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## INTEREST RATES, FINANCIAL MARKETS AND THE ECONOMY

### WHEN WILL IT END?

The Official Cash Rate remains at 6.25% as the Reserve Bank of Australia (RBA) has decided to leave rates on hold following their board meeting on 5 June 2007. It almost seems like Australia is operating within a utopian economy, one with high production, low unemployment and sturdy retail expenditure, all with negligible inflation.

Evidently, key business sentiment remains upbeat which is dutifully proven by the increase in the Westpac-Melbourne Consumer Sentiment Index and the NAB Business Sentiment Index, which have risen considerably this year. The sharemarket has also strengthened ahead of good news concerning long-term international resource demand, which should keep metal prices at a premium for many years.

### QUOTE

"Don't judge each day by the harvest you reap, but the seeds you plant."

- Robert Louis Stevenson

Furthermore, domestic residential buildings completed rose by approximately 3.5% in the March quarter, indicating that our economy, despite the recent softening of price expectations following inflationary data, remains relatively strong. While recent inflationary figures surprised financial services firms there seems to be a feeling that price drivers (e.g. raw materials, consumables, electricity etc) will present in the medium to long term; the only question is precisely when?

With unemployment levels dwelling at 4.5% and domestic demand increasing at more than 1% in the September 2006 and December 2006 quarters, it should be no surprise if inflation heads upwards to reflect productivity tightness as output peaks. Put simply, it would be unfair to suggest that any economic regulator, including the RBA, could maintain these ideal business and consumer conditions indefinitely.

### STOP PRESS

The \$1,000,000 undeducted contribution limit for superannuation ends on Friday 29<sup>th</sup> June 2007.

If you want to take advantage of the superannuation co contribution please note that your funds must be banked by the superannuation fund by Friday 29<sup>th</sup> June.

As mentioned in previous newsletters superannuation withdrawals will be tax free for lump sums and pensions drawn for superannuation members over the age of 60.

**For more information or clarification please contact MCP Financial**

While impossible to accurately gauge, we believe that rates should remain on hold for the remainder of the year,

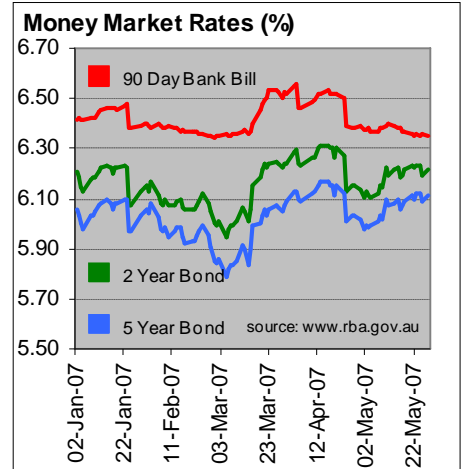
## Market Statistics

Official Cash Rate: 6.25%  
U.S. Fed. Funds: 0.00%  
90-Day Bill Rate: 6.47%  
10 Year Bond Rate: 6.27%  
Aust. Dollar (US) 84.23  
All Ordinaries (Aus): 6317.1

As at 18th June 2007

with a slight possibility of a rate rise in the fourth quarter if inflation increases and labour markets remain tight.

### Money Market Rates



**Money Market Rates:** Two and Five Year Bond rates have increased since May, following a positive medium to long-term outlook for the Australian economy. Conversely, the 90 Day Bank Bill rate has declined.

**Evan Tepper, MCP Group**

### QUESTIONS AND ANSWERS

The MCP Group team will answer a selection of our clients' queries in each edition of our monthly newsletter. To submit your query to our office please contact our Group by phone on (03) 9620 2001 or email ([enquiries@mcpgroup.com.au](mailto:enquiries@mcpgroup.com.au)).

## LEGAL

### I've heard about Binding Death Nominations being offered by my Superannuation Fund. What are the advantages and disadvantages of Binding Death Nominations? Should I take out a Binding Death Nomination?

The reason that Superannuation Funds offer Binding Death Nominations is to carry out your wishes if you pass away. Even though your superannuation is protected and held in a Trust it is still your asset, money that you have worked hard to accrue. Many people argue that **they** should decide whom it be paid to, not their executor.

Conversely, there are several reasons why Superannuation Funds should not offer Binding Death Benefit Nominations. As your circumstances can change rapidly, a Binding Nomination may leave a new spouse and minor without proper access to your benefit. Alternatively, if the Binding Nomination is made to your estate, there may be a likelihood that creditors could receive a large portion of your assets to the detriment of your spouse and/or dependents.

To provide for further certainty in relation to your estate we suggest making a Will and regularly updating it.

Please speak to Michael Poynter or myself if you require any further information in relation to our Wills and Probate services.

Shane Frost, MCP Legal



## INDEMNITY

### WHAT IS AN INDEMNITY?

An indemnity allocates risks under an agreement and shifts liability from one party to another in a pre-agreed acceptance of liability.

Arriving at clear indemnities can save stress and funds in the future for you and your business.

### WHEN AN INDEMNITY IS USED?

A party may wish to use an indemnity for the following reasons:

- Many commercial agreements such as lease, franchise or sale of business contracts;
- To guarantee against any loss which another party may incur. For example, two parties settle a dispute over goods supplied which may be faulty. One party may agree to pay any claims which may arise due to the faulty goods in the future;
- Protection against future loss;
- Legal exemption from liability for damages;
- To remove another party's ability to claim defences and make cross-claims (e.g. claims of contributory negligence).



**Misunderstandings?** Indemnities are designed to clearly allocate risks, shifting liability from one party to another.

### WHAT SHOULD AN INDEMNITY SAY?

Ensure that the indemnity is tightly drafted and suitable for your needs and those giving the indemnity. While many parties are reluctant to provide an indemnity, if you manage to persuade the other side to give an indemnity you do not want it to be struck out for being ambiguous.

Further, there is no point in having an indemnity unless it spells out clearly the extent of the losses recoverable.

### CAN I STILL LIMIT MY LIABILITY?

If you have a limitation of liability clause, make sure that the relationship between your indemnity and the limitation of liability clause is clear.

### INSURANCE

If you are required to give an indemnity, consider whether you need to notify your insurer before you do so (this will obviously depend on the reach of the indemnity and the insurance cover held).

### WHAT VALUE IS THE INDEMNITY?

Always consider who is giving the indemnity. It is pointless having an insolvent company or bankrupt natural person provide an indemnity.

A well drafted and a good understanding of an indemnity can be critical. It is important that both parties in a transaction understand clearly their responsibilities and rights. It is strongly recommended business advisers including accountants and lawyers are involved in the process, to ensure rights and obligations are respectively protected and honoured.

Shane Frost, MCP Legal



## GROWTH VERSUS INCOME SHARES

The total return on a share is comprised of two components - dividends and realised capital gains.

The ultimate decision regarding a company's dividend yield and profit payout rate lies with its board of directors. If a company's primary goal is to increase market share by reinvesting profits, its board may not decide to offer dividends, or offer a relatively small one at that. Shares in these type of businesses are often coined to be "growth stocks", as company emphasis revolves around expanding operations to increase profits.

Growth stocks have a tendency to trade at higher Price to Earning (PE) ratio than income shares, as profits are forecast to be higher in future years when compared to the company's current earnings. Put simply, the company is striving to grow its revenue faster than the market average by investing in the business. Therefore, the current P/E ratio is not a good representation of future profitability.

An extreme example of "growth

stocks" may be internet shares prior to 2000. While demand for these companies was extremely strong amongst personal and institutional investors, many of the concerning stocks in question traded at an extremely high PE ratio (or no PE as no profits had been realised). This is because many investors believed that forecasted future earnings would make the underlying stock profitable in due course, hence the reason for their trading price at the time.

Growth stocks tend to be volatile investment vehicles, as the company's share price is based on sentiment towards existing projects, macroeconomic business conditions and forecasted earnings, all of which can change rapidly.

Conversely, companies that opt to pay a relatively higher dividend rate to its shareholders are termed to be "income stocks". These types of securities are often identified by their strong market position, steady stream of profits and higher dividend yield relative to the market. Income shares generally have a lower P/E ratio, as the company is in the process of realising profits now, rather than investing into their operations to realise profits in the future.

One of the most common predicaments investors face is whether they should invest into growth or income stocks, which isn't always an easy question to answer.

Various factors must be considered when deciding on an appropriate portfolio construction, including the risk profile and objectives of the underlying investor as well as the requirement for periodic income.

### SCENARIO – THE BENEFITS OF GROWTH-BIASED COMPANIES

Two companies operate within the same industry and have a return on invested profits of 15% per year. Each company has 100 shareholders and an income of \$250 per. Company A is growth orientated, distributing 6% of their profits to shareholders (0.5% yield). Company B distributes 84% of profits to shareholders (7% yield). To simplify proceedings we will assume that both companies trade at a Price to Earnings Ratio of 12 times. Both companies reinvest retained profits.

Year	Share A (Profit Payout Ratio of 6%)						
	Company		Shareholder				Total
	Dividend	Earnings	Share Price	Dividend	Capital Gain		
2007	\$ 15	\$ 250	\$ 30.00	\$ 0.15	\$ -	\$ 0.15	
2008	\$ 17	\$ 285	\$ 34.23	\$ 0.17	\$ 4.23	\$ 4.40	
2009	\$ 20	\$ 325	\$ 39.06	\$ 0.20	\$ 4.83	\$ 5.02	
2010	\$ 22	\$ 371	\$ 44.56	\$ 0.22	\$ 5.51	\$ 5.73	
2011	\$ 25	\$ 424	\$ 50.85	\$ 0.25	\$ 6.28	\$ 6.54	
2012	\$ 29	\$ 483	\$ 58.02	\$ 0.29	\$ 7.17	\$ 7.46	
2013	\$ 33	\$ 552	\$ 66.20	\$ 0.33	\$ 8.18	\$ 8.51	
2014	\$ 38	\$ 629	\$ 75.53	\$ 0.38	\$ 9.33	\$ 9.71	
2015	\$ 43	\$ 718	\$ 86.18	\$ 0.43	\$ 10.65	\$ 11.08	
2016	\$ 49	\$ 819	\$ 98.33	\$ 0.49	\$ 12.15	\$ 12.64	
<b>Total</b>						<b>\$ 71.25</b>	

Year	Share B (Profit Payout Ratio of 84%)						
	Company		Shareholder				Total
	Dividend	Earnings	Share Price	Dividend	Capital Gain		
2007	\$ 210	\$ 250	\$ 30.00	\$ 2.10	\$ -	\$ 2.10	
2008	\$ 215	\$ 256	\$ 30.72	\$ 2.15	\$ 0.72	\$ 2.87	
2009	\$ 220	\$ 262	\$ 31.46	\$ 2.20	\$ 0.74	\$ 2.94	
2010	\$ 225	\$ 268	\$ 32.21	\$ 2.25	\$ 0.75	\$ 3.01	
2011	\$ 231	\$ 275	\$ 32.99	\$ 2.31	\$ 0.77	\$ 3.08	
2012	\$ 236	\$ 281	\$ 33.78	\$ 2.36	\$ 0.79	\$ 3.16	
2013	\$ 242	\$ 288	\$ 34.59	\$ 2.42	\$ 0.81	\$ 3.23	
2014	\$ 248	\$ 295	\$ 35.42	\$ 2.48	\$ 0.83	\$ 3.31	
2015	\$ 254	\$ 302	\$ 36.27	\$ 2.54	\$ 0.85	\$ 3.39	
2016	\$ 260	\$ 309	\$ 37.14	\$ 2.60	\$ 0.87	\$ 3.47	
<b>Total</b>						<b>\$ 30.56</b>	

**Growth versus Income Stocks:** Growth companies intend to use profits to grow their revenues. This can often be very rewarding for shareholders due to the premise of compounding. Share Price is based on a PE of 12 times.

### CONCLUSION

The scenario has been simplified due to the assumption that return on investment and the company's P/E ratio remain fixed at 15% and 12 times respectively. However, the core results of the example are important to note. This being that income and growth-biased shares return value to shareholders differently. In some cases, stocks that are able to grow their earnings are extremely profitable in the long run due to the effect of compounding returns.

We must advise that there are certain risks associated with investing in growth-orientated shares, including the heightened variability of investment returns. Please speak to John Ross or myself at our office for further information.

**Dave Mac Manus, MCP Financial**

### YEAR END TAX PLANNING

The Australian taxation system allows a tax deduction where there is a reasonable nexus (connection) with the receipt of assessable income. Hence expenses incurred while earning assessable income are deductible. (subject to some restrictions) Therefore it makes sense to bring forward expenses if possible to this financial year, and if possible defer the receipt of assessable income to next financial year.

Interest expense which produces assessable income such as dividends (shares) and rental income (property) is an allowable expense. Negative gearing means that your interest expense exceeds the income from the investment and you have a loss available for offset against other taxable income. You can prepay interest for twelve months and claim a tax deduction. Please contact our office for further informa-

tion on repayment of interest expense.

Superannuation is also a significant tax planning tool. Superannuation contributions for which you or your



**Medical Package Benefits:** Some financiers waive Lenders Mortgage Insurance Premiums for Medically trained First Home Buyers.

employer claims a tax deduction are taxed at 15% on entry to the super fund. This may be contrasted with the individual tax rates particularly if you have no debt it may make sense to increase tax deductible contributions to super. If you run your own business there may still be an opportunity to contribute in this financial year. Once again please contact our office for further information.

**John Ross, MCP Financial**



**THE DISCOUNTS AVAILABLE TO MEDICAL PRACTITIONERS**

There are a number of financiers that provide exceptional discounts to accredited medical practitioners working in the health industry.

Orthodontists, dentists, doctors of medicine, physiotherapists and medical specialists can all receive special financial discounts as a result of their occupation, providing they meet minimum income level requirements (approximately \$50,000 per annum).

Offered by a range of primary and second tier lenders, Medical Professionals Packages provide discounts and fee waivers for commercial or residential borrowers. These include

Financial Benefits Available to Medical Practitioners	
RESIDENTIAL	COMMERCIAL
<i>Secured by First Mortgage Over Residential Property</i>	<i>Secured by Registered Mortgage Over Commercial Property or Business Assets</i>
<p><b>p</b> Access to a suite of bank professional packages, offering discounts of up to 0.8% off the Standard Variable Mortgage Rate.</p> <p><b>p</b> Additional interest rate discounts for borrowings greater than \$1M.</p> <p><b>p</b> Waived Lenders Mortgage Insurance ("LMI") for medical professionals buying their first residential property. This allows medical professionals to borrow as much as 95% of the purchase price without LMI.</p> <p><b>p</b> Ability to waive standard fees such as the application fee and account keeping fees.</p>	<p><b>p</b> The ability to borrow up to 90% of the valuation of converted or standard commercial property. (e.g. Medical / Dental / Veterinary)</p> <p><b>p</b> Ability to obtain unsecured working capital finance against the business assets. (Subject to underwriting standards)</p> <p><b>p</b> Ability to negotiate additional interest rate discounts for borrowings greater than \$1M. Extended loan terms are also available in some instances.</p> <p><b>p</b> 100% funding for Equipment Finance needs.</p>

**Medical Practitioner Packages:** Medical Practitioners may be able to receive the above benefits with selected financiers. Contact MCP Finance to find out which ones!

the ability to lend at a relatively high Loan to Value Ratio (LVR), particularly when securing a commercial loan with business assets.

**HOW CAN MCP GROUP HELP?**

MCP Finance is able to provide a suite of benefits for Medically Qualified loan applicants.

These include, but are not limited to:

- Access to multiple financiers who offer Medical Practitioner Packages (to allow you to obtain the most beneficial lending terms and conditions for your particular circumstances);
- Preparation of detailed loan proposals that communicate the lending process in a clear and succinct manner;
- Conveyancing services and a pre-purchase contract review;
- Access to support services, including those with experience in Law, Accounting and Finance;
- Access to discounted legal support including contract reviews, Wills & Probate and other commercial legal services; and
- The preparation of employee handbooks and contracts.

**Adam Maciejewski, MCP Finance**

**FINANCIER NEWS**

**Mortgage Market Update**

A recent mortgage publication identified that a Variable Rate Loan with a Repayment Cap option may be offered to home buyers in the future. The loan would be a variable rate loan with a fixed repayment, with the loan term varying to accommodate for this. For example, future rate rises would see an extension to the loan term.

This is believed to make home ownership more affordable by managing the issue of risk which wards off many potential buyers, especially first home buyers.

**GE Money**

GE Money specialise in loans for borrowers who've had credit defaults lodged against their record. For example, GE Money will ignore credit defaults which are less than \$500 if they have been paid, and will often ignore such defaults if outstanding but paid before the loan settles.

Credit defaults above \$500 will not be taken into consideration if discharged more than 2 years ago. Borrowers with credit defaults are categorised by their number of defaults and are charged a buffer to GE Money's standard rates accordingly. However, these rates are often still competitive within the mortgage market.