



Newsletter

Spring 2009

Welcome

In this Spring issue of our newsletter we look at a strategy for investing in the share market that takes advantage of market volatility. With dollar cost averaging you don't have to try to guess if the market is going to rise or fall. You can actually make money out of share price ups and downs.

We also examine the importance of Trauma Insurance – an insurance policy that actually helps to finance your survival if anything nasty happens. And finally, we look at the phenomenon of mental money buckets - which explains why \$50 might be a reasonable lump of cash one minute and throwaway mad money the next. It seems that it's simply human nature – but it can affect your wealth potential. Read this entertaining article and find out how and why.

Cheers



The team at Eclipse

Latest news

It is Spring at last, and it seems the end of our economic winter of discontent may be in sight. A major long term liquid natural gas deal with China has been heralded as the beginning of a new resources boom. The Australian share market has been climbing fairly consistently (if not spectacularly) for weeks. Consumer confidence remains relatively high. And although the number of Australians in full time jobs has declined, the number of those in part time jobs has swelled to compensate, keeping overall unemployment figures well below many pessimistic forecasts.

It is far too early to call it a recovery, but it could be the preamble to one, and the good news is that there are signs of hope in Western Europe and the USA too. There are still a few dark clouds on the horizon concerning strained relations with China over iron ore pricing and Chinese interference at a political level. But at the same time major resource projects are still going ahead.

The way forward to reduce greenhouse gas emissions is still a hot political issue that might contribute to an early election. On the interest rate front, there has been a warning from the Reserve Bank that it will not hold interest rates at artificially low levels if the economy continues to improve. Not all good news, but at least the sun is out!

Is it safe to get back in the water?



Take advantage of market fluctuations!

The Australian share market has rebounded by over 30 per cent since hitting a low in March this year. To mid August, this proved to be Australia's best five-month run in over 20 years.¹

Despite this, there's still doubt as to the strength of the economic recovery in Australia. The possibility of higher interest rates and reduced consumer spending can dampen the recovery and analysts are divided as to whether the share market has hit rock bottom - that magic point beyond which the market will begin its sustained recovery. What is known, is share markets have recovered each and every time after major world crises.

Dr Shane Oliver, Chief Economist at AMP put it this way. "I have gone through some dusty record books and calculated that if this is the start of a bull market, then history says there is a very long way to go in this charge. Since 1894, the average bull market has seen shares gain 150 per cent, and since 1950 the average gain has been 132 per cent."²

So is it safe to get back into the water yet?

To take advantage of the normal volatility of share markets even in market downturns, there is a strategy that enables investors to minimise the risk of trying to 'time the market'. This strategy, called "Dollar Cost Averaging" (DCA), is one way for

investors to enter or get back into the market whether it is rising or falling. Instead of investing all your capital in a lump sum, you drip feed it at regular intervals - say once a month or once a quarter.

With DCA, you actually take advantage of market fluctuations instead of worrying about them! By investing a regular amount on a periodic basis, you avoid making a large single commitment to the market and average your purchases over a range of prices.

Consider the following example:

Scenario 1: Invest \$50,000 as a lump sum in January

Scenario 2: Use DCA and invest \$5,000 each month for ten months

As long as unit fund prices are volatile but eventually rise (as in the table below), the value of the investment will be higher using DCA.

Under both scenarios \$50,000 in total is invested but the number of units purchased is different. Under the first scenario 7,143 units are purchased (\$50,000 / \$7) but we purchase 9,359 units under scenario two (see the table below). At the end of the investment period (October in this example), the value of the two investments is:

Scenario 1: \$50,000 (7,143 units x \$7)
Scenario 2: \$65,513 (9,359 units x \$7)

DCA enables you to acquire more units if prices fall. When the share market recovers, these extra units increase the value of your investment.

If you are making regular super contributions or reinvesting your dividends, you're already taking advantage of Dollar Cost Averaging and you can be confident that whenever the market does recover, you won't miss the upturn.

¹ Trading Economics, August 13 2009
² Richard Webb The Age, 2 August 09

Scenario 1	Investment Amount	Unit Price	Number of units
Jan	\$50,000	\$7	7,143 units
Scenario 2	Investment Amount	Unit Price	Number of units
Jan	\$5,000	\$7	714
Feb	\$5,000	\$6	833
Mar	\$5,000	\$4	1,250
Apr	\$5,000	\$3	1,667
May	\$5,000	\$5	1,000
Jun	\$5,000	\$8	625
Jul	\$5,000	\$9	556
Aug	\$5,000	\$5	1,000
Sep	\$5,000	\$5	1,000
Oct	\$5,000	\$7	714
Total	\$50,000		9,359 units



It's tempting to think
"it couldn't happen to me
or my family"

An insurance policy especially for survivors!



You are more likely to survive a serious accident or life threatening illness these days thanks to advances in medical science. Yet while survival rates are a lot higher than before, so are the associated medical costs.

Unlike term life insurance policies which pay out only if you die from an illness or in a bad accident, there is an insurance policy available that helps financially should you face a serious illness or injury and survive. It is called Trauma Insurance.

A trauma insurance policy pays you an immediate and tax-free sum upon diagnosis of an illness or condition specified in the policy. You get the money as soon as the claim has been approved - typically confirmation of diagnosis of the major illness from a specialist doctor. The lump sum you receive can be used to pay medical costs, upgrade hospital or medical treatments or pay for private nursing or therapy. In fact, you can do anything you like with the cash, including paying off your mortgage and other debts so you can recover with less financial stress.

Many families see a trauma insurance payout as a 'fighting fund', enabling the family to pull together to fight an illness (e.g. cancer), allowing them to cease or reduce work commitments, go on a family holiday or generally spend quality time together.

There is often confusion between

trauma insurance and income protection insurance, but they are completely different products. Income protection insurance pays you an income while you are unable to work - it replaces part of your pay cheque. Trauma insurance, on the other hand, is a one-off payment to help you financially survive the effects and treatment your condition requires. So for complete financial protection, you're likely to need both.

Some insurance companies also provide optional child trauma insurance cover. If your child was diagnosed with a serious illness or had a bad accident, trauma insurance would make it easier for you to afford the best available medical treatment. Or you could hire home help for example, enabling you to spend more time with the child who needs you most.

It's tempting to think "it couldn't happen to me or my family" but consider the following:¹

- Women have a one in four chance of suffering a critical illness between ages 30 and 64
- Before age 65, you're three times more likely to suffer a critical illness than you are to pass-away

- Every year, 1.1 million Australians are disabled by long-term heart, stroke and vascular diseases
- Each year 200,000 children fall critically ill

Your need for trauma insurance depends on your age, income, liabilities, family make-up, individual medical history and other personal circumstances. The illnesses and injuries covered (called "events" in policy-speak) also vary from policy to policy, and you are only covered for the events specified.² For these reasons, it is important to consider your trauma insurance needs carefully before committing to a policy cover amount or the inclusion of specific events to be covered.

Ask us about Trauma Insurance, the insurance policy for survivors!

¹ Comminsure Statistics 2007, Austin Research Institute, University of Melbourne 2007, National Heart Foundation of Australia Annual Review 2004

² Serious injuries and illnesses often (but not always) specified in trauma policies include heart attack, coronary artery bypass surgery, malignant cancer, stroke, major brain injury, coma, paralysis, multiple sclerosis, blindness, deafness, chronic kidney failure, major organ transplant, motor neurone disease, severe osteoporosis and more. However, these events may or may not be included in specific comprehensive trauma policies. It is therefore important to study the specific policy definitions and insured events included in any policy and you should always seek advice before acting.

Penny-wise, pound foolish?



It's something our grandparents used to say: "He's penny-wise but pound foolish."

Perhaps our grandparents were on to something because an award winning University of Chicago economist, Richard Thaler¹, has discovered we treat money differently depending on how we categorise it!

Consider the following examples:

- A man walking along the street picks up a \$50 note! He's \$50 richer. Did you know he is more likely to spend this \$50 than he is to spend the \$50 already in his wallet from his hard earned wages?
- A woman has a casino betting limit of \$10. Tonight, as she enters the casino, she wins \$100 in a lucky door prize. Because the \$100 is an unexpected gain, she's more likely to gamble this money, even though it's in excess of her normal limit.
- Ever driven around the block a couple of times looking for a free parking spot but later spontaneously purchased something on credit? You may have saved \$2 on parking, but

you've spent far more than this in time and petrol (not to mention that thing you bought that you didn't really need).

So what's going on? Without getting too technical, the simple explanation is that we tend to place our money into psychological buckets. Where we place the money depends quite a bit on how we came into that money. The bucket into which we mentally place our funds influences how we use it. And how we spend is often determined by the mental bucket we're going to be taking the funds out of.

People who have to work hard for their money often respect it more than those who 'come into wealth'. Those who gain wealth through a big lottery win or a large inheritance have been known to fritter it away and suddenly wonder "where did all the money go?" This is the mental buckets at work!

Of course, a dollar is a dollar. According to Thaler, however, the subconscious use of mental money buckets alters our perspectives on money and investments. It can result in a sometimes irrational attitude to spending and investing decisions.

The bottom line is that many of us

could improve our wealth by being more objective and rational when it comes to our hard earned money, our investments and any fortunate gains that come our way.

Here are some tips.

First, a dollar you had to work hard to earn is worth just the same as a dollar you win or are given. So be as careful with the latter as you would with the former.

Second, before spending, ask yourself the question: "Could I make better use of these funds"? Maybe it would be better to pay off part of your mortgage or top-up your super than buy that new plasma TV with the \$1,000 you received from your tax return.

Third, recognize that money should be working for you and not sitting around idle. It doesn't matter if you received the funds through hard work or pure luck... either way the best option for creating long-term wealth is to get your money working.

Of course, we're not robots...we still need to have fun. So remember to treat yourself but treat yourself more wisely now you're aware of the mental traps we can fall into.

¹ Michael M. Pompian, Behavioral Finance and Wealth Management John Wiley 2006

This article has been prepared on a general advice basis only. The information has not been prepared to take into account your specific objectives, needs and financial situation. The information may not be appropriate to your individual needs and you should seek advice from your financial adviser before making any investment decisions.

Disclosure: Whilst all care is taken in the preparation of this material no warranty is given with respect to the information provided and accordingly no responsibility for errors or omissions, including responsibility to any person by reason of negligence is accepted by the company or any member or employee of the company. Please note: these articles have been sourced from Advant Group Pty Ltd.