Profile's Corner

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IN THIS ISSUE

PROFILE
FINANCIAL SERVICES

PROFILE UPDATE

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

We are pleased to welcome two new staff members to Profile. Helen Du Bois has joined us from Macquarie, as a Client Service Officer. Elizabeth Barr has started with us in reception, coming from IRESS (a software supplier to the financial services industry).

Save the date!
Our annual seminar for all review service clients will be held on 18th October 2011. Stay tuned for more details closer to the time.

The Profile Portfolio Solutions project
Regular readers of our newsletter will recall that we have been developing a set of implemented investment solutions, to ensure that we can deliver our best investment ideas to all clients more quickly and efficiently, in a way that meets their specific investment goals.

> **Project re-cap**
> We have been frustrated by some of the limitations and inconsistencies of the traditional strategic asset allocation (SAA) approach to portfolio construction. SAA's approach to risk, assumptions about investor psychology and behaviour, assumptions about long-term asset class returns and diversification characteristics, and ability to react to market changes have been found wanting. So particularly during times of market stress, traditional methods and products sometimes haven't allowed us to move as quickly or substantially as we would like to do. And traditional fund managers need to primarily manage their risk in relation to each other and to passive benchmarks – whereas our risk, and that of our clients, hangs more on not delivering against plan, and against cash as the true opportunity cost of investing. We have worked with industry participants and clients to refine an investment methodology that instead puts the client and their unique goals at the heart of the process - "Objectives-based investing".

As we couldn't source existing products that delivered what we were looking for, we set out to create a set of funds that are genuinely driven by client needs, where the planners who are accountable to clients make the key investment decisions. We undertook a rigorous tender process involving four of Australia's leading asset consultants to find the right partner to help us deliver these objectives.

We are pleased to announce that we have selected an asset consultant to assist us with delivering our implemented solutions. While Profile will be the investment manager, we believe that partnering with the right firm will give us access to valuable additional investment resources, financial models, risk management systems and comprehensive research – as well as greater pricing power when negotiating with fund managers that we might invest with through the implemented solution!

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The successful firm is **Select Asset Management**, a specialist investment and asset consultant. To come to our decision, there were five key areas in which we compared the asset consultants:

Services. It was important to work with a firm which could provide strong support to our investment committee in terms of research and models, and could also bring additional support in negotiating fees and services with other external providers. Select demonstrated a strong ability to deliver to our needs in these areas during the tender process, and has successfully worked with a number of corporate clients to deliver similar objectives. Their clients include Commonwealth Financial Planning, Commsec, Finovia, Futuro, Genesys, Julliard, Magnitude, Managed Financial Services, Securitor, and Snowball.

Fees. Although Select was not the cheapest provider we reviewed, we were impressed by their flexible fee structure as well as the real value (ie, after fees returns) they have delivered to their clients.

Investment track record. We were also looking for a firm with demonstrated success in delivering absolute returns through varied market conditions. Again, Select was the clear winner here, having consistently "produced absolute returns well above the Lonsec Fund Sector Average and benchmark and with less volatility." (Lonsec research).

Investment philosophy. A key objective for Profile is to work with a consultant which has an investment philosophy very closely aligned with our own. They must share our views on the importance of valuations in asset selection, have a genuine commitment to delivering absolute (rather than relative) returns to clients, and a willingness to operate outside traditional strategic asset allocation boundaries. Select was the clear winner in this area, as a firm that was formed with the aim of preserving and enhancing wealth across varied market conditions, focusing on delivering strong risk adjusted absolute returns using a value/contrarian approach.

People, resources and corporate. We were looking for an organisation that was financially sound, with a depth of talent and experience, and a demonstrated ability to retain key people. Select is a profitable firm, incorporated in NSW and 95% owned by employees, past employees and directors. It has around $650 million in FUM and 20 permanent staff, and has an additional Investment Advisory Panel to provide more coverage in strategies and areas where Select desires additional resources. Its key investment staff have significant industry experience with over 15 years of average experience, and an average of 6 years tenure with the firm. The Chief Investment Officer, Dominick McCormick, has over 25 years industry experience and is a founder and director of Select.

Overall we are confident that Profile partnering with Select offers the best value solution to our clients' needs, in a way that is closely aligned with our investment philosophy and values.

The other key roles involved in delivering our implemented solutions have also been decided, they are:

- Legal: Baker & McKenzie
- Custodian and registrar: BNP Paribas
- Accountants and auditors: Ernst & Young
- Select will also act as the Responsible Entity (RE) of the portfolios.

We are completing the Product Disclosure Statement (PDS) for the portfolios, and intend to have this ready to share with clients from March. We are also working with Macquarie to make the portfolios available via Macquarie Wrap from April of this year.

Your financial planner will explain the changes in more detail, and whether they think you should consider the new portfolios as part of your investment strategy, at your next review (starting from March of this year).

In the meantime, if you would like more information about the thinking behind Profile's implemented solutions, please contact us for a copy of our detailed paper on objectives-based investing.

Disclaimer: This article is general information only and does not take account of any particular investor's objectives, financial situation or needs. Select Asset Management Limited is the responsible entity of the Profile Portfolio Solutions and issuer of the Profile Portfolio Solutions product disclosure statement (PDS). The PDS should be considered before deciding whether to invest or remain invested in any investment product. The Profile Preservation Portfolio and the Profile Accumulation Portfolio will be available to Profile's clients through the Macquarie Wrap Account and via a retail PDS with a $25,000 minimum investment. Expected launch date is April 2011. Investors should discuss their personal situation with their Profile planner and seek taxation advice before making investment decisions or changing their investments.

OUTLOOK 2011 - THE TOP FIVE THINGS I'LL BE WATCHING THIS YEAR…

By Jai Parrab, Head of Investment Research

Period returns to 31 December 2010

Asset class*	1 mth	3 mths	1 Yr
Australian shares	+3.8	+4.7	+1.9
International shares	+0.2	+2.3	-3.1
Fixed interest	+0.0	-0.2	+6.0
Cash	+0.4	+1.2	+4.7
Gold	+2.5	+8.6	+29.3

As 2010 drew to a close, the world economy was growing in aggregate, but true impetus was lacking. Global trade and manufacturing activity are both decelerating. The advanced countries remain patchy, output gaps remain wide and the legacies of the North Atlantic banking crisis are still painfully evident. Taking these facts together with governments' desires to consolidate their fiscal positions, and it is clear that easy monetary policy settings will be required for a considerable time yet.

The emerging world is also slowing, but factor utilisation levels are significantly higher than a year ago, capital inflows are generally strong, and in many instances policy now looks overly accommodative. Australia is caught between these two worlds and is consequently experiencing a multi-speed recovery that will challenge policymakers in the coming years.

Looking ahead to 2011 and beyond: while certainty may be the most valuable commodity in an uncertain world, nothing in life is certain, and markets are no exception...

1. THE GLOBAL V12 ENGINE THAT IS CHINA

China is in the midst of an economic rebalancing of the three core pillars of growth—exports, fixed-asset investment and consumption. The speed with which China has switched its focus back toward sustainable growth represents confident policymaking. It also reflects the recognition that the extreme investment surge that stabilised growth in the early stages of the global recession is not sustainable

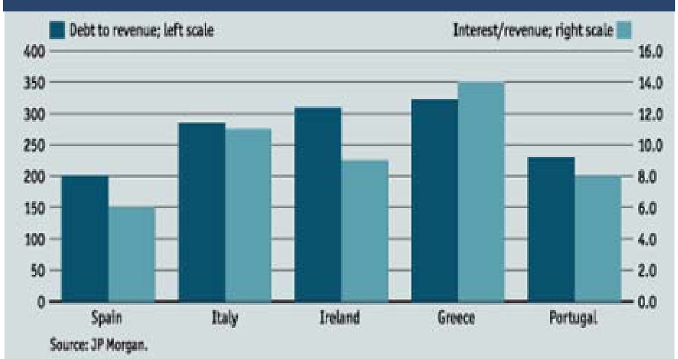
Although China's property market has attracted much attention, and wage growth has caused concerns that China may lose its competitiveness, overall the long-term structural story for investing in China remains robust. It continues to be supported by growing urbanisation and industrialisation, as well as by increasingly strong domestic consumption supported by rising wages.

Over the next few years, economic policy in China is likely to focus on structural reforms, with an occasional emphasis on shorter-term stabilisation as growth and/or inflation concerns arise. There will be increased emphasis on achieving more sustainable and better quality growth, along with an increased social focus. This is the long-term goal, but the reality is that markets tend to focus on short-term issues, and this is likely to result in ongoing volatility in equities, currencies, and investors' outlook for world growth prospects.

2. THE US & EUROPE – STILL 50% OF WORLD GROSS DOMESTIC PRODUCTION

The euro zone remains in crisis as investors question its viability as a currency union without fiscal and political union. The large debt burdens and loss of competitiveness affecting peripheral euro zone members have caused markets to lose confidence in their solvency and ability to grow.

EURO ZONE GOVERNMENT DEBT RATIOS



EU policymakers have introduced measures to protect the euro zone that would have seemed inconceivable just a year ago. These include large loans to Greece and Ireland, €750bn in emergency financing facilities, and substantial purchases of government bonds. But EU policymakers have so far failed to contain the crisis. Following Ireland's bailout in November 2010, concerns have shifted to Portugal and Spain. Bond spreads for Italy and Belgium have also risen, increasing the risk that these countries could experience funding difficulties. While short-term liquidity issues may appear to be somewhat under control, the long-term risk of insolvency remains.

In the US, congress has approved a second round of fiscal stimulus measures that should provide a boost to the economy in 2011, mainly in the form of higher consumer spending. However, the US economy remains plagued by structural problems that will constrain its growth rate. At this stage of a recovery from recession, an economy usually grows at a rate comfortably above its trend, as it puts idle workers and capital back to productive use. However the damage that has been done to households' balance sheets by the house price collapse means that recovery has been tepid. Job creation remains disappointing and, notwithstanding the recent improvement in retail sales, consumers still appear to be cautious.

The core of the problem with the US economy is the high indebtedness of the household sector. Debt levels are still high compared with disposable income and around one-quarter of home owners also are trying to work their way out of negative equity. House prices were down by around 30% on their 2006 peak in the third quarter of 2010.

The other worrying aspect of the US economy is its inability to create jobs. In December 2010 the unemployment rate stood at 9.4%, well above the 5% average in the decade before the financial crisis. The economy needs to create around 125,000-150,000 jobs a month just to keep up with growth in the working-age population; only once in the last seven months has this been achieved. Long-term unemployment remains a concern.

3. A DIVERGENCE IN POLICY MEASURES BETWEEN EAST AND WEST.

Between the second half of 2009 and the first half of 2010, the US recovery was driven by fiscal and monetary stimulus and by the end of destocking by companies. However, when fiscal support for the economy started to wane, autonomous private-sector demand proved too weak to generate a sufficient rate of job creation to bring down the unemployment rate. The administration has responded with a new package of stimulus measures. In addition to extending all of the Bush-era tax cuts, the package includes a 2% payroll tax reduction in 2011, a 100% tax deduction on purchases of business equipment and an extension of unemployment benefits for another 13 months.

As markets had already expected an extension of the Bush tax cuts, the measures are worth about US$300bn (around 2% of GDP) in extra stimulus, with most of the effect coming in 2011. The direct boost to the economy will be a good deal smaller, but it should be enough to prevent a significant slowdown in the economy next year.

One risk is that investors are spooked by the government taking on additional debt without explaining how it intends to set its finances on a more sustainable path in the longer term. The president's bipartisan fiscal commission has suggested ideas for narrowing the budget deficit, but so far has not reached a consensus on the correct approach. Moreover, the recent negotiations over the Bush tax cuts have shown how difficult it can be to raise taxes.

Yields on US government debt have risen since the announcement on fiscal stimulus. The rise predominantly reflects improved confidence in the economic outlook (which has reduced demand for US Treasuries as a safe haven) and fears of an imminent rise in inflation, but some investors may be worrying about the ability of the US government to service its debts.

Monetary policy has also provided massive support for the economy. The Fed announced in early November 2010 that it would pursue another round of QE, dubbed QE2, purchasing around US$600bn of US Treasuries by mid-2011. So far QE2 appears to have contributed to a rise in stock market prices, which has been influential in the improvement of recent economic data. Whether this is sustainable or not is a question markets are attempting to answer.

In the UK, British Prime Minister David Cameron is urging other governments to follow his country's efforts to cut costs and reduce debts, calling sovereign debt an obstacle to trade and growth. Cameron, whose Conservative-led coalition government has imposed a series of tax hikes and budget caps to reduce the country's debt, said that building up debts and keeping barriers to money and trade flows has made European countries their own worst enemies. He is also calling for more deregulation across the continent to help bolster recovery. However many Western European countries are only just embarking on deficit-reduction packages. These strict austerity measures have been imposed on them not only by their 'political' lenders, but also by bond market vigilantes driving a hard bargain.

Looking east, the ASEAN economies (Indonesia, Malaysia, the Philippines, Singapore, Thailand and Vietnam) have benefited from the strong recovery in global trade and strength of demand from China. Most have introduced massive stimulus programs, although the effects are beginning to fade. More recently, they have been boosted by capital inflows, which have raised some concerns about overheating and rising inflation. In 2011 they will be focused on rolling back fiscal stimulus measures, and tightening monetary policy, However they will be wary of the effects that higher interest rates will have on their exchange rates (which have already appreciated strongly since early 2009).

4. INFLATION, THE COUNTER-BALANCE

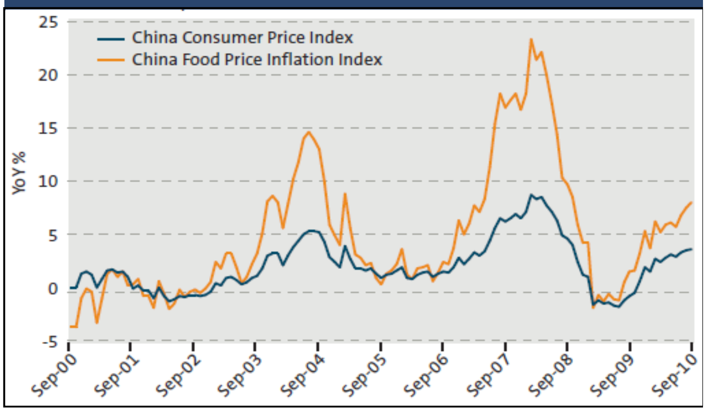
China's official inflation rate is 5% (at the consumer level). But some doubt the methods used to measure this, suggesting the real figure may be up to twice as high. China imposed price controls on food in mid-November to limit inflation. But those controls might be ineffective, as a drought in the north has damaged the winter wheat crop and frost has spoiled part of the vegetable harvest in the south.

Inflation is starting to slow China's exports, as buyers from Western multinationals balk at higher prices and cut back their planned spring shipments. Markups of 20 to 50% on products like leather shoes and polo shirts have sent Western buyers scrambling for alternative suppliers, although few low-wage developing countries can yet match China's manufacturing might.

In 2010 agricultural commodity prices benefited from the return of investor risk appetite and from weather-related disruptions to supply in many key producers. Prices are expected to remain strong in 2011.

A rebound in consumption growth, coupled with persistent OPEC supply constraint, will likely support oil prices in 2011. It is also likely that speculators will continue to invest in the market, given the ultra-low interest rate environment and uncertain outlook for other asset markets. However, relatively high global stocks and ongoing economic uncertainty will prevent significant price increases. Prices may in fact start to fall in the second half of 2011 owing to renewed strength in the US dollar and investors starting to factor in monetary tightening in 2012.

CHINESE INFLATION: to 30 September 2010



5. GEOPOLITICS, THE FINAL FRONTIER

At the time of writing (end January 2011), Egyptian protesters were camped out in central Cairo and vowed to stay until they had toppled President Hosni Mubarak. Six days of unrest has killed more than 100 people but the two sides have reached a stalemate. Protesters refuse to go, while the army is not moving them. The longer protesters stay unchallenged, the more untenable Mubarak's position seems.

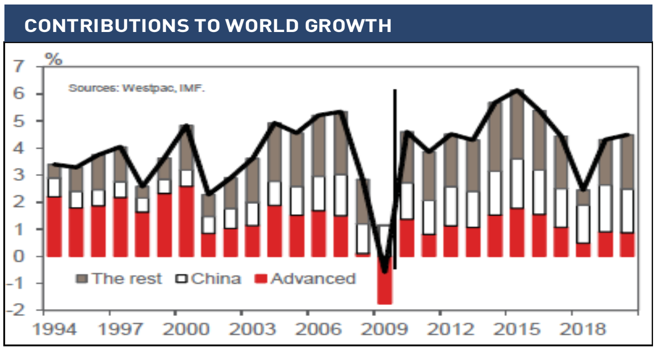
Looking at oil markets, heightened civil unrest is also expected in Nigeria in the first half of this year in the wake of their January 2011 election. Offshore output in Nigeria should grow, but this will be offset by lower production in the Delta region.

Tensions between the West and Iran over its nuclear program are expected to take more of a back seat in 2011 as sanctions cause economic hardship in Iran. However, other red flags remain in the Middle East region, with tensions rising in Lebanon, political instability in Tunisia and uncertainty surrounding the Saudi succession.

As austerity bites, Western Europe also faces increased protests and unrest in 2011 which is likely to hit markets and reduce governments' appetite for reform, but not affect policies dramatically. In some of the worst affected nations such as Ireland and Latvia, acceptance and even apathy has prevailed, while Greece has seen deaths and street clashes. Britain recently saw its worst clashes in two decades as students demonstrated over tuition fee rises. More unrest is expected next year as unions protest against much broader cuts.

IN SUMMARY

Despite continued strong forecasts for non-OECD countries (particularly China), in the developed world US policy cannot indefinitely support private consumption, nor can European short term-liquidity bandages convert insolvent nations into solvent ones. It's going to take a lot of hard work. We expect to see ongoing volatility in markets as investors attempt to wrestle with these facts. We remain pro-active in managing these risks, while maintaining adequate exposures to the growth centres of the 'new world'.



Additional sources and commentary: Bloomberg, T.Rowe Price, The Economist Global Forecasting Service, CNBC, Financial Times, JP Morgan and Westpac

STRONGER SUPER

By Kurt Ohlsen, Financial Planner

It has been over 20 years since compulsory (SG) superannuation contributions were introduced. Over this time Australia has accumulated over $1.3 trillion in retirement savings and established around 430,000 Self Managed Super Funds (SMSFs). While there have been many changes over this time, until recently there had been no comprehensive review of the overall super system's operation since its inception.

In May 2009 Jeremy Cooper (Chairman of the Review and former Deputy Chairman of ASIC) was commissioned to review the governance, efficiency, structure and operation of Australia's superannuation system. The Cooper Review handed down its 177 recommendations to the Government in June 2010. Now the Government has responded with "Stronger Super" – supporting 139 of the recommendations.

Below we outline some of the government's views in a few key areas. Remember, these changes are not yet legislated - however they are a strong indication of the changes the government plans to make. We will keep you posted as legislation is finalised.

SMSFs

Cooper recommended a number of changes to the SMSF sector.

Collectables and in-house assets

Most notable was the recommendation to ban investments in collectables and in-house assets. This was highly unpopular with Australia's art community, forcing a pre-election statement from Government that they did not support this recommendation. However I would not recommend rushing out and buying your favourite painting for your SMSF as yet, as tightened legislative standards are still proposed on how art can be stored and held. If the proposed standards are enacted, new investments will need to comply from 1 July 2011 and existing investments by July 2016.

Gearing

Gearing was once again in the spotlight, however there are unlikely to be any immediate changes. Cooper recommended a further review be carried out of this issue in two years to ensure that gearing is not becoming a significant part of superannuation.

Penalties

The ATO is to be granted greater powers to penalize SMSFs that break the rules, with a sliding scale to include monetary fines (payable by the trustees personally), criminal sanctions against promoters of early access schemes, and mandatory education for trustees.

The changes are expected to result in increased costs for the ATO and ASIC which will be offset by an increase to the annual SMSF levy, to come into effect in the 2010-2011 financial year.

Off-market transfers
Moving a personal share portfolio into your SMSF may soon come at an increased cost, as off-market transfers and contributions are to be banned. This will result in share brokerage costs that can currently be avoided.

Minimum pension drawings
If you are in pension phase and holding assets on the books at cost (quite common with property), you may be facing an increase to the minimum pension drawing as valuations will need to be done at net market value (rather than at cost price).

More training
On a positive note, minimum training standards for SMSF financial advisers will be introduced. From an advice and strategy perspective, SMSFs bring their own set of complexities and specialist training and experience is required to give good advice.

MySuper
Cooper recommended that a new super product, "MySuper", be created. The Government has strongly supported the recommendation.

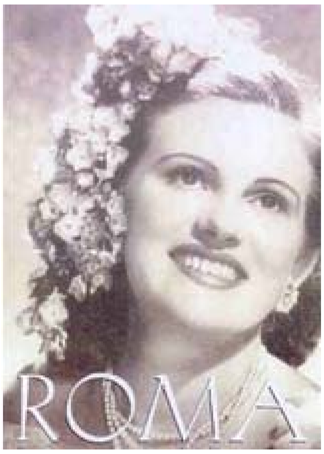
MySuper will be for those who do not want to take an active role in the management and direction of their superannuation. MySuper **will not** be a government provided super fund, but will be able to be issued by existing and new Superannuation providers. There will be a detailed and specific set of standards legislated for the product, covering fees, reporting, insurance, investment strategy and so on. The requirement for MySuper products to include Life and TPD insurance on an **opt-out basis** shows strong support by the Government to deal with the under-insurance problem faced by many Australians.

Once MySuper products become available (expected by July 2013), employers must make a MySuper product their default superannuation option.

Super Stream
The Super Stream recommendation addressed updating the "back office" of the superannuation system. It applies to APRA regulated (ie, non-SMSF) products. It supports online processing as well as using TFNs to identify members. For most people this should mean that it becomes easier and quicker to deal with your fund. The Government also expects significant efficiencies to be gained over the long term, ideally resulting in fee savings for members. The changes are expected to be phased in with most measures in place by July 2015.

One of the most frustrating things we regularly see as Financial Advisers is people's lack of trust in superannuation due to the ongoing "tweaking" of the system by government. This constant rate of change has resulted in some people avoiding super - in many cases to their own financial detriment. I hope the new Superannuation Minister Bill Shorten can hold true to his speech about the changes, made at the Moonee Ponds Bowls Club on 16 December 2010: "If this is done right, we in government can take our hands off the lever, and cease to fiddle with superannuation."

CLIENT PROFILE – ROMA BLAIR



Recently one of Profile's longstanding clients, Roma Blair, gave an inspiring speech to the women of Profile. Her life story is an amazing tale of courage and persistence in the face of adversity.

Roma was referred to Profile by a relative. She has been a client of our firm since 1997.

Things started off well - she was born (in Malaysia in 1923) with a caul, traditionally supposed to be a sign of good luck. However after moving to Australia at a very young age she had many problems at school, being a dyslexic at a time the condition wasn't recognized. She left at the age of 13 and started modeling. At 17 she fell in love with a beautiful man who shared her love of dancing. Soon they were married by proxy (Roma was the first Australian bride to marry this way) and Roma moved to Indonesia, where her new husband Leo's family had a Persian carpet business.

The war came, her husband was called up, and shortly afterwards the Japanese arrived. Roma was taken prisoner (after a spirited attempt to escape by jumping out the window!) and, 3 months pregnant, Roma was interned in a prisoner of war camp. She had a terrible time in the camp where food was scarce and hard physical labour was the order of every day. Roma became so ill that at one stage she was coughing up worms, and was unable to breastfeed her son Arnold when he was born. Far from discouraged, she obtained powdered milk from the Red Cross to feed her son and bargained secretly with locals to obtain food. However she was betrayed and caught, and subsequently suffered terrible mistreatment.

We wanted to know how Roma got through this and managed to remain sane! Roma tried to explain her mental resilience to us – how she used to visualize dancing while in solitary confinement, for example – but we still could not really comprehend how she managed it, and were left in sheer awe and admiration at her toughness and spirit.

The war finally ended and Roma has had many adventures since!

For many years Roma was a well-known TV personality, hosting the popular TV yoga show "Relaxing with Roma" on Channel 9 from 1958, which ran for 14 years. She also taught yoga at the June Dally-Watkins School of Deportment. Yoga has been a passion of Roma's throughout her life, and she credits yoga with her recovery from health issues she suffered after being a prisoner of war.

She was initiated in the Bihar school as Swami Nirmalananda (the first female Australian swami), founded the International Yoga Teacher's Association (IYTA), and is still able, at 87, to perform this 'seated splits' pose: (the lady pictured is not Roma)

She has been married three times (twice to Leo) and is now blissfully in love with a glamorous man named Dayal who she first met in the 1960s. On her last trip to see him in Singapore mid last year, she took no less than 16 outfits with matching shoes and handbags!

We were enthralled throughout Roma's talk and continued to question her relentlessly over lunch afterwards. Her advice we remember most was, to seize the day! This is a mantra Roma is certainly abiding by as she crams her life with experiences and lives each day to its full.

Roma Blair at the races (Magic Millions Luncheon, 2011)

GETTING TO KNOW OUR TEAM AT PROFILE – Rod Bowen

Paraplanner

Rod has had a lifelong interest in and passion for understanding financial analysis and markets. So after a solid career in civil engineering and property development he decided to change careers, studying to complete a Diploma of Financial Planning.

He worked for a number of years as a financial planner and as general manager with another boutique financial planning firm in Sydney, prior to joining Profile Financial Services in 2008 as a paraplanner. He is now also Profile's compliance manager.

Rod's role at Profile includes research, analysis and modeling of individual clients' financial positions to produce written advice. He draws on technical knowledge and expertise to ensure that each client receives advice that is best tailored to their unique needs.

Rod's strengths are in the technical detail and mathematics required to be a good paraplanner. He is driven by the desire to help others in this complex area.

He is also responsible for implementing the programs that help to ensure Profile staff are knowledgeable about and compliant with the huge amount of government legislation that regulates our industry.

Rod is kept busy outside of work spending time with his young family. He is married to Kim and has three children aged from 3 months to 6 years of age.

His personal interests include swimming and snow skiing. Having completed his university degree he enjoyed six months working in Japanese ski fields, and he has recently set to learning the pitfalls of swimming pool maintenance (who knew how complex it could be)!

He holds a degree and Masters in Engineering as well as a diploma in Urban Estate Planning from the University of Technology, Sydney. Rod also holds a Diploma of Financial Planning from Kaplan.

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