

your FINANCIAL WEALTH

A regular check up on your investments for a healthy future

May 2010

Sovereign Debt. Who rescues the government?

In this edition of Your Financial Health, we take a look at the sovereign debt crisis affecting Greece and other European countries. Also in this edition, are updates from the MAP Investment Team and MAP Financial Planning.

The global financial markets have been volatile recently as the euphoria of 2009 makes way for the cold hard reality of the major global imbalances that still exist today.

We witnessed the first signs of market nervousness in January 2010. This surrounded Greece in particular but more commonly PIGS (Portugal, Ireland, Greece and Spain) from which the market recovered by the end of March 2010 as earnings, short term interest rates and signs of a global bottoming in economic activity reassured investors.

In late April the European Union argued how to fund a short-term debt problem in Greece while the financial markets stood back and asked "is Greece the canary in the coal mine and just the start of the bigger issue where governments rescued the banks and the private sector in 2008 and 2009 from their mistakes?". Who rescues the governments from their mistakes? In this environment, global equities are down 10% in two weeks, the Euro is depreciating and the future of the Euro and monetary union is being questioned.

What happened?

This sovereign crisis exposed the biggest issue in the European monetary union, which the markets knew about 20 years ago when the concept was first discussed. Specifically, different countries, cultures, economic and financial structures linked together by a common currency and monetary policy with open financial borders need to have a high level of political and fiscal integration.

The Maastricht criteria that all countries had to abide by and the Stability and Growth Pact (SGP) were a step in the right direction. The problem with the initial setup was the lack of structure, rules, scrutiny and penalties and while many of the initial countries failed the test, they were still let in to the Euro. As the Euro expanded to include other countries, they failed the test again.



In good times, no one really cared. PIGS made the mistake of running budget deficits during the good times when there should have been surpluses. Now, in bad times, growth is weak and to reduce budget deficits they are forced to send their economies into recession. The widely reported hostile reactions of German citizens to the idea of the Greek bail-out and those of many Greek citizens to the IMF and some EU members may have been predictable, but they represent a worrying development for Europe.

The development of the European sovereign crisis and the torturous and fractious manner in which the Greek package eventually came to be agreed have made the Euro a structurally weak currency.

The solution

The 27 members of the European Union (EU) have reached an agreement to set up a European emergency fund. Funding will be provided by borrowing €60bn from the Commission. This would be topped-up by €250bn from the IMF and €440bn of bilateral loans from Euro member states, totalling €750bn.

In essence the package is an effort to backstop sovereign bond markets with a combination of credit facilities and selected European Central Bank (ECB) sovereign bond purchases.

There is nothing in the plan or ECB response that stimulates growth in the Eurozone. The fundamental challenge facing Europe remains the inadequacy of demand in countries undergoing significant fiscal and structural adjustment. Accordingly, fundamental sources of sovereign (Greece) or private sector insolvency have not been addressed.

Finally, the combination of fiscal tightening in the Eurozone, coupled with an indefinite period of easy monetary policy, suggests an even weaker Euro. While Euro depreciation will boost net exports, the structure of the Eurozone suggests the benefits may be unevenly distributed. Fiscal retrenchment will be skewed toward Greece, Portugal, Spain, Ireland and possibly France or Italy. Meanwhile, the competitiveness benefits of a lower Euro will disproportionately benefit Germany.

Financial market impact

The initial market reaction to the package was positive and the sums involved were indeed impressive. Further measures to deal with deficits ought to remove short-term uncertainties over funding costs, and bring down risk premia. This is evident by the steps Spain and Portugal have announced in reducing their budget deficit. There is little prospect of offsetting growth stimulus for those countries. The plan does little to address the deep-seated problems confronting the Euro....*Continues on page 2*



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MAP Investment Update

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However in the absence of a genuine improvement in the growth outlook, fiscal tightening, especially if accompanied by ECB easing, is likely to remain a headwind on the Euro. The European Central Bank's decision to intervene in government bond markets and the re-opening of dollar swap lines between the ECB, Federal Reserve, Swiss National Bank and Banks of England, Japan and Canada will all help the Euro, risk assets, emerging markets and commodity currencies. But medium term the Euro's policy mix for tighter fiscal policy and looser monetary policy will undermine the single currency.

What risks remain?

Investors remain unconvinced by government plans, largely as a result of the experiences of the last couple of years. Banks and other market participants had little choice but to seek official assistance while they massively wrote down their balance sheets, took huge losses and reorganised their capital. Investors question whether governments have any alternative but to do the same. In the Euro, the great hope is a debt-for-debt swap. Governments are to club together to buy out the problems of the PIGS. To achieve this, governments need to raise huge sums as they fund their own budget shortfalls at the same time as their austerity measures limit future economic growth. (Source: UBS)

Markets are unconvinced by all of this. The general view last week has been that the funding announced will simply postpone the restructure of Greek debt rather than eliminate the risk. The markets may get nervous that the only solution is to abandon the euro and monetary union. That will result in enormous market volatility, something the politicians will attempt to avoid.

MAP strategy

We moved in September 2009 to an underweighted position in international equities. We hedged our overseas investments and in the event that the Euro weakens against the \$AUD, we can hold the maximum hedging position allowed to minimise the impact on our international investments. In October 2009 we sold our international sovereign debt in favour of cash and investment grade debt. We also sold all of our emerging market debt and significantly reduced our high yield debt.

Equity and credit markets had mixed results during March and April as illustrated below:

ASSET CLASS	March 2010	April 2010	30 April 2009 to 30 April 2010
Cash	0.35	0.35	3.6
Australian Fixed Interest	(0.6)	0.6	3.3
International Fixed Interest (Hedged)	0.3	0.7	6.6
Australian Equities	5.7	(1.4)	32.5
International Equities (Unhedged)	3.5	(1.0)	7.8
Emerging Markets (Unhedged)	5.4	0.0	24.3
Global Listed Property (Hedged)	7.4	2.8	53.0
Unlisted Australian Direct Property	1.1	0.5	-3.7*
Listed Private Equity (Hedged)	10.2	3.4	67.9
Hedge Funds (Hedged)	1.7	1.0	12.6
\$A/USD	0.917	0.928	0.732**

Source: MAP, Datastream

Source: MAP, Datastream, *Estimate, **30 April 2009

Cash & Fixed Interest

Australia's official interest rate is currently 4.5%. Given continued strength in the Australian economy, interest rates are expected to increase to around 5% by the end of 2010. We are investing in shorter-term deposits of around 80 days with rates over 6.0% in order to take advantage of higher interest rates as they become available.

Globally, interest rates in the major economies are expected to remain on hold. US interest rates are expected to remain at zero well into 2010. Global yield curves (10 year Government bond rates less cash rates) are currently at extreme levels and not attractive from a valuation perspective. Global fixed interest markets continue to focus on sovereign debt risk and this has seen the spreads on investment grade and high yield debt improve. As the spreads are not as compelling as they were a year ago, we maintain a market neutral weighting in credit and no exposure to global sovereign debt.

Global Equities

Global equities were subject to a two-way pull during the month - encouraged by a solid corporate earnings season while still unsettled by the Greek financial crisis. US equities posted gains, delivering relatively strong performance on positive signs from the housing and labour markets that the economic recovery is building momentum. Unsurprisingly Europe lagged. Further weakness in the Euro magnified losses for many overseas investors as a rescue package for Greece was negotiated. Japanese equities were bolstered by sentiment that corporate earnings for exporters would benefit during the global economy's recovery phase as well as from a weaker currency. The broader emerging-market indices showed little change for the month. Asian countries outperformed while Latin America was comparatively weak. (Source: T Rowe Price).

MAP maintains an underweight exposure to international equities and emerging markets.

Australian Equities

The Australian equity market finished the month 1.4% lower, the second monthly decline of 2010. Risk aversion returned on renewed concerns of China's strategy to slow its economic growth, the Icelandic volcano disrupting air traffic across Europe, the re-emergence of sovereign debt risks and the 'windfall' tax on mining profits.

In commodities, spot oil (TWI +2.9%) gained ground on positive US economic data, while base metals declined (spot copper -4.7% and aluminium -4.5%) over expectations of slowing Chinese demand. Spot gold rose in USD terms (+5.9%) over sovereign debt concerns.

The Resources sector (-4.0%) underperformed Industrials (-0.3%), as investors considered the risk of a shift to tighter monetary policies in China, the possible growth impact of fiscal strain in Europe and the uncertainty associated with the proposed Resources Rent Tax following the Henry Tax Review. The smaller companies, represented by the S&P/ASX Small Ordinaries (0.0%), outperformed the large cap stocks (-1.7%), represented by the S&P/ASX 50 Leaders Index.

At a sector level, Telecommunications (+5.5%), REITs (+3.9%) and Financials ex REITs (+0.9%), were the best performing sectors with the major stock contributors being Telstra (+6.4%), Telecom NZ (+1.2%), Goodman Group (+9.2%), Westfield (+7.1%), and Macquarie Group (+6.4%). The worst performing sectors over the period included Healthcare (-6.7%), Metals & Mining (-4.5%) and Consumer Staples (-4.0%). The major underperforming stocks were CSL (-11.1%), Primary Health Care (-8.5%), BHP Billiton (-6.5%), Rio Tinto (-8.0%) and Wesfarmers (-7.9%). (Source: Ausbil).

MAP currently holds a neutral exposure to Australian equities with an overweighting to large-cap companies relative to small-cap companies.

Diversified Property

MAP's property exposure is predominantly through Listed Property Trusts, the valuation of which can be influenced by movements in equity markets.

In the US, REIT gains can be attributed to a number of factors. Firstly, the US economy continued to recover. Notable positive economic data relating to growth in the manufacturing and services sectors, improving housing data and strong retail sales, helped push stocks higher. Exceptionally low interest rates are allowing for the "re-flation" of the private commercial real estate sector.

Asia Pacific property gained 0.7% in April. Although performance was mixed, Japan and Australia continued the upward trend. Hong Kong and Chinese property corrected sharply, as sentiment towards developers with exposure to the Chinese residential market collapsed when China State and local government announced new policy measures during the month. Australian property rose 4.0% during April. The best performers over the month were Goodman Group (up 9.2%), Charter Hall Group (up 8.5%) and Westfield Group (up 7.1%).

European property performed poorly in April, as government debt concerns intensified and the potential range of implications broadened. Property stocks were down around 4%, significantly underperforming the global property markets. The debt problems are widely acknowledged in the PIIGS countries (Portugal, Ireland, Italy, Greece and Spain) but they represent only 0.12% of the Global property index.

We have a slight overweighting to listed property and we continue to favour global listed property trusts.

Alternative Assets

Our hedge funds continue to reduce exposure to equities as momentum measures have turned negative, particularly for some European markets. As a result, the net long equity allocation has been reduced, mainly by increasing short positions in Spain and Italy. In currencies, long position in the Japanese Yen has been reduced and extended to a long position in the US dollar. It has also extended a short position in the Euro and holds other large short positions in the Swiss Franc and British Pound.

Within commodities, a long position is held in gold while the long position in gasoline has been reduced. Short positions are held in natural gas, corn and coffee. Low risk exposures are maintained in bond markets with long positions in US and UK offset by a short position in Japan.

Listed private equity returns continue to perform well as equity markets recover. Listed private equity increased 3.4% in April. Anecdotally, banks are starting to lend again, particularly in the mid market space. Deal making is expected to trend up in 2010 and we expect ongoing M&A activity to be prominent in healthcare, technology and pharmaceutical sectors. While it's difficult to predict what the rest of the year holds, the trend in IPO markets is encouraging. Notably 8 venture backed IPOs in Q1 (US) equate to the same number for all of 2009.

MAP maintains overweight exposure to hedge funds to reduce portfolio volatility in an environment of volatile equity, bond and FX markets. We have a neutral exposure to infrastructure while underweight to private equity.

Table 1: MAP Superannuation Plan

Returns to 31 March 2010 net of all fees and taxes

POOLS	% PA 10 YEARS	% PA 7 YEARS	% PA 5 YEARS	% PA 3 YEARS	% PA 1 YEAR
AUSTRALIAN EQUITIES					
MAP	n/a*	n/a*	7.4	(2.1)	37.9
MARKET	n/a*	n/a*	7.4	(1.9)	40.1
VARIANCE	n/a*	n/a*	0.0	(0.2)	(2.2)
INTERNATIONAL EQUITIES					
MAP	n/a*	n/a*	0.5	(6.9)	20.1
MARKET	n/a*	n/a*	(1.0)	(8.9)	19.2
VARIANCE	n/a*	n/a*	1.5	2.0	0.9
DIVERSIFIED PROPERTY					
MAP	n/a*	n/a*	(3.2)	(16.8)	50.6
MARKET	n/a*	n/a*	(3.2)	(15.0)	31.3
VARIANCE	n/a*	n/a*	0.0	(1.8)	19.3
CASH					
MAP	4.8	4.9	5.0	4.6	6.1
MARKET	4.7	4.5	4.6	4.2	3.0
VARIANCE	0.1	0.4	0.4	0.4	3.1
BALANCED					
MAP	4.6	6.7	4.0	(2.9)	23.4
MARKET	5.3	6.8	4.0	(1.9)	20.3
VARIANCE	(0.7)	(0.1)	0.0	(1.0)	3.1
CAPITAL STABLE					
MAP	4.8	5.2	4.1	0.9	13.4
MARKET	5.0	6.0	4.2	1.3	12.2
VARIANCE	(0.2)	(0.8)	(0.1)	(0.4)	1.2
GROWTH					
MAP	4.5	8.2	4.4	(4.2)	29.9
MARKET	4.8	7.6	4.0	(3.7)	25.4
VARIANCE	(0.3)	0.6	0.4	(0.5)	4.5

- * Pool opened for investment from 1 March 2004.
- 'Market' is taken from the median manager performance from the Selecting Super surveys.
- Returns are compound annualised averages net of all investment and administration fees.
- The returns quoted above are subject to audit.
- Past performance should not be relied upon as an indication of future returns. The actual returns will be determined by the investment strategy adopted and prevailing market conditions

Portfolio Management

Within diversified fixed interest we have made an investment in the DWS Diversified Fund. This fund aims to achieve a return of 250bps over cash. This manager is part of the strategy to reduce sovereign risk in the portfolio and protect against any future inflationary pressures as cash is a lagging hedge against inflation.

Outlook

We expect the markets to remain volatile throughout 2010 as they digest the global impact of huge deficits faced by the majority of governments and the impact on global activity.

Diversification across all asset classes is the key to minimising investment risk as liquidity concerns give rise to 2008 all over again.



MAP Financial Planning Update

Planning for retirement

Many of us think about retirement and focus on the amount of money we want to accumulate to enable the lifestyle that we have become accustomed to in the years preceding retirement.

What many of us simply overlook is how long we may need the funds to last. At a recent seminar we attended, we were presented with some astonishing statistics. For example, a female baby boomer has a 50% chance of living beyond age 90 and a male has a 34% chance.

Longevity is becoming a real possibility for many of us due to improvements in our health both through lifestyle and medical advances. You can estimate your own longevity at www.mylongevity.com.au. This calculator takes into account your lifestyle and family history to provide a guide as to the probability of you living a longer life than you may think.

Now here's the scary bit! We may have had plans of retiring at say 55 or 60 years of age

but if there is a likelihood that we could live well into our 90's, then we simply will need more money than we originally thought. In effect, we could have more years in retirement than in the workforce. This may give us cause to think more about delaying our retirement to save more, or alter our strategy in later years.

The Government is clearly thinking along the same lines with changes to superannuation from July 2013. These changes allow Super Guarantee payments for persons aged between 70 and 75 years and increase eligibility for the Centrelink Age Pension to 67. The Government has already started encouraging the mature workforce to continue working well into their 70's. The gradual increase in Super Guarantee payments from 9.25% in 2013 to 12% by 2019 is another sign that the Government isn't confident we are saving enough for future generations of retirement savings.

Whilst we may consider financial capital when planning for our retirement, another

important asset is our human capital (that is, our ability to maximise our educational background and earn income over a period of time). For example, a young medical graduate of 26 years of age would normally have far greater human capital than say a medical professional nearing retirement because there are less years available in the equation to generating wealth.

Ultimately, we need to think about the number of years we are able to continue in our current job, the impact of higher income versus a part-time position or taking a new job with less responsibility and less income. We need to protect our human capital by ensuring that if our working life is suddenly cut short, we have alternative strategies to protect our lifestyle.

Retirement planning is simply not just about accumulating a certain amount of wealth and retiring early. It's also about making the right decisions to maximise both the human and financial capital for the long term.

End of financial year strategies

If you are still working then it's that time of year again when you need to ensure that you have everything in order to maximise your tax position as 30 June approaches.

Following are some of the things that you should be reviewing in preparation for the end of financial year:

- Maximise Salary Sacrifice and SG contributions – capping limits of \$50,000 if over 50 and \$25,000 if under 50 years of age.
- Check non-concessional (personal) super contributions to ensure a breach of capping limit has not occurred.
- Review investment losses and consider offsetting capital losses against any gains in order to minimise capital gains tax.

- Review the structure and ownership of investments in relation to applicable tax rates.
- Spouse super splitting and spouse contribution
- Prepaying interest expenses
- Income protection premiums
- Related work expenses

Now is a good time to be reviewing your long-term financial strategies. Many of the above items are best to have in place at the beginning of the next financial year and it is important to seek advice on these strategies to avoid common traps and take advantage of the opportunities available to you.

Our professional financial planning team is able to assist you with advice and guidance.

The value of advice

The 24th – 30th of May marks the Financial Planning Association's 10th 'Financial Planning Week'. This Week is designed to bring to consumers an awareness of the value of financial planning advice.

Financial Planning is about taking our clients from where they are now to where they want to be in years to come. It's about making sure we identify individual goals and establish a plan that is constantly reviewed and monitored against changes to legislation. Everyone has different personal and financial goals so there is no 'one size fits all approach'. Your financial plan is tailored to your specific needs and objectives.

The Financial Planning Association (FPA) has produced a case study booklet that demonstrates the value of advice. You can access this on the FPA website at <http://goodadvice.com.au/life.html>.

If you cannot access the website but would like a copy, phone MAP Financial Planning Assistant Erin Hill on 07 3838 1237 who will be happy to post one to you.



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