Bramwell Brown Ltd

INVESTMENT ADVISERS – BROKERS

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Bramwell Brown Limited – Newsletter – September 2011

Volatility

August proved to be a month of volatility on global sharemarkets, with the Dow Jones Industrial Average bouncing up and down on each and every piece of statistical data announced to the market. The following table shows a few points throughout the month.

Date	Dow Jones Industrial Average	Variation
August 1st	12,132	
August 10th	10,719	(- 11.65%)
August 15th	11,482	(+ 7.12%)
August 18th	10,990	(- 4.28%)
August 31st	11,613	(+5.67%)

Unfortunately whenever the U.S or European markets take a hit, our sharemarket tends to follow suit. Often there is no real rationale for our corporates to drop in value when the U.S economy falters, but that's exactly what happens. Take Ryman Healthcare as an example. What does U.S employment data or Greek debt levels have to do with Ryman's ability to carry out their business? The answer is "absolutely nothing", but that doesn't stop the sell-off, and the subsequent drop in value.

I fielded a number of calls in the first week in August from investors wondering what they should do. I have never suggested people try and time markets – it's something that has proved almost impossible to achieve over any length of time. My philosophy is to buy good companies and hold on to them. Provided the companies you buy have the fundamentals of a solid balance sheet, sound management, and good future prospects, then short-term volatility should not concern you. If anything, the volatility we experienced in August can present opportunities to buy more of the companies you hold, at discounted prices. For those investors who had difficulty seeing the value of their shares fall through August, the question needs to be asked whether you should have money invested in equities at all. For those investors currently sitting on the sidelines waiting for the right "time" to enter the market, you might consider investing in stages rather than all at once.

Compromise

The recent volatility in sharemarkets, together with the general global financial problems of the last few years highlights the difficulties investors face on an ongoing basis. Managing money, like life in general, is all about compromise. In an ideal world we will retire with a debt free home, and would have squirreled enough money away over the years to fund a comfortable retirement. If we're lucky we can invest all of our money in Government bonds so we don't need to take any risk. Even better, we have enough money that we struggle to spend all the interest, our capital then keeps pace with inflation, and we can leave a nest-egg to our children. Is this realistic? Not for the vast majority of people.

The first thing investors should do to determine what sort of compromises need to be made is to try and quantify some of their retirement planning needs. If you can put numbers to some of the following questions you can start putting strategies in place to achieve your goals.

- When do I want to retire?
- What standard of living am I aiming for and what will that cost each year?
- How much capital do I need to generate that level of income?
- How long does my capital need to last?
- Do I want to leave a legacy for my family?

The maths is relatively simple once we start putting numbers to the questions. For example a sum of $500,000 generates $25,000 per annum before tax at a return of 5.00%. Or, if you have determined you need $500,000 as a nest egg in twenty years time, you need to save approximately $15,200 per annum at a compounding return of 5.00% after tax to achieve that goal. The difficulties arise in the more qualitative aspects of financial planning.

- How long will I live?
- What returns will I receive ten years from now?
- Can I depend on Government funded superannuation?
- What level of inflation can I expect?
- Will I have unexpected health costs?

The best you can do when trying to answer these questions is have an educated guess. Most of these things are moving targets and need to be assessed on an ongoing basis, but pinning a number on them initially at least gives you something to work with. The variability in answers to all of these financial planning questions is what makes it an inexact science, and leads to some of the compromises mentioned earlier.

So where do we begin to compromise? For most of us the problem is that we simply don't have the amount of money to achieve the dream retirement lifestyle. The areas we can influence include:

- Retirement date – pushing it out allows us to build more capital, and leaves less time to use it
- Spending – it might not be palatable but we at least have the ability to curb our spending
- Leaving a legacy for the kids – not necessary in my opinion – spend it yourself
- Risk – instead of investing in Government bonds, we have the ability to take on risky investments such as shares and corporate bonds in an attempt to boost returns
- Capital – we have the ability to erode our capital over time

All of these strategies involve some sort of compromise that will have an effect on our standard of living in retirement. Eroding our capital is possibly the hardest one to come to terms with because it's a double-edged sword. As we eat our capital we reduce our ability to earn, which causes us to have to erode our capital further. Adding to the complexity is the fact we don't know how long we will live. Spending your capital in the belief you will live to eighty-five will look like a poor decision when you are still battling away at one hundred.

Taking on riskier investments is also a compromise. We are giving up the security of a risk-free investment in the hope we can generate a higher income. The problem, of course, is when the "risk" turns into "loss." Retirees don't have the time or the earning capacity to make up for losses in the same way a younger investor with a reliable job has. Share investments require a longer-term view due to their potential for volatility, and this in itself is a compromise. Does an eighty-year old retiree really want to be worried about riding out the peaks and troughs of a volatile sharemarket?

I've written previously about people of my parent's generation going without in retirement so they can leave a legacy for their children. In my opinion we owe a debt to our parents, not the other way around. We enjoy a far better standard of living than our parents and grandparents ever did and I'm certain that will continue. I've provided my kids with a quality education, and have hopefully instilled good morals and a good work ethic, so they should have the ability to make their own way in life.

Probably the most influence we can have in terms of managing our money is in our personal spending. Choosing Riversdale Beach over the Gold Coast, Cobb & Co over the Countryman, Farmers over Rodd & Gunn, (or Ford over Holden) are all compromises, but have the ability to influence our finances in a positive manner. Unless you are one of the lucky few who have the funds to lead the retirement lifestyle you desire without risking your capital, you are going to be faced with some of the compromises mentioned here.

Global Financial Crisis

I've written previously about the GFC, and the United State's propensity to try and solve its problems by printing more money. It's clear the world's financial problems have moved from a corporate level to a sovereign level. We can see it to a lesser degree here in New Zealand, where the finance company collapse is now a burden on the Government (ultimately the taxpayer) rather than the individual companies themselves. The key point I think many people are missing in all the bailouts, money printing, and quantitative easing that is going on around the world is that the debt hasn't miraculously disappeared – it still has to be paid back. All that has happened is that debt is now being carried by Governments on behalf of their citizens. I saw an interesting quote on the Internet from a Greek professor commenting on the Greek bailout. "Greece was not bailed out. It was given an expensive credit card with which to pay off the mortgage, having lost its job."

Financial Markets Authority

The Financial Markets Authority took over from the Commerce Commission as the regulator of financial markets participants in New Zealand. Part of their job is to oversee financial advisers, and review their practices. This can involve gaining access to client files. The FMA are currently visiting financial advisers in the lower North Island, and there has been concern expressed by advisers regarding their access to clients' records. Advisers are expected to have gained clients' consent for the FMA to gain access to their files prior to their visit. However, under Section 25 of the Privacy Act the FMA has the ability to serve written notice on anyone to obtain any information it considers necessary or desirable. So gaining consent seems like a fruitless exercise in my opinion if the FMA can legally gain access to the information anyway. If you have any concerns regarding this issue please call the office at any time.

Air New Zealand

Air New Zealand has announced it is issuing up to $150 million of unsecured, unsubordinated bonds.

- Interest rate – to be set on September 5th (indicative range between 6.90% and 7.20%)
- Maturity Date – November 15th 2016
- Interest paid semi-annually (May 15th and November 15th)
- Minimum investment – $5,000
- Closing date – September 23rd

Please call the office as soon as possible if you would like to discuss this opportunity.

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