FIDUCIAN FOCUS
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SEQUENCING RISK – WHAT DOES IT MEAN FOR YOU?

Sequencing risk is talked about, but what does this term actually mean? FFS planner Richard Press talks with FOCUS about this concept

Sequencing risk is the risk of drawing regular instalments from assets at the wrong time and crystallising losses in investment markets – the key to managing this risk is to have adequate defensive assets to ensure we don't sell our growth assets at the wrong time.

So how do we manage this? Historically, cash assets produce a positive return that may be slow but it's always steady.

Conservative, or capital stable, funds are by their nature more volatile than cash, but less volatile than balanced funds. The worst returns we've seen for these funds was following the credit crunch of 1994, where – from crash to recovery – it took three years. If your assets were in these funds and 1994 occurred again, we wouldn't want to crystallise this loss and we'd aim to hold these funds for three years. So, we start by ensuring we have three years of income payments allocated to cash.

Over time, balanced funds outperform capital stable funds, so we'd allocate some assets to these more growth-biased funds – but how much? Again, the risk we want to avoid is the risk of selling and thus crystallising a loss by selling the asset at the wrong time.

Looking at balanced funds, the worst situation was in 1987 and then the GFC – from which it took nearly six years for funds to recover. So, if we allocate three years to capital stable funds we can be comfortable that we won't be selling down assets and crystallising losses.

This leads to assets allocated to three 'buckets':

1. short-term cash assets to meet immediate cashflow requirements (three years of pension payments)
2. capital stable assets to meet medium-term income needs (three years of pension payments)
3. balanced funds/growth to ensure the fund can grow long-term, without compromising cashflow in the short- to medium-term.

Now, imagine these 'buckets' sit on what's called a 'wrap platform' that has a 'cash hub'. Income generated from assets returns to the cash hub to help ensure two things: that cash assets meet pension payments over time, and growth is consolidated in the asset part of the wrap service.

Over time we may take some profits from these assets if required to top up the cash hub.

In addition to the three main 'buckets', we can also allocate money to buckets for specific purposes. Such buckets can be labelled according to their uses: education, travel, funeral expenses.

Within a wrap platform strategy, we may also allocate a specific amount to a known expenditure, say an upcoming holiday, renovation or car purchase (being typical examples).

With a wrap profile, this may mean allocating part of the fund to a specified term deposit (TD), say $10,000, to a 6-month TD to meet a known travel expense.

Or, we can use separate accounts to save for different purposes and then, by linking those accounts, we can manage the fees whilst still clearly identifying different assets for different purposes – this is less common, but does occur.

Inside this issue...

SUPER CHANGES – WHAT DO THEY MEAN FOR ME?

What concessional contributions can I make?
Annual before-tax caps

Now	From 1 July 2017	From 1 July 2018
$30,000 age 48 or under **$35,000** age 49 & over	**$25,000** for everyone*	**$25,000***

* You can contribute more than the annual cap if you haven't fully used the cap before and your super balance is $500,000 or less. From 1 July 2018, you can carry forward unused cap amounts for up to 5 consecutive years. If you make personal super contributions, you can claim a tax deduction to eligible super accounts – up to the concessional contribution cap

Tax on concessional contributions in cap

Income now	%
</= $250,000	15
$250,000-$300,000	15
$300,000+	30

From 1 July 2017	%
</= $250,000	15
$250,000-$300,000	30
$300,000+	30

What non-concessional contributions can I make?
Annual after-tax contribution caps

Now	From 1 July 2017
$180,000pa or **$540,000** using 3-year bring-forward rule if conditions are met	**$100,000pa** or **$300,000** using 3-year bring-forward rule if conditions are met

Transitional rules apply to contributions between now and 2018-19

Spouse contributions

You can tax-offset spouse contributions only when the recipient's income is less than:

Now	From 1 July 2017
$13,800	**$40,000**

What are the super pension limits?
Annual before-tax caps

Now	From 1 July 2017
No limit	**$1.6 million**

If you have a pension over $1.6 million, you must reduce your total pension balance to $1.6 million or below by 1 July 2017 so you're not penalised. Any amount over $1.6 million can be in an accumulation account

What is the earnings tax in accumulation accounts?

This stays at **15%** (10% on capital gains)

What about my transition-to-retirement (TTR) pension?

TTR pensions supplement your income so you can cut your work hours but not your lifestyle

Earnings tax rates

Now	From 1 July 2017
Tax-free	**15%**

Contact your Fiducian financial planner today to determine what the proposed changes mean for you

AUSTRALIAN EQUITIES – THINGS ARE NOT THAT BAD

SEAN MARTIN, CHIEF INVESTMENT OFFICER, SOLARIS INVESTMENT MANAGEMENT – AN UNDERLYING MANAGER FOR THE FIDUCIAN AUSTRALIAN SHARES FUND

We believe Australian equities will produce attractive returns in 2017, underwritten by a surprisingly resilient economic outlook.

Despite a highly tumultuous 12 months politically, the local and global economic outlook looks remarkably solid – buoyant even – compared to the political one. The US economy is continuing its recovery at a reasonable pace, the Chinese economy appears to have stabilised and the Australian economy (boosted by the resultant commodity bounce) is showing solid growth, solid employment levels and low inflation.

We forecast these economic conditions will underwrite a 7% - 9% growth in the ASX200 in 2017 comprising a 4% (pre-franking) yield and a 3% - 5% capital growth – not that bad at all.

What's working within the market?
Within the ASX there's been a huge change in performance of growth vs value stocks.

Growth stocks in this discussion are simply stocks with higher Price to Earnings (PE) multiples while value stocks are stocks with lower PE multiples.

Growth stocks materially outperformed value stocks for the 4-5 years to mid-2016 and were looking very expensive at that point. Since mid-2016, a large style rotation has occurred with value stocks dominating.

Our process at Solaris has no preference for growth or value stocks – merely for the best opportunities at any point in time. We thought that growth stocks had run too far and reduced our weighting to close to its lowest level since the fund's inception having sold positions in Brambles, Realestate.com and Dominos to name a few.

We were too early with most of these sales but what often happens in extreme valuation situations such as this is that you wait and wait for things to change, wondering if they ever will. But, when the change occurs, it happens very quickly and very dramatically.

The graph demonstrates the change with value-stock outperformance in just 7 months, largely unwinding the growth-stock outperformance of the previous four to five years.

We've taken advantage of this retreat to buy some much more reasonably priced growth-stocks.

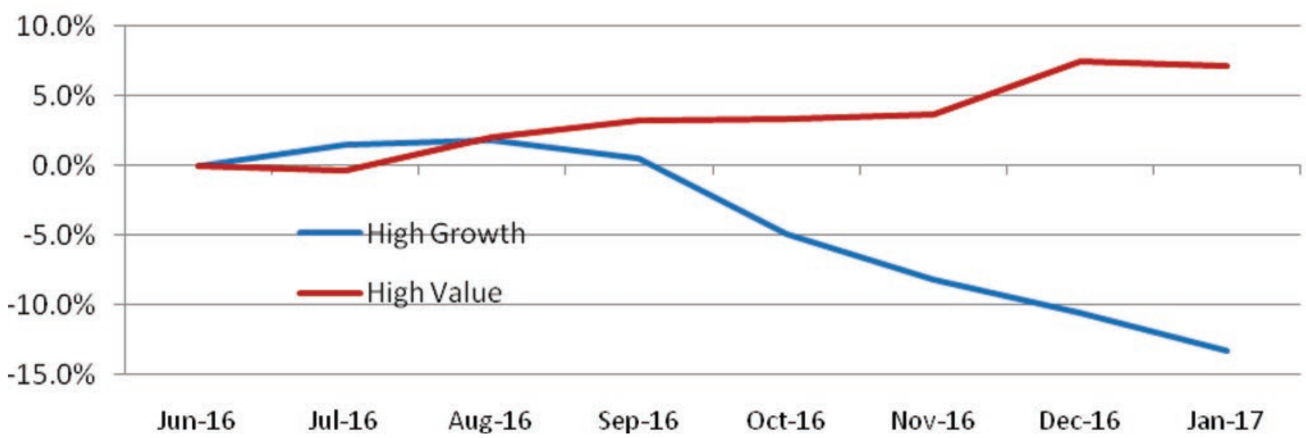
Carsales.com and Resumed are examples where we never disliked the stock – just the stock price – and we've added both to the portfolio recently and we're optimistic about their prospects.

In the value space, the resources sector still appeals to us, with valuations remaining reasonable, more cautious management (following the sector's rout), better commodity prices and strong balance sheets combining to underwrite our view.

"Despite a highly tumultuous 12 months politically, the local and global economic outlook looks remarkably solid"

Growth vs Value Relative Performance

Performance vs ASX 200



Source: Solaris

FIDUCIAN IN THE COMMUNITY

VISION BEYOND AUS – EVERY DOLLAR SAVES SIGHT

VBA has come a long way since its early projects in 2011. VBA funded a team of 9 to travel to Rishikesh in the foothills of the Himalayan Mountains. This group restored eyesight to 180 people. Throughout the years, VBA has put all donations towards reaching as many people as possible and providing them with the best care possible. To date more than 20,500 surgeries have been performed.

If you would like to donate, please visit www.visionbeyondaus.org.au

Surgery, Battambang, Cambodia

Patients after surgery, Battambang, Cambodia

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