

## FMD In The Community



FMD Sydney supports the fund raising activities of the Rotary Club of Sydney Darling Harbour (RCSDH). Some of the projects include Project Dignity in India, The Station 'drop - in centre' and clean water for a Fijian school. John D'Alessandri, a planner/director in the Sydney Office is President Elect of the RCSDH. John is encouraging men and women to consider joining Rotary. Contact John for further details or visit [www.rotanet.com.au/sdh](http://www.rotanet.com.au/sdh)



Say Hello to FMD Sydney's newest family member, Erica Chai.

## And baby makes 4...

We offer our congratulations to proud parents Penny and Graham Chai on the safe and happy arrival of baby Erica born on 25th July at 10.49pm. Erica weighed in at 3.245 kg and was 48cm long. Erica is Penny and Graham's 2nd daughter and Serena's little sister.

We hope that Penny and Graham get some shut eye with their little treasures waking one another with their crying. Here's to more precious moments, love, laughter and happiness in the Chai household.



## FOX SPORTS TIPPING WINNERS

Congratulations to **John Masters** and **Gary Priest** 1st place winners of the 2007 AFL Premiership Season Footy Tipping Competitions. FMD would like to thank all tipsters. It was an interesting season with many tipsters picking 8 in a round. Please contact your state office for details on how to join the 2008 tipping competition.



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# NEWS

## Testing the Resolve

The September quarter for investments has been an interesting experience, with the magnitude of movements in investment markets testing the resolve of all investors and advisers alike.

The All Ordinaries Index closed at the end of June 2007 at 6,310 points, yet by the middle of August the All Ordinaries Index reached a closing low of 5,670 points, a decline of 11% in 6 weeks. Interestingly, on the 17 August, a computer failure at the Sydney Futures Exchange caused mayhem on the Australian share market with the market falling in excess of 300 points intraday before closing down 70 points for the day at 5,670. Yet by the end of September, a mere 6 weeks later, the All Ordinaries had reached an all-time high of 6,600 points, some 16% above the low point in August.

In addition to the movement in equity markets the wholesale debt and credit markets have experienced a crisis never before seen by many fixed interest traders in their lifetime. This has resulted in the failure of a number of mortgage origination businesses in the United States and substantial issues for RAMS home loans in Australia and Northrock PLC in the United Kingdom.

These issues, coupled with the constant information available to the investing public through the media, often provide an overload of information that is sometimes difficult to put into perspective.

So, what does this all mean to an investor?

The most important message is to maintain your resolve. The preceding events I described have happened in the last 90 days and by maintaining investment strategies during volatile times we find ourselves in an environment where the Australian economy continues to maintain its strength, corporate Australia continues to produce record profits, and investment markets have once again stabilised. All investors need to understand and accept that investment markets will have periods of time when market movements are larger and sometimes more uncomfortable than normal. However, using a diversified

investment strategy and maintaining these positions during the uncomfortable times will ultimately reward investors for their patience.

Dr Shane Oliver, in his monthly brief to markets 'Oliver's Insights', reminds us that October 2007 is the 20th anniversary of the famous October 1987 share market crash. He says "while the anniversary itself has the potential to create jitters, the current situation in share markets is very different to that before the 1987 crash. Share price gains and valuations have been much more reasonable this time around."

The table below provides a detailed analysis of the Australian share market comparing the state of play in September 1987 and September 2007.

Australian Shares	87	07
Prior 12 Month Share Price Gain %	88.4	29.6
Prior 4 Year Price Gain % PA	34.0	20.1
Prior 12 Month Profit Growth	24.5	14.7
Prior 4 Year Profit Growth % PA	15.5	25.0
Historic PE Times*	20.4	16.2
Prior 10 Year Average of PE, Times	11.0	20.7
Forward PE Times*	15.8	15.4
Prior 10 Year Average of Forward PE	N/A	15.3
Inflation %	8.5	2.7
10 Year Bond Yield %	12.5	6.2
Forward Earnings Yield Less Bond Yield %	-6.2	0.3
Dividend Yield %	2.5	3.6
Dividend Yield Less Inflation %	-6.0	0.9

Source: Thomson Financial, AMP Capital Investors

The data reiterates our view that the Australian economy and corporate Australia are still in a very good position going forward.

In closing, FMD would like to wish all our clients a safe and prosperous period leading up to the forthcoming Christmas and holiday season.

FMDfinancial  
Delivering strategic financial advice & innovative solutions



# WHAT WE DON'T KNOW WILL HURT US



The recent machinations on global equity markets were a long overdue reminder that it is the unknowns – the ones we don't know – that matter.

Financial markets, far from being 'perfect' and rational, by always anticipating the events which move them, are in fact highly imperfect and irrational. Moreover, financial markets are very different to goods markets for two main reasons.

The first is that supply does not simply adjust to changes in demand.

In goods markets, a sharp fall in demand can produce a fall in prices and then supply. But in financial markets, as we saw recently, a sharp fall in share prices does not see a sharp fall in supply.

This is because financial markets, unlike goods markets, really do not have a supply side, as the majority of trades involve the exchange of existing, second – hand shares.

The second main difference between goods and financial markets is that when one buys a good it is much easier to place a value on a good than a financial product, because one only has to decide what the good is worth to you now.

With a financial product, you have to decide what the product will be worth to someone else, some indefinite time into the future.

In other words, by their very nature, financial markets have much more uncertainty and thus, not surprisingly, much more volatility.

Human beings thus have no choice but to try and work out what their fellow investors are going to do – and then try and follow the herd.

The trouble is most other members of the herd do not have any more information and certainty than any other herd members.

Yet, as we have seen in recent years, rising markets encourage herd members to think that some members in the herd must know something they don't and they thus join the stampede.

They adopt a 'safety in numbers' approach. But like lemmings, what they think is the right thing to do because many others are doing it, can turn out to be disastrous.

Conversely, falling markets can produce panic sell – offs, which greatly exacerbate price falls.

In short, investor sentiment is very much a product of changes in perceived market 'moods', which are not based on anything like perfect knowledge or certainty. Hence, the wild swings in financial markets.

Uncertainty has also been increased by the greater use of much more sophisticated financial instruments: for example, securitisation.

This refers to the practice of bundling sub-prime mortgages, which are loans to less credit-worthy

borrowers, into separate securities that are then assigned a rating by an agency and resold to investors around the world.

However, the risk profiles of such instruments are very difficult to determine, even by the most experienced ratings agencies.

Last month's disclosure of previously unsuspected levels of risk in US housing loans, which set off the sharp equities fall, was a good example that the key 'facts' are often hidden from even the most sophisticated market players.

Uncertainty is also worsened by the fact that investors – and their advisors – also have far from perfect memories.

For example, last month's credit crunch had plenty of precedents.

We had one spurred by high-yield bonds in the late 1980s, followed by the savings-and-loan crisis of the early 1990s, the Long-term Capital Management fiasco, the Asian crisis in 1997 and 1998, and the bursting of the Internet bubble in 2000 and 2001.

Indeed, we should expect one every five to 10 years, if recent history is any guide.

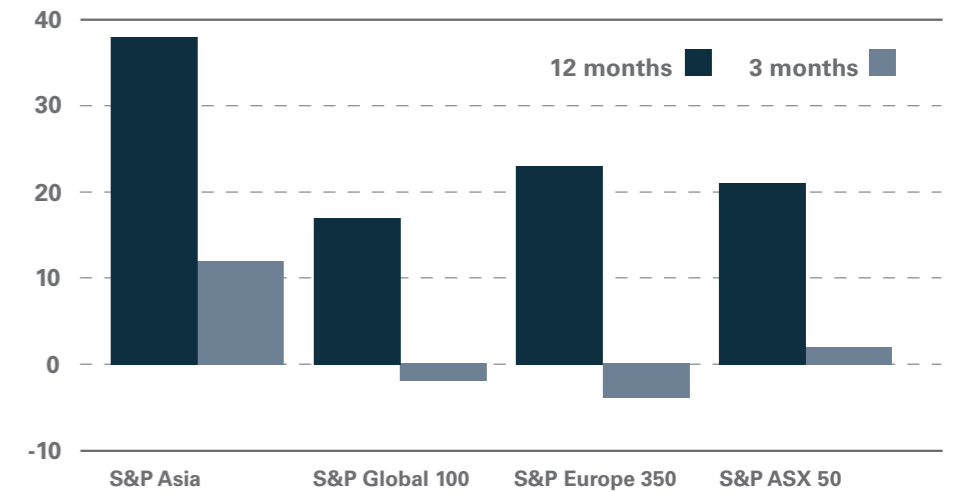
In short, last month's sudden disclosure of the extent of risky lending in the US, which

## Uncertain markets: volatile returns. Index total returns, cash dividends re-invested, \$US

forced lenders to re-assess risk profiles and raise interest rates, was a salutary and overdue reminder of the key importance of uncertainty in all financial markets – something which is simply forgotten by most investors during periods of prolonged upswing.

Most importantly, it was also a reminder of three key things in a world of great uncertainty: the dangers of 'short-termism' – of making investment decisions based on the latest headlines from the financial pages – of the need to hold a diversified portfolio, and of the attractiveness of indexed funds.

*Source : Dr David Clark - Vanguard*



## Questions & Answers

John D'Alessandri – Financial Planner (Sydney)

**Q: I'm 56 and still working on a salary of \$120,000, with a superannuation benefit of around \$500,000. I'd like to build my retirement savings more quickly but have other commitments to meet like the kids' education. How can I better organise my finances to achieve this?**

**A:** A lot of people put off accumulating money for retirement because they have other major commitments like the mortgage and the kids' education. Normally expenses like these are paid from your after-tax income. However, if you take advantage of salary sacrificing and accessing your super via a 'transition to retirement' pension, which could potentially pay for these expenses in a much more tax effective way, boosting your super and meeting your commitments without a major impact on your cashflow.

**Q: I've heard about 'transition to retirement' pensions but I thought I couldn't touch my super until I had retired, and in any case I'd be concerned about drawing down on my super this early... shouldn't this be set aside for retirement?**

**A:** That's where combining a salary sacrifice strategy with a 'transition to retirement' pension can deliver the best of both worlds...you can cover off on all your existing commitments, yet build your super at an ever increasing rate. The 'transition to retirement' rules, which were introduced in July 2005, allow people over 55 to access their super while still working.

Before that you couldn't access your super until you had retired or reached age 65, whichever occurred first, so the new rules provide a lot more flexibility.

And while the strategy involves drawing down on your super early, it is offset by you salary sacrificing an amount from your existing salary into your super fund, so that your super ends up growing at a faster rate.

**Q: It sounds too good to be true, can you explain a little more how this works?**

**A:** First, we would look at rolling over some of your existing super into a 'transition to retirement' pension. This is also called a 'non-commutable' income stream, which pays you a regular income between minimum and maximum limits, but doesn't allow you to withdraw a lump sum. You can use this extra money coming in to pay expenses, freeing up your finances so that you have more money you can save and put into super via salary sacrifice. And because salary sacrifice uses pre-tax dollars you can actually contribute more to your super than you withdraw by way of the pension, without seriously affecting your cash flow.

The strategy becomes even more attractive upon turning age 60 when pension payments become fully tax free. But for anyone over 55 with a reasonable sum invested in super, a 'transition to retirement' strategy may be a very attractive option.



## Staff Profile

Daniel Arcadiou

Financial Planner (Adelaide)

Daniel has worked in the financial planning industry since 2002, completing his Diploma of Financial Planning through Deakin University and has recently obtained CFP status by completing the Certified Financial Planning Certification Program.

Daniel has recently joined the Adelaide practice upon moving from Melbourne to live with his fiancé, and is looking forward to spending less time in traffic and more time on the golf course.