

Financial **Focus**

Summer 2016



Welcome to Financial Focus. I hope you enjoy the articles and find them interesting and informative. If you have any feedback, questions, or would like to review your financial plan, please contact me.

Would downsizing be worthwhile for you?

It seems to make logical sense. You retire, sell the now cavernous family home, buy a cosier place and use the cost difference to boost your retirement income – win-win right? The answer is: it depends. Here's what you need to consider.

Where you could save

Super

If you own your home outright and choose to downsize, that extra money could be contributed to super where it could substantially improve your retirement income. The attraction of contributing money into super is that investment earnings are generally taxed at 15% while you build up your super, and 0% when your super is used to pay you a pension outside super. Alternatively, if you invest outside super the earnings are generally taxed at your marginal tax rate which could be up to 49%¹.

Mortgage

If you're still paying off your home, downsizing could help you minimise your repayments or eliminate them entirely. You could even downsize and continue to make the same repayments to pay off your mortgage much sooner.

Utilities

A smaller home typically runs more economically. Why pay to heat or cool space you no longer need? If your new home provides renewable energy options such as solar power, you may even be able to sell energy back to the grid and make money.

Maintenance

Less space to occupy means less space to maintain. In the case of larger properties, downsizing could offer substantial savings on cleaning and garden maintenance.

Continued on page 2 ►

¹ Includes Medicare levy and the Temporary Budget Repair Levy of 2% on taxable income exceeding \$180,000.

Continued from page 1 ►

Travel

Downsizing can help you relocate to a more convenient location. If the local shops, public transport and amenities are all within walking distance, you could make substantial savings on fuel.

Garage sale

Selling your home is a great time to sell any items you no longer want, need, or will fit into your new house. Any money you make could be contributed towards moving costs.

Costs to consider

Home value

If you sell your home during a market lull, you could lose some or all of the equity you've built up. This could eat into, or erase entirely, the cost saving you make by purchasing a less expensive property.

Selling costs

Home selling is a highly competitive market. To ensure your home is positioned favourably to sell, you will likely need to appoint a real estate agent and pay for marketing services, which will cut into your profit margin.

Moving costs

If it's been a while since your last move, you might be surprised at how much it costs to pack up and transport all of the items you've accumulated. That's why it's a good idea to offload all the items you can live without before your move.

Strata fees

If you purchase an apartment or townhouse you'll likely have to pay quarterly strata levies. Although these fees can end up saving you money in the long term, compared to paying for the maintenance of your home and yard, they will eat into your profit margin in the short term.

Stamp duty

You'll generally have to pay stamp duty to buy a new home or apartment, so you'll need to include this cost in your calculations.

Storage costs

One drawback of buying a smaller home is you have less space to store your treasured belongings. If you run out of room, you may need to purchase additional storage which can add up quickly.

Doing the sums

Balancing the potential savings and costs of downsizing can be tricky, and that's before you consider potential impacts on your lifestyle. A financial adviser can help you work out if downsizing makes sense for you as a part of a tailored financial plan.

The investor's guide to growth assets (Part 2)

In this second instalment of our two part series, we delve deeper into the fundamentals of international property securities, direct property and alternative assets.

International property securities

International property securities are investments listed on international stock exchanges, providing exposure to a portfolio of direct property investments. These are referred to as Global Real Estate Investment Trusts (GREITs). GREITs own a range of properties such as residential, commercial, retail and industrial. Some invest across all of these property types, while others focus on specific areas.

Investing in GREITs enables you to diversify your portfolio, not only across a broader range of countries but also property assets and sectors which do not exist in the Australian market.

International property securities primarily earn income from rent. Property securities generally produce higher levels of income than other listed equities.

Continued on page 3 ►



Continued from page 2 ►

Be aware

- Both the capital value and the income return of the investment may be influenced by currency exchange rates.
- In the short to medium-term, the value of listed property trusts is expected to increase or decrease in value in accordance with movements in both the listed property trust sector and the sharemarket generally. As a result, property securities are more volatile than defensive assets and should be viewed as a long-term (5-year plus) investment.
- Property securities tend to generate higher returns in income than capital growth.

Direct property

Buying a residential or commercial property to rent out is a way of investing directly in property.

Property investors have personal control and management over their investment. Capital appreciation over the longer term is likely to keep pace with or exceed the rate of inflation, depending on the location and physical condition of the property. Tax deductible expenses may include depreciation, maintenance, insurance and financing costs. Furthermore, the equity in a property may be used to leverage other investments.

Be aware

- Large amounts of capital are required to purchase a direct property, plus your portfolio may lack diversification.
 - There are significant establishment costs and ongoing costs associated with maintenance of the property.
 - Direct property assets can be illiquid, resulting in the inability to draw down a portion of your capital in the future.
- You risk being heavily reliant on the income stream from a single investment sector.
 - You risk losing income whilst the property is untenanted.

Alternative assets

Alternative assets cover a wide range of investments which are not considered traditional assets, unlike those already described. Some examples include hedge funds, infrastructure and gold.

These types of investments are generally included in portfolios to increase diversification and provide returns that aren't strongly linked with the performance of traditional assets.

Be aware

- To access some alternative investments you generally need to do so through a managed fund.
- As most alternative investments aren't listed on an exchange, determining their value for a fund's unit price can be difficult and may involve a considerable time lag.
- Some alternatives such as hedge funds involve greater complexity and therefore may be more difficult to understand.
- Some alternatives are illiquid, which may make them difficult to buy or sell when you want to.
- Alternatives may be included in a portfolio for their growth or defensive characteristics.
- Hedge funds may use a range of uncommon investment management techniques to achieve objectives and may use leverage, short-selling and derivatives extensively.
- Alternative fund managers may charge relatively higher fees.



Offset accounts: A better way to manage your mortgage

If you want to repay your mortgage quickly while still having easy access to your additional repayments, an offset account may be worth using.

What's an offset account?

An offset account is a transaction account linked to your home loan. The money you deposit into it offsets the loan balance before interest is calculated. For example, if you owe \$400,000 on your home loan and have accumulated \$50,000 in an offset account, interest will be calculated on \$350,000.

Continued on page 4 ►

Continued from page 3 ►

Benefits over regular savings accounts

If you hold your surplus cash in an offset account you can save interest at home loan rates, and no tax is payable on the interest savings. This is effectively like 'earning' the home loan interest rate tax-free.

Alternatively, you could hold your surplus cash in a regular savings account, but the interest rate you earn is usually much lower than what you pay on your home loan. Plus, every dollar in interest you earn is taxable at your marginal rate, which could be up to 49%².

Benefits over direct loan repayments

When you make additional repayments directly into the loan you can achieve similar benefits to having an offset account. However, limits often apply to the frequency and amount of withdrawals you can make and withdrawal fees are usually charged. With offset accounts, you typically have ready access to the money via an ATM, cheque book and internet, and withdrawal fees are generally not charged.

The best of both worlds

You may even want to have your salary paid directly into an offset account and withdraw money as needed to meet your living expenses. This can enable you to make the interest savings available with direct loan repayments and have easy access to your money.

	What interest rate is earned/saved?	Would interest earned/saved be taxable?	Would you have ready access to the money?
Cash account	Deposit rates	Yes	Yes
Direct loan repayment	Home loan rates	No	No
Offset account	Home loan rates	No	Yes

Other things to consider

- If you'd prefer not to have easy access to your additional loan repayments, you may want to make repayments directly into the loan where you are less likely to spend the money impulsively.

² Includes the Medicare Levy and Temporary Budget Repair Levy.

Important information and disclaimer

This Financial Focus newsletter has been prepared by GWM Adviser Services Limited (ABN 96 002 071 749, ASFL 230692) ('GWMAS'), an MLC related company and member of the National Australia Bank Limited group of companies ('NAB Group'), Registered office 105–153 Miller Street, North Sydney 2060, for use and distribution by its authorised representatives and the representatives or authorised representatives of National Australia Bank Limited, Godfrey Pembroke Limited, Apogee Financial Planning Limited, Meritum Financial Group Pty Ltd and Australian Financial Services Licensees with whom it has a commercial services agreement. Any advice in this publication is of a general nature only and has not been tailored to your personal circumstances. Please seek personal financial and/or legal advice prior to acting on this information. Any general tax information provided in this publication is intended as a guide only and is based on our general understanding of taxation laws. It is not intended to be a substitute for specialised taxation advice or an assessment of your liabilities, obligations or claim entitlements that arise, or could arise, under taxation law, and we recommend you consult with a registered tax agent. Information in this publication reflects our understanding as at the date of issue. In some cases the information has been provided to us by third parties. While it is believed the information is accurate and reliable, the accuracy of that information is not guaranteed in any way. Opinions constitute our judgement at the time of issue and are subject to change. Neither GWMAS nor any member of the NAB Group, nor their employees or directors give any warranty of accuracy, nor accept any responsibility for errors or omissions in this document.

- If you would like to credit your salary into an offset account, you should check that your payroll provider is able to do this.
- Some lenders allow you to establish multiple offset accounts, to help you better manage your cash flow.
- Some lenders pay an interest rate on the balance of the offset account that is less than the home loan rate. These are known as 'partial' offset accounts and are not as effective in saving you interest as an offset account which offsets 100% of the home loan interest rate.
- Offset accounts can usually only be linked to loans with variable interest rates, not fixed rate loans.
- To maximise your interest savings you may want to pay for the majority of your living expenses on a credit card and repay the card in-full before the end of the interest-free period. This enables you to use the credit card provider's money to fund your living expenses, while applying your own funds to reduce your average daily loan balance.
- If you want to invest some of the money held in an offset account, you should consider paying the money directly into your home loan and establishing a separate loan to fund the investments. By taking out a new loan for investment purposes, the interest would usually be tax deductible.