From the Chair of the Editorial Board

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AS THIS ISSUE OF JASSA GOES TO PRESS, the dust is starting to settle from the global financial crisis. Most major share markets are up, for the year to date, though none by as much as the Australian market. Some semblance of normality has also returned to credit spreads and, although central bankers remain cautious about the possibility of a second wave of financial distress, the overall prognosis is starting to appear more positive. With some of the lessons from the crisis also becoming clearer, the papers in this issue of JASSA make an important contribution to the current review process. The topics covered in this issue span banking, insurance, insolvency, superannuation and investment management, each highlighting key factors, risks and opportunities that we would be well advised to assimilate.

Lakshman Alles F Fin examines two key factors that contributed to the global financial crisis viz. fair value accounting and credit rating agencies, and the combination of these factors in producing a continuing pro-cyclical destabilising effect on financial institutions. Noting that the authorities are far from resolving these issues, he indicates that an important lesson to be learnt is the importance of maintaining strict regulatory oversight of the level of risk exposures in financial institutions as well as of individual investment activities, irrespective of the prevailing investment climate.

Andrew McRobert SF Fin provides some thoughts on leverage, identifying key areas where he suggests a new approach to assessing leverage is required, which is very different from that of 20th Century financial analysis. His paper highlights the extent to which actual leverage had blown out to extraordinary levels prior to the global financial crisis. He indicates that analysts should measure leverage by reference to all committed debt facilities, regardless of whether the accounting treatment requires them to be included in the balance sheet or disclosed only in the notes.

A number of articles examine strategies for mitigating various forms of risk, for lenders, insurers, investors and superannuation fund members. Eric Flaye notes that in the wake of the global financial crisis, it has become increasingly common for lenders to pursue 'informal workout' arrangements with distressed borrowers in an attempt to avoid the destruction of value often associated with formal insolvency proceedings. His paper provides some practical suggestions that may assist Australian lenders in mitigating these risks.

John Evans F Fin examines the findings of a recent survey of Australian and New Zealand insurers to determine their key success factors in prevailing market conditions. He observes that there is now a new focus on capital management within the industry. Insurers, he suggests, are recognising the need to manage their risks better; they are relying less on investment returns as a component of profits, and are using reserves instead of investment returns to manage profits.

With most self-funding lump sum retirees taking pensions by regular drawdown from a managed fund, the paper by Roger Gay F Fin raises the question of whether drawdown is too risky. He indicates that when an indexed pension is taken from a lump sum invested in a market index fund, the probability of retaining the original value of the lump sum in real terms (or better) reduces in direct proportion to the amount of the annual starting pension. His paper proposes an alternative retirement income strategy that is generally preferable to drawdown if term annuities can be purchased at a reasonable price, particularly if guaranteed by government.

Tariq Haque's study of butterfly strategies in Australian fixed income markets is also quite topical as a growing number of investors are now likely to invest funds in the bond market instead of equity markets. With these investors likely to invest funds with active bond fund managers, his paper provides some insights into the profitability of the butterfly strategy, which is commonly used by active bond fund managers to boost portfolio returns by taking advantage of the different convexities of bonds with differing maturities. His paper suggests that the cash and dollar duration-neutral butterfly does not, on average, generate positive profits after transaction costs.

Phil Preston F Fin reviews *Opportunities beyond carbon*, a collection of essays edited by John O'Brien which, he suggests, provides an efficient way for a non-carbon savvy reader to get abreast of the key issues on climate change. He notes that a key strength of the book lies in the diversity of the contributors, including perspectives from academics, entrepreneurs, industrialists and environmental practitioners.

The latest book by the famously successful hedge fund operator, George Soros, *The crash of 2008 and what it means: the new paradigm for financial markets*, is reviewed by Allan Barton. He indicates that Soros brings extensive experience and analytical skills to his examination of the operations of financial markets and proposals to reform them so that they do not involve the boom/bust cycles that have regularly occurred. Academic, professional and government policy makers will find the study of great benefit and interest.

Finally, a new Finsia report, *Changing tides – consumer finance and the generational wealth divide: trends and insights*, provides some interesting insights on a broad range of issues including household debt and savings levels, and retirement planning and investment strategies.

I would like to express my satisfaction with the range of contributors in this issue. Some are new, some are 'repeat offenders'; some are from academe but many are practitioners. It is this mix, together with the incisiveness of the peer-review process, that makes JASSA such a uniquely valuable publication for the Australasian finance sector. For those interested in submitting an article, the guidelines for submission are available at www.finsia.com. Any comments on these or any previous articles in JASSA are also welcome at m.fahrer@finsia.com