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## Australia and The Economic Crisis

(Time of writing, 16th June, 2009)

by Paul St. Clair, F.C.A., Dip. Fin. Services

Australia like many countries was not involved in creating the current Global Financial Crisis (GFC). Being part of the global financial system, and a large trading nation, Australia found itself caught up in this crisis in the same way as countries in the Asian area were, drawn into the crisis after it was established in the USA and Europe.

The economic fundamentals in Australia at the time the crisis hit were excellent. Australia was experiencing a mining boom and near full employment. Also the high interest rates experienced as a result of boom conditions are now allowing plenty of room for Australia's economic managers to adjust to new economic conditions. The Federal and all six State Governments had no borrowings and all operated on surpluses. As well, a large sovereign fund had been created by the former government. Exports and imports were powering upwards. Some improvement was being achieved on Australia's international balance of payments which, although large, was well contained. The Australian Stock Exchange (ASX) prices were, in general, of fair value. Businesses were operating well and our banking system was, and is, strong and well regulated. Regulation in many advanced economies 'plays catch up' and their regulators either lack the money or the will to enforce it, which is mostly not the case with Australia's banking regulators. Australian banks were not involved in sub-prime debt. Australia's economy was efficient with good fundamentals.

When the crisis hit the USA and Europe, every day brought bad news. The crisis started to unfold at an alarming rate. The lowest point seems to have been reached on the weekend of 14th September, 2008 with disastrous news from Lehman Brothers, Insurance America Group (IAG) and others.

At this early stage of the crisis in Australia, fear, the crisis of confidence and the freezing of credit from overseas, dominated. World leaders including Australia's own acted promptly and at this point, their actions would seem to be working. The Reserve Bank of Australia has borrowed some \$US20 billion from the Federal Reserve in the US. Interest rate reductions have been made by the Reserve Bank and the Federal Government has undertaken stimulus packages, infrastructure spending of \$22 billion over the next four years, and taxation incentives on a scale not undertaken previously. Unemployment is on the rise in Australia and has now climbed to 5.7 percent and estimated to peak next year at about 8.5 percent. Incomes are falling as people work less overtime, contractors are cut back, and workers are retrenched.

Whilst some twenty-three countries in the world are in recession or depression, Australia has managed to avoid recession at this stage. It was thought that Australia may be in recession in the March, 2009 quarter but trade data recently released unexpectedly showed the best balance of payments figures in 50 years. A few days later the National

Accounts figures reported that the economy grew at 0.4 percent for the March, 2009 quarter. Some authorities say avoiding a recession so far is an aberration and that Australia is likely to slip into recession later this year. Whilst economics is not a science, there are at least two things we can be sure of: first, the world will get through the GFC and prosper again and second, the stock market sees 'the light at the end of the tunnel' before the general economy. World stock exchanges have lifted substantially since March, 2009. This rebound may be built around the absence of more bad news. However we are getting a lot of conflicting data at the moment which is consistent with a bottoming economy.

The ASX is up by over 25 percent from its lowest point - an encouraging sign. The question is, are we in a bull market or is it a 'dead cat bounce' within a bear market? Economic history tells us that since World War II each recession has had at least two 'dead cat bounces' before a bull market has emerged. In the current situation if it is a 'dead cat bounce' then Australia is in its second bounce. This is the dominant question now for investors. No one knows the answer to this question.

Emerging good news from the US is evidence that the world economic Armageddon has been averted as Goldman Sachs, J P Morgan and eight other banks have offered to repay \$US68 billion (\$AUD83 billion) to the US Treasury lent under the "Troubled Asset Relief Program" (TARP). Whether the US economy starts to recover is critical and whether China avoids recession and powers along are the key drivers to improve confidence and business investment.

Australian mining companies in general are still trading on highly priced boom condition contracts. However it is believed the new contracts presently being negotiated will have prices at least thirty percent lower. This will have some flow on effect to the Australian economy.

Retail sales are up on previous years no doubt helped by the government's stimulus package. Consumer confidence is also in good shape. The Westpac-Melbourne Institute Consumer Index is up 13 percentage points - its biggest increase in 22 years. But with unemployment rising, will consumer confidence and retail sales collapse? On the other hand population growth is strong. This leads us to the question of what the future holds for Australia?

Are we seeing the first signs of green shoots or are we trailing the Atlantic countries? Let us examine this question. Australia is still 'the Lucky Country' coined some forty years ago by writer Donald Horne. The meaning of this phrase, then, as now, is based on these interesting facts: that Australia has more known minerals in the ground than any other country, it is an exporter of energy, it has great farming lands, it is a very large country slightly bigger than the USA and from east to west (Sydney to Perth) is a greater distance than from London to Moscow. It also has a harsh but generally good climate, is blessed with a peaceful democracy and is well respected in the world of nations, with a well educated people. But now in the GFC Australia can add more pluses to 'the Lucky Country' tag. Australia happens to be in the part of the world which is faring best in the GFC namely the Asian region where growth, and Australia's biggest customers reside. The ramifications of the GFC hit manufacturing economies hardest whereas Australia is big in raw material exports many of which are a necessity of life regardless of the GFC. An exception is China which swung export manufactured products to domestic consumption. Furthermore the sub-prime disease did not spread to Australia. No Australian banks have failed. In fact in a survey of the ten strongest banks in the world, Australia has four. In going into the GFC Australia's economic credentials had a triple 'A' rating.

While all this is very nice, Australia like any other country must be very careful. We are living in very difficult times. We should consider the following:-

- Is the GFC likely to get worse and how would that affect Australia?
- Is China's economic situation stabilised?
- What is the impact of large reductions in mineral pricing?
- When the effects of the stimulus packages end what will the consequences be? Will the general economy be strong enough to take over, or will there be new stimulus packages (the government getting deeper in the red) or will the planned massive infrastructure spending 'kick in'?
- How well will the confidence factor and retail sales stack up when unemployment is anticipated to increase, or some other unforeseen economic event happens?

The important question for Australia is how much the world recession is knocking us about. Ross Gittins of *The Sydney Morning Herald* suggests: 'it's mixed but there's worse to come'.

We indeed live in interesting economic times.

by Karen Huynh, Adv. Dp. Acc.

All of us want to be happy. All of us feel we have the right to be happy. So how do we achieve it and recognise it when we have it?

Happiness is rarely achieved through isolation and separation from others so it follows that to be happy we must foster close relationships with our fellow human beings. We do this by being interested in their joys and sorrows. If someone we are close to is miserable, then it is difficult for us to be happy.

Enjoy your time spent socially with others and say yes to all the opportunities that come your way. You never know whom you might meet or where the occasion might lead. Appreciate their efforts on your behalf and return the favour and entertain your friends.

Listen and remember the details of people's lives so that you can talk to them with genuine warmth and empathy.

To be happy with our lives we must be happy in our major activity. Our work brings in the resources to sustain our standard of living so we must find an occupation that brings fulfilment and satisfaction and enough money to give warmth, shelter and clothing and everything else we personally find essential for material life.

Finally, it is often not what happens to us or what our particular circumstances are, that makes us happy or unhappy. It is how we react to them which is determined by our attitude to life. Do you see the glass as half empty or half full?

## FINANCING CHILDREN'S FUTURE

by Vikash Chand, BA, ASA

Financing children's future is certainly one of the top priorities for parents (and grandparents). Apart from day to day expenses, saving towards a son's or daughter's university education, helping to finance the start of a business, footing part of the deposit for a home are some of the financial goals many parents strive for.

If a child is academically inclined, it is always advisable that parents give him/her a chance in university. This can cost up to \$16,500 annually depending on the kind of course the child is enrolled in. Starting early savings can put parents in a good position to finance their children's university education.

If a child shows interest and ability for business parents can make it a little easier by saving for start-up capital. Sourcing funds, especially for a small start-up business can be difficult. Parents can give their children a head-start in the business world by initiating early saving accounts to earn interest and

accumulate funds. Other avenues are investment in shares or property and insurance policies are also available for financing future financial needs.

Having funds for your children's future can also allow them to purchase their own home earlier. This requires a financial plan. Having a systematic financing plan can let parents take advantage of the power of compounded interest or investment. Compound interest becomes more powerful if money is held in an interest savings account for a longer period so it's crucial to start as early as possible.

Look for a bank that offers a high interest savings account, say 6%. Start with \$600.00 and every fortnight set aside \$70.00 (\$5.00 per day). An **investment of \$70.00** or roughly the equivalent of a full tank of petrol every fortnight will give a final amount of about **\$93,000.00 if this plan is adhered to for 23 years!**



by Marc Hurwitz, B. Com, (Accounting)

Within the last few years Australia has been hit by numerous natural disasters and tragedies. The droughts that have affected the farmers, the fires in Victoria and floods in New South Wales and Queensland have all caused massive hardship and many have been affected. This includes financial difficulties with the loss of properties, possessions and businesses. In order to minimise the financial hardship there are many possible ways in which you can get help. Some of these are: insurance, government agencies and special arrangements with the bank.

In order to prepare for a natural disaster you need to constantly monitor your insurance as this will be your major source of reimbursement in the event of a natural disaster. To ensure you obtain the best benefit

from your insurance you will need to ensure that your policy covers you for the various natural disasters that you might be exposed to. You also need to ensure that you are covered for the current value of your property/business. You should review your level of cover on an annual basis.

Various government agencies will be able to help you in the event of a natural disaster occurring. These will often take the form of government grants or tax rebates.

Talking to your bank manager is also useful as many banking organisations are allowing people to defer or readjust payments on mortgages/loans in order for them to cope with the financial hardship, caused by these natural disasters.

## **WOMEN IN BUSINESS**

by Nuha Awad, B. Bus, (Accounting)

In the last 30 years women have come a long way in the business world. They now represent around 45 percent of the workforce. Barriers that once existed have been largely broken down by government regulation and changed community attitudes.

Here are some tips for women to be successful in business:

1. Trust your instincts. One of the best assets women business leaders have is their instinct.
2. Set your goals. Research your market and write your business plan.
3. Gain confidence through failure. Failing and surviving gives you confidence. Recognise that failures do occur, take responsibility for your part, reflect and identify the factors that contributed to the failure, take inventory of any behavioural shortcomings, forgive yourself and move on.
4. Be yourself, but be the best you can be: know your unique strengths and use these to support your success. Success follows when you use your gifts. Be courageous enough to be yourself.

5. A good idea alone is not enough: Women must know how to brand, market and sell their ideas to others.

6. Re-frame the way you view power: in order for women to make a difference in business, they must be seen to be influential and part of the inner circle of decision-makers. If women reframe power as the ability to get things done, being powerful becomes palatable.

7. Love what you do.

8. Network with successful, motivated people. You will be inspired, learn from their experiences and build your own confidence.

9. Understand your cash flow. Learn how to read a profit and loss statement and get to know what a healthy balance sheet looks like.

10. Invest in yourself. Make a habit of keeping your professional and business knowledge up to date.



by Peter Small, B. Bus, F.C.A., Dip. Fin. Services

## ❑ TAX RATES – 2009 / 2010

A reminder that personal income tax cuts have effect from 1st July, 2009, so the rates for the year ending 30th June, 2010 are:-

### Tax thresholds from 1st July, 2009

Income range (\$)	%
0 – 6,000	0
6,001 – 35,000	15
35,001 – 80,000	30
80,001 – 180,000	38
180,001 +	45

The income tax rate for companies remains unchanged at a flat 30%.

## ❑ SUPERANNUATION RATES – 2009/10

The superannuation contribution caps that will apply from 1st July, 2009 have been announced. The maximum concessional contribution amount will be \$25,000 (down from \$50,000 in 2009), while the cap for transitional contributions (applicable to those aged 50 – 74) has also been halved, to \$50,000. Non-concessional contributions are to be capped at \$165,000 for the 2010 year (\$150,000 in 2009), with the three-year bring-forward amount will be \$495,000 (previously \$450,000). The small business CGT exemption cap (for proceeds on disposal of a business that are rolled over into superannuation) will be \$1.1 million (previously \$1,045,000).

## ❑ SALARY SACRIFICED SUPERANNUATION LIMITED

As from 1st July, 2009, any amounts contributed to superannuation under a salary sacrifice arrangement are counted towards the 10% limit used to determine whether a person is eligible to claim a deduction for personal superannuation contributions. Anybody who has been using this strategy to reduce their taxable income and top up their superannuation should recalculate their salary package for the 2009 / 2010 year.

## ❑ BUSINESS INCENTIVE – INVESTMENT ALLOWANCE

As part of its response to current economic conditions, the government has announced an incentive to assist businesses. A temporary investment allowance is to apply to eligible expenditure incurred between 13th December, 2008 and 30th June, 2009, provided that each asset acquired is installed and ready for use by 31st December, 2010. The allowance for small business taxpayers, namely those with annual turnover under \$2 million, is an additional tax deduction of 50% of the value of expenditure on items of capital equipment. As well, the equipment must be new, and also must be subject to the depreciation rules and cost a minimum of \$1,000. The rules are different for large taxpayers, who should contact us for details of how the allowance applies to them. Each asset is counted individually in applying the qualifying amounts above, although parts of a single asset can be grouped.

## ❑ CHILDREN'S TAX LIMIT – 2008 / 2009

The increase in the low income offset to \$1,200 for the 2009 year means that children under the age of 18 will be able to earn up to \$2,667 of investment income in the 2009 year without being taxed if there is no other income. This effective tax-free threshold may be useful to some parents who can structure their affairs so as to legally direct investment income to a child. These rates apply only to investment income; personal exertion income is subject to the standard tax-free threshold of \$6,000.

## ❑ CAR EXPENSE CLAIMS – 2008 / 2009

New rates for motor vehicle expense claims using the cents per kilometre method have been announced for the 2008/2009 year. As a result, the rates now are:

Engine capacity (cc) #	Rate per Kilometre (cents)
0 - 1,600	63 cents
1,601 - 2,600	74 cents
2,601 +	75 cents

# Conventional engines only; half these rates for rotary engines.



Whilst gathering your tax information for preparation by us, you may like to check the undermentioned items to see if you have included them in your summary of information. Although the following list is not exhaustive, it will serve as a useful guide.

- **ASSESSABLE INCOME**

PAYG Payment Summaries  
Interest and royalties  
Business/Partnership – income and expenses  
Commissions received  
Trust income  
Allowances, benefits, earnings, tips and directors' fees  
Dividends, including imputation details

Share transactions (full details)  
Rent received  
Sale of any asset where the asset was acquired after 19th September, 1985  
Termination payments received (with accompanying documents)  
Social Security benefits received  
Pension/Annuity payments

- **ALLOWABLE DEDUCTIONS**

Advertising  
Bad debts (written off during the year)  
Bank charges applicable to earning income  
Business Expenses  
Commissions paid  
Convention/Seminar expenses  
Contributions to approved superannuation, provident or retirement funds (generally non-employees)  
Donations & gifts over \$2.00 (approved)  
Education expenses - for income producing Purposes  
Film investments  
Home office expenses  
Telephone expenses applicable to the earning of assessable income  
Travelling expenses (including overseas with details)  
Insurance premiums (business)  
Interest on borrowings for business purposes

Leasing costs  
Legal expenses (in certain cases - full details)  
Losses of previous years  
Motor vehicle expenses (including business use proportion and log book if applicable)  
Newspapers essential to your business  
Plant, furniture, fittings, motor vehicles etc., subject to depreciation (limited to \$57,180 for a vehicle purchased during the 2009 year)  
Stationery, postage, printing costs  
Superannuation contributions  
Subscriptions to trade, business or professional associations  
Sun protection, where exposure is a risk.  
Purchases for resale  
Rates and taxes on income producing property  
Repairs to income producing property (not alterations, additions or improvements)  
Tools of trade  
Tax agent fees, accounting and audit fees  
Wages and salaries

These claims are subject to the substantiation provisions, where applicable.

- **REBATES**

Spouse and dependants (subject to any amount of Parenting Allowance received)  
Sole Parent

Net Medical expenses (over \$1,500 in total)  
Franked dividends

- **OTHER**

Education tax offset is available on eligible education expenses such as home computers and related expenses (eg internet, software, printers), text books study guides and tools for school based apprenticeships provided certain conditions are met  
Trade debtors (at 30th June, 2009)

Private Health Insurance - rebate and surcharge details required, and Fund membership number  
Stock value at 30th June, 2009 (valued at cost or market replacement value)  
Depreciable assets acquired – for each asset, cost and date of acquisition  
Trade creditors (at 30th June, 2009, listed under suitable headings)

by Paul St. Clair, F.C.A., Dip. Fin. Services

**PRESIDENT of the USA.** Congratulations to President Barack Obama on his election to the Presidency of the USA and his first 100 days in office. An article in *The Australian Financial Review* quoted a partner of Mallesons Stephen Jaques who was at Harvard Law School with Barack Obama who said that Obama "... was one of the leading students on campus at the time. It was clear that he was going somewhere." This snippet reminded me of my sister telling me that a friend of hers also attended Harvard Law School at the same time and his remark was that, "He was one of the most intelligent persons he had ever met." The tasks before President Obama are immense, particularly in the area of economics – we all can be affected. It seems that the abilities are there. For all our sakes let's hope he can deliver.

**ECONOMIC brighter side.** Recently the Group of 20 leading economies met in London. They contribute to 78 percent of the world's output. Of the G20 it is estimated that 6 may be or are in recession, (two or more consecutive quarters of negative gross domestic product.) None are expected to go into depression, (two or more consecutive years of negative growth.) Therefore 14 of the 20 leading economies will be in growth, 9 being estimated to be over 2 percent. Predictions for 2009 are the world will have 110 million businesses, a labour force of 3 billion with 2.4 billion households and 6.7 billion people all consuming from the world's marketplaces. This situation will not disappear.

**NEW ZEALAND gets a new government.** Our important near neighbour had a change of government in November, 2008. John Key is the new Prime Minister who led the National Party to victory winning 59 seats in the 122 seat parliament. In order to govern he will need the support of a small party known as ACT (Association of Consumers and Taxpayers) with their five seats. The ACT stands for small government, is libertarian and its main policy is a flat-rate of personal tax of 15 percent.

**STOCK MARKET strategies.** In the current market with volatility, falling and now rising prices and many countries in or heading towards recession some experts say: -

- Stay out of the market; "don't try to catch a falling knight";
- Be careful of the bounce – we may still be in a bear market;
- others say, enter the market using the dollar cost averaging

technique. That is invest in smaller sums regularly averaging out if the market falls lower.

- Don't be in a hurry to invest – study the market well.
- Be prepared to hold the stock up to five years at least.
- Only consider the top 50 or so stocks and particularly those that pay regular dividends with yields over 5 percent in this market.
- Non-mining and energy stocks are historically less prone to market fluctuations.
- Don't buy stocks with a price earning ratio over 20. Under 10 is more desirable in this market.
- Rebalance your investments, may be on a yearly basis. Rebalancing involves resetting your portfolio's asset allocation to your long term markets.

Note: the above points are for the current market and there are exceptions to every rule. Should you wish to discuss the above further do contact Paul St. Clair on (02) 9221 4088.

**DEMENTIA** is a terrible illness. If you have a loved one with symptoms you should seek medical and legal advice. From the legal advice point of view a professional assessment should be made to establish the mental capacity as to whether competency is enough to enter into the following legal documents:

- A Will or amendment thereof (A document regarding the financial affairs on death.)
- An Enduring Power of Attorney (EPA) (A document appointing one or two, usually spouse and/or adult child, to attend to the persons on-going financial affairs)
- A Guardianship Agreement (GA) (A document dealing with the non-financial issues, eg choice in health and medical treatment, nursing home, etc). These documents need to be attended to early or State appointees make the decisions. Is that what your family would want?

**GETTING a return on your money.**

Those living on interest income are having it hard. Interest rates are falling and will continue to fall for the short to medium term at least. No magic is going to lift interest rates while the economy is in gloom. A move to high yield dividend quality stock may be the answer. Dividend yield is becoming greater than cash by a big margin. The Deputy Governor of the Reserve Bank of Australia, Mr Battellino, recently gave the following illustration, \$100 put into a government bond 100 years ago would have grown to \$800. Put into the sharemarket it would be up to \$130,000.



- ❖ The national unemployment rate has remained steady over the latest period, and is now at 5.7% (and 6.4% in NSW). Inflation is currently 2.5% annually (2.4% in Sydney). The current account deficit for the December quarter was \$3.676 billion, a 42% reduction over the previous quarter.
- ❖ The number of mobile phones continues to expand worldwide, with six out ten of the world's population now having a mobile phone subscription. According to a UN report, there were some 4.1 billion subscriptions at the end of last year. Also, use of the internet has more than doubled over the last 6 years, from around 11 percent of people on the planet in 2002 to about 23 percent in 2008.
- ❖ Economic growth in China has slowed from over 11% pa several years ago to 7.7% for the 2008 year, but China will still build as many new houses over the next 15 years as there are houses in the entire USA.
- ❖ A survey of international banking has found that Westpac is the world's most profitable bank, based on its return on equity, and that Australia is the "most lucrative banking market" in the world. The country with the next most profitable banking sector is Canada.
- ❖ A report that the world financial turmoil has wiped \$1.2 trillion from Britain's national wealth, has been taken further by a curious analyst who calculated that if somebody tried to give away \$1 every second to achieve the same result, it would take over 85,000 years to do it!
- ❖ The increase in the number of government grants available to first-home buyers has proved to be successful, with record numbers of buyers taking the plunge into the property market. Those considering taking advantage of the grants should move quickly, however, as the grants are currently due to be reduced after 30th June.
- ❖ The number of margin calls reached a record in the December 2008 quarter, according to Reserve Bank figures. The number of margin calls per day was 9.77 per 1,000 clients, compared with the previous record of 8.04 in September, 2001, and more than 12 times the number recorded in the December, 2007 quarter.
- ❖ Hard pressed shop keepers may have developed an advantageous negotiating position in the economic conditions. There are indications that landlords are increasingly willing to reduce rents in preference to having their properties vacant, as retailers see declines in sales volumes at a time of inflexible fixed costs. Some reports suggest that rent reductions of up to 15% have been negotiated by tenants who threatened to vacate their shop premises rather than renew their lease.
- ❖ A study has calculated that, despite the reverses experienced over the last 18 months or so, Australia's superannuation sector is expected to grow over the next 5 years from \$1.2 trillion to over \$2 trillion, and to reach \$3 trillion within the next decade.

## ONE LAST THOUGHT

There will always be death and taxes, but at least death is not an annual event.

*St. Clair partners*

*Help save our environment - please do not throw this newsletter away.*

*When you have finished with it, give it to a friend!*

