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How to read Reserve Bank interest rate decisions

Warren Bird

How can we interpret the Reserve Bank's (RBA) decisions about interest rates? One important tool is to understand the statement that it issues with each decision. This article provides a guide to reading and interpreting these statements (the statements can be accessed on http://www.rba.gov.au/monetary-policy/ go to 'Interest Rate Decisions').

The structure of the RBA's interest rate decision announcements

On the first Tuesday of each month, except January, the RBA Board meets to decide the level of the official cash rate. At 2:30 pm (Sydney time) a statement is released in the name of the Governor announcing the decision and outlining the reasons for it.

Since early 2009 these statements have had a consistent structure to them. They almost always include the following items in the same order:

- An opening sentence announces the decision that was made that day
- Then follows an outline of the global backdrop to the decision. This always has three components
    - A summary of the Board's view of global economic growth prospects
    - A statement about the trend in commodity prices
    - An overview of global financial conditions, including the stance of monetary policy in the major nations.
- Then follows a discussion of the domestic scene:
    - Domestic economic growth;
    - A comment on labour market developments;
    - A comment on inflation.
- Next is a statement about whether domestic monetary policy is easy, neutral or tight, followed by an outline of developments in credit growth and financial markets, usually explicitly mentioning the exchange rate
- The penultimate comment is about the expected impact of monetary conditions on the economy
- The final paragraph is a summary of the Board's judgment about the stance of policy, focussing on how their objective of keeping inflation within the target range is being served. Sometimes a comment is added to provide some degree of guidance regarding the Board's expectation for interest rate decisions in the near future.

There are occasional exceptions to this structure such as late 2010 when European sovereign risk

dominated market sentiment. A comment about serious developments is included when necessary, taking over from one or more of the regular topics.

What emerges is a clear insight into the RBA's decision-making process. It shows us the range of factors that the RBA believes are the most significant drivers of the outlook for inflation, which is the yardstick by which it judges the appropriateness of the current level for the cash rate.

Not all media commentaries after the RBA Board meeting show an awareness that the RBA has a process. You'd think that the RBA picks an 'issue of the month' and bases the decision around that. Whether it's house prices or a change in the labour market or a single CPI reading, you could easily get the impression that the RBA is merely reacting to particular data releases.

Nothing is further from the truth. Were the RBA forced to front something like an asset consultant for a review, they would receive top marks for the quality and clarity of their process.

Interpreting wording changes

With that framework in mind, tracking the evolution of the RBA's thinking needs a comparison of what is said from month to month about each of the topics, reading those changes in context.

There are three reasons for changes to the wording of the monthly statement:

1. Nothing of substance has changed, but the RBA has an innocent reason for deciding to use different words this month compared to last time
2. Time has moved on and the tense of the comment needs to remain contemporary
3. Something of substance has changed and the RBA is telling us of their change in view.

The skilled RBA watcher can tell the difference and focus their analysis on changes that fall under category 3.

Category 1 wording changes mostly arise because there is little that changes from month to month and the RBA writers don't want readers to get bored with exactly the same words. The RBA keeps those sort of changes to a minimum and we often see the same sentences appearing for months on end. However, sometimes when the same thing has been repeated a few times the statement will change in some way, eg. repeated ideas will be given in a more abbreviated form.

Category 2 comments are generally easy to pick for what they are – not a change of view, but an update to keep the remark contemporary. An example is found in comparing statements before and after the release of CPI data. Unless there has been something surprising in the outcome, the RBA moves from saying how they are expecting prices to behave to describing that behaviour as reflected in the latest data. That is relevant information, but not a change of view.

Category 3 comments convey a change of view and require closer scrutiny by those seeking to decipher any potential future change in policy.

There are examples of category 3 changes in the February 2016 statement, including:

- Compared with December, the RBA believes the global outlook has deteriorated. Although there's been continued growth in the advanced economies, this is being offset by conditions in some emerging economies becoming 'more difficult'. As a result, the RBA's summary adds that global growth is at "a slightly lower pace than earlier expected"
- Following a more expansive discussion of commodity prices than in December, the RBA reveals a greater degree of concern about financial conditions tightening for the emerging economies. The degree of concern shouldn't be overstated as the RBA also highlights that "monetary policy remains remarkably accommodative" with funding costs for high quality borrowers still "very low"
- On the domestic side, the RBA reveals a more positive view of developments. December's view that a "moderate expansion" was continuing has been replaced by the more fulsome statement "that the expansion in the non-mining parts of the economy strengthened during 2015 even as the contraction in spending in mining investment continued". This is further emphasised by the change from referring to steady unemployment to a decline in the unemployment rate. However, the RBA seems at pains to emphasise that this doesn't flow into a revised view of the inflation outlook. The February statement is much more detailed on inflation than was December. A brief statement last time has been replaced by a 50-word summary of their CPI forecasting model and the conclusion that "… consumer price inflation is likely to remain low over the next year or two".

The final step is to decide if they are signalling an overall change of thinking about monetary policy. Remember that the RBA's process is to base its decision on the combined significance of all the issues summarised in their statement, not to read too much into one or two specifics.

To help us with this, the RBA draws it all together in the last couple of paragraphs of the statement, which more than any others reward close reading.

The first thing to note is that the RBA said once again in February that right at this moment they judge a 2% cash rate to be appropriate. Therefore, they haven't changed their target rate. This automatically tells us that whatever their changes in view about the economy, inflation and how monetary policy is interacting with those things, no change in policy is required. It will take more changes from the current situation to drive a new policy.

The final comment in the February statement confirms that the RBA Board has a higher level of uncertainty about how things may transpire than in December. Will the labour market continue to improve? Will global turbulence continue and hurt world and domestic growth? In that context they repeat last month's assurance that "… continued low inflation may provide scope for easier policy, should that be appropriate to lend support to demand".

Conclusion

To me, all of this is clear: the RBA's process has resulted in them identifying two new trends, but which are in opposing directions in terms of the economic outlook. These trends do not yet result in an overall change of view about monetary policy. They add to the uncertainty of the outlook and there is a continued sense that if there is a change in future it will be towards lower rates, but the RBA always puts this in the context of inflation being low enough. They can cut rates if needed to support growth without compromising their inflation-targeting objective.

If and when the RBA's view changes, there will be no magic formula or secret ingredient. The RBA will follow its process and explain their thinking by reference to the same range of factors that they've been telling us about for the past seven years.

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This is an edited and updated version of an article that originally appeared as a 'Bird's Eye View' column in the June 2014 edition of KangaNews. Used with permission.

Do 'January' returns foretell the full year for equities?

Ashley Owen

In Part 2 of our 'January effect' examination, we respond to several readers who asked whether the poor January 2016 in the share market foretells a bad result for the whole year, or is the market more likely to rebound because it has been over-sold?

Put another way, based on what happens in January, is there either:

- a '**momentum'** effect, where January returns tend to be continued for the rest of the year, or
- a '**reversion'** effect, where January returns tend to be the opposite for the rest of year?

History favours a small momentum effect

Historically, positive returns in January have turned into positive full year returns most of the time (80% of years in the US and 72% in Australia). Conversely, low returns in January have turned into low full year returns most of the time. Since 1900, the statistical correlation between January returns and full year returns have been 0.40 in the US market and 0.46 in the Australian market. These moderate positive correlations may indicate the presence of a momentum effect in both markets.

But there is a little sleight of hand going on here. Since the January returns are included in the full year returns, the correlations are artificially high because they double-count January. High return years end up being high partly because of the good start in January (in Part 1, we observed that, on average, January has been the best month in both the US and Australian markets for more than a century).

The problem is that after January's result is known at the end of January, unless you are Marty McFly or Doctor Who, you can't go back in time to sell or under-weight shares at the start of the year if January was bad, or over-weight if January was

good, in order to get the full year return. All that is important now is the future - the likely return for the rest of the year from the start of February to the end of December.

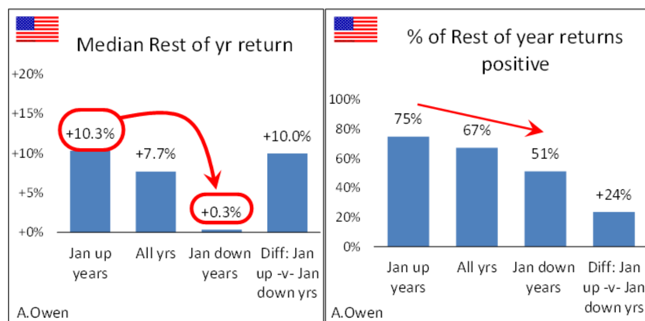
Since 1900, the correlation between *January returns* and the *'rest of year'* returns have been 0.19 in the US market and 0.23 in Australia. These are much lower than the full year results but they indicate a possible weak momentum effect.

If such a momentum effect did persist, we could make excess returns by over-weighting shares for the rest of the year after a good January and under-weighting after a bad January. This sounds like another market anomaly or inefficiency (another 'free lunch'!).

As statistical correlation numbers are often misleading, ambiguous and say nothing about underlying causes let's look at the actual results.

Rest of year returns after January – US market

The first pair of charts show that the 'rest of year' returns in the US have been higher in years when January was up, compared to years when January was down.

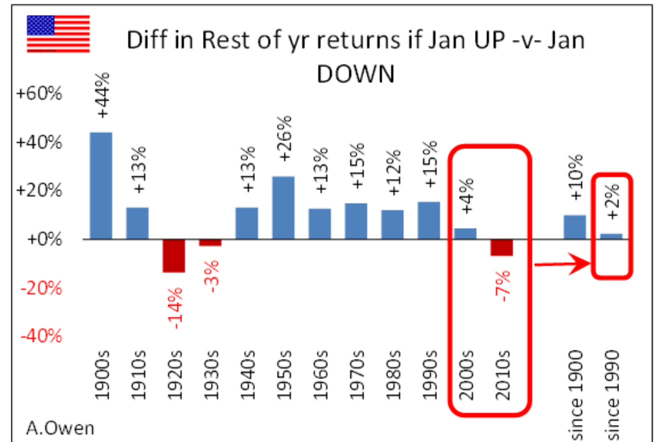


The 10% median rest of year return in years when January was up is significantly higher than the 0.3% median rest of year return in years when January was down.

Also the right chart above shows that in years when January was up, the rest of the year was up 75% of the time, but in years when January was down, the rest of the year was up just 51% of the time. This means the incidence of losses over the rest of the year were more frequent in years that started off with a down January.

The problem with exploiting the January effect

Unfortunately, just like the original 'January effect' we analysed in Part 1, what appears to be another 'free lunch' also disappears on closer inspection. The above charts look at the period from 1900 to 2015 as a whole, but the next chart takes the 10% median 'rest of year' return difference between 'up January' years and 'down January' years and breaks it into decades.

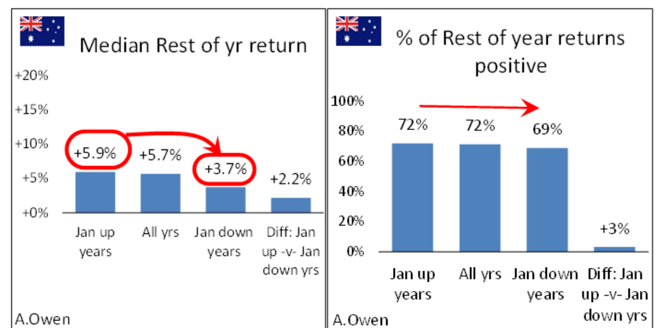


Positive blue bars indicate decades when the rest of year returns following positive Januaries exceeded rest of year returns following negative Januaries (momentum effect). Red negative bars indicate the opposite - a reversion effect - when the rest of year returns in negative January years were higher than rest of year returns in positive January years.

The decade by decade results show that this effect has largely disappeared in the past couple of decades. The bar on the far right shows the difference since 1990 to be much smaller than the 10% difference over the whole period.

Rest of year returns after January – Australian market

The first pair of charts for Australia show that the rest of year returns have been a little higher in years when January was up, compared to years when January was down, but the difference has not been statistically significant (unlike in the US were the difference has been much larger).



Also the right chart shows that in years when January was up, the rest of the year was up 72% of the time, but in years when January was down, the

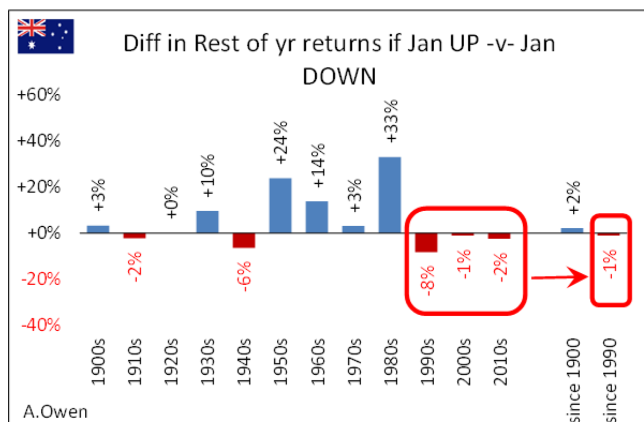
rest of the year was up 69% of the time. Here too there has been no significant difference in Australia, unlike the US market where the difference has been large.

Reasons for difference between US and Australia

Rather than just look at the numbers, I always try to understand the fundamental drivers at work.

January is a big month in the US: 4th quarter and full calendar year-end profit results, payment of the 4th quarter dividend, and often the announcement of annual dividend increases after the full year results. Much price-changing news for investors to digest and act upon. In contrast, January is quiet in Australia – the long summer break (whereas the US has its long summer break mid-year), no profit reports (most Australian companies have June year-end), December half-year reports are released in February here, not January) and few dividend payments, and rarely if ever any dividend announcements. It is no wonder the results for January compared to the rest of the year have been quite different in Australia and the US markets.

The next chart shows the difference in Australia in rest of year returns between 'up January' years and 'down January' years broken down into decades.



This shows that the effect has been much patchier and inconsistent than in the US, and is mainly the result of two isolated decades – the 1950s and 1980s. I would not base a strategy on such an effect in the past 100+ years.

The bar on the far right shows the difference since 1990 to be insignificant in recent decades, as in the US market.

Conclusion

In the US stock market there was a relatively strong momentum effect for 'rest of year' returns following January's return. It persisted for many decades in the US but appears to have largely disappeared in recent decades. The reasons for its disappearance are probably the same as for the disappearance of the original 'January effect' – widespread access to low cost computing, brokerage rates, futures markets and ETFs, that enabled investors to capitalise on the advantage until it was 'arbitraged away'.

The Australian market had no such 'rest of year' momentum effect. If it existed at all in Australia it has disappeared since the 1990s, as in the US.

It is a reminder to always try to get behind the numbers and understand the fundamental causes and effects before committing investors' funds to what seems to be a seemingly high correlation suggesting an opportunity for outperformance.

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Safe withdrawal rates for Australian retirees

Anthony Serhan

I love it when someone takes a complex question and answers it with something simple. The danger with elegant simplicity, though, is that people forget the details that sit behind it, and what question it was actually answering. This was one of the catalysts for the recent Morningstar research paper 'Safe Withdrawal Rates for Australian Retirees' that I co-authored with David Blanchett and Peter Gee. The '4% rule' is often referenced in understanding what you can spend in retirement given a certain amount of savings, but where did it come from, and how relevant is it today?

1. What is this '4% rule' we hear so much about, and where did it come from?

The '4% rule' actually started in 1994 with an article published in the *Journal of Financial Planning* by William Bengen. He was a US-based financial planner who wanted to answer questions about how much his clients could spend in retirement. The way people interpret the 4% rule can vary, so let's set

out some important parameters that underpin the number:

- 4% of the portfolio is used to calculate the first year's payment only, and each subsequent year that amount is adjusted for inflation
- it assumed a minimum 30-year retirement period
- historical return data from 1926-1994 was used, based on a portfolio comprised of 50% US equities and 50% US bonds
- 4% was selected as 'safe', because at that level there was no past period where that rate would have exhausted all assets by the end of the 30-year period. So it was not a number based on an average return, but rather one that assumed returns at the very low end of the spectrum.

Before taking this framework forward, I'd like to tip my hat to Mr Bengen, who 22 years ago wrote a thoughtful and practical paper. The 51 simulations that he ran do not quite match up with the Monte Carlo simulators of today, but the paper still captured many important concepts.

An inflation-adjusted, constant income stream is pretty intuitive when you think about the way you want to plan retirement.

2. Does this 4% rule apply to Aussie retirees today?

The methodology can still apply in Australia today, but there are some important areas of improvement. First, we've included a fee assumption. Whether you're paying for someone to manage the portfolio, an advisor, an accountant, an administration platform, or some combination of these, there are costs. For our calculations, we've assumed an annual fee of 1% per annum. If you repeated the same study as above with the 1% fee, using Australian share and bond returns, but increase the return history to 1900–2014, that 4% would have come out closer to 2.5%. Why lower? Apart from the impact of fees on the returns, the Australian equity market has been more volatile than the US, and our inflation higher in the 1970s and 1980s, so you need a lower withdrawal rate to weather the worst-case scenario.

The full paper also shows that Australia has experienced some of the highest historical returns from markets when compared to 19 other countries. While the US has led the world in retirement research, we need to be careful about localising those results. Australia has outperformed historically, but it's arguable whether this will continue.

The next step was to replace past returns with our long-term expected returns, which take account of where equity markets and interest rates are today. In addition, if you diversify the portfolio further to include a mix of Australian and international assets, you get different answers again. If you want 99% certainty, the initial withdrawal rate is 2.8%, helped by the portfolio's reduced volatility. If you're prepared to lower that probability of success down to 80%, then that initial withdrawal rate can increase to 3.9%.

3. What is the probability of success or 'success rate'?

This idea of a 'success rate' is incredibly important. While it may be complex mathematically, the underlying principle isn't. It speaks directly to the sort of trade-offs we all have to make. Quite often, people talk about 'expected returns', and use these to build their plans. Even if someone has made a good forecast, an expected return will only have a 50% probability of coming through, and the final result may be higher or lower. You might be happy around this level, or you may want to be more certain that the path you're taking will meet your minimum goal. In our analysis, the goal is to make sure that whatever initial withdrawal rate you use, your account balance will run out exactly at the end of that period. Pick a success rate that you can be comfortable with, from the conservative 99% certainty, to the more optimistic 50% level, or somewhere in between.

4. What is the key message for Australians?

Equity returns over the next 20-30 years are likely to remain attractive relative to cash, but we're projecting them to be 2% lower than history. We need to adjust our expectations and plan accordingly.

Safe withdrawal rates for retirees now need to start at 2.5%, not 4%. Withdrawal rates could be even lower if life expectancy continues to increase. So we need to accept either spending less in retirement, OR saving more for retirement, OR running a greater risk of moving on to the aged pension sooner. It's important to understand the trade-offs, and where you're sitting.

The mandatory minimum withdrawal rates for account-based pensions in Australia are set higher than the safe minimums in our paper. The way these two rates operate is different after the first

year, but the impact of the higher relative withdrawal rates still needs to be considered. Just because you've been paid an amount from an allocated pension doesn't mean you have to spend it. Some retirees will need to invest some of their pension payments outside tax-concessional superannuation to ensure they still have savings in the future.

Once again, the benefits of a diversified, balanced portfolio shine through in the study. Adding equities can help a portfolio, but only if you accept a lower probability of success. Most of the incremental benefit to withdrawal rates of adding equities is achieved when 50 – 70% is allocated to growth assets.

Lastly, while the paper provides some useful pointers, the reality is that we're all different, and reviewing your own personal circumstances will give you a much better answer to what you need in retirement than a rule of thumb.

Anthony Serhan, CFA, is Morningstar's Managing Director Research Strategy, Asia-Pacific. For a full copy of the report and data, click here. This material has been prepared by Morningstar Australasia Pty Ltd for general use only, without reference to your objectives, financial situation or needs. You should seek your own advice and consider whether the advice is appropriate in light of your objectives, financial situation and needs.

China's paradigm shift and why I'm (still) cautiously bullish

Brian Ingram

China's national bureau of statistics recently revealed that in 2015 the country's gross domestic product grew at its slowest rate in the past 25 years, reigniting fears of a prolonged slowdown for 2016. As expected, this headline added to nervousness and even panic in global markets. Decades of exceptional double-digit growth rates and unquestioned over-reliance on China's ability to drive growth have built some very high expectations.

But the recent economic volatility may be a signal of an important social shift happening now in China. This transition, like similar transitions over the past 20-30 years, could prove to be a key driver of China's future growth and the transformation of the country's economic model.

A necessary paradigm shift

In order to understand this transition, it is important to consider how China's national balance sheet - the sum of all of the country's assets and liabilities - has evolved over time. One way to interpret China's recent economic slowdown is that China's domestic assets - its financial assets, real estate, factories, labour, et al - have all become less productive.

This is not the first time that China has faced a challenging national balance sheet. Under the 'iron rice bowl' economic system that dominated the first three decades of the founding of the People's Republic of China, the productivity of the nation's key asset, the labour of Chinese citizens, steadily dropped as people lost motivation to work hard or to innovate on the job.

Leaders like Deng Xiao Ping in the 1980s and Zhu Rongji through the late 1990s took steps to remove the guarantees in employment, housing, and pensions for Chinese citizens, while simultaneously providing new rights and privileges to the people. New economic reforms meant that Chinese citizens would be allowed to own and trade a broader group of assets, including real estate, factories, stocks, and bonds. While the principal value of labour as an asset was no longer fixed, the principal value of these new types of assets was implicitly guaranteed by the government.

This was an extremely significant change in the 'social contract' between the Chinese government and its citizens: from now on, employment and wages would be at risk. There were no more salary guarantees, no more assigned housing slots, and no more guaranteed pensions. But if these same citizens took their capital and invested it in any of the new assets available to them - e.g. buying their own home or purchasing mutual fund shares - they could expect that the government would reimburse them for any capital losses. Note that the government did not explicitly state this guarantee, but from its actions in a number of well-known cases through the early and mid-2000s, the concept of this implicit 'government put' was repeatedly reinforced.

Almost immediately, the Chinese economy reaped significant benefits from this change in the social contract. The new assets that people were buying were highly productive, and Chinese GDP growth began its heralded streak of 30 years of double-digit expansion. However, over time the government's

new guarantee on the principal value of a broader set of assets became a significant problem.

Namely, the aggressive expansion of credit in the market, first in response to the financial crisis in 2008 and then as part of an aggressively loosened monetary policy through 2012-13, contributed to the sharp rise in asset prices and the decreased productivity of these assets. Similarly, credit growth also increased the number and diversity of the citizens holding these assets. It was no longer a limited number of wealthy and well-connected people who owned unproductive assets like mortgaged properties in ghost cities. Any and everyone was buying these type of properties. Similarly, investments in overvalued securities markets were no longer the domain of a select few institutional investors. Citizens across the country were buying stocks and investing in shadow banking products to take this exposure.

The government is now faced with the problem of unaffordable capital guarantees for a large swath of assets held all across the country.

Here is where the earlier pattern of actions around the change in the 'iron rice bowl' social contract helps explain current Chinese government policy. Many of the government's market actions through late 2014-15 can be interpreted as signals to the population that principal values of market assets are no longer implicitly guaranteed. In other words, people should no longer expect the government to guarantee the 'floor price' of less productive assets like real estate in 3rd or 4th tier cities, or small cap stocks with P/E ratios north of 100x.

Driving growth

To compensate for removing this guarantee, the government will institute new reforms to establish a nationwide health insurance system and a pension scheme. These reforms have been pre-announced but our expectation is that the government's efforts to provide tax-advantaged personal and employer retirement schemes and a nation-wide framework for quality healthcare will gain pace over 2016. This new version of the safety net may not be the equivalent of the iron rice bowl, but for a Chinese populace who will need to adjust to volatile property prices, the removal of shadow-bank product guarantees, and an increasingly volatile share market, any sort of reformed social protection will be welcome.

This change in the social contract will affect asset price volatility. These types of changes are often revealed and understood in fits and starts as the government and the citizens reach a new settlement. This unsteady process of learning and adjustment invariably introduces volatility, and we expect domestic secondary markets and real estate prices to remain volatile over the next 2-3 years.

Over the medium to long term, this type of inflection point in Chinese society should prove extremely positive and bullish for China's future growth. In fact, I would argue that this change in the social contract is a pre-requisite for a real, credible transition from a manufacturing-led to a consumer-driven economy. This type of safety net and the transparent pricing of risk that this new social contract represents should drive an aggressive expansion in China's private economy. The near-term period of volatility is unavoidable, but the potential for sustained, strong growth proceeding from this should be attractive to investors.

On a wider scale, other initiatives are under way, include deregulating utility prices, experimenting with free trade zones, allowing local governments to issue conditional debts, revamping the ownership model of some state-owned enterprises, reforming the *hukou* (household registration) system, reinforcing anti-corruption measures and relaxing the one-child policy.

Cautiously bullish

The bright spots in 2016 will be in the booming sub-economies. The services sector, for instance, will remain a key driver of growth. Education, law, finance, entertainment, research, business, and accounting services are in high demand. This vast array of services represented some 20% of the economy in 2015, and they should continue to prosper in 2016.

Recent policy changes have also made it easier for foreign firms to invest in China's online retail sector. Growth in this sector over the next five years is expected to come not from expansion into foreign markets, but from the nascent demand in China, set to be worth more than US$1 trillion by 2018 and to comprise some 750 million online shoppers by 2020.

While several major challenges remain – weak exports, high debt levels, currency devaluation, stock market volatility, and slowing investment – overall the Chinese economy shows no signs of coming to an abrupt halt. In fact, far from putting China on the verge of collapse, overcoming these challenges is likely to present a range of new opportunities.

Overall, I remain cautiously bullish about China. The country has been able to seize growth opportunities

during many paradigm shifts since the 1980s. For now, it will more than likely experience slower economic growth and continued asset volatility through much of 2016.

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The merits of reversionary versus non-reversionary pensions

Monica Rule

Superannuation legislation is full of complexity which unfortunately disguises valuable financial planning opportunities. One example is the decision whether to commence a reversionary pension or a non-reversionary pension as part of estate planning. Both pensions can be paid from an SMSF provided the Trust Deed allows for these benefits, but it's important to know the differences.

A **reversionary pension** is a pension that, upon the member's death, continues to be paid to the nominated reversionary beneficiary as though the reversionary pensioner were the original pensioner. The reversionary pensioner retains the same percentages of tax-free and taxable components of the deceased's pension account calculated at the beginning of the pension. Therefore, if the deceased pension account commenced with a 100% tax-free component, then the pension will continue as 100% tax-free.

A **non-reversionary pension** is a pension that ceases upon the member's death. Because the pension stops, the deceased's remaining superannuation at their death will need to be paid from the SMSF as either a lump sum death benefit and/or a new pension to the deceased's beneficiaries as soon as practicable. If a lump sum death benefit is payable, assets may need to be sold to make a cash payment. If a new pension is to commence, the percentages of the tax-free and taxable components of the pension may need to be re-calculated as explained below.

Benefits of a reversionary pension

1. Favourable tax treatment of insurance proceeds

If insurance proceeds from the deceased member's life insurance policy are paid to the reversionary beneficiary, then the proceeds also retain the tax-free and taxable components of the reversionary pension. The components are not re-calculated despite the insurance proceeds having a taxable component.

However, if the pension were non-reversionary, then the insurance proceeds are added to the taxable component of the new pension. This may make a difference to the amount of tax payable by the deceased's beneficiary if they are under the age of 60.

2. Estate security

Upon the death of an SMSF member who was in receipt of a reversionary pension, the trustee is not required to make a determination as to who should receive the deceased's superannuation as the pension will revert to the nominated beneficiary. This provides some level of certainty to the member as to whom their benefit will go to once they die. If the deceased member has a binding death benefit nomination, the nomination would need to state that the nominated reversionary pensioner is entitled to the receipt of the deceased's pension.

3. Assets can be retained in the SMSF

As the reversionary pension automatically reverts to the nominated beneficiary, there is no need to sell assets to pay out a lump sum death benefit.

Disadvantage of a reversionary pension

Where a member divorces or separates from the reversionary beneficiary, the member will need to commute the pension and start a new one with new terms and conditions (i.e. such as naming a new beneficiary).

ATO officials were asked at a technical meeting in March 2013 whether it was possible to change a non-reversionary pension to a reversionary pension. The ATO said it was possible as long as the terms under which the pension was payable and the SMSF's Trust Deed allowed it. However, the ATO also stated that a pension cannot be changed after the death of the pensioner. As the ATO has not made their view widely known, I would suggest you seek the ATO's approval if you are intending to change your non-reversionary pension to a reversionary pension.

Monica Rule is an SMSF specialist, adviser and author. See www.monicarule.com.au

Hello from the other side of Asia

Graham Hand

It's widely claimed that the next few decades will see hundreds of millions of Asians pulled out of poverty by world trade, technology, economic growth and better education. In this context, Asia is often equated with a billion people in each of China and India rather than the relatively-developed Japan or South Korea. By these standards and numbers, it's easy to think the rest of Asia does not matter much. But what are my impressions from three weeks in Sri Lanka, Bali and Singapore? It's a tiny snapshot with quick judgements on a small part of the continent, more travelogue than any claim to remarkable economic and social insights.

Sri Lanka

Sri Lanka will be very different 10 years from now. 'Visit before it changes' is said for many Asian countries, although [our travels last year in Burma] (Myanmar) still felt a long way from the majority of people joining a global prosperity trend. Even Yangon (the old Rangoon, once one of the wealthiest cities in the world) showed few signs of gain for most, and its formerly splendid public buildings were falling apart with little effort to retain them.

Not so in Sri Lanka. It's hard to believe this country was still racked by civil war as recently as 2009, when it took the sacrifice of 40,000 Tamil supporters to bring an horrendous end to decades of internal conflict. While not condoning such destruction of life, the locals we spoke to argue it was a necessary step to end the military insurgency that was destroying the country. Now, there is a pride in Sri Lanka and great hopes for its future. Streets in the capital of Colombo which only a year ago were closed to the public are now open. There is no security fear on the streets. Public buildings are undergoing proud restorations and being offered on long leases rather than sold, ensuring they remain in public ownership for locals and tourists to see forever, unlike their Burmese equivalents.

There's a good chance that a decade from now, Colombo will be a vibrant city on the hot list of places to see, alongside the great iconic cities of the world. The hotel industry has already recognised this, with almost every major intersection in the city now the site of a grand new hotel from an international chain. Go out at 11:30 at night, when it's difficult to find anywhere decent to eat or drink in Sydney, and Colombo is still buzzing. Of course, the balmy temperature and a culture of eating late both help, but it's amazing to see restaurants full of people in the middle of their meals at midnight, when our city restaurants are more worried about lock-out laws.

Of course, wealth spreads to the vast majority slowly. For the moment, it's still possible to jump in a three-wheeler 'tuck-tuck' for a few dollars and take a harum-scarum ride across the city. As a tourist, it puts the entire city at your fingertips in the way an efficient underground system does in first world cities. Obviously, the poor sod driving the tuck-tuck is still doing it tough in his world of diesel fumes and truck tyres higher than his roof, but there are a lot of tourist and business dollars now on the street.

It's the same for the thousands of car drivers who show people around the island. Sri Lanka is perfectly set up for this one form of transport, and arguably only one, for the tourist. The unique experience goes like this. Plan your circular trip around the island, usually starting at the only international airport in Colombo, and heading clockwise around the island, taking in Negombo, Kandy, Nuwara Eliya, Kandalama, Sigiriya, Galle, Sinagawa and back to Colombo, or further north if you have time. This covers vibrant cities, spectacular beaches, verdant scenery with cascading waterfalls and tea plantations in the high country. Send your schedule to a driver and he will pick you up from the airport and deposit you back to the same spot a couple of weeks later. Every night he will find his own accommodation, and pick you up every morning. The deal will cost about USD70 a night for driver and car. If you're prepared to pay, Sri Lanka already has amazing hotels across all these destinations - this trip is not a struggle through an impoverished country. It is travel with the best of everything laid on, provided you’re prepared to eat spicy and unique Sri Lankan fare. And maybe because Sri Lankans love their cricket, or because many locals have family or friends there, Australians are popular everywhere.

Bali

On to Bali for the first time for us in 30 years. Top of mind instinct was that it's the place of Australians drinking too much Bintang, pestering massages on the beach, red skin from a harsh sun, cheap T-shirts from shouting street sellers, drugs smuggled in surfboard bags and just about everything anyone over 40 wants to avoid. Right? Wrong. The Bali we hear about in the news obviously exists if you want to find it, but the other Bali is an island almost as interesting as Sri Lanka with arguably better food in the right places.

On arrival at Denpassar, instead of heading for the dreaded Kuta of the bars and beers, we are driven up the coast to a remote spot near the temple of Tanah Lot. The waves roll in like in a surfing movie, the nearby fields are for the moment still rice paddies, it claims the best golf course in Asia and it's only 15 minutes to the still unspoilt Canggu. Regular visitors tell us this place has changed in the last year or two, and chances are in five years, it will be one long development from Kuta north. But for now, there are enough new restaurants to raise the standard of eating without suffocating the place. This part of the trip is long lazy days by the pool then a quick taxi ride to a local eatery, but not a T-shirt shop or noisy Australian in sight. This other side of Bali remains relatively cheap for the Australian traveller shocked by European prices, but a long way from the $1 DVDs and $2 wood carvings in Kuta.

One disappointment was Ubud, renowned for its meditation, Buddha and writing festivals. No third world village can sustain such innocence faced with thousands of moneyed visitors every day, and it's now crowded with surf shops, tourists, taxi drivers and traffic. No doubt there is still a good side of this busy town, but if aiming for seclusion in the countryside, find the next Ubud. Stock up on board shorts and you're fine, and the massages are cheap, but it'll be hard work finding mindfulness and peace in a place the west has well and truly swamped.

Singapore

And on to Singapore, the place that Lee Kuan Yew built. He made no apology for the techniques he imposed on the nation to drag it out of poverty:

"I am often accused of interfering in the private lives of citizens. Yes, if I did not, had I not done that, we wouldn't be here today. And I say without the slightest remorse, that we wouldn't be here, we would not have made economic progress, if we had not intervened on very personal matters - who your neighbour is, how you live, the noise you make, how you spit, or what language you use. We decide what is right. Never mind what the people think."

The Singapore we visited 20 years ago seemed stifled by this dogma, limiting freedom and imagination in its desperation to grow as a first world destination and manufacturer. A visitor in the 1980s and 1990s found a sterile place, with little of the old retained and not much of the new to boast about. The mediocre theme park of Sentosa was a poor substitute for old authenticity of a genuine China town, hotels like Raffles and drinks like Singapore slings.

It's as if Singapore realised the error of its business-only approach, and started to make the city worth visiting. Gardens by the Bay is one of the world's great reconstructed waterfronts, even if the biggest trees are man-made. In fact, the SuperTree Grove works well in the waterfront gardens, with the skywalk a delight for something that could be so kitsch. The laser water shows each night attract the crowds, and a walk around the harbour on any evening, with its balmy weather and much to see, make it a rival to any late night saunter.

Not far from the water is Lau Pa Sat, or the Telok Ayer Market, a decent competitor for Newton Circus, and recommended by a local as the real thing and 'not air-conditioned'. Hundreds of food vendors of all global styles demand attention. At 7 o'clock each night, a street is closed off and tables and chairs instantly appear by the dozen as sate sellers churn out thousands of pieces of meat and fish cooked over charcoal. The beer flows, the night is warm, and the meat is smokey. Hard to beat.

Singapore has made itself worthy of two to three days for any Aussie on the way to Europe, while not quite a tourist destiny in its own right. Unlike most other parts of Asia, it seems to set new standards for accessibility, with all the new developments perfectly flat for anyone using a wheelchair or stroller, and a cleaner and more accessible underground train network than anything Paris, New York or London has managed to build. Designers of Sydney's transport system should take a look before they build any more inaccessible stations.

It's every bit a financial centre like the global cities of the west. The financial district is big and glassy and commands the city and its harbour, shouting the names of the banks and insurance companies across the water. Young people dress smart, laugh in optimistic groups, eat at expensive restaurants, exercise vigorously, buy the best brands and tap away at their iPhones. It feels a million miles from the villages of Burma, Sri Lanka and Bali.

A quick snapshot

It's only three weeks in three relatively small countries, so let's not draw too long a bow about the whole of Asia. But outside of those dealing directly with business and tourists, for every person dragged out of poverty, there will probably be five more wondering where the next meal is coming from. In Singapore it's still the old Chinese who clean up the plates and chop the vegetables, in Bali it's still the old women doubled up in muddy water planting the rice, and in Sri Lanka the street sellers hawk coconuts for 50 cents a pop and make a few sales a

day working dawn until dusk. They might wear a Manchester United or Chelsea shirt but it's dirty and was sewn in a factory down the street. And apparently, many in the new generations are less willing to care for the old in the traditional ways.

It's easy to see only the millions who are being lifted from poverty by global trade and the rapid influx of tourists, but this is the tip of an iceberg, and hundreds of millions will be left behind. If the uneducated and elderly look on enviously at the younger generation who embrace the ways of the west, while the disadvantaged still wipe the dishes with no social security system to protect them as they age, then they will care little for the gains being made.

In both Sri Lanka and Indonesia, chat to a local and you'll find most would love to live in Australia. It's worth doing a trip like this to appreciate what we have, how most of the world would like the same, and yet the vast majority will never see it in their lifetimes, especially when they see our borders as even less welcoming than when their friends migrated here many years ago.

Graham Hand is Editor of Cuffelinks and takes no responsibility if you catch Bali Belly.

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