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**Money makes the world go around**

*The classic 70's film Cabaret perhaps did not coin the phrase "Money Makes the World go Around" but it certainly put it on the map. But what is money, how does it work and what role does it play in our lives? Money always has and always will be an important part of our lives. Yet most of us know little about it other than how to spend it and (hopefully) save it!*

A recession is a curious beast. It gives us time to question things again. Like money and inflation and what on earth they are and what role they play in our lives. Money doesn't have any inherent value. It is simply pieces of paper or numbers in a ledger. A car has value because it helps us get where we need to go. Water has value because it has a use; if we don't drink enough of it we will die. Money has no more practical use than any other piece of paper.

**Back in the day**

It didn't always work this way. In the past money was in the form of coins, generally made of precious metals such as gold and silver. The value of the coins was roughly based on the value of the metals they contained, because you could always melt the coins down and use the metal for other purposes. Paper money was, until a few decades ago, based on the *gold standard* or *silver standard* or some combination of the two. This meant that you could take some paper money to the government, who would exchange it for some gold or some silver based on an exchange rate set by the government. The gold standard lasted until 1971 when President Nixon announced that the United States would no longer exchange dollars for gold. This ended the *Bretton Woods System* (see sidebar on pg 2) and was widely replaced by a system of *fiat money* (see sidebar on pg 2), which is not tied to any other commodity.

So why do Rand notes (or dollar, Euro or any other paper money) have value and some other pieces of paper do not? It's simple: money is a

commodity with a limited supply and there is a demand for it because people want it. The reason we want money is because we know other people want money! Therefore we can use money to get goods and services in return. They can then use that money to purchase goods and services that they want. Goods and services are what ultimately matter in the economy, and money is a way that allows people to give up goods and services which are less desirable to them, and get ones that are more so. People sell their labour (work) to acquire money now so as to purchase goods and services in the future. If we believe that money will have a value in the future, we will work towards acquiring some.

**Delicate balance**

Our system of money operates on a mutual set of beliefs; so long as enough of us believe in the future value of money the system will work. What could cause us to lose that belief? It is unlikely that money will be replaced in the near future, because the inefficiencies of a *dual coincidence of wants* (see sidebar on pg 2) system are well known. If one currency is to be replaced by another, there will be a period in which you can switch your old currency for new currency. This is what happened in Europe when countries switched over to the Euro. So our currencies are not going to disappear.

Then why else would we think that our money might be of no value to others in the future? Well, what if we believed our money wouldn't be nearly as valuable in the future as it is today? An increase in prices

(called inflation) causes a devaluation in the buying power of money over time. High inflation, and the rational way citizens react to it, causes great misery for an economy. People will not sign into profitable deals which involve future payments because they'll be unsure of what the value of money will be when they get paid. The belief in the future value of money is not an innocuous thing. If citizens lose faith in the money supply and believe that it will be worth less in the future then economic activity can grind to a halt (think Zimbabwe). Business activity sharply declines because of this and excessively high (hyper-) inflation will cause all sorts of other problems, from the café changing its prices on a regular basis, to the homemaker taking a wheelbarrow full of money to the bakery in order to buy a loaf of bread.

**Give and take**

Money is essentially a good, so as such is ruled by the axioms of supply and demand. The value of any good is determined by its supply and demand and the supply and demand for other goods in the economy. A price for any good is the amount of money it takes to get that good. Inflation occurs when the price of goods increases; in other words when money becomes less valuable relative to those other goods. This can occur when:

- The supply of money goes up.
- The supply of other goods goes down.
- Demand for money goes down.
- Demand for other goods goes up.



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### The Bretton Woods System

The Bretton Woods system is commonly understood to refer to the international monetary regime that prevailed from the end of World War II until the early 1970s. Taking its name from the site of the 1944 conference that created the International Monetary Fund (IMF) and World Bank, the Bretton Woods system was history's first example of a fully negotiated monetary order intended to govern currency relations among sovereign states. In principle, the regime was designed to combine binding legal obligations with multilateral decision-making conducted through an international organization, the IMF, endowed with limited supranational authority. In practice the initial scheme, as well as its subsequent development and ultimate demise, was directly dependent on the preferences and policies of its most powerful member, the United States.

### Fiat Money

The term **fiat money** is used to mean:

- any money declared by a government to be legal tender.
- state-issued money which is neither legally convertible to any other thing, nor fixed in value in terms of any objective standard.
- money without intrinsic value.

The term derives from the Latin *fiat*, meaning "let it be done", as the money is established by government decree. Where fiat money is used as currency, the term **fiat currency** is used. Today, most national currencies are fiat currencies, including the US dollar, the euro, and all other reserve currencies.

### Coincidence of Wants

The **coincidence of wants** problem is the great barrier to why a barter system is not used instead of money. The problem is caused by the improbability of the wants, needs or events that cause or motivate a transaction occurring at the same time and the same place. One example is the bar musician who is "paid" with liquor or food, items which his landlord will not accept as rent payment, when the musician would rather have a month's shelter. If, instead, the musician's landlord were to throw a party and desire music for it, hiring the musician to play it by offering the month's rent in exchange, a double coincidence of wants would exist.



Liza Minnelli and Joel Grey singing "Money makes the world go around" in the 1972 film Cabaret

*... money has value because people believe that they will be able to exchange their money for goods and services in the future.*

*This belief will persist so long as people do not fear future inflation.*

The key cause of inflation is the increase in the supply of money. Inflation can occur for other reasons. If a natural disaster destroyed stores but left banks intact, we'd expect to see an immediate rise in prices, as goods are now scarce relative to money. These kinds of situations are rare. For the most part inflation is caused when the money supply

rises faster than the supply of other goods and services.

So to answer our question, money has value because people believe that they will be able to exchange their money for goods and services in the future. This belief will persist so long as people do not fear future inflation. To avoid inflation, the government must ensure

that the money supply does not increase too quickly.

So does money make the world go around? Literally it doesn't but it certainly provides momentum for the world economy. Without money we would not grind to a halt but would certainly slow down!

## Turning a downer into an upper: 9 tips

*The economic downturn has made people all the more aware of the importance of husbanding their money carefully. Here are the 9 key steps to save and invest wisely.*

### 1. Pay off debt

The repayment of debt is the best investment you can ever make. The recession means fewer job opportunities, wage cuts, and rising unemployment. In order to protect yourself, it is wise to repair your personal balance sheet.

Reduce your spending and use the money you save to reduce personal debt first (credit cards, overdrafts, store cards, loans), then your bond. Build a cash cushion to help meet unexpected bills or to cover expenditure if your income falls.

### 2. Investment basics

Try not be swayed by media hype and remember the basics of investment. Assess how much risk you want to take, take into account how long you wish to invest for and apply an asset allocation (split between equities and fixed interest) appropriate to your risk profile and term of investment.

Choose low-cost funds that are adequately diversified in order to reduce risk and rebalance periodically to ensure that the correct risk profile is maintained.

### 3. Inflation will return

Equities here and overseas are now probably, on the whole, fair value, if not cheap. The question is what to buy. One needs to hedge one's portfolio against inflation, which, although months and possibly years away, will come back and bare its teeth.

In SA but perhaps especially overseas one needs to invest in companies that do not rely on high leverage to prosper, and where the drive towards a sustainable world will see profits, so the themes of water, pollution, carbon credits, renewable energies and population, including pharmaceuticals and biotechnology, should be to the fore. Going for green may well pay out a handsome reward in...green!

### 4. It's not about finding the next Microsoft

A diversified approach has made sense in the past, makes sense today and will continue to make sense in the future.

Broadly diversifying a portfolio minimises the risk of owning any single shareholding. Successful recessionary investing is not about finding the next Microsoft. Don't be enticed into thinking you can easily get rich quick. Focus on the less glamorous concept of diversification.

Overconfidence and under-diversification do not serve investors well.

### 5. Why will someone pay more than you did?

Remember that investment is as much about scepticism as it is about identifying opportunities. Never invest in anything that you do not understand.

Before investing, consider how you will realise your investment in the future, when you want to or need to. Ask yourself why someone would be willing to pay more for your asset in the future compared with the cost at which you are investing.

These principles apply equally in a recession or in a boom.

### 6. Use tax breaks

Always take advantage of tax breaks. Don't erode your returns by allowing inefficient taxation on your gains. Tax relief on RA's boosts funds immediately.

We will recover from the recession and stock markets will rise. For those who are well-positioned, opportunities will arise to pick up assets at great value.

### 7. Look for resilient investments

We are in a "balance sheet recession" – banks won't lend to you on the terms required and neither are consumers looking to borrow in droves. The Gov-

ernment too is suffering.

In this environment the aim is to minimise debt rather than maximise profit. Debt minimisation favours investment funds with a bias towards non-cyclical stocks such as utilities, telecommunications, pharmaceuticals and tobacco. These are resilient stocks that remain in demand no matter the economic climate and provide the most reliable dividend.

### 8. A portfolio for all seasons

Rather than speculating on which funds are best to invest in during a recession, consumers should spread their risk by investing in different asset classes (equities, property, commodities, bonds and cash).

This creates not only a "portfolio for all seasons" but also one that gives you the best chance of achieving your short to long-term financial objectives.

Finally, if timing the markets is of concern then "drip feeding" money back in over the next six to 12 months may be a practical solution, albeit a costly one if market sentiment improves soon.

### 9. Consider structured products

Structured products play a useful role in portfolios and enhance returns by either:

- Offering capital guarantees
- Offering access to sectors or securities that complement your portfolio
- Offering a level of participation that can enhance returns

Structured products carry an underlying level of risk that is understandable and in line with your individual risk tolerance, notwithstanding any guarantee. These innovative products provide a more flexible asset allocation and easy access to defensive investment strategies for fast-changing market conditions.

# Big Business 2010



Port Elizabeth

*Unless you have recently returned from an extended holiday on Mars, you will have been aware that South Africa appears to have been annexed by a group of people from a place called "FIFA".*

The *Fédération Internationale de Football Association* (or translated from its official French name, the "International Federation of Association Football") is the international governing body of "association football", or what we South Africans commonly call "soccer". In this quarter's issue we take a closer look at FIFA, and in particular how it makes its money and how its finances stack up.

As a response to the spreading of the popularity of soccer from its birthplace in England to Europe and other parts of the globe at the beginning of the 20<sup>th</sup> century, FIFA was founded in 1904. Its original founder member states were Belgium, Denmark, France, The Netherlands, Spain, Sweden and Switzerland.

## Soccer structure

FIFA now has 208 national member associations, which is three more than the International Olympic Committee. In fact, FIFA has more member states than the United Nations— this is largely because it recognises several non-sovereign countries as distinct nations, most notably the four Home Nations within the United Kingdom. It is perhaps surprising to learn that South Africa were the first country outside Europe to join FIFA, in 1908 (thus joining even before Brazil, Argentina and the first world champions, Uruguay). South Africa was suspended from FIFA in 1961 owing to its government's Apartheid policies and finally expelled in 1976, following the Soweto riots. South Africa was, however, readmitted to FIFA in 1991.

FIFA is legally structured as a non-profit organisation established as an "association" under the laws of Switzerland. Its headquarters are located in Zurich, Switzerland and its current president is a man whose face and name have become so familiar to us in recent months, Sepp Blatter. FIFA's principal mission is to promote the game of soccer throughout the world and its statutes require it to use its

profits, reserves and funds in pursuit of this mission.

FIFA is responsible for the organisation and governance of football's major international tournaments, most notably the FIFA World Cup, held every four years since 1930 (barring a twelve year hiatus from 1938 to 1950 due to the Second World War). It is this four-yearly World Cup that is FIFA's main money spinner. The event is by far the world's most watched sporting tournament measured in terms of worldwide television audiences. In fact FIFA's financial health is almost entirely dependent on a successful staging of the World Cup and the current 2010 tournament has posted record revenues that surpass all previous tournaments. The World Cup is so important to FIFA's finances that the organisation even reports its finances in four year periods each beginning in the year following a World Cup tournament.

FIFA generates its revenue from the World Cup mainly by selling the tournament's broadcasting rights to international television companies and the associated marketing rights to numerous multinational corporation "partners" such as Coca-Cola, Sony and Visa. The revenue from the ticket sales for the 2010 World Cup is earned and retained by the South African Local Organising Committee with the profits derived from that source being ploughed into local soccer.

Financially, FIFA seems to go from strength to strength. According to its latest audited financial statements, FIFA's revenue for 2009 was 1,022 billion US dollars (about R7,7 billion), the first time in its history that its annual revenue exceeded the one billion dollar mark.

And with a potentially even more lucrative World Cup to be hosted by Brazil in 2014, it appears FIFA has transformed itself from a mere sporting organisation into a billion dollar global business.

## FIFA's finances – How the figures play out

US\$ 1,022 billion – FIFA's revenue earned during 2009 (equivalent to about R7,7 billion)

US\$196 million – FIFA's net "result" (profit) for 2009 after incurring expenses such as event-related expenses (think 2010!), football development, and governance and operating expenses

US\$3,8 billion – FIFA's budgeted revenue for the 2011-2014 period (equivalent to almost R30 billion) - it is forecast that most of this revenue will be generated by the Brazil 2014 World Cup

US\$305 million – the amount reputed to be paid by corporate sponsors such as Coca-Cola and Sony to be "FIFA partners"

US\$420 million – the total prize money awarded to the 32 national associations participating in the 2010 FIFA World Cup

US\$30 million – the prize money awarded to the winner of the 2010 FIFA World Cup (about R228 million)

US\$49 million – FIFA's salary and wage bill for 2009

361 – average number of employees employed by FIFA during 2009

## Staying Onside

In South Africa, the portion of prize money which the participating associations in the 2010 World Cup pay their players in the form of bonuses is subject to SA tax. FIFA will withhold part of the prize money until the participating associations have discharged their

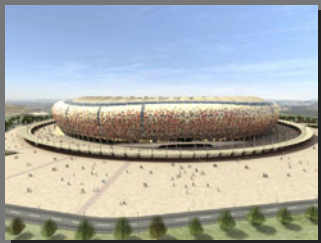


## Scoring for South Africa

It has been estimated that the 2010 FIFA World Cup will sustain have a gross impact of R93-billion on South Africa's economy

A report by UBS Investment Research (from February 2010) estimated that preparation for the World Cup – which commenced four years ago – has added between 0.5% and 2.2% to South African GDP (depending on which infrastructure projects one considers); and overall had created in excess of 300,000 jobs since 2006 – a 2.7% contribution to employment figures





Soccer City, Johannesburg



payment obligations to the local tax authorities.

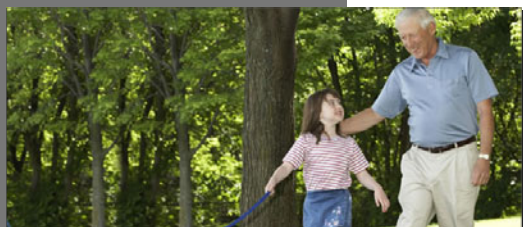
#### Messi's Millions

According to a recent report in *France Football* magazine, Argentinian forward Lionel Messi has become the highest-earning footballer in the world, putting an end to David Beckham's two-year reign. The 22-year-old Barcelona and Argentina player pocketed an estimated US\$44 million (about R334 million) during 2009 in salary, bonuses and publicity contracts. Messi was ranked as the fourth highest-earning sports person in the world, behind golfers Tiger Woods and Phil Mickelson, and basketball star LeBron James.



#### Tales from the crypt

The longest known legal will is that of Englishwoman Frederica Evelyn Stilwell Cook. Probated in 1925, it was 1,066 pages, and had to be bound in 4 volumes; her estate was worth \$100,000. The shortest known legal wills are those of Bimla Rishi of Delhi, India, and Karl Tausch of Hesse, Germany; each consisted solely of three words



## 10 Estate Planning essentials

*Estate planning is certainly not something that most people look forward to. However, it is imperative to make sure that everything you have worked long and hard to acquire ends up in the right places after you die.*

Estate planning is more than simply having a Will, and many other aspects need to be considered. Below are ten estate planning essentials that should be considered.

#### 1. Review / update your will:

Having a Will is the cornerstone of any estate plan. For anyone with children the consequence of not having a Will may be devastating. Once you have a Will, it is important to review it regularly, and also to ensure that your family know where to find your Will when you aren't around to show them.

#### 2. Appointing guardians for minor children:

This issue is often overlooked by parents, especially as a surviving parent remains guardian in the event of the death of the other parent. However, couples should always stipulate a guardian for their children to cover the eventuality of their simultaneous death. Deciding who will raise your young children should you die is a tough task - so tough that many parents never do it. Some just procrastinate, while others find themselves deadlocked, unable to agree with their partner over a suitable candidate. For parents who have minor children, it is imperative to take time and special consideration when deciding who will take guardianship of their children in the event that they die. Your nominated guardian should be stipulated in your Will.

3. Review beneficiaries:  
As your family situation changes over the course of a lifetime, you may need

to change the names of beneficiaries not only in your Will but also in life insurance policies and other documents that list beneficiaries, such as trust deeds and group life funds.

#### 4. Appointing trustees for minor children:

Trustees should not be confused with guardians – trustees are appointed in a Will to administer monies inherited by young children, or heirs who are not capable of doing so. Guardians look after and care for minor children. The appointment of trustees is crucial for inheritances by minor children (i.e. under 18 years) as in the absence of provisions in a Will creating a trust, a minor child's cash inheritance must be paid over to the Master of the High Court's Guardian's Fund for safekeeping.

#### 5. Record-keeping:

It is a traumatic time for the surviving family when someone passes away. This trauma can be exacerbated when your loved ones cannot find important documents, keys to safety deposit boxes, financial statements and other necessary information. It is essential to create a list of where all-important information can be located and give the list to someone you trust.

#### 6. Donations:

In terms of current legislation, a person is allowed to donate up to R100,000 each tax year, free of donations tax, to children, trusts or other persons. There is no limit on the amount that spouses may donate to one another tax free. By making donations, large estate can be reduced to avoid significant estate taxes.

#### 7. Estate taxes:

There are various ways to limit the

taxes payable on your estate (such as estate duty and capital gains tax), depending on the size of your estate and your family situation. It is worthwhile to discuss the options with your financial advisor.

#### 8. Liquidity:

One of the most common problems in winding up an estate is the situation where there is not sufficient cash to settle the estate's liabilities, such as mortgage bonds, vehicle finance, taxes and winding-up costs such as executor's fees and conveyancing costs. In such a situation the outcome can be a forced sale of assets (such as the family home). Life insurance is an easy and affordable way to provide estate liquidity.

#### 9. Offshore assets

If you should have offshore assets when you die, you'll also have a foreign estate that will have to be administered. Each country has its own legislation dealing with inheritance and the signing of Wills. Your South African Will won't necessarily meet with the legal requirements of the country where your assets are situated. A solution is to execute a separate Will in the foreign jurisdiction dealing only with those assets.

#### 10. Make a living will:

Many people today draw up living wills. A living will is an advance document reflecting a person's wishes regarding the type of medical care he or she would or not want if the person lacks the physical capacity to communicate his or her needs, especially where there is no hope of recovery or significant improvement. One of the most important roles of a living will is that it may be the only written evidence of what a person's wishes are.