

FROM THE MD'S DESK



BRAD MARTYN

What a difference a year can make. While there is no guarantee that the global economy is totally out of the woods yet, most indicators are suggesting that a solid turnaround is underway. This is in total contrast to the outlook 12 months ago, when the world was completely engulfed in doom and gloom. As mentioned in the past, the share market is generally a leading indicator, usually changing direction somewhere between six and 12 months before the economy does. This has happened again, with the Australian share market rebounding significantly, despite the real economy not looking particularly strong. The Dow Jones in the USA has also recovered significantly despite the US economy having experienced a much deeper and longer recession and facing a less positive outlook.

The difficult issue that Governments face is deciding how quickly they start winding back the substantial financial stimuli currently in place and when, and by how much, they increase interest rates. The risk of too much too soon is that economies could slip back into recession, whereas waiting too long risks further bubbles and booms.

One of the biggest impacts of the global financial crisis on investment portfolios was the substantial fall in interest rates, which in most cases significantly reduced the level of income that portfolios have been generating. Governments around the world took the unprecedented action of slashing interest rates in an attempt to avoid falling into recession. The Reserve Bank of Australia has confirmed that rates were set at "crisis" levels (3% in Australia) and will return to "normal" levels once the RBA is satisfied that Australia is out of the financial crisis. As such, it is not unreasonable to expect that rates may increase to between 5% and 7% over the next few years. This in turn will assist portfolios to generate a more attractive level of income. Investors who are worried about over-drawing through this period of lower income levels should discuss it with us to determine if the impact on the portfolio is likely to be temporary or permanent.

While the worst of the crisis may now be past, we continue to encourage investors to contact us if ever they have any concerns or queries. We are working for you and prefer you to discuss things with us rather than you worrying about them. ■

*'Price is what you pay,
value is what you get.'*

Warren Buffett

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STOP PRESS

Over Contributing Can Be Taxing

With recent changes to the limits on superannuation contributions, investors need to be aware of the significant penalties that can result from exceeding the limits. Until June 2007 there were limits on how much you could withdraw from super without incurring significant tax penalties. Since then the limits on withdrawals from super have been removed, but limits on contributions have been introduced.

The current limit on concessional (before tax) contributions is \$25,000 per annum for those under age 50, and \$50,000 per annum for those 50 and over. For non-concessional (after tax) contributions the limit is \$150,000 per annum. However, anyone under 65 can use a three year averaging provision and bring forward up to two future years' contribution limits permitting up to \$450,000 of non-concessional contributions in the one year. But, no further non-concessional contributions can be made for the following two years.

The penalty for exceeding the limits can be severe, even if it is made in error, as the tax rate on the excess is 46.5%. Because of the complex manner in which the averaging rules are applied, a simple or even a logical mistake can result in a very large unexpected tax bill.

If you are planning on transferring significant sums of money or assets to super (for example you have sold a rental property and have surplus funds) please seek professional guidance. ■



PAUL BEGLEY

INCOME FROM SHARES

When assessing investments it is important to understand that the return on every asset has two dimensions: capital value and income. Many investors have a tendency to focus solely on the current value of their investment against its purchase price. This obsession can completely ignore a significant part of the overall return – income – and can give a very distorted view of the potential return from the asset.

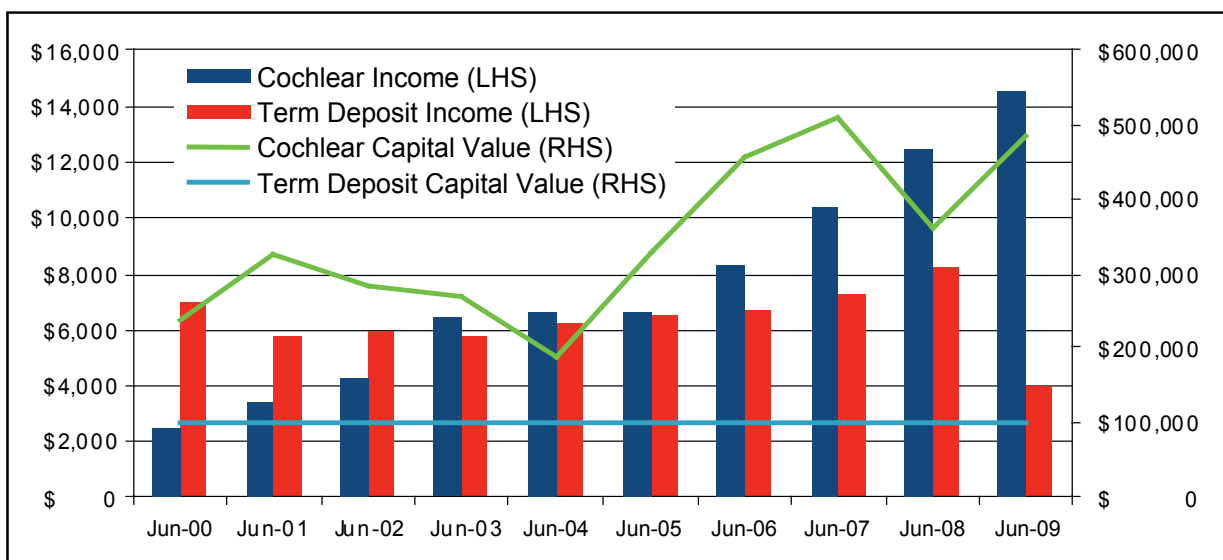
While it is easy to focus only on the capital value of your investment and its short term fluctuations, it is important to remember that a good long-term share investment should also provide a stable (and growing over time) dividend income. By comparison, capital stable investments such as term deposits usually offer only an income stream and provide no potential for capital upside.

The table and graph below illustrate a hypothetical scenario where two investments of \$100,000 are made on June 30, 1999: one in Cochlear Ltd shares and the other in an Australian 12 month term deposit (which is automatically rolled over for a further 12 months whenever it matures).

| Date | Cochlear | | | Australian 12-Month Term Deposit | | |
|--------------|------------------------------|---------------------------|--------------------|----------------------------------|---------------------------|--------------------|
| | Current Yield on Cost (% pa) | Income Distributions (pa) | Capital Value (\$) | Current Yield on Cost (% pa) | Income Distributions (pa) | Capital Value (\$) |
| 30-Jun-00 | 2.50% | \$ 2,501 | \$ 239,727 | 7.00% | \$ 7,000 | \$ 100,000 |
| 30-Jun-01 | 3.42% | \$ 3,418 | \$ 325,104 | 5.75% | \$ 5,750 | \$ 100,000 |
| 30-Jun-02 | 4.25% | \$ 4,251 | \$ 283,841 | 6.00% | \$ 6,000 | \$ 100,000 |
| 30-Jun-03 | 6.42% | \$ 6,419 | \$ 269,253 | 5.75% | \$ 5,750 | \$ 100,000 |
| 30-Jun-04 | 6.59% | \$ 6,585 | \$ 189,394 | 6.25% | \$ 6,250 | \$ 100,000 |
| 30-Jun-05 | 6.67% | \$ 6,669 | \$ 326,771 | 6.50% | \$ 6,500 | \$ 100,000 |
| 30-Jun-06 | 8.34% | \$ 8,336 | \$ 455,396 | 6.75% | \$ 6,750 | \$ 100,000 |
| 30-Jun-07 | 10.42% | \$ 10,420 | \$ 508,496 | 7.25% | \$ 7,250 | \$ 100,000 |
| 30-Jun-08 | 12.50% | \$ 12,504 | \$ 361,532 | 8.25% | \$ 8,250 | \$ 100,000 |
| 30-Jun-09 | 14.59% | \$ 14,588 | \$ 485,989 | 4.00% | \$ 4,000 | \$ 100,000 |
| TOTAL | 75.69% | \$ 75,691 | | 63.50% | \$ 63,500 | |

Over the ten year investment period a term deposit provided interest income of \$63,500 in contrast to the Cochlear investor who has received about \$75,700 in dividend income. Also, the latter excludes the value of the attached franking credits which significantly enhances the value of Cochlear's dividends.

Not only did Cochlear's dividend income stream grow over the period, but so too did the investor's capital value. A steady rise in profits in addition to growing dividends commonly results in a general rise in the company's share price over the longer term. Cochlear is no exception. This compares with an unchanged capital value for the investment in term deposits.



While recognising the importance and necessity of capital stable investments, such as term deposits in a well diversified portfolio, it is valuable to understand that well-managed companies that achieve sustainable profit growth over the longer term should provide a growing level of dividends to investors. This should also result in an increasing share price over the longer term. ■



SCOTT STANLEY

A GUIDE TO SALARY SACRIFICING

Sacrificing some of your salary to super can be a very tax-effective way to increase your retirement savings. The amount you sacrifice is deducted from your assessable income and may reduce your total tax liability.

Instead of paying tax at your marginal tax rate (of up to 46.5%), when you salary sacrifice your pay to super it becomes a taxable contribution received by your super fund. The contribution (plus any future income earned from the investment) is generally taxed at a maximum rate of 15%.

Example

Joan is 52 and earns \$100,000 per annum plus 9% superannuation and is considering sacrificing \$20,000 of her salary to her super fund. The table compares her current strategy with a \$20,000 salary sacrifice strategy.

| | No Salary Sacrifice | \$20,000 Salary Sacrifice |
|---------------------------------|---------------------|---------------------------|
| Salary (pre tax) | \$ 100,000 | \$ 80,000 |
| Tax on salary | \$ 26,950 | \$ 19,050 |
| Salary (after tax) | \$ 73,050 | \$ 60,950 |
| Super contributions | \$ 9,000 | \$ 29,000 |
| Tax on super contributions | \$ 1,350 | \$ 4,350 |
| Net salary + net super benefits | \$ 80,700 | \$ 85,600 |
| Total tax paid (salary & super) | \$ 28,300 | \$ 23,400 |
| Total tax saved | - | \$ 4,900 |

Joan's annual take home income is \$12,100 less, but her net annual super contributions have increased by \$17,000 and her overall annual package increases by \$4,900 (the amount of tax she saves). Over the long term, this strategy has clear benefits for Joan and gives a huge boost to her super for when she retires.

Things You should Consider

If you are under 55, don't salary sacrifice funds you think you may need before you retire. If you're younger, it may be more beneficial to pay off non-deductible debt (such as your home loan) instead.

If you are over 55, the reverse may be true. Generally, salary sacrificed funds will have been taxed at 15% and once you retire and are over 60 you can access the funds tax-free and pay off outstanding debts. Make sure you have a written agreement with your employer before making the contributions.

Limits on Salary Sacrifices to Super

Because of the generous tax concessions, the Commonwealth Government restricts concessional contributions (which include superannuation guarantee, salary sacrifice and personal deductible contributions).

An employer can contribute to super on your behalf and claim a tax deduction for an unlimited amount, but if you are under 50 and your concessional contributions exceed \$25,000 in a year, you will pay tax at 31.5% (in addition to the 15% tax paid by the super fund) on the excess. You will receive the tax bill, but you'll be allowed to withdraw money from your super to pay it. If you're 50 or older at any time prior to June 30, 2012, your concessional contribution limit is \$50,000 (instead of \$25,000) before excess tax is charged. The \$50,000 limit applies in each financial year you're over 50 until June 30, 2012, when it reverts back to \$25,000.

If you want to investigate salary sacrificing further, it is important that you seek assistance from us to ensure you are aware all of the implications. ■

REFERRAL

Do you know someone that would benefit from Alliance's services?

We sincerely thank all of our clients and business associates who have referred potential clients to us. These referrals represent a very real vote of trust in us.

If there is anyone else you think would benefit from using our services, please feel welcome to refer them on to us. For example, if you are aware of someone who either doesn't have the time or perhaps the expertise to manage their financial affairs, or needs investment and strategic advice to structure their affairs in the best possible way, we would appreciate the opportunity to discuss our services with them.

As a further thank you to existing clients, we provide a rebate on your fees for any referrals that become clients. ■

PROFILE FIVE MINUTES WITH JAN WILLIAMS



1. Marital status:

Very happily married to Brian for 39 years.

2. Children:

I have two wonderful daughters, Jodie and Alison, and two terrific sons-in-law, Shayne and Richard. I have two beautiful grandchildren, Aiden (8) and Aimee (6) and am looking to increase this number in the future by way of Alison and Richard who are now residing in Sydney (not happy Jan!).

3. Place of birth:

Born at the South Perth Community Hospital many moons ago and lived in South Perth until I was married.

4. Favourite holiday destination:

Loved New Zealand, but happy to go anywhere. Had a wonderful time a few years ago when in Brunei and was lucky enough to be there to see the Royal Wedding cavalcade pass in the gold-plated stretch Mercedes. Aspire to travel to all the wonderful exotic places that Alliance clients come home from.

5. Favourite food:

French and Italian plus crabs fresh from the pot.

6. Best way you relax:

Reading a good book, walking along the beach and the odd glass of red.

7. Hobbies/interests:

Sewing and knitting – keen to try at anything crafty, (made Aimee a dolls cot last year for Christmas – love power tools). Also play a good game of pennant squash (just ask Peter).

8. Something people may not know about you:

I am a keen West Coast Eagles member and attend all of their games - rain or shine (though I have avoided buying the sequined cap!). We have recently bought a caravan and have grand future plans for seeing our beautiful country. This year I have increased the plantings in my vegetable garden – nothing quite like walking out the back door to pick something for dinner. ■

WHO TO CONTACT AT ALLIANCE

Jan Williams
General Queries

Peter Eastman, Steven Hendry or Your Adviser
Investments or Financial Planning



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