

## Disasters: looking at the economic effect

The economy today is progressively becoming more interconnected. This means a natural disaster across the globe can have a financial impact here at home in Australia. As we know, recently there has been a spate of disasters which have wreaked havoc locally and globally.

It can be hard to predict the economic impact after a disaster. Often the first reaction is a sharp drop in the stock market. This can be a lasting downturn but sometimes it can recover quickly. When Hurricane Katrina hit the US in 2005 for example, the Dow Jones Industrial Average recovered in less than ten days. But the previous two hurricanes created lasting drops in the stock market.

When China's Sichuan Province was hit by a huge earthquake in May 2008, the devastation was monumental, but the Chinese government say it ultimately helped their economy. Within a month of the quake, a massive rebuilding effort was underway and billions of dollars were pumped into the Chinese economy. This boosted the national economic growth by 0.3 percent during the period. This was particularly significant given that it was during the depth of the Global Financial Crisis.<sup>1</sup>

Since the economic effects of a disaster can vary significantly, they're not often well-captured by the simple headlines provided by the media. It's important to delve a little deeper to properly understand the various impacts of a disaster and how they flow through the economy.

### Direct damage

The loss of life is undisputedly the hardest part of any disaster. As people search for survivors, or even attempt to make areas safe, there is often a huge expenditure needed for relief and emergency response.

The second direct economic impact is the destruction. This is often the focus in mainstream media as they show horrific images of residential and business areas which have been hit by the disaster. There are substantial economic consequences in rebuilding these areas, but also in replacing finished and semi-finished goods, raw materials and spare parts.

An example of the massive cost of direct damage is in the recent Queensland floods, the Queensland State Government's 2010-11 Mid Year Fiscal and Economic Review, has estimated that the cost of rebuilding public infrastructure will be \$5 billion over 3 years.<sup>2</sup>



### In this issue...

- Disasters: looking at the economic effect
- Superannuation: the long and short of it
- Aged care: making an informed decision

1 Source: Boston Globe, How disasters help, by Drake Bennett, July 6, 2008

2 Source: Queensland State Budget 2010-11 – Mid Year Fiscal and Economic Review – [www.treasury.qld.gov.au](http://www.treasury.qld.gov.au)

# Disasters:

## looking at the economic effect (continued)

### Indirect damages

Goods and services that will not be produced because of a disaster can have a significant negative economic effect. It can take a lot of time to fix machinery and source new materials. Cost can increase even more if there is a need to use alternative means of production or distribution. As delays impact exporting, losses in revenue can impact international market shares.

One way disaster affected areas can mitigate this loss of income is to focus on sectors which were not as affected. For example, when Jamaica was hit by

Hurricane Gilbert, instead of focusing on the decimated agricultural industry they rebuilt hotels. Within three months they had recovered the tourism industry and had minimised the loss of market share.

### Secondary effects

Disasters can interrupt a country's economy as a whole. Demand for building material, food and energy increases, at the same time as supply is restricted due to damaged infrastructure. This can cause spikes in inflation. Often, rebuilding efforts result in a shortage of skilled labour which forces wages to increase. This also impacts inflation.

Local and federal government finances often receive a double hit. Reduced economic activity results in lower tax revenues at the same time as they need to massively increase expenditure on infrastructure and disaster relief. These effects can be felt over a number of years as few governments budget for the unknown.

### How might this affect your investments?

Many of the impacts of a disaster can have direct influence on your investment portfolio or superannuation. This is especially evident if you opt into a global share investment option or choose to own direct shares.

Another impact which can seem less obvious, but can have a huge impact on your day-to-day life, is the effect on commodity prices. An example of this is when petrol prices increased significantly in the aftermath of Hurricane Katrina.

### The bottom line

Disasters can be heartbreaking and have a horrific impact. But when looking at the economic impact, there is a danger in automatically predicting doom and gloom, as the media is fond of doing.

When a disaster occurs, there will undoubtedly be a negative economic impact, but how long this lasts and how it effects your investments will depend on a large number of factors. Ultimately, rebuilding after the disaster will result in growth. It is best to assess the situation with your financial adviser to find the solution which suits your needs.



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# Superannuation: the long and short of it

Financial markets have a natural tendency to go up and down and in recent years, we've seen some remarkable examples of both. Superannuation funds are not impervious to these fluctuations and if you regularly review your statements, you would have seen the impact on your account. So what should you do?

You hear about it all the time – investors selling stocks after a negative earnings release, super funds being promoted because of one quarter's results and even sports fans who start supporting a team because they start winning. These are all scenarios which have a short-term focus, but what about the long-term perspective?

Short-term focus can be hard to avoid as we live in a time where we expect instant

rewards and recognition. However, we can't expect the same for our superannuation.

Super is a long-term investment and to get the best results you need to think about the bigger picture. This article looks at some of the ways you can consider your super.

## Look to the long-term

It can be tempting to look at your super statement, see an investment option which performed better than yours and then move your super into it. But it can be a mistake to assume that the investment option will continue to perform well in the future. Instead, look at the options over a long-term, such as 5-10 years.

The chart below shows the returns of three investment options over 35 years if you initially invested \$1,000. You can see there has been a steady growth in all categories from the original \$1,000 investment.

## Bad years are normal

It can be easy to look at the chart below and only focus on the dips. Any number of events can affect markets, anything from wars or recessions to changes of government. But you will see that after most drops, prices tend to recover and, over the long term, this results in substantial growth.

## Think of your tax

Superannuation is not just about the returns you get, it can also be a tax-effective way to invest your money. You can potentially receive tax benefits when you make contributions, on investment returns and when you withdraw your super at retirement age. This helps you save more than you could outside of super, growing your investment faster.

## Know yourself

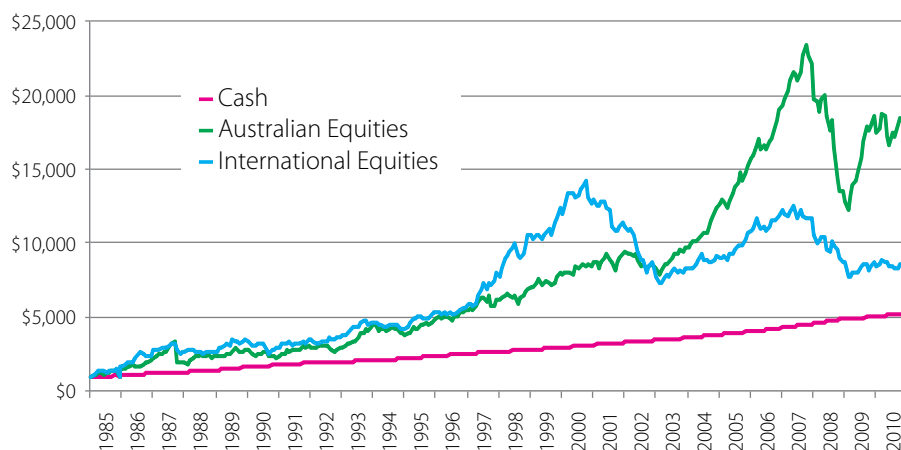
It is important to know your situation and your reaction to risk. All investments carry some risk, but some carry a higher risk of negative returns. On the other hand those same investments also often carry the highest potential for growth.

The amount of time you have until retirement is also a big factor in your risk tolerance. If you are only a couple years away from retiring, a loss can hit you hard, whereas if you are 30 years away, you may have more time to ride out a financial dip.

## Ask for help

The best way to find out if your investment options are suited to you and your needs is to speak to your financial adviser. They can help you understand your situation and how to cope with market fluctuations.

## The growth of \$1,000 invested since January 1985 in Australian shares, International shares and Cash



**Please note:** Asset class: Index used. Cash: RBA Bank accepted Bills 90 Days. Aust. Equities: S&P/ASX 300 TR. Int. Equities: MSCI World NR AUD

# Aged care: making an informed decision

It can be difficult to plan, either financially or emotionally, for the move into an aged care facility. Whether the move into care is for yourself or a family member, there are a lot of questions and decisions which need to be addressed. Making the wrong decision could result in a loss of age pension, increased aged care costs and a reduced estate to be passed onto the next generation.

Aged care homes charge a range of fees to cover care, accommodation costs and living expenses. These can vary enormously between facilities and from resident to resident. The following are the four basic fees associated with aged care:

**Basic daily fees** – Residents in aged care can be asked to pay a basic daily fee as a contribution towards accommodation costs and living expenses. This includes items such as meals and refreshments, cleaning, laundry, heating and cooling. The basic daily fee for all permanent residents who enter an aged care home is 84 per cent of the annual single basic age pension (if they entered on or after 20 September 2009).

**Income tested fee** – Residents in permanent aged care may be asked to pay an income tested fee in addition to the basic daily fee. The amount payable depends on the residents' income and the level of care required. This contributes towards the cost of care.

**Accommodation payment** – There are two types of accommodation payments which apply:

- **Accommodation bond** – Residents in low care with sufficient assets may be asked to pay an accommodation bond. The amount of the bond is dependent on the resident's assets.

The the Australian Government sets a minimum amount, so that the resident will not be left without any money. Within this bond, the aged care provider is able to retain a monthly amount for the first five years. The bond is refundable within 14 days of when the resident leaves the aged care facility. The bond can be paid as a lump sum or periodic payment or a combination of the two.

- **Accommodation charge** – Residents in high care who have sufficient assets may be asked to pay an accommodation charge. The actual amount payable can be negotiated between the resident and the aged care provider.

**Extra service fees** – Some aged care facilities provide extra services which can be offered across the whole facility or to a designated part. Extra service means that the facility will provide the residents with a higher standard of accommodation and/or services. Examples of extra services could be a bigger room, a wider choice of meals or wine with meals. This does not mean that the resident will get a higher level of care, as all homes have to provide the same level of care.

## Renting out the family home

Retaining and renting the family home could provide an exemption for social security purposes, provided:

- the resident is paying an accommodation charge to their high level aged care facility
- the resident has not paid an accommodation bond in full and the resident is paying interest on the outstanding amount of the accommodation bond via periodic payment to the low level aged care facility
- the former family home is retained and rented out.

If these criteria are satisfied, the asset value of the former family home and the income (rent) will be exempt from both age pension assessment and aged care fees (income tested fees).

When retaining and renting the former family home it is important to consider the income tax impact (as the rental income is assessable for tax purposes), the capital gains implications and whether renovations are required.

## Get advice

Seeking advice from your financial adviser or an aged care specialist will ensure that you can make the right financial decisions. This could make a difference to your overall quality of life by being able to afford the standard of care that you require.

### Disclaimer

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