Financial Freedom

QUARTER 3 2013

NEWSLETTER

OUR SERVICES

- **Full financial planning**
- **Retirement planning**
- **Personal insurances**
- **Investments**
- **Employer group insurance schemes**
- **Health insurance**
- **UK pension transfers**
- **Business protection insurance**

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Would you sooner receive your copy of our newsletter via email? If so please give me a call on 07 5715333 or let me know via email cathy@g3freedom.co.nz

What Investors Can Learn From California

California - the land of sun, surf, Hollywood and all things silicon - including the valley. The state is not a place we usually associate with high finance and hard-headed investment decisions, even though California, if it was a separate country, would have the 12th largest economy in the world.

But an announcement made by a Californian pension fund earlier this year has grabbed the attention of the global financial community. The California Public Employee Retirement System, or CalPERS is the largest public pension fund in the United States with over US$250 billion in assets. Its sheer scale makes it an important feature of the investment landscape. This is why, when it announces it is considering a significant departure from its previous investment strategy, everyone sits up and pays attention.

Why Active Fund Management just can't deliver

In essence, CalPERS is considering dumping some, and possibly all, actively managed funds and switching its assets into passive investment funds. The reason for the change? A CalPERS investment consultant told the investment committee that at any given time, around a quarter of external (active) managers would be outperforming their benchmarks, whereas the remaining 75% would not. The consultant questioned whether the results from outperforming managers, who are constantly changing, are cancelled out by other, managers that are underperforming. Once again, fees and costs are the issue - once fees are taken into consideration, CalPERS' passive investments have outperformed active managers over the last 5 and 10-year periods.

For decades the active vs passive debate has raged. The idea that you should entrust your wealth to fund managers who are able to beat the market thanks to their intelligence, information-gathering tools, investment algorithms and suchlike, is one that has held great sway for many years. The weight of fund management advertising has focused on the highly selective performance of funds, where dazzling growth for 2 or 3 years suggests that here is a manager that really does have the edge on everyone else.

Post –GFC Reality

For decades, academic research has demonstrated that no fund manager can consistently out-perform the market. During the glory days leading up to the GFC, the active vs passive debate seemed less relevant: even if your fund manager under-performed, chances are you were still getting double-digit returns.

The sobering reality post-2008 however, has made a lot of people, including CalPERS, re-think. Now it is not a question of ignoring the weight of academic and scientific evidence. It is also the experience of investors, whether they are individuals wondering where to secure their core wealth, or massive institutions who have the money to conduct reviews like CalPERS, which reveal the extent to which active fund management has not served them well.

As investors have got back into stocks in the US, they have done so increasingly through passive funds - in the first two months of this year alone, the respective figures were $65 billion into passive, and $40 billion into active, a ratio that would have been the reverse just a few years ago.

Your personal investment plan

This isn't to endorse passive investment models as an ideal outcome. They offer advantages over active funds, but they have pitfalls of their own, including the costs of having to constantly re-balance portfolios to reflect the indexes they mimic. These pitfalls are avoided through a whole of asset class solution which is the one we advocate. This method not only captures market returns, like passive funds, it also offers massive diversification across global assets - shares, properties, bonds and others. This strategy protects investors when times are tough, and demonstrably supports growth during market upswings.

As always, the most important thing is to get professional financial advice tailored to your circumstances. Like CalPERS, is it time you reviewed your investment strategy?

Article by Plan B Wealth Management

G3 Financial Freedom Editorial from the desk of Cathy Fletcher (G3 Office Manager)

With the Reserve Bank imposing some new rules on the banks around the ratio of lending to the value of a property for home buyers, I thought this a very opportune time to look at personal guarantees, how they work and what the pitfalls might be. When our children are stuck for a solution to a problem, as a parent, we like to help them out. Is offering to guarantee a loan for them the right thing to do for a money problem?

* * * * * * *

We have included a flyer this quarter with information important to anyone who has transferred or is thinking about transferring a UK pension. If you know anyone who this may be relevant to they may appreciate you passing this on to them or suggest they contact us to talk to one of our two experts here, Jane or Charlene.

* * * * * * *

We are hosting a client evening on the 12th of September in Tauranga at 5.30pm with guest speakers from the new owners of Plan B Wealth Management, IOOF. If you would like to come to this please check out the details below or contact me.

Email: cathy@g3freedom.co.nz

Phone 07 5715333

You're Invited

It's about time we had a party in Tauranga!

So we would like to invite you to join us for drinks and nibbles.

Our guest speakers will be
Max Young Head of Investments &
John Atkinson CEO NZ

IOOF

Plan B
WEALTH MANAGEMENT

You are welcome to bring your business partners, colleagues and family member if you wish

G3 FINANCIAL FREEDOM
Goals + Guidance = Growth

Time: 5.30pm

Date: 12th September 2013

Where: The Quest Hotel
(formally Kingsview Apartments & Resort)
Durham Street, Tauranga

RSVP by 10h September

Cathy Fletcher: 075715333

Email: cathy@g3freedom.co.nz

G3 Financial Freedom Ltd
Level 1
20 Wharf Street
Tauranga 3141

Loans Involving Family and Friends

Reality continues to ruin my life

Bill Watterson

Have your children or a friend ever said to you that there is something really special they want to buy - house, car or tv perhaps, but they just can't get the deposit together or they just don't qualify for a loan for one reason or another? Have you been tempted to say "I'll help"? After all, there is some money sitting on term deposit which is really only there as a backstop; what would be the harm in helping out family/friends in need?

I often remember being told by my grandparents "neither a borrower nor lender be" and 'if you can't pay cash for it, you can't afford it." Neither a borrower nor lender be is a quote from Shakespeare's Hamlet and the next line says; "for loan oft loses both itself and friend."

There is a murky area in the overlapping between finance, family and friendship. A loan to someone you love, turned bad, can cause family feuding and ruin relationships.

."...but I only want you to be a guarantor ....you won't be making any payments..."

If you really want to help, the next thing to say is "I'll think about it"......below is what you need to think long and hard about

What is a guarantor?
A guarantor is a person who undertakes to be responsible for the debt of another person. Being a guarantor is a serious obligation, If the borrower fails to meet their payment commitments under a credit contract, the guarantor may be required to pay the debt, or (if the guarantor has provided property as security for the debt) the creditor may repossess/sell the property.

When is a guarantor required?
Creditors may insist on a guarantor if (for example) the borrower :

- Presents an unacceptable credit risk (bad credit rating)
- Does not meet the creditors lending criteria
- Is under 18 years of age

What will guaranteeing a loan give you?
Being a guarantor does not get you anything. You don't have any rights to own the property or items bought with the loan. You won't get a good credit record if the borrower pays off the loan...but you may end up with a bad credit record if you and the borrower can't pay back the loan. The loan will be listed as a default or non-payment on your credit record, making it hard for you to borrow money for quite a few years.

What type of loan am I guaranteeing?
Be very careful about guaranteeing a loan that has no specific payback time, such as an overdraft. This kind of loan could potentially go on forever.

What should I consider before agreeing to be a guarantor?
Before you agree to be guarantor, ask yourself:

- Why do they need a guarantor? (Do they have a poor credit history? Is it likely they will have problems making the payments?)
- Is the borrower responsible enough to have a loan?
- Do you know if they already have other obligations and to what extent?
- Will they keep you informed if they find it difficult to keep up their payments?
- Will they inform you if they increase their obligations further?
- Is the loan a wise one? (Is it for something they really need, or could they just save up for it?)
- Would you be willing and able to back the loan (plus recovery costs) if the borrower can't or won't?
- What would you list as security? Are you willing to risk having it repossessed if the money can't be paid back?
- How would they manage the payments if they were made redundant? Do they have insurance in place if they could not work through disability or life insurance if they died?

What can I do to protect myself as a guarantor?
Get independent legal advice - get your solicitor to check the guarantee/loan agreement as to your obligations and fully explain this to you before you sign anything.
Try to limit your liability - many guarantees cover all of a borrower's obligations to a lender. This means that if you agree to guarantee someone's car loan, you could without realising, also be guaranteeing their mortgage, other personal loans and credit card debt as well.
Make sure you receive the documentation - when guaranteeing a loan the lender must give you a copy of the loan agreement so that you know what the payment schedule is, and also obtain a copy of the guarantee contract. Make sure that the lender understands you want a copy of all future correspondence to do with the loan. If you change your address make sure you update it with the lender.
Don't have your bank accounts with that same lender - if the borrower defaults the lender may just take the money directly from your account, the easiest and least costly way to get the payment due.
Don't provide security worth any more than what is being borrowed- don't use your house to secure a car loan.

Continued overleaf

Loans Involving Family or Friends *continued from page 3*

How long is a guarantee for?
Generally for the life of the loan. As soon as the loan is paid off you should immediately write to the lender and ask for the guarantee to be released. The lender will then generally release you, however, some will leave a 2 year window where you will still have a liability they can call upon.

Unlimited guarantees cover future borrowings, not just the loan in question, so beware!

If the borrower has built up equity in their house (if that is what you are guaranteeing) and or increased their income and are able to stand on their own two feet, then you could suggest approaching a new lender to refinance the debt with the objective in mind of not requiring a guarantor, thus releasing your obligation with the current lender.

What other options are there?
So that all your other assets are safe, you could consider loaning or gifting the money that would make up the borrowers shortfall. This still requires thought before leaping in with the offer, and perhaps consider whether the funds will ever be returned. Does this impact in anyway on your own financial security? Is this your only nest egg for your retirement? How close is your own retirement? Do you have working time left to replace those funds if they are not returned? If you lend the money, set clear terms and draw up an agreement. It doesn't have to be done by a lawyer but it should layout the time frame the loan is to be paid back, what the payments are, how frequently, when they are to start and what happens if the loan repayments default. It may sound cold, but this way everyone is on the same page and expectations are managed . It won't end up in a he said/she said situation. The written agreement adds legitimacy to the expectations should it end up in court. You might decide gifting the money is something you would prefer to do. If you are gifting to a couple and one of the partners leaves the relationship, they will be taking half that gift with them. Just another thing to consider!

A few things to think about
Your adult son reckons he's onto a winning business idea. Family and friends have already ploughed a fair bit of cash in, but it's still losing money. You decide to take a chance and invest $75,000. A foolish move, surely?

Not if your name is Jo and Gareth Morgan. When entrepreneur son Sam flicked off his online auction site TradeMe in 2006 for a cool $750 million, the leap of faith netted mum and dad around $50 m. Quite a return on investment.

If no one was prepared to take a chance on loaning to family or friends, plenty of Kiwi Start-ups would never get off the ground. And some people might lend $1000 on a handshake and think nothing of it. It all comes down to personal circumstances.

Dealing with a request for a loan by a loved one can be uncomfortable, to say the least. But rather than feeling flustered into agreeing on the spot, at least stall for time. Getting independent advice is good for a handy scapegoat, too. If you decide to turn down a loan/guarantee request, you can always blame it on the third party to soften the blow a little.

Information sourced:

Citizens Advice Bureau - www.cab.org.nz

Community Law - www.communitylaw.org.nz

Learn from the mistakes of others. You can never live long enough to make them all yourself

Groucho Marx

G3 Financial Freedom Ltd
Level 1, 20 Wharf Street
PO Box 13563
TAURANGA 3141

Phone: 07 571 5333
Fax: 07 571 5339
E-mail: admin@g3freedom.co.nz

G3 Financial Freedom Ltd - We Make Every Day Count

We are the financial advice company that can help you create the financial future you desire with peace of mind, security and confidence. We operate under the rules of the Financial Markets Authority and abide by the Financial Advisers Act 2008. We are voluntary members of the New Zealand Institute of Financial Advisers.
We are a group of Certified Financial Planners, Chartered Life Underwriters, Accredited Investment Fiduciaries and we are all Authorised Financial Advisers. Talk to us about your financial future now. It is never too late to begin.