

## Overhaul of Financial Advice

The Government has recently announced reforms to financial advice that is aimed at improving the trust and confidence of Australian retail investors in the Financial Planning Sector.

Capstone Financial Planning is an independently owned national licensee and is, through its affiliated Financial Planning practices, committed to the delivery of professional advice. Our client relationships are born through trust and always putting the client's interests at the top of the decision making process when providing advice. As such, we welcome the Government's push to ensure this ethic is more widespread through the industry.

Recent business collapses such as Storm and Opes Prime are seen by many, including the Government, as the catalyst for exposing flaws in the advisory system in Australia. The Global Financial Crisis affected many but a positive outcome would be that more advisers are required to act in the best interest of their clients, as conflicts are exposed.

The Minister for Financial Services, Superannuation and Corporate Law, Chris Bowen MP has been quoted as saying "These reforms will see Australian investors receive advice that is in their best interests, rather than be directed to products as a result of incentives or commissions offered to the Financial Adviser".

We applaud this sentiment. Capstone Financial Planning does not provide incentives to its advisers for the recommendation of any particular product. Each client's needs, therefore, can be appropriately addressed through the recommendation of product solutions that are not conflicted by our advisers being rewarded for their recommendation.

Jo-Anne Bloch, the recently departed CEO of the Financial Planning Association, acknowledged that Capstone Financial Planning was at the forefront of the industry in terms of how we provide advice to our clients, through a non-conflicted structure.



It is proposed there will be a number of reforms that come into effect from 1st July 2012. These reforms will need to be legislated but you are likely to see more articles on this matter over the coming months. All components of the industry are addressing these reforms and working with the Government to ensure that the outcome is balanced for all parties.

We believe that Capstone and our affiliated practices are already adhering to many of the proposed reforms and therefore will see little impact on the way we provide advice to our clients.

One of the key Government reforms is to introduce a statutory fiduciary duty that advisers must act in the best interest of their clients. We believe we already achieve that.

However, with reform there will always be change and as such we will keep you informed how, if at all, it will affect your interaction with us. In the meantime if you are concerned or interested in learning more about something you have heard, or read, then as usual feel free to speak to us.

# Economic highlights

## Sovereign debt in Europe

Amid signs that Greece's sovereign debt was threatening to undermine broader European economic and monetary stability, the European Union (EU) and the International Monetary Fund (IMF) took the unprecedented step of making an announcement of a substantial financial support package.

The package essentially involves the provision of financing facilities to enable the most heavily indebted European Governments to meet their short-term debt commitments. The major components and contributors to the facility are: €60 billion in loan funds (European Commission); €440 billion in loans and guarantees (EU member states, Sweden and Poland); and €250 billion in loan funding (IMF).

In addition to the support package, the European Central Bank (ECB) announced that it would be acting with the US Federal Reserve and the central banks of the UK, Switzerland, Canada and Japan to re-establish joint swap facilities to alleviate a shortage of US dollars in the markets.

It is estimated that the funding package, which in total represents approximately 8% of the European Gross Domestic Product (GDP), will enable the region's Governments to fund themselves for at least a year. However, it should be recognized, that while funding and liquidity-related issues have been temporarily addressed, the long-term solvency challenges facing these countries remain. Moreover, countries with high levels of debt will be obliged to implement harsh austerity measures, which may prove to be socially unpopular.

## Australia

The highlight of domestic financial news flow in May was the Federal Treasurer's Budget delivery speech. This year's budget appears to have been framed with a view of returning to a surplus position over the medium-term, however its detail was largely overshadowed by ongoing media and financial market commentary related to the earlier announcement of a proposed Resource Super Profits Tax (RSPT).

A total of 33,700 jobs were added to the Australian labour force over the course of April, with the trend towards increased full-time employment at the expense of part-time positions continuing. This latest result has left the unemployment rate steady at 5.4%. In comparison, unemployment in the US presently stands at 9.9%, the UK 8% and Europe 10%.

Retail sales figures for March revealed a disappointing rise of barely 0.3%, following a fall of 1.2% in the previous month. Underlining the lackluster nature of the result was the fact that the annual rate of growth has slowed to 1.2%, amid a sideways trend in turnover since November last year. The waning affect of the Federal Government's cash handout stimulus last year has no doubt reduced consumers' propensity to spend. Other factors that have weighed on spending levels include moderate rates of wages growth, rising interest rates and sharp increases in utility prices.

## United States

Retail sales momentum continued rising a further 0.4% in April bringing the year-on-year rate of growth to 8.8%. Building materials represented the key driver of growth, with sales over the past two months rising by 7.8% and 6.9% respectively. The results from other areas were somewhat mixed, with gains in health stores (+0.9%) and petrol (+0.5%) contrasting with weakness in department stores (-1.5%) and furniture (-1.2%).

The resurgence in building materials sales was reflected in the housing report, which showed housing starts rising by 5.8% in April. In annual terms, the rate of growth currently stands at 40.9% compared to just 2.9% in December last year. It was disappointing to note that the more forward-looking permits data is showing signs of moderation, falling 11.5% in April, lowering their year-on-year rate of growth to 15.9%.

Industrial production rose by 0.8% in April, lifting its year-on-year pace of growth to 5.2%. The manufacturing sector showed signs of renewed growth, posting its second consecutive monthly increase of 1.0%. At the industry level, computer production rose by 0.7% over the month, following respective gains of 1.7% and 2.1% in the previous two months. Given the ubiquitous nature of computers in the modern economy, any rebound in demand within this area is clearly indicative of burgeoning economic momentum. Rising levels of industrial production have been reflected in a corresponding fall in the level of surplus capacity within the US economy. From a level of 72.8% at the start of the year, the measure of capacity utilization has risen steadily to its latest reading of 73.7%, with further gains likely as demand conditions strengthen.

## China

For some time, investors have been concerned that the rapid pace of growth in China may be placing the country's economy at risk of overheating. Industrial production for the month of April did little to allay these fears, with year-on-year rate of growth easing only slightly to 17.9%, down from 18.1% the previous month. Upward pressure on prices added to the tone of caution, with the Consumer Price Index (CPI) posting a greater than expected annual increase of 2.8%. Of even greater concern to investors and the Chinese monetary authorities was the continuing rapid climb in housing costs, with urban prices accelerating to a year-on-year rate of increase of 12.8%.

## United Kingdom

Sovereign debt issues aside there are signs of underlying economic resilience within Europe. The initial estimate of the March trade balance with the rest of the world showed a surplus of £4.5 billion, compared with a surplus of £1.6 billion a year earlier. The strong performance of exports was a standout, posting a 7.0% rise in seasonally adjusted terms from the previous month. China (+47%) and India (+36%) were among the countries that posted the largest increases in imports from Europe over the past year. In line with Europe's solid export performance, industrial new orders within the region posted a monthly rise of 5.2% in March. Of particular importance in terms of the outlook for production was the fact that new orders for capital goods rose by 5.7% over the month, lifting their year-on-year rate of growth to 15.6%.

In the UK, the May edition of the Confederation of British Industry (CBI) Industrial Trends Survey revealed that export orders for UK manufactured goods rose to a positive net balance for the first time in over two years. Of the total respondents, a net 3% indicated that export orders were above normal. This represents significant improvement from the previous month when a net 16% indicated that orders were below normal. Importantly, this was the first positive net monthly outcome since March 2008, when the net balance was similarly at +3%.

Source: ING

# Get healthy and save



**In Australia, we're lucky enough to have one of the best lifestyles in the world. Plenty of sunshine, beautiful parks and beaches, and an abundance of good and healthy food. There's no reason for Australians to be out of shape.**

Unfortunately, despite our blessings, and a pretty good awareness of health and wellbeing, the general state of the Australian population does not seem to be improving.

For a number of years, the most common killers in Australia have been heart disease and cancer. Believe it or not, they're actually becoming more common.

- Cardiovascular disease affects 1 in every 6 Australians, or 67% of Australian families. By 2051, that's expected to increase to 1 in 4 Australians<sup>1</sup>.
- Diabetes is Australia's fastest-growing chronic disease, with 275 Australians developing the disease every day<sup>2</sup>.

While some of this can be attributable to our ageing population, it's also largely due to the fact that many Australians live with a combination of poor diet and a lack of physical activity.

According to the heart foundation, around 80% of cardiovascular disease is largely preventable<sup>3</sup>. Likewise, Diabetes Australia estimates that up to 60% of cases of type 2 diabetes can be prevented<sup>4</sup>.

## Lifestyle changes could save your life... and your wallet

When a life insurance company calculates your premiums, they take into account a number of risk factors – some of these include your age, gender, blood pressure, smoking status, your Body Mass Index (BMI), cholesterol and blood glucose levels.

If you fall into a high-risk category for some of these risk factors, it can be reflected in how much you pay for your insurance each year. These additional costs are called 'loadings'.

By making changes to improve your lifestyle, you could reduce your high risk factors for serious illness. You can also ask your life insurance company to re-assess your insurance premiums – potentially reducing or removing your loadings.

Not only are you giving yourself a better quality of life now and in the future, you could also be saving yourself money. More importantly, you'll be starting some good habits that could stay with you for a long and happy lifetime.

Source: Asteron



1. 'The shifting burden of cardiovascular disease' – Report by Access Economics to the Australian Heart Foundation, 2005
2. 'Diabetes in Australia' – Diabetes Australia website, [www.diabetesaustralia.com.au](http://www.diabetesaustralia.com.au)
3. Media release – the Heart Foundation, 18 March 2009
4. 'Diabetes in Australia' – Diabetes Australia website, [www.diabetesaustralia.com.au](http://www.diabetesaustralia.com.au)



# The Emerging Opportunity

The Organisation for Economic Cooperation and Development (OECD) has raised growth forecasts for 2010 and 2011 as emerging economies, such as China, outpace the debt-burdened developed countries to drive global expansion.

The projections highlight the divergence in growth rates throughout the global economy as it emerges from its worst slump in more than half a century. The OECD warn that while the economies of China and India risk overheating, the expansion in the developed world will continue to be challenged by indebtedness.

The consumer in the developed world has entered the Global Financial Crisis (GFC) with the highest level of debt relative to income on record. Households have been living beyond their means for the past two decades because of the availability of cheap credit and rising asset prices. A severe drop in asset prices in 2008 forced many into the realisation that their levels of gearing were unsustainable and in the developed world many are now living with the consequences of excessive borrowings. Households and businesses alike are being forced to improve their debt ratios and this quite simply means cutting spending and increasing savings.

Consumers in developing nations however, have been much more conservative while the consumption party was happening elsewhere. These emerging economies are experiencing above average population growth, as well as a growing wealth effect and structurally rising disposable incomes.

## What does this mean for investors?

Increasing incomes and overall wealth essentially means more than a billion people will move out of poverty and into the middle class over the next 20-30 years. They will move from remote rural existence to urban centres that have the facilities, living standards and the goods and services that these new consumers desire.

For savvy investors, this presents an opportunity; to be part of a growth story that is likely to happen despite the problems facing much of the developed world.

Global businesses that are well exposed to these consumers will benefit.

## What if China experiences a slowdown?

Although there is much discussion of a potential slowdown in the rate of expansion in China, this does not necessarily suggest a slowdown in the consumer story. China's recent years of spectacular growth in the face of a global downturn has been predominantly a result of massive levels of fixed asset investment. They stimulated their economy by investing in property, infrastructure and manufacturing capacity, and this has upheld their headline growth rates. The consumer has been consistently growing at near 15% annually. So even if the Chinese have invested too much, too fast and an impending decline in certain areas eventuates, it is anticipated the consequences are unlikely to impact on consumers.

## Example... Yum! Brands

Yum! Brands, better known for their major brands; KFC, Taco Bell and Pizza Hut, earn ~40% of their revenue from China. KFC is one of the most recognised foreign brands in the country and they already have 3400 restaurants with 600 stores being opened every year! This business is not exposed to fixed asset investment in China, nor to commodities or financials in a significant way. This business is more directly exposed to the growing incomes and numbers of consumers in China who desire KFC and the western culture it represents... as well as the 'finger lickin' goodness' it promises. With near 50% return on invested capital on each store it opens, Yum! Brands are confident of delivering superior growth rates for years to come.

Source: Magellan Asset Management Limited



PERSONAL FINANCIAL ADVICE

### Head Office:

Capstone Financial Planning  
Level 5, 350 Collins Street,  
Melbourne Vic 3000

Phone: 1300 306 900

Visit our web: [www.capstonefp.com.au](http://www.capstonefp.com.au)



AFSL No: 223135

ABN: 24 093 733 969

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