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FINANCIAL SERVICES PTY LTD

Timely Tips

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Did you know?

The latest statistics released by APRA show the impact on Superannuation funds of the decline in investment markets over the past six months.

The total invested in Superannuation in Australia as at the end of March 2008 was \$1103 billion, a drop of \$75 billion over the quarter.

Source: APRA Quarterly Superannuation Performance – Release 26th June 2008



Investing for Income

During times of volatility in investment markets many investors may be tempted to cash out their investments and move to more conservative assets such as cash, term deposits and fixed interest type securities. By cashing out investments at times when the markets are in turmoil simply results in “paper losses” being crystallised.

When we invest we are generally looking to achieve one of a number of possible outcomes. We are looking to generate income in order to meet or supplement day-to-day living expenses, we may be after capital gains, or perhaps we are seeking a combination of some capital growth supported with some income.

Different stages of life may dictate the type of result we are seeking. For example, a wage or salary earner may not need additional income from their investments so capital gains may be their main focus. However, a retiree may be far more interested in generating a regular income stream.

What is the difference between income and growth?

When we lend money to someone (a company or an individual) we generally expect them to pay “rent” for the money we have lent them. That “rent” may be in the form of interest, dividends or distributions. It is the compensation we receive for lending our money.

However, when we buy (property, shares, managed funds) we are hopeful that, over time, our investment will also grow in value.

If we require a regular income from our investments then we need to be focussing on income producing investments. If a need is for a regular income, and we only invest in investments that target capital growth, we will have to be continually selling down out investments in order to generate the cash we require. Quite a complex process.



Types of income

Interest is the return we receive when we lend our money to others. Interest may be derived from private loans but more likely it will come from bank deposits. These deposits may pay a variable rate of interest (that is, the rate we receive moves up and down with broader interest rate movements), or we may receive a fixed rate of return for a set period of time – such as is paid for a term deposit. In general terms, the more risky the loan, the higher the interest we are likely to receive.

Interest bearing investments do not generally have the capacity to produce a capital growth or loss. Certain fixed term government securities and company loans may have exposure to capital movements where the investment is withdrawn prior to the end of the investment term.



Rent is the regular income we receive from property investments. Whether it is residential or commercial property, our tenants pay us a regular income for the use of the property. In addition to rental income, property investments will hopefully provide a capital gain when the property eventually sells.

A **dividend** is the income we receive when we invest in shares. By investing in shares we own a portion of the company we are investing in. As an owner of the business, we are entitled to a share of the profits the company makes. Companies generally pay dividends twice each year. Dividends will vary in line with the profitability of the specific company and are set by the company's board of directors. During difficult times, dividends may be suspended and are not paid to shareholders.

Distributions are paid by managed funds. Many investors choose to invest in managed funds rather than holding shares or property directly. As managed funds invest in a range of assets including shares, cash and property, the manager of the fund receives income from the underlying investments. Fund Managers simply pool this income and, after deducting their fee for managing the fund, pay the proceeds out to investors in the form of distributions. Depending on the type of managed fund, distributions may be made monthly, quarterly, half-yearly or yearly. Distributions may also include capital gains made by the manager from the sale of the underlying assets that the managed fund has invested in.

When setting an investment strategy, it is important to understand what our objectives are. Are we looking for income, capital growth, or a combination of both. Part of the investment process involves getting this mix right to ensure that our investments are delivering the results we need.

Source: Peter Kelly - Professional Investment Services.



Time to Review your Pension Income

The increasing popularity of Superannuation has seen a significant increase in the number of Australians drawing income streams from their Superannuation fund to provide for both retirement and pre-retirement income needs.

Many readers will be familiar with Allocated Pensions. First introduced in the late 1980s, allocated pensions provide Superannuation investors with the opportunity to draw a flexible income stream from their Super whilst enjoying favourable tax treatment. Things got a whole lot better from 1st July 2007 when Superannuation pensions (paid from a taxed Superannuation source) became tax-free for those aged 60 and over.

One of the popular features of the allocated pension was a person could decide on the level of income they wish to draw.

There are parameters in place that dictate the minimum and maximum levels of income that can be taken each financial year and these are determined as at 1st July each financial year, based on the member's pension account balance and their age as at 1st July.



From 1st July 2007, a new type of Superannuation pension was introduced - The Account Based Pension. An account based pension operates in a similar manner to an allocated pension with a couple of notable exceptions.

Whilst there is a prescribed minimum level of income that must be drawn each year, where a member is aged 65 or over, or if under 65 has met a "condition of release" (e.g. they have retired), then there is no restriction on the maximum amount of income that must be taken.

However, for those aged under 65 and have not yet retired - that is they are drawing a pension under the "transition to retirement" rules, the maximum income they can draw in a financial year is limited to 10% of their account balance.

Because the pension income rules for account based pensions are more flexible than those applied to allocated pensions, many Superannuation funds have transitioned their allocated pension members to the new rules.

As we are now in a new financial year, it is time to give thought to the pension income you will need to draw during the coming year. If you are a member of a public Superannuation fund, you can expect to receive correspondence from your fund advising you of the minimum level of income you need to draw (and maximum where applicable). However, if you run your own self-managed Superannuation fund, as trustee of the fund, you will need to determine the appropriate levels of income and implement the appropriate payment level. Your accountant, financial planner or administration service should be able to assist you with this.

Source: Peter Kelly - Professional Investment Services.

About our services:

We provide financial strategy advice and assist in implementing the appropriate financial plan for you, via a wide range of services and investment structures.

Services & Strategies we offer include:

- Investment & Estate Planning considerations
- Retirement Planning
- Financial Strategies
- Financial Structures
- Self Managed Superannuation Fund strategies & legislation
- Asset Protection
- Personal & Group Insurance
- Savings & wealth creation strategies
- Divorce & Separation strategies
- Business Succession planning
- Superannuation

Contact your adviser at:

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