raise community awareness and also to encourage people affected by depression to engage in conversations and reach out for help and understanding.

Another important cause is the abolition of nuclear weapons (SGIA work together for this cause with ICAN – the International Campaign to abolish Nuclear Weapons).



ican imagine a world without nuclear weapons

Back in 2004, a 5 year business plan for SGIA was formulated, presented to the board and accepted. This was no small achievement as it is not uncommon in volunteer organisations for a business plan to be non-existent (after all, it takes a lot of time and effort and volunteers only have so much of this valuable resource!)



As one result of the plan, it was possible to employ the newly appointed General Director Greg Johns to implement the plan. Greg himself is a great example of how organisations like SGIA can help people realise their potential and overcome seemingly insurmountable obstacles in their lives. Greg had a terribly difficult childhood, with an alcoholic and abusive father, life-threatening asthma and associated obesity (caused by the steroidal drugs he needed to treat it).

Bullied by schoolmates and ignored by uncaring teachers, he became suicidally depressed. However things began to turn around for Greg after moving to the city, where he met a member of SGIA through a shared love of music. Gradually Greg spent more and more time visiting members of the organization, discussing philosophies of life and being exposed to many caring and generous people with a genuine desire to help. While Greg's depression didn't suddenly disappear, over time it dissipated as Greg came to believe he could be happy and make a positive contribution to the world. Greg is an inspirational individual and we at Profile feel privileged to be able to work with him and the many other caring members of the SGIA organisation.

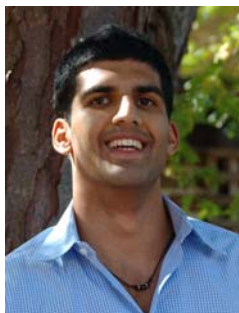
Another element of the business plan was to engage the services of a financial services firm to advise on the management of SGIA's financial assets. SGIA met with a number of firms and finally settled on Profile Financial Services. Greg says, "We were impressed with Profile's sincerity and clear commitment to professionalism, as well as their genuine interest in our organisation." SGIA has been a client of Profile Financial Services since 2006 and we regularly attend the Annual General Meetings to provide an outline of how the assets are performing, and answer any questions members may have regarding their investment management.

If you would like to find out more about SGIA, you can visit their website at:

<http://www.sgiaust.org.au/home>

GETTING TO KNOW THE TEAM AT PROFILE:

Jai Parrab - Head of Investment Research



Jai joined Profile in 2006 while completing his final year of university. Since completing his studies, Jai has moved into a focused portfolio management and investment research role within the business.

Jai was born in Toronto (in Canada, the English part) and attended a French school before temporarily moving to Sydney in 1990. Jai finally immigrated permanently to Australia with his family in 1995. He was fortunate to return to the same school (International Grammar) the second time around, and retained his relationships with now long standing friends!

Jai has had a passion for financial markets from a very young age. He has pursued a keen interest in the writings of various investment titans, most notably: Benjamin Graham, Warren Buffet, George Soros and Ray Dalio. Jai's particular interest in these individuals was their ability to build great independent businesses and manage exceptional long-term investment portfolios throughout market cycles.

Having started his career by Garry Ohlsen's side, meeting with clients and their families on a daily basis, Jai's approach to managing wealth is grounded in personal knowledge and a strong understanding of the impact of markets on real people.

This is in stark contrast to most investment managers – who in many cases have never sat down with a 'real' client in their lives. A deep understanding of investors' motivations – their fears, ambitions and objectives – is a vital part of Jai's investment philosophy and informs the way he invests and communicates.

Interestingly, Jai moved into his dedicated investment research role at what was almost the peak of the market in mid-2007. Since that time Jai has had plenty of experience in managing wealth during very challenging times, focusing on downside protection and risk management while still being open to pursuing opportunities – at the right price! During this difficult period for markets, Jai has also had many opportunities to deal closely with some of the industry's best and most experienced investment professionals. These opportunities are rare, and by experiencing these circumstances early in his career Jai feels he has had an unmatched chance to learn more in five years than some investment professionals have the opportunity to in their whole careers!

Jai holds a Bachelor of Economics degree from the University of Sydney with a double major in Economics and a major in Finance. Jai will be starting his CFA (chartered financial analyst) accreditation in the coming year to support his perpetual thirst for knowledge.

Away from work Jai enjoys the gym, great food and a bottle of wine with friends, the beach and outdoor sports, and most importantly, his appointment of late to the status of uncle/part-time babysitter (of an amazing little girl named Isabelle and her little brother named Zachary).

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