

The Recession

- how bad is it really?

If you read almost any newspaper or watch the television news you could be forgiven for thinking the best course of action is to go home, take the phone off the hook and wait for the end of life as we know it, but is that really the case? It cannot be denied that we're in recession, but just how bad is this recession, and what should your response be?

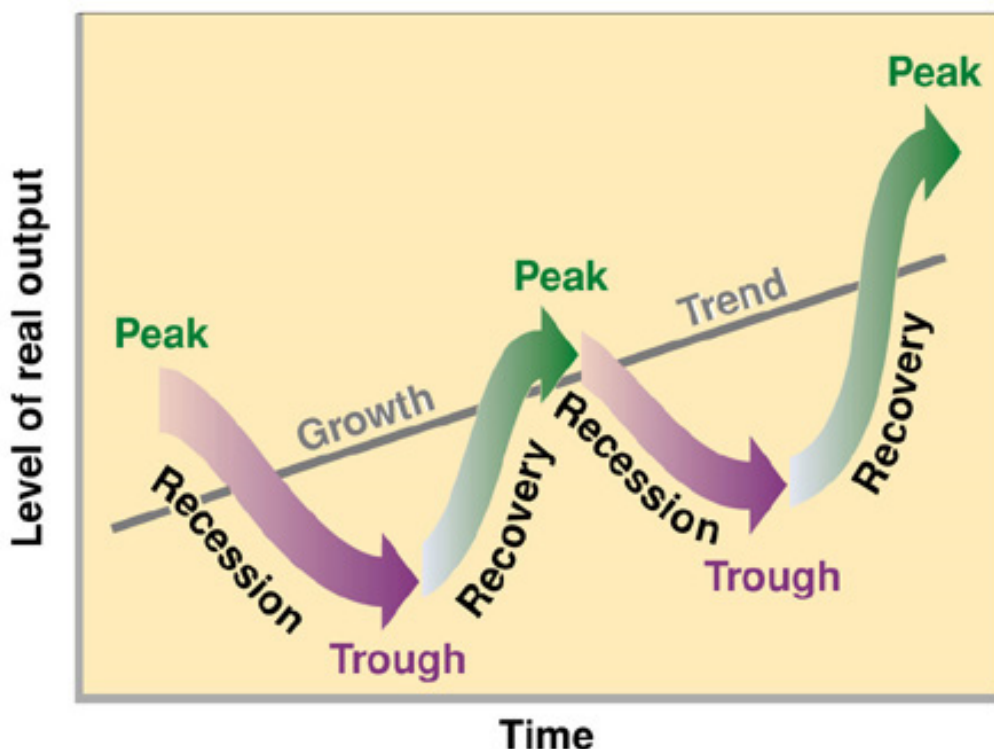
The first thing we should all remember is that markets are cyclical, and expecting constant boom times are like expecting 365 days of summer. As we go to press spring flowers are emerging, the days are getting longer and temperatures are rising, and before too long our biggest problem will be keeping cool; yet just a few weeks ago the days were short, cold and wet. The same thing applies to "recessions" - they are a natural and inevitable part of life, they come and then they go.

The second thing is to look at how this so-called global economic crisis, apparently the worst since the great depression, compares to other downturns. Most of us will remember the 1987 sharemarket crash, but how many of us can remember how bleak things were in the years following? Unemployment was 11%, compared to the current level of 7.5% and business failures were a constant event. Then we had the mid 70s downturn with 15% inflation, carless days and the highest unemployment since the end of the war.

Finally and most importantly we need to look at how we respond to this event. Just as a gardener won't plant tomatoes and courgettes in winter, but will instead prepare the soil in their gardens for spring and summer growth; we need to use this time

to prepare for the coming recovery. It may be a long time before we see another boom like the one we experienced in the first few years of this decade, but we will experience growth and recovery soon, so now is the time to prepare. That means managing, and where possible retiring debt. Sometimes it means consolidating, retrenching and rebuilding but sometimes it means expanding and growing into new opportunities and markets, or at least preparing to do that.

Just as winter has caused the abundant growth of summer to die back leaving empty soil ready to be planted, so the last few years have cleared the way for tomorrow's growth. Will you be ready to take part in the coming recovery? The key is to have goals and a plan to achieve those goals. We work with first home buyers to business owners to look at their goals and develop and implement strategies to achieve those goals. Give us a call and let's make a time to help set you up for tomorrow.



THIS ISSUE:

1. Is the recession as bad as it's made out to be?
2. We've heard about leaky homes, but what about leaky trusts?
3. What kind of mortgage is best for you?
4. Tax changes affect property investors

Is your family trust leaky?

Family trusts have become an increasingly common part of personal financial planning with many thousands of ordinary Kiwis taking advantage of their many benefits, but how many of them will fail to do their job if challenged? And how many trusts have there been setup without a Financial plan or strategy to support their purpose. There may be a potentially massive problem, largely caused by a lack of understanding and administration by those who settle their assets into Trusts.

Common problem areas include:

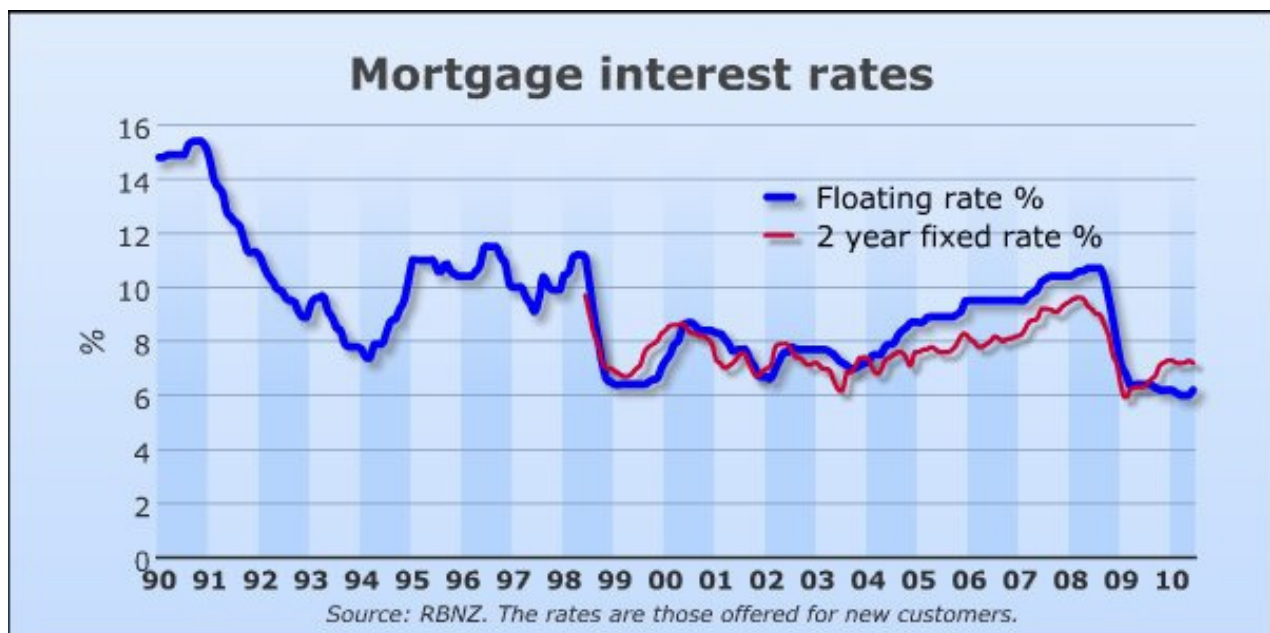
- Failure to gift into the trust appropriately. Many people only gift assets into the trust for one or two years meaning very little of the assets are owned by the trust.
- Poorly drafted trust documentation that means a surviving trustee can resetttle the trust and exclude current beneficiaries. For example, if one partner in a mixed family dies the surviving partner may be able to exclude the deceased partner's children from the estate.
- People tainting a trust fund by using it as a working account and purchasing personal goods through it.
- Injecting new capital without acknowledging gifting

- Losing out on tax benefits by gifting 100% of the shares of a company into the trust.
- Failure to hold required annual meetings or complete paperwork including the minutes book
- Loss making rental properties placed in a trust meaning they can't be used to reduce the settlor's taxable income.
- Not reading the trust deeds thoroughly and getting them explained when required.

In our experience all of these are far too common, and we regularly encounter clients with trusts that just won't stand up if challenged and/or are failing to deliver all the benefits of a well set-up trust. If you have a family trust we suggest you give us a call and we'll review it with a Trust expert as part of your overall financial plan, to make sure it's doing what you want it to do. Experts in the field say that 75% of trusts could fail when challenged, make sure yours isn't one of them.

Leaky homes have been a nightmare, leaky trusts could be your worst nightmare. Call us now to discuss your trust and financial plan, and we'll check that it won't leave you high and dry.

Interest rates stable



The most recent two reviews of the OCR saw the Reserve Bank increase the rate 0.25% in June and July meaning the OCR has increased from 2.50% to 3.00%.

Despite this there has been little upwards pressure on home loan interest rates with floating rates still below 7.0% and fixed rates reducing.

So what should you do? The answer to that question is not

simply determined by interest rate movements, but by your personal circumstances. You need to look at your personal cashflow, future life events (wage movements, family changes etc) and your medium and long term goals to make the right decision. The following article on mortgage structure covers both the importance of strategic thinking in your mortgage planning, and not allowing yourself to be driven by interest rates alone.

*"No great man ever complains of want of opportunities."
- Ralph Waldo Emerson*

Do you have the right loan?

- Home loan structure key component of financial planning

Split Loans

It is said that the one thing we can depend on is change, and every one of us has experienced changes to our financial circumstances that have made a significant difference to our overall situation. Your mortgage is quite probably the biggest part of your financial situation, and a very common approach to managing finances is to introduce a split home loan structure.

There are two major benefits to a split home loan structure:

1. It gives you flexibility. The drawback to a fixed loan is that you may find it harder to pay chunks off your mortgage, or face a penalty if you pay your loan off early. With a split loan you have the stability of a fixed rate loan but can pay off chunks of the floating loan.
2. It reduces risk from changing interest rates. The risk with fixed rate loans is you could lock in to a given rate just before the rates fall, or come out of a fixed rate into a much higher rate, resulting in sudden cashflow pressure. The risk to a floating rate is lack of certainty in your budgeting and the risk that rates will rise.

The questions that we ask when we decide how to structure your loan include:

Do you anticipate paying your loan off early? If so we'll increase the percentage in floating so you don't incur penalties.

How sensitive is your weekly budget to changes? The more sensitive you are to changes, the more we'll put in fixed.

Are you likely to sell your property within the next 12 months to 2 years? If you're at all likely to sell your property, then you need to look at the fixed component, if any, of your loan.

Do you want to make the most of current low rates, but can afford higher payments? Then we'll increase the amount set in floating but make your payments higher than they need to be.

It's important to remember with split loans that you need to regularly review and reassess them, and we recommend at least an annual review. If you have a split loan and haven't reviewed it for more than a year, give us a call. And if you would like to explore whether a split loan works for you, let's have a look at your situation

Flexi type loans

Flexi or revolving credit loans are not new, but are still an extremely useful option, especially for self employed people and those with variable incomes and/or expenses. It is also possible to save quite a lot of money in interest by using a flexi loan. The way they work is that your mortgage and working account are joined together, and as your wages are deposited, the overall balance owing decreases, and then you draw down money against your total loan balance as you pay your bills and conduct your daily affairs.

Advantages:

1. Cheap and easy finance. You're paying mortgage rates on overdrafts and can access money for short term finance like hire purchases. Also every time your wages go into your account the total balance against which you are paying interest decreases.
2. Faster repayment of your home loan. With discipline and careful management it is possible to pay your home loan off faster.
3. You get a simplified financial situation with one account.

Disadvantages:

1. It's easy to get caught in a trap and continuously use the equity available for consumption meaning your home loan never decreases. It takes discipline and management to avoid this trap.

Flexi loans offer greater flexibility, increased simplicity and can save money for some people, but can be a major problem to others. If you're interested in exploring whether a flexi type loan would work for you, then give us a call.

"First say to yourself what you would be; and then do what you have to do."
- Epictetus

Changes to the taxation of investment property

LAQCs

The recent budget introduced some sweeping changes to how property investment is taxed, specifically the introduction of limitations to the ability of investors to claim tax deductions by attributing losses accrued by a rental property against the investor's other income, typically something that is done through the use of an LAQC.

The changes announced in the budget include that an investor's profits and losses will be taxed according to the rules that currently apply to a limited partnership. That means losses will be limited to the actual investment the shareholder has made in the company.

If you currently derive losses from an LAQC we suggest you contact us to look at how these changes impact on you personally as for some investors an LAQC still has significant benefit. It may be that you need to look at an alternative mechanism, and what is the most appropriate solution varies from investor to investor, and we will need to look at your overall investment strategy before making recommendations.

Depreciation changes

Depreciation has been removed from buildings with an expected life of 50 years or more, which has traditionally been an area where investors have been able to gain tax benefits. Some buildings are able to have depreciation claimed against them, and it's important to know what these are, so check your current situation with your accountant if you have any doubts.

However depreciation is still able to be claimed against chattels. Historically investors generally didn't worry about chattels because there was significantly more benefit to claiming depreciation against buildings, however separating chattels out from the building will become an important consideration. There are some situations where you will be unable to claim this depreciation against your tax bill, but for many people chattel depreciation presents an opportunity to cut your tax bill. Before you make any decisions please contact us and we can advise you as to the best options for you.



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Yes please, I'd like to find out about:

Reviewing my mortgage or refinancing

Investing in property

Buying a Business

Buying a first home

Reviewing my insurance

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