

W E A L T H C R E A T I O N



1 Invest in other people's businesses ... for a high performance portfolio

If you want to make your savings work as hard as possible for you, then you must invest a portion of your money in other people's businesses. This is the part of the economy where most wealth is created.

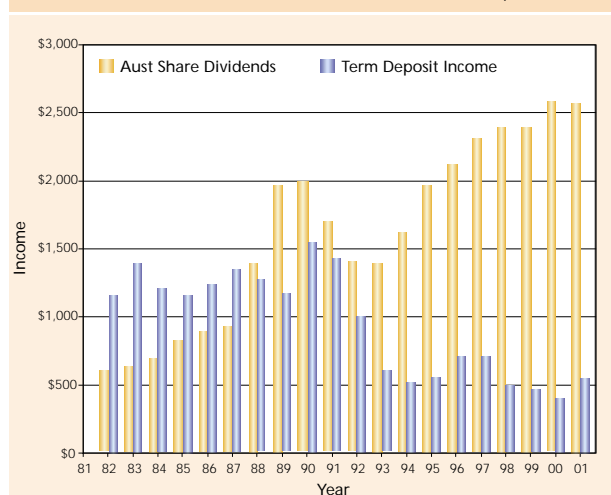
The most efficient and safest way to access other people's businesses is to invest in quality businesses listed on the stock exchange. Buying shares in those businesses means that you become a part-owner of the business and, as such, you are entitled to share in the profits and capital growth generated by that company.

Over time, the profits and capital value of a quality business should both grow to significant levels.

For example, if you had invested \$10,000 into the 200-odd shares which make up the Australian All Industrials Index in 1981, your dividends would have grown from \$598 initially to \$2,566 last year, as shown in Chart 1.

Compare that to investing \$10,000 in term deposits in 1981. Your income would have fallen from \$1,150 in 1981 to just \$575 last year.

Chart 1*: Investment income: Shares Vs Term Deposits



Source: Zurich

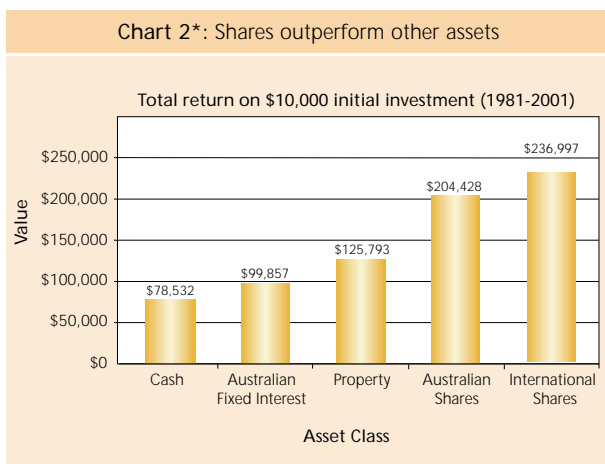
In fact, over the 20-year period, the total income from the term deposit investment was significantly less than that from shares, as shown in the table below.

Income on \$10,000 investments (1981 – 2001)*		
	Total income	Income in 2001
Shares	\$32,423	\$2,566
Term deposits	\$18,955	\$ 575

And, as you would expect, shares also grew in value over the years, with your \$10,000 growing to \$78,069 by 2001, while your term deposits would still have a value of \$10,000.

Capital growth on \$10,000 investment (1981 – 2001)*		
	Initial Investment	Value 2001
Shares	\$10,000	\$78,069
Term deposits	\$10,000	\$10,000

Quality shares do not only outperform term deposits – they consistently outperform all major asset classes over the long term. For example, a \$10,000 investment in international shares 20 years ago would now be worth \$236,997, while a similar investment in Australian industrial shares would have grown to \$204,428 (assuming income was re-invested) as shown in Chart 2. Listed property trusts - which invest in retail, commercial, industrial and residential property – would have turned \$10,000 into just \$125,793, while the performance of cash and fixed interest lagged even further behind shares.



Source: Zurich

2 Take advantage of the Government's tax concessions

The Government has made available a number of tax concessions to help Australians create wealth. Here are three of those concessions:

"Quality shares consistently outperform all major asset classes over the long term"

Income splitting

This is where your investments are made in the name of either you or your spouse - depending on who has the lowest marginal tax rate.

Here's an example. Let's say you earn more than \$60,000 a year, and are therefore on the top tax rate of 48.5%. If your investments generate, say, \$10,000 income, you'll lose almost half of that income in tax. However, if your spouse is a homemaker who earns no assessable income, they would be taxed just \$530 tax on that \$10,000 income.

	You (48.5% tax rate)	Spouse (0% tax rate)
Invested income	\$10,000	\$10,000
Tax	\$4,850	\$530

Franked share dividends

Another tax saving strategy is to invest in shares and managed funds which pay franked dividends. These dividends have had tax paid on the dividends before you receive them, then you pay any tax owing on those dividends.

The end result is that high-income earners pay little tax on fully franked dividends, while low income earners pay no tax.

For example, if you receive a fully franked dividend of \$1,000 and your tax rate was 48.5%, you would pay tax of just \$264.

Superannuation

Superannuation is still the most tax effective way, if you are a medium to high income earner, to save for retirement. And it is still the most tax effective way to draw an income in retirement.

Money invested in super on a salary sacrifice basis, or if you are self-employed, effectively qualifies for a tax deduction. As a result, you'll have more invested day one in super than you will in other investments, even though your contributions to

super will be subject to contributions tax (15%) and possibly superannuation surcharge tax (up to 15%).

Another advantage of super funds is that they pay a maximum of only 15% tax on earnings and capital growth. In fact, most funds pay tax of 10% or less because of the benefits of franked dividends. This means that your money in super will grow much faster than in most other investments.

Further, in retirement, it's possible for you and your spouse to generate a retirement income from allocated pensions (that is, super funds which pay a regular income) of around \$53,000 pa combined ... tax free.

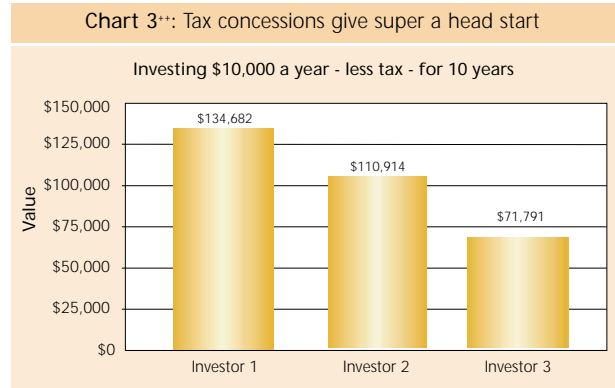
CASE STUDY

Let's look at the tax position of three people who each invest \$10,000. The first investor salary sacrifices into super and pays 15% tax on entry to the super fund. The second also salary sacrifices, but they pay 30% tax on entry. The third investor takes their money as salary and then invests outside of super. This means they pay tax as shown in Table 1 below.

Now, look at what would happen if they each invested this \$10,000 - after paying the appropriate taxes - every year for the next 10 years. As you can see in Chart 3, the investors in super are well in front, even when the entry tax is 30%. Note though, that additional tax may be payable if this amount is taken as a lump sum (ie. relevant for Investor 1 & 2).

Table 1	Investor One	Investor Two	Investor Three
	Salary sacrifice into super (adjusted taxable income less than \$85,242)	Salary sacrifice into super (adjusted taxable income more than \$103,507)	Take as salary then invest (taxable income more than \$60,000)
Portion of salary	\$10,000	\$10,000	\$10,000
Tax	\$1,500	\$3,000	\$4,850
Net invested	\$8,500	\$7,000	\$5,150

Source: Zurich



Source: Zurich

3

Use other people's money to 'fast track' your wealth plans

Borrowing to invest or 'gearing' can be a fast track to wealth - but if it's not used properly, it can also be a fast track to ruin.

Here's a very simple example, ignoring loan costs, to show you how it works.

Let's say you have \$10,000 to invest, plus you borrow another \$90,000 to invest. So, you have \$100,000 invested. If that investment increases in value by 10% you'll be \$10,000 better off. In other words, you've made a 100% return on your initial investment of \$10,000.

As you can see, while investments are going up in value, gearing is a good thing.

But what happens if the investment falls in value by 10%? You will lose \$10,000 - or 100% of your initial investment.

That's why you must only use high quality investments when you employ a gearing strategy... and it's also why you must give your investments time to grow by investing for the long term.

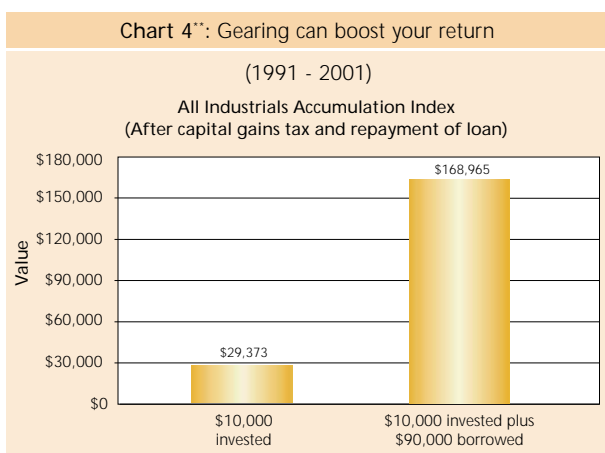
Keep in mind, also, that the Government will give you a tax deduction on the interest you pay on the loan. This deduction can be substantial if you are on the top tax rate of 48.5%.

CASE STUDY

Let's now look at how a gearing strategy might have fared over the past 10 years. We'll use quality Australian shares as the investment.

If you invested \$10,000 of your own money into Australian shares 10 years ago, you would now have \$29,373 (assuming dividends were re-invested). That's an 11.38% pa return.

However, if you invested your \$10,000 plus another \$90,000 you had borrowed, you would now have \$168,965 - after paying back the \$90,000 loan, as shown in Chart 4.



Source: Zurich

How to create wealth

Although each of the steps to creating wealth is reasonably simple, there are many traps along the way.

Your financial planner can help you to avoid those traps... and advise you on tax effective strategies and asset allocation models. They can also show you the performances of Zurich's range of managed funds.

You can also visit our website at www.zurich.com.au

"Superannuation is still the most tax effective way, if you are a medium to high income earner, to save for retirement"

+Assumptions for Chart 1:

- Dividends/income not re-invested.
- Shares: Australian All Industrials Index.
- Dividends are derived from the Price & Accumulation Indices.
- Term Deposits: Reserve Bank of Australia Interest Rates and Exchange Rates Statistical Table.

* Indices used in Chart 2:

- Australian Shares: All Industrials Accumulation Index (S&P/ASX 200 Accum) - a measurement of the average movements in share price of major Australian Industrial companies listed on the Australian Stock Exchange. It is an accumulation index, which means that it assumes that dividends have been reinvested.
- International Shares: MSCI World ex Australia in SA Net Return.
- Property: S&P/ASX 200 Property Trusts Accumulation Index.
- Bonds: UBSWA Composite Bond All Maturities Index.
- Cash: UBSWA 90 Day Bank Bill Index.

++Assumptions for Chart 3:

- Earning rate of all investments (before tax but after fees) - 7%, comprising 4% growth and 3% income, with 50% of the income component being fully franked.
- Inflation rate of 3% applied to contributions for all investors.
- Marginal tax rate for all investors - 48.5%.
- Investments not encashed at end of 10 years.
- Adjusted taxable income = taxable income + salary sacrifice superannuation + reportable fringe benefits.

**Assumptions for Chart 4:

- Tax rate over 10 years 48.5%.
- Interest-only loan repaid at end of 10 years out of investment (at 7.5%).
- All income tax and after-tax interest costs paid out of other monies.
- Investment is in All Industrials Accumulation Index.

Disclaimer:

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MJOY-5813BS-2002