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An introduction to investing

Introduction

The principle of saving is well known. Money is put away in a savings account or a term deposit, generally achieving a fixed rate of interest with minimal risk. Unfortunately, a savings account can offer returns little better than inflation. In real terms, that means you may end up losing money on your initial investment.

Investing, on the other hand, is the commitment of money today which, with an appropriate level of risk, comes with the expectation of realising your future financial goals. It's about making your money work harder for you than just saving alone can!

With its rewards, however, investing can also be challenging and confusing. Whether you dream of a new house or an investment property, money for your children's education or the comfort of security and freedom in retirement – understanding the principles of good investing is the foundation of achieving your financial goals. Achieving these goals shouldn't be luck. It requires commitment, research and patience, to ensure the outcome will be anything but uncertain. And, as with most things, you should plan ahead before you start.

This guide aims to build your understanding of the basics of investing and help get you started today on the path to securing your financial independence tomorrow. However it is just one part of understanding your investments. We strongly recommend engaging with a financial adviser to develop the strategies you need to reach your financial goals.

Understanding risk

Risk and investing are intrinsically linked. In fact, risk is defined as the chance you will lose money on an investment – however, crucially it is also the driver for making money.

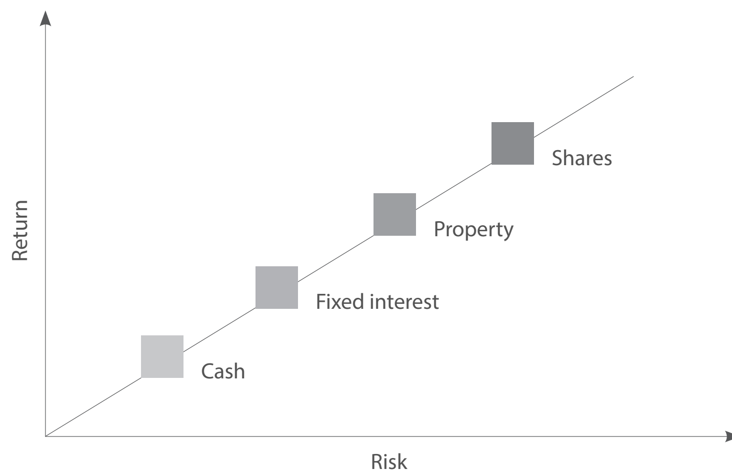
While every investment carries some risk, your appetite for risk will probably be very different to the next person. For some, crossing the road against the lights might seem risky, while others wouldn't think twice about skydiving. Risk is a perception based on your unique experiences and personality.

As all investments come with varying degrees of risk, it is important to recognise your appetite for risk and build a portfolio that suits your risk tolerance. There are several factors that, when considered wholly and in line with your goals, will measure your risk tolerance.

- Desire to take risk – some investors enjoy the inherent uncertainty of investing and are inclined to take on high-risk investments. More common however is an aversion to the stress that a large fall in an investment's value can produce. As a test, ask yourself how you would feel if you woke up and the value of your investment had fallen by 10 per cent? 20 per cent?
- Financial capacity to take risk – a couple with a new baby and a mortgage will have a considerably different capacity to take risks than a single person just starting out in the workforce.
- Your need to take risk – this is tied to your investment time frame. If you are 30 years old and planning 35 years ahead for retirement, you will probably be happy to accept greater risk (as short-term volatility is smoothed out), to achieve your goals. On the other hand, if you are nearing retirement, you'll probably not want to risk losing your money as there isn't the luxury of time to recover from losses.

With greater risk, there is the opportunity for greater returns. Different types of investments, as shown in the graph below, have greater risk – and the possibility of higher returns.

Risk and return comparison



Types of risk

Business risk – this is the risk that a company's value will decrease or even go bankrupt. This may be unique to a company, or even a sector of the economy, however if you are invested heavily, your portfolio can face significant losses.

Market risk – also known as systemic risk. This is the risk that market-wide downturns will diminish your portfolio.

Currency risk – this is risk that arises from the change in value of one currency against another. For example, if your investment is in US dollars, a stronger Australian dollar will diminish your returns when the investment is repatriated to Australia.

Political risk – changes in government, or government policy, can significantly affect the returns on an investment. While this affects foreign investment in volatile developing countries, in Australia legislative changes, such as taxation law, can still pose a risk to investment returns.

Interest rate risk – if your investment is tied to the interest rate, such as property or bonds, then changes in the interest rate can affect your investment returns.

Liquidity risk – this is the risk that an investment may be difficult to sell at the time you want to sell. While shares are usually very liquid, assets such as property may take longer to sell, creating liquidity risk.

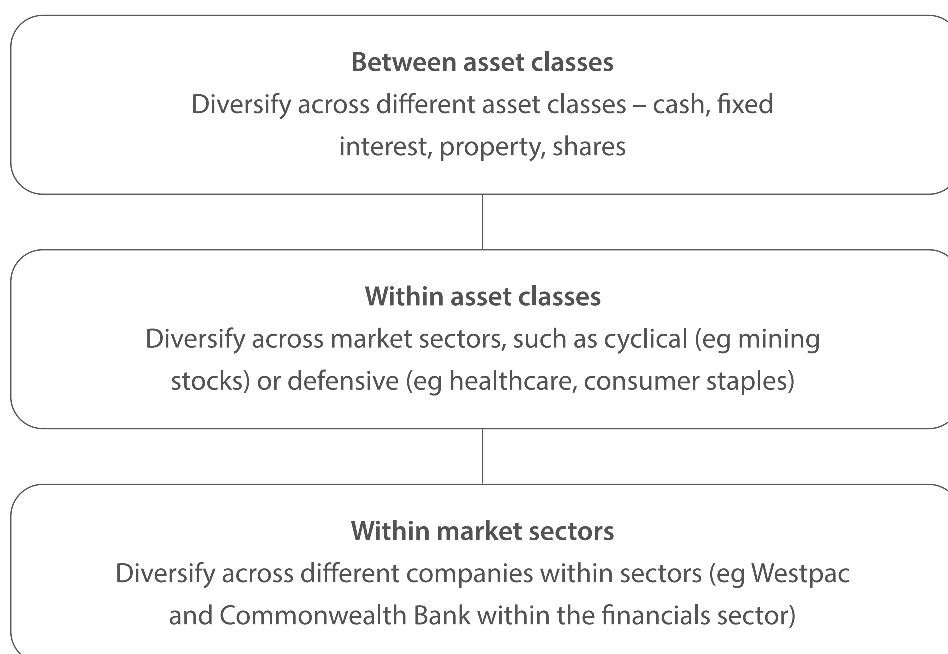
Inflation risk – this is the risk that your investment will not keep pace with inflation – and will lose money in real terms.

Avoiding risk

While risk is an unavoidable part of investing, there are steps you can take to minimise your exposure to unintended risk.

Diversification

As the saying goes, don't put all your eggs in one basket. Different types of investments, such as shares and bonds, perform well at different times. With a mix of investments, if one part of your portfolio suffers losses, other investments may remain steady or even appreciate. Over time this will smooth out the returns of your portfolio and protect against the risk of catastrophic losses. There are different levels of diversification to properly manage risk:



Long-term investments

While your age, investment goals and financial situation will affect where you put your money, generally speaking longer-term investments present smoother returns as short-term volatility is smoothed out.

Research

The more you understand about an investment and the financial markets, the less likely you'll be to make an investment which doesn't match your financial goals.

Investment Concepts

Compound interest

Compound interest is your money working for you. You earn interest on the money you deposit, and in time you earn money on this interest. When you are earning interest on your interest – that's compound interest, and it's one of the most important principles of investing and a great reason to start investing as early as possible.

Compounding interest can have a big impact on your final portfolio value. Here's an example of how it works. You invest an initial sum of $**50,000 at eight per cent interest** and have the choice to have this interest paid out to you – or you can re-invest it.

	Interest paid out		Interest re-invested	
End of year	Investment amount	Interest amount	Investment amount	Interest amount
1	$50,000	$4,000	$50,000	$4,000
2	$50,000	$4,000	$54,000	$4,320
3	$50,000	$4,000	$58,320	$4,666
4	$50,000	$4,000	$62,986	$5,039
5	$50,000	$4,000	$68,024	$5,442
6	$50,000	$4,000	$73,466	$5,877
7	$50,000	$4,000	$79,344	$6,347
8	$50,000	$4,000	$85,691	$6,855
9	$50,000	$4,000	$92,547	$7,404
10	$50,000	$4,000	$99,950	$7,996
		$40,000		**$57,946**

After 10 years, with interest paid out, you would have received $40,000 in total interest payments. Meanwhile if you chose to re-invest the interest instead, you would have $57,946 in interest – that's nearly $18,000 or 45 per cent more at the end of 10 years! And just as with most investments, time invested makes all the difference. Starting early can leave you with a larger balance at retirement than investing more money later in life.

Dollar cost averaging

Dollar cost averaging (DCA) is the strategy of investing regular, incremental amounts into your portfolio – such as setting up automatic deposits from your regular pay. As the same amount of money buys you more of something when the price is low, regular deposits over time (for investments such as shares which rise and fall in value over time) could lower the average cost of your investment. This method of investing also lessens the down-side risk of investing a large lump sum right before a market fall.

DCA is most effective in falling markets, however predicting when a market will rise or fall is never simple. This strategy lets you take the emotion out of investing and frees you up from watching the market every day.

Case study

John chooses to invest a regular amount of $1,000. As the unit price rises and falls over the course of the year, by investing each month, John is investing at different unit prices and achieves a lower unit cost than if he had invested from April to September.

	Amount invested	Unit price	Number of units
January	$1,000	$22	45.45
February	$1,000	$24	41.67
March	$1,000	$27	37.04
April	$1,000	$32	31.25
May	$1,000	$31	32.26
June	$1,000	$36	27.78
July	$1,000	$35	28.57
August	$1,000	$34	29.41
September	$1,000	$32	31.25
October	$1,000	$27	37.04
November	$1,000	$26	38.46
December	$1,000	$27	37.04
		Average $29.42	**Total units 417**

If John had invested $6,000 in each of June and July, he would have only been able to buy 338 units, against 417 by investing steadily over the whole year.

Borrowing to invest

Borrowing to invest, or gearing, is an investment strategy usually considered by more experienced investors and those with a higher risk appetite. This is because, while gearing can increase the value of your portfolio faster than otherwise possible, it will also magnify your losses in a market downturn.

The principle behind a successful gearing strategy is that the value of your investments will increase faster than the after-tax cost of servicing the debt. However in volatile markets a loss on the investment may mean you are unable to service the debt and can be forced to sell the investment at a loss. The following tables show the benefits and risks of gearing an investment in Australian shares:

Chris' own capital	$100,000	$100,000
Loan	Nil	$75,000
Total Investment	$100,000	$175,000
Dividends received	$40,000	$70,000
Market value at end of year 5	$200,000	$350,000
Total value at end of year 5	$240,000	$420,000
Less borrowing costs	Nil	($26,250)
Potential tax deduction in borrowing costs @ 47%*	Nil	$12,338
Less loan repayment	Nil	($75,000)
Net portfolio value (end of year 5)	**$240,000**	**$331,088**

**Top marginal tax rate + Medicare levy*

If the share price halves:

Chris' own capital	$100,000	$100,000
Loan	Nil	$75,000
Total Investment	$100,000	$175,000
Dividends received	$40,000	$70,000
Market value at end of year 5	$50,000	$87,500
Total value at end of year 5	$90,000	$157,500
Less borrowing costs	Nil	($26,250)
Potential tax deduction in borrowing costs @ 47%*	Nil	$12,338
Less loan repayment	Nil	($75,000)
Net portfolio value (end of year 5)	**$90,000**	**$68,588**

**Top marginal tax rate + Medicare levy*

Note: there could also be a benefit from franking credits received on dividends. This would be greater for the geared portfolio as it receives more dividends.

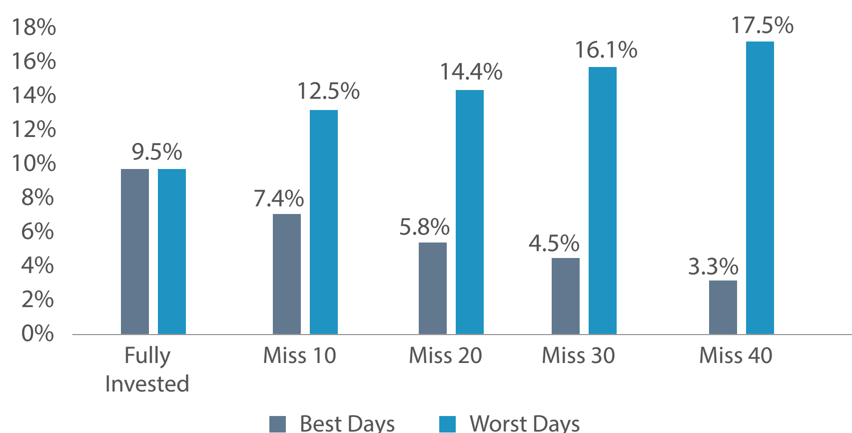
Time in - not timing

In times of uncertainty its temping to try and time the market, ie to sell ahead of falls and buy in anticipation of gains. But without a proven asset allocation or stock picking process, trying to time the market is very difficult. A good way to demonstrate this is with a comparison of returns if an investor is fully invested in shares versus missing out on the best (or worst) days.

The following chart shows that if you were fully invested in Australian shares from January 1995, you would have returned 9.5%pa (including dividends but not allowing for franking credits, tax and fees).

Missing the best and worst days

Return on Australian Shares, % pa (All Ords Accumulation Index 1995 - 2022)



Source: Bloomberg

If by trying to time the market you avoided the 10 worst days (blue bars), you would have boosted your return to 12.5% pa. If you avoided the 40 worst days, it would have been boosted to 17.5% pa.

But this is very hard to do, and many investors only get out after the bad returns have occurred, just in time to miss some of the best days and so end up damaging their longer term returns. For example, if by trying to time the market you miss the 10 best days (grey bars), the return falls to 7.4% pa. If you miss the 40 best days, it drops to just 3.3% pa.

That's why it's important to remember 'time in the market is more important than timing'.

Tax-effective investing

When you receive money from most investments, or crystallise a capital gain by selling an asset, that's considered income and the government will tax you on it. In fact, income taxes or the capital gains tax (CGT) will usually take the largest proportion of your investment and since nobody likes paying taxes, it's important to consider the impact of tax on your investment and how tax-effective investments can improve your returns.

A tax-effective investment is one which offers a significant taxation benefit to your marginal rate of tax and could include investment bonds, negative gearing, superannuation and pensions, and Australian shares.

Investment bonds

Simply put, an investment bond is a tax paid investment. This means that the tax on investment earnings is paid by the investment bond issuer at the current company tax rate of 30%.

While funds are invested, there is no need for the investor to include any earnings in their tax return.

After ten years from the start date of the investment, or when the life insured passes away, (regardless of the time invested), the growth and earnings are free of any personal tax liability to the investor upon withdrawal.

Negative gearing

If you borrow to make an investment and the expenses of owning that asset (including depreciation and interest on the loan – but not capital repayments) are greater than the income the asset produces, you may be able to claim a tax deduction for interest costs against other assessable income. While many investors are familiar with negative gearing on property, it is also available on shares purchased where costs such as interest and bank fees associated with the loan may be tax deductible.

Superannuation and pensions

To encourage people to contribute to their super and build their retirement nest-egg, the Government has provided a series of generous tax concessions making super one of the most tax-effective investment strategies available. Some of these concessions include:

- Super contributions – either salary sacrificed through your salary or from the employer Superannuation Guarantee (up to certain limits) contributions are taxed at just 15 per cent, not your marginal tax rate.
- Money you earn on your investments is taxed at just 15 per cent, or 10 per cent for capital gains.
- If you are over 60, for most people, money taken out of super is tax-free.
- In a super pension, investment earnings are tax-free.

Australian shares

Australian shares potentially offer the lowest effective tax rate of all the investment asset classes. This is due to franking credits associated with share dividends.

Dividends and franking

As owning shares represents ownership of part of a company, it also entitles you to a share in profits. Companies can reinvest some or all of the profits back into growing the company (known as retained earnings) or alternatively distribute profits through payments to shareholders. These payments to shareholders are known as dividends. Dividends can be taken as cash or, in some circumstances, automatically reinvested to buy more shares in the company.

In Australia, if you receive a dividend from a company, this is considered a form of income and you may be required to pay tax. However because the company also pays tax, this is a form of double taxation.

For this reason when you receive a dividend, they often come with franking credits. Also known as dividend imputation this means you only pay the difference between the company tax rate (usually 30 per cent) and your marginal tax rate.

Returns on investments

Generally speaking, returns on your investments come in the form of either **income** or **capital** growth.

Income assets

Income assets provide a cash flow to meet living expenses or save. In some instances, such as with some shares, they can be reinvested to grow your portfolio. However, the income will likely be taxed, while the returns may be subject to inflation and interest rate risk. The return from assets in the form of income, whether reinvested or not, is known as the yield. Income includes:

- rental income on properties
- dividends on shares
- interest on cash deposits and fixed interest

Growth assets

Growth assets are those that can be expected to increase in value – such as property or shares. As growth assets are intended to generate a rise in the underlying value of the asset, they are popular for general wealth accumulation. However they can be more volatile than income assets and face the risk of significant capital losses. While they don't have tax payable while the asset is in your possession, capital gains tax may be payable on disposal of the asset.

In reality, many investments have both capital growth and income attributes, and your total investment returns are often a combination of both:

Capital growth + **Yield (dividends, rent, interest etc)** = **Total return on investment**

Asset classes

Types of asset classes

An asset class is simply a type of investment and they are the building blocks of your portfolio. There are four main asset classes:

- Property
- Shares (equities)
- Cash
- Fixed Interest

Each asset class has individual characteristics and carries a different level of risk and return to suit a range of investor types. A diversified portfolio – an important risk mitigation strategy – contains investments across these different asset classes. Asset classes fall into two main groups: **defensive** and **growth**.

Defensive characteristics	Growth characteristics
Focused on preserving capital	Usually longer-term than defensive assets
Generate income for investors	Higher risk than defensive assets
Considered less volatile and safer than growth assets	Can produce income, however focus is on capital growth
Cash and fixed interest are usually considered defensive	Property and shares are usually considered growth

Cash

Investments in cash include bank deposits, term deposits, savings accounts and cash management trusts. While cash is considered the safest investment type, the returns are usually low and investors run the risk over the long term of returns being less than the rate of inflation.

Fixed interest

Fixed interest assets, also known as bonds or debentures, are agreements where the investor is paid fixed amounts of money at predetermined dates in the future – usually twice a year, plus the original amount repaid at the end of the term. Bonds can include the debt issued by government, banks or corporations both internationally and within Australia. Like cash, they are considered a safe investment with moderate returns over the longer term.

Property

Generally, there are three ways to invest in property:

- *Direct property*

  Direct property involves the investor buying the property directly. For retail investors these are usually residential properties. Income can be in the form of rental returns or capital growth. There are also tax considerations, such as negative gearing, which can reduce the cost of ownership for investment properties.

- *Listed property trusts*

  A listed property trust (LPT), commonly known as real estate investment trusts (REITs), involves pooling your money with other investors, which is then used to buy and manage property, such as industrial properties, shopping centres, office buildings or hotels. As an investor you own units – similar to shares – of the trust, which can be bought or sold on the ASX. As units in LPTs are easier to buy and sell than unlisted property funds, they are usually more volatile.

- *Unlisted property funds*

  Unlisted property funds are similar to REITs, however your investment is not traded publicly on the stock exchange. As a result the investment is usually more illiquid, but less volatile than listed property trusts.

Shares

Shares (also known as equities or stocks) represent ownership of part of a company. Historically shares have provided the greatest returns of all the asset classes, with returns through the growth in share value or through dividends. However they also represent a greater risk than other asset classes.

Australian shares are bought and sold on the Australian Securities Exchange (ASX). Within the ASX there are different market sectors.

Generally there are two ways to own shares:

- *Direct ownership*

  You have total control to choose the company and the quantity of shares purchased. They are usually purchased through a stockbroker.

- *Managed funds*

  An investment manager pools the money of all the investors, then researches and buys and sells shares on your behalf. In this case you own 'units' of the managed fund rather than the shares in the companies themselves. Managed funds allow for greater diversification across different types of shares, or even different asset classes, however usually have a fee structure associated with the service.

International versus domestic shares

With Australia representing around 3 per cent of all listed companies, you may be interested in buying shares in international share markets. This presents diversification benefits as the Australian share market has a large exposure to mining and financial stocks, with less exposure to technology and consumer stocks.

As purchasing international shares directly can be difficult, many investors hold international shares through managed funds. It's also important to remember international shares represent a range of new risks to consider, including currency risk (losing money moving into and out of Australian dollars) or political risk (the government of that country could pass laws affecting your investment).

Asset allocation

Asset allocation in its simplest form is deciding how you will allocate your investments across different asset classes, such as cash, fixed income, shares or property. Asset allocation is a way to diversify your portfolio recognising that different asset classes perform differently in different circumstances. As some asset classes carry more risk than others, asset allocation is also a way to reflect your risk level in your overall portfolio construction.

Types of asset allocation

There are several different ways for asset allocation to be applied to a portfolio:

- *Strategic asset allocation*

  Strategic asset allocation involves deciding what proportion of your total portfolio you would like in each asset class. For example, you may decide to have 20 per cent in cash, 40 per cent in property and 40 per cent in shares. For strategic asset allocations this involves periodically rebalancing your portfolio (that is, buying and selling assets to ensure your overall asset allocation matches, as much as possible, your original investment allocations) as different investment gains on different assets change this balance.

- *Tactical asset allocation*

  Moving assets tactically means moving assets to take advantage of better performing asset classes.

- *Dynamic asset allocation*

  Dynamic asset allocation involves highly active management of the portfolio that involves rebalancing a portfolio to bring the asset mix in line with a long-term target. This involves selling down outperforming asset classes and adding to any underperforming asset classes.

Managed funds

Unlike direct investing, in a managed fund your money is 'pooled' with other investors to buy assets. Each investor in the managed fund owns 'units' of the managed fund, the value of which rise and fall with the value of the underlying assets in the fund.

Each managed fund will have a profile which outlines the objective of the fund and the asset allocation, allowing you to decide whether the fund matches your investment goals and risk tolerance. An investment manager will make the decisions of what to buy and sell based on the fund's profile.

Advantages of managed funds:

- Managed funds allow an investor with a relatively small amount of money to invest in assets that may otherwise be out of reach, for example international shares or commercial property.
- Trying to invest directly may not leave enough money to adequately diversify your portfolio.
- Managed funds are, as the name suggests, managed by professional investors with the skills, experience and research resources not generally available to individual investors.
- It can be relatively easier to change your investment profile – say from income to growth assets – than to change a portfolio of individual assets.
- Some managed funds can take a regular payment plan from your salary, however this is not generally the case with individual investments in shares.

Types of managed funds

Single sector funds

A single sector fund invests in just one asset class, such as cash, shares or bonds. Single sector funds may also specialise within the fund, for example small cap companies or resource companies.

Multi-asset funds

Multi-asset funds invest across more than one asset class. Diversifying across different asset classes reduces the risk of investing solely in an equity fund, however may have more risk – and return – than a bond fund.

Multi-manager funds

A multi-manager fund is a fund comprised of more than one specialised fund. Each fund has a separate fund manager, with different investing styles. Multi-manager funds work on the premise that investment managers operate differently in different environments and by diversifying across fund managers, risk is reduced.

Active versus passive funds

A passive fund (also known as an index fund) is a fund which is built to mimic an index, such as the ASX100 or the US S&P 500. The fund manager makes no decisions on individual stocks – either good or bad – instead accepting the average performance of all stocks in the index. Periodically the fund manager will buy or sell shares to reflect the weighted changes in the index the fund is designed to copy.

Actively managed funds, on the other hand, involve the fund manager actively buying and selling shares to try and invest in the best performing assets classes and investments. The intention of the active fund manager, by being able to make individual investing decisions, is to outperform the broader market.

As the fund manager doesn't make as many decisions in passively managed funds, usually the fees are lower than in actively managed funds.

Other types of funds

Exchange traded funds

An exchange traded fund (ETF) is similar to an index fund. While they can track a basket of assets like an index fund, they also can track commodities, such as oil or gold, or even bonds. Unlike managed funds their share price actively changes through the day (managed fund prices are calculated at the end of each day). Furthermore, ETFs usually have higher liquidity (easier to buy and sell) and lower fees than managed funds.

Hedge funds

Hedge funds are similar to managed funds in that they pool investors' funds to invest. However they usually have little or no restrictions on how and where they invest. They also use a wide range of financial instruments, including derivatives and futures. Many hedge funds are 'absolute return' funds which means they aim to make money in falling or rising markets.

Master trusts, wraps and platforms

Master trusts

A master trust is an administrative service that lets you hold a portfolio of investments, usually managed funds, under one umbrella. As your investments are held in one place, master trusts present a simpler way for you and your financial adviser to manage your portfolio.

Features of master trusts include:

- A trustee operates the master trust and holds the clients' investments on their behalf.
- The clients' investment is determined by a 'unit price' based on the value of the underlying investments.
- Income is paid to the trustee and distributed to the investors.
- The 'unit price' usually has fees, taxes and franking credits bundled into it.
- Your investments are specific to each master trust, which means to move your investments you will need to sell, possibly incurring a tax on any profits.

Wraps

Similar to master trusts, a wrap is a product which allows you to hold your investments in one centralised place. Wraps usually hold a more diverse range of investments including managed funds, direct shares and term deposits. As wraps hold more than just managed funds, they usually have more powerful reporting and tax management functionality.

Features of wraps include:

- Like master trusts, a trustee operates the wrap, however investments are held in the clients' own names, giving them direct or beneficial ownership.
- One central cash account into which interest and dividends are paid and from which fees are taken.
- When investments are sold the proceeds are paid into the cash account, and equally when investments are bought the money is taken from the cash account.
- Investments don't need to be sold to move to different wrap products.

Platforms

Platforms are similar to wraps, offering one central place online for an adviser and the client to manage their investments. As with wraps, under a platform there are usually many different investment options, from managed funds to term deposits. A platform might also incorporate some financial planning and advice tools.

Assets can provide income, capital growth, or both. Shares and property are generally regarded as growth assets, while cash and fixed interest are regarded as income producing.

Fees

To help understand the true cost of investing, here are some key terms associated with the fees on managed funds:

Entry/establishment fee – this is the cost of setting up an account.

Performance fee – if your investment performs well, or at least beats a benchmark, the fund manager might take a proportion of the outperformance.

Redemption fee – this is a charge when you exit a fund.

Switching fees – this is the fee charged to move from one fund to another.

Indirect cost ratio – the fees above however don't necessarily include all the costs involved in running a fund – such as legal and regulatory compliance and auditing. These indirect costs are attributed to all members on a proportional basis and are known as the indirect cost ratio or ICR.

Administration fee – this represents the fees and costs charged for operating and managing your account.

Buy-sell spread – this fee may be incurred when managed investments are bought or sold and reflect the brokerage and other transaction costs incurred by the relevant investment manager.

Of course, with different investments and with different fund managers, any number of these fees may be reduced or waived.

Superannuation

For most Australians, superannuation (super) will be the second largest asset you own, behind the family home. It will also be the foundation of your retirement nest-egg. That's why it's important to understand how your super works and make the right financial decisions to reach your retirement goals.

Saving in super isn't just about what you put in – with the right investments it will grow. You can choose from different types of investments inside super which can have a big impact on your balance in the years ahead. Some people may opt to invest in the default options provided by their super plan while others may choose to invest in a variety of different investments including Australian and international shares, term deposits and cash.

This suits people who are more comfortable investing in ready-made portfolios where investment managers do the work as well as those who want to select options that match personal investment risk tolerances and goals.

Super isn't just an investment for retirement either. Your super can be used to protect the financial wellbeing of you and your family now. You can pay for different types of insurance cover through your super which means your future can be protected with the added benefit of not having to make extra out-of-pocket payments.

Types of workplace super funds

There are four main types of workplace super funds:

1. Corporate funds

A workplace super fund can be set up and run by a company 'in-house' solely for employees (and sometimes their spouses). These are often referred to as corporate super funds, and are usually the preserve of Australia's largest companies..

2. Retail funds

Retail funds are a type of fund set up and run by large financial services organisations. Retail super funds are available for anyone to join and often have a wide range of investment options available.

3. Industry funds

Industry funds are often set up by a particular industry or unions to provide super for people in those industries, however they are usually open to employees of any industry.

4. Government super funds

Also known as public sector funds, these are super funds set up by governments – Federal, State or local – and are similar to corporate 'in-house' super funds.

Other types of super funds

Self-managed super funds (SMSFs)

An SMSF is a super fund you run for your own benefit. Generally speaking, you can choose where your money is invested, however there are strict rules and compliance regulations, including:

- regular audits (including the costs of doing so)
- acting as a trustee or director
- only using the money invested for your retirement benefit

Types of contributions

Superannuation Guarantee

If you are over 18 years, or under 18 years and working over 30 hours a week your employer must contribute at least 10.5% of your salary into your super fund.

This is known as the Superannuation Guarantee or SG. If you don't nominate a fund, your employer must make contributions to a MySuper default fund.

The employer is obliged to pay you super whether you are working full-time, part-time or on a casual basis.

The SG is set to increase to 12% by 1 July 2025.

Government co-contribution

Subject to certain conditions, if you are earning less than $57,016 in the 2022/23 financial year, the Government co-contribution is one way to boost super balances. For after- tax contributions of $1,000 or more you make into super, the Government will make a co-contribution of up to $500. The $500 maximum applies for those earning less than $42,016 in the 2022/23 financial year and reduces by 3.333 cents for every dollar of income over $42,016, before phasing out completely once you earn $57,016.

Salary sacrificing

One way to top up a super balance is to use salary sacrificing to take advantage of the concessional tax rate of 15 per cent on pre-tax contributions (which can be lower than your marginal tax rate). Salary sacrificing, particularly for those who have spare cash flow can be particularly effective. This is shown in the table below which assumes an individual earning $50,000 has the choice to salary sacrifice $1,000 or receive the same amount as income:

	Taken as salary	Salary sacrifice into super
Gross contribution	$1,000	$1,000
Marginal tax rate*	34.5%	15%
Tax payable	$345	$150
Net benefit	$655	$850

**Includes Medicare levy*

If you are on a marginal tax rate of 34.5 per cent (including Medicare levy), you may be $195 better off for every $1,000 you choose to salary sacrifice. Depending on your salary, this benefit can be even greater, however it's important to remember that salary sacrificing doesn't make sense in every situation.

Taxable income and benefits	Marginal tax rate* (%)	Contributions tax rate (%)	Net savings on contributions (%)
$0 to $18,200	0	15	Negative
$18,201, to $45,000	21	15	6
$45,001 to $120,000	34.5	15	19.5
$120,001 to $180,000	39	15	24
$180,001 to $250,000	47	15	32
Over $250,000	47	30	17

**Includes Medicare levy*

Remember – concessional contributions are capped at $27,500. Please note SG contributions are included in this amount.

Nominating beneficiaries

Unlike directly owned property or shares, super doesn't form a part of your estate. Nor does it transfer to your estate after death. Instead, your super is held 'in trust' by the super fund. Usually the fund trustee will distribute it in accordance with superannuation law and the trust deed. Nominating your beneficiaries for your super allows you to have more control over who gets your super if you die.

A binding death benefit nomination is one of a variety of nominations – outlined in the table below – which legally allows a member to advise the trustee who is to receive their super benefit when they die, provided they meet certain eligibility criteria.

Type of nomination	Description	Positives	Limitations
No nomination	Trustee will generally pay the benefit to the estate.	No need to renew nominations.	There is a chance super benefits could go to someone the member didn't intend them to go to.
Non-binding nomination	A member can tell the trustee whom they want their benefits to go to. It will be considered by the trustee, but is not binding.	No need to renew nominations.	There is a chance super benefits could go to someone the member didn't intend them to go to.
Binding nomination	The trustee must pay benefits to the dependants and in the proportions set out.	The trustee must pay benefits in accordance with the member's wishes.	The definition of an eligible dependant can be restricted for different super funds. The nomination must be renewed every three years to remain valid.
Reversionary benefit nomination	This applies when opening a pension account. The member nominates who will automatically get their pension after they die.	A pension can continue with very little interruption.	The reversionary nomination can only go to an eligible dependant. A reversionary benefit nomination cannot be changed once a pension starts.

Investment bonds

Investment bonds (otherwise known as insurance bonds) are investment vehicles which may offer tax efficiency for investors.

In an investment bond, investors contributing either a lump sum or regular deposits, benefit from 'tax paid' returns while funds are invested. The income from the underlying investments is taxed at the current company tax rate of 30% and does not need to be included in the investor's tax return. The investor may be an individual (up to three individuals holding the one investment), a trust or a company. The following example assumes the investor is on the top tax rate, including Medicare levy.

Investment bond		Managed fund	
Investment earnings	$10,000	Investment earnings	$10,000
Tax paid by bond manager	$3,000	Tax paid by fund manager	$0
Net return (at maturity)	$7,000	Assessable income	$10,000
Assessable income	$0	Tax paid by investor	($4,700)
After tax return	$7,000	After tax return	$5,300

Access to funds

One of the best features of an investment bond is that they are accessible. Not only is there no limit on the amount you can invest in the first year, but the investment is accessible at any time. There are no preservation requirements or the need to meet a condition of early release. There are, however, different implications on personal income tax liabilities that are dependent on the year the investment is withdrawn. We have outlined the various scenarios below.

0-8 years*	8-9 years*	9-10 years*	10+ years*
Withdrawals before the eight year anniversary date:	*Withdrawals during the ninth year:*	*Withdrawals during the tenth year:*	*Withdrawals after the 10 year anniversary date:*
Investment earnings are subject to personal income tax. A 30 per cent tax offset applies to cover the tax already paid within the investmentbond.	Two thirds of investment earnings are subject to personal income tax at the investor's marginal tax rate. A 30 per cent tax offset applies to cover the tax already paid within the investment bond.	One third of investment earnings are subject to personal income tax at the investor's marginal tax rate. A 30 per cent tax offset applies to cover the tax already paid within the investment bond.	There is no personal income tax liability for withdrawals made after the end of the tenth year from the start date.*

** From the start date for tax purposes, which may be different to the date of initial investment.*

A wide range of managed fund investment options are available within an investment bond structure, including diversified funds, multi-manager funds, Australian and international share funds, property funds, fixed income funds and cash funds.

Investment bonds may be suitable for:

- Investors who need an alternative tax structure outside of super
- Investors wishing to save in a tax effective structure
- Investors with specific estate planning needs
- Investors wishing to lower their taxable income

Of course, an investment bond has many more features and benefits for all types of investors. Please contact us for guidance if you are unsure if an investment bond is the right investment vehicle for you.

Investments are not 'set and forget'

It's important to remember that your investment is not a set and forget proposition. There are number of reasons why your investments might change:

- The investment value may change
- The markets may change
- Your needs may change
- You may need to rebalance

We can keep your portfolio under review and recommend appropriate changes.

The true value of advice

The number of Australians seeking financial advice is growing and there are good reasons for this. In today's environment of frequent legislative changes and increasingly sophisticated financial choices, it can be difficult to find out what is the best path for you to take to achieve your financial goals.

We can help you:

- understand your current investment profile and attitude to risk
- help identify your lifestyle goals and put a plan in place to achieve them
- help you avoid expensive financial mistakes
- set a plan to protect your assets and loved ones
- ensure you're ready for the retirement you deserve
- transition you to retirement and assist planning for the next generation

Further information

To find out how we can help you look forward to a secure financial future please feel welcome to contact us.

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