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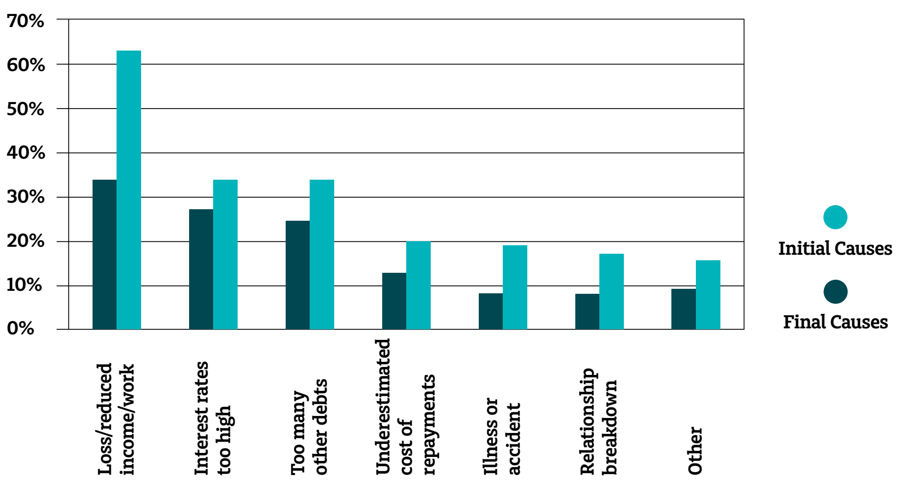
Keys to de-stressing a mortgage

We all have a tendency to be overconfident in our ability to repay loans and we tend to underestimate the likelihood of things potentially going wrong[1]. But in life things can, and sometimes do, go wrong.

What causes mortgage stress?

A study completed in 2009 for the Royal Melbourne Institute of Technology (RMIT)[2], looked at the specific causes of Australian households not being able to meet their mortgage repayments. The following graph details the initial causes and, if they changed, the final causes of mortgage stress.



1 *Understanding human behaviour in financial decision making: Some insights from behavioural economics*. Paper to accompany presentation to No Interest Loans Scheme Conference "Dignity in a Downturn" June 2009. Ian McAuley, Centre for Policy Development and University of Canberra.

2 *Mortgage default in Australia: nature, causes and social and economic Impacts*. Authored by Mike Berry, Tony Dalton and Anitra Nelson for the Australian Housing and Urban Research Institute, RMIT Research Centre, March 2010.

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Tips to reduce mortgage stress

Like most things in life, it's difficult to completely remove stress from a mortgage, but there are a few things you can do to reduce it.

Don't borrow the maximum amount

Unless you're disciplined with your budgeting, borrowing the maximum amount offered to you by a financial institution may stretch you financially.

Build up a buffer

It's a good idea to keep (or build up) a cash reserve in a mortgage offset account, to provide a buffer which can be drawn upon in emergencies.

Consider personal insurances

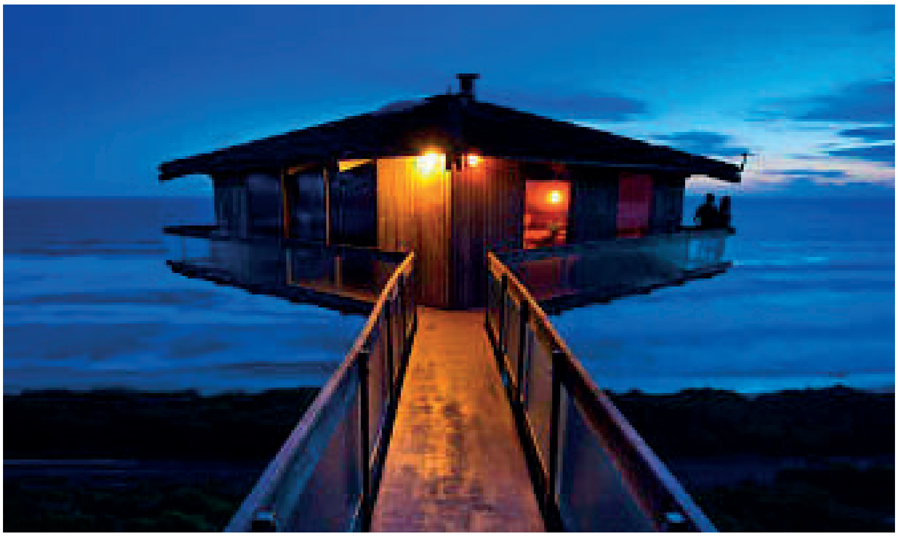
- Income Protection Insurance – can replace up to 75% of your income if you are unable to work due to illness or injury.
- Critical Illness Insurance – can help you service or pay off your mortgage and meet a range of expenses in the event you suffer a specified illness, such as cancer or a heart attack.
- Total and Permanent Disability (TPD) Insurance – can help you service or pay off your mortgage and provide an ongoing income if you become totally and permanently disabled.
- Life Insurance – can be used to service or pay off your mortgage and provide your family with an ongoing income if you pass away.

Consider fixing your interest rate

This can protect against rising interest rates. The downside is you're often restricted from making additional payments into a fixed rate loan. Many people find a split fixed and variable rate loan works best, as additional repayments can be made into the variable rate portion of the loan.

Don't add fuel to the fire

Steer away from using credit cards to compensate for the difficulty of meeting your mortgage repayments. Using debt to service debt is very likely to compound the problem.



The investor's guide to growth assets (Part 1)

Growth – it's what we all like to hear when the subject is our money. However, seldom is there growth without a certain level of risk. Accordingly, growth assets have the potential to earn a higher rate of return over the long-term, but are also generally more volatile than defensive assets.

In this first instalment of our two part series, we take a closer look at three major growth asset classes, and discuss their potential risks and benefits for your investment portfolio.

Australian shares

Australian shares represent a part-ownership in an Australian company. They can provide the opportunity for capital growth, income and tax benefits through the dividend imputation system. The dividend imputation system generally allows an investor to receive a tax credit for any tax the company has already paid on the income distributed to them.

Although Australian shares can be expected to outperform many other investment classes over the long-term, due to share market volatility, share investments are likely to fluctuate in value across all time periods, particularly in the short to medium term.

Be aware

- Investing in a single share or a very small number of individual shares is more likely to expose you to greater fluctuation in the value of your investment, as opposed to investing across a range of shares. It's possible to further reduce fluctuations by investing across different economic sectors.

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- Small companies are generally considered higher risk investments.
- Share prices can rise and fall suddenly in response to many factors, including company profits, market sentiment, industry issues and economic trends. For this reason Australian shares are generally viewed as long-term (5-year plus) investments, as they can experience significant levels of short to medium term volatility.

International shares

International shares represent a part ownership in a foreign company. Investing in International shares enables you to diversify your share market exposure, not only across a broader range of countries, but also in companies and industries which are not significantly represented in the Australian share market.

Be aware

- International shares have similar characteristics to Australian shares, with two important differences:
  - the income return from international shares generally does not provide a dividend imputation tax benefit, and
  - both the capital value and the income return of the investment may be influenced by currency exchange rates.
- In the short-term, adverse market conditions may result in a significant decline in the value of International shares, and it may take some time for the value of the investment to recover. For this reason, International shares are generally viewed as long-term (5-year plus) investments.

Australian property securities

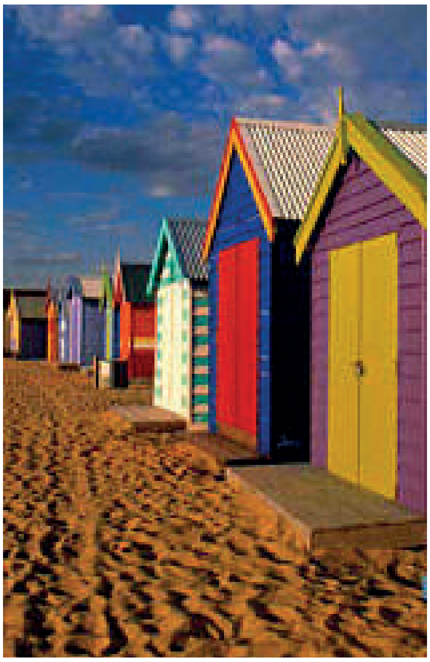
Investing in property securities as an asset class is different to buying a house or an investment property. Property securities are referred to as Australian Real Estate Investment Trusts (AREITs). AREITs are investments listed on the Australian stock exchange, which provide exposure to a portfolio of direct property investments. They 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 sectors.

Some managed investment funds invest in a portfolio of AREITs. The advantage of this is investors access the benefits of investing in property (for example, capital growth and income), whilst their investment remains liquid. Also, managed funds may spread investors' risk, as they generally provide a more diversified property portfolio.

Property securities primarily earn income from rent. Historically, this type of investment provides a reasonably regular income, relative to other growth assets. Over the long-term, they generally appreciate in value and offer a portfolio some protection against the impact of inflation.

Be aware

- In the short to medium-term, the value of AREITs is expected to increase or decrease in value, in accordance with movements in both their specific sector and the share market generally. As a result, property securities tend to be more volatile than defensive assets and are generally viewed as long-term (5-year plus) investments.
- Property securities tend to generate a higher proportion of their return through income and a lower proportion through capital growth.



Maintain your family's living standard

Did you know, one in five families will be impacted by the death of a parent, a serious accident or illness that renders a parent unable to work[3]?

Life insurance is one way you can consider using insurance to provide financial protection for your financially dependent family, in the circumstance that you unexpectedly pass away.

What are the benefits?

- you could provide your family with an ongoing source of income, and
- enable them to meet their living expenses.

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3 The Lifewise / NATSEM Underinsurance Report, *Understanding the social and economic cost of underinsurance, February 2010.*

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How do you prepare?

It is important to make sure you consider having enough Life insurance, to enable your family to meet their ongoing living expenses if tragedy struck and you suddenly passed away.

As a starting point, you should consider:

- working out what your family spends each year on groceries, education, household bills and other living expenses, and
- how long your family needs to be financially supported in your absence.

Once you determine these two elements, your financial adviser can help you calculate the level of Life insurance cover you'll need to provide the necessary income over the desired time period.

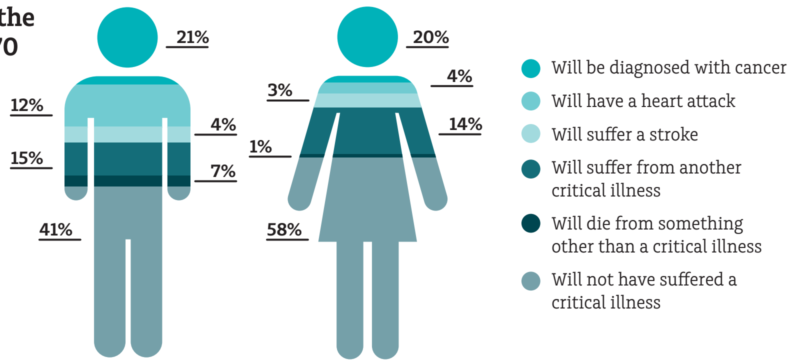
When doing this, a financial adviser can also take into account tax that may be payable on the income your family will receive, and allow for the impact of inflation.

To find out if this strategy suits your needs and circumstances, speak to your financial adviser.

You should also consider other types of cover, such as Income Protection Insurance, Critical Illness Insurance and Total and Permanent Disability Insurance. They could help secure your family's future in the event that you do not pass away, but are permanently or temporarily disabled, or suffer a critical illness

For example, 59% of Australian males and 42% of Australian females are likely to suffer a critical illness prior to age 70[4]:

Before the age of 70



4 Munich Reinsurance Group in Australasia, 2009. This is general population data based on those who are currently 30.

Tips and traps

- When determining the amount of Life insurance you require, it's also important to take into account how you cover funeral and estate costs, in the event you pass away.
- You may want to review your Life insurance cover regularly as your needs may change over time. Your financial adviser can assist you with this.
- If you are the primary income earner, you should also consider insurance which enables your family to meet their ongoing living expenses, in the event you become ill or injured.
- If your partner is not working, they should consider insurances which cover medical, childcare and housekeeping expenses, if they become critically ill or pass away.
- There may be some advantages in taking out Life insurance through a super fund; however there are restrictions on who you can nominate as a beneficiary. Tax charges may also apply to eligible beneficiaries when a death benefit (including insurance proceeds) is paid as a lump sum, pension or a combination of both, by the super fund.
- It may be more cost-effective over the longer term to pay level premiums, rather than stepped premiums which increase each year as you age.