The INVESTMENT COLLECTIVE

INVESTMENT MARKET UPDATE

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MESSAGE FROM MANAGER

When I went to university, the discipline of economics prided itself on carefully constructed hypotheses, and did its best to correct for errors along the way. It's a shame that many people who call themselves economists have let go of those high ideals.

The Grattan Institute's latest paper, for example ("Money in Retirement More than Enough", which I have read word for word) is nothing more than a collection of 'thought bubbles', loosely connected by an 'us and them' narrative.

How can The Grattan Institute even remotely defend its argument that too many people are saving too much in super? Almost every day we are hearing of caps on super contributions, deferral in payments of the age pension, and all manner of proposed changes to an already vague retirement incomes policy, including the tax treatment of assets. In that environment a sensible person would be completely correct in believing that they will have to fend for themselves – especially if they have the interest and ability to read and comprehend matters relating to longevity, the fact that less than 50 percent of the population is paying net tax, and measures (suggested by the Labor Party) intended to reduce retirement incomes for many people.

Grattan seems to think that good policy involves essentially locking people into a predetermined socio-economic status, based on some notion of historical earnings. The Institute's choice of 'replacement earnings' as a desirable income level (a number based on some measure of former salary) ignores any aspirational goals of intending retirees, many of whom work for the very reason that saving now will see them better off in retirement, when they will have the time to do things they want to do and really value.

In the Australian Financial Review (Ignore the Fear Factory – retirees have enough cash - 7 November, 2018) John Daley claims it is a myth that savings on the age pension outweighs tax concession on super. Such a claim is at best disingenuous, but more likely probably borders on professional negligence. By my calculations, assuming someone starts on $40,000 per annum, reaches peak earnings of $120,000 in year 8 and retires at 65, and that the superannuation portfolio earns 4% real, then the balance of the fund at retirement will be very close to $1 million. Working in real dollars and returns, whether a single or a couple, a superannuation balance of this size precludes any Age Pension benefits. Assuming a life span of 20 years following retirement, for a cost of about $175,000 in forgone tax, the Government therefore enjoys a return of between $359,000 and $718,000, depending on whether an Age Pensioner is claiming as a single or a couple. The results are not much different if income maxes out at average weekly earnings.

It is true that the superannuation industry amps up the fear factor and the paper does raise some useful issues - some of which have been off the table for far too long. The asset class of the 'home ownership' for example, is unique for its exemption from capital gains tax and the Centrelink assets test, for it being the preferred security for almost all bank lending, and it being the asset class on which Australian Prudential Regulation Authority (APRA) has essentially based the integrity of the whole Australian banking system.

The constant changes as regards retirement incomes policy, are a concern for all people – working and retired, but the Grattan report contains a bias that is difficult to understand from an independent think tank. Whatever it is, the report is not a robust piece of economic analysis.

David French
Managing Director

Tips For First Home Buyers

If you are looking to buy your first home, here's some things to consider to improve your chances of finding the right property, securing the funding, and realising your dreams.

Watch your spending

Due to recent pressure from Australian Prudential Regulation Authority (APRA), and the fallout from the banking royal commission, lenders are under increased pressure to tighten credit eligibility guidelines and ensure stricter adherence to responsible lending practices. The lender will need to assess that an applicant can more easily afford to service the debt by applying actual living expenses, as opposed to the Household Expenditure Measure used until recently.

The lender will scrutinise your usual living expenses, check your spending habits and financial discipline by obtaining your transaction account(s) and credit card statements.

You could be jeopardising your chances of getting approval for a home loan if you are overspending on discretionary items such as entertainment or holidays. There have been recent headlines in the Australian Financial Review about lenders reviewing spending patterns on Netflix, Afterpay and Uber Eats. Set a budget and minimise your discretionary spending. Most importantly, make sure you have the discipline to stick to it!

Check your credit rating

A key part of your success in obtaining a home loan will be your credit score. A lender will lodge an enquiry on your credit file to check your credit history, and to confirm if you have had any history of late payments or defaults with other providers.

Credit reporting agencies such as Experian, Equifax and Illion (previously known as Dunn & Bradstreet) obtain information from banks, credit providers and utility companies to calculate a credit score. Your credit rating is based on the amount of credit you have borrowed, the number of applications you have previously made, if you have any overdue or unpaid debts, and if you have any history of bankruptcy or insolvency agreements.

Lenders use your credit rating to determine if you are suitable for a loan. Understanding what makes up and affects your credit rating is important for any homebuyer. You can obtain your own credit rating - including any defaults listed against your name by registering online. There can be mistakes on your report - if you pick up on them you can request they get altered. This could be the difference between a loan application being approved or declined!

The Australian Securities and Investments Commission (ASIC) MoneySmart website provides links to the credit reporting agencies which offer an online credit score check.

Reduce your credit and store card limits and minimise other debt

If you have larger credit card limits or other debt, you may not be able to borrow as much, or be eligible for a home loan approval. Reduce your credit card limits and decrease/pay off any existing debts you may have before you apply for a home loan, especially high-interest debts such as credit cards and store cards.

Due to credit policy changes in line with the tightening of responsible lending guidelines, lenders have increased the assessment rate on the servicing of existing credit card limits when reviewing a loan application. This may affect your eligibility for approval on a home loan at the required amount. Reducing debt or lowering your existing card limits will increase the likelihood of your loan being approved.

Higher deposit, better outcome

If you've saved less than 20% of the purchase price, there are a limited number of lenders who can offer a loan. Deposits of less than 20% may require Lenders Mortgage Insurance (LMI) to qualify for the loan, and the rate offered and fees may be higher to offset the increased risk to the credit provider.

While some lenders offer lower deposit loans, if you have saved a deposit of 20% or more, you may be eligible for a loan with a wider range of lenders with reduced rates/fees, and you will save the cost of an LMI premium.

Be aware of purchase costs and your eligibility for first home buyer grants and/or stamp duty concessions in your state

Buying a home incurs costs in addition to the purchase price. Allow for property inspection fees, loan application costs, mortgage registration fees and stamp duty. Loan establishment costs, mortgage registration and stamp duty can be covered via the lender if you qualify for the amount required. You may be eligible for the First Home Owners Grant (FHOG) or stamp duty exemptions/concessions. If you're eligible, you'll save thousands of dollars. Check online with your state revenue office to see if you qualify.

Check the features and options available with the lender

The interest rate is not the only thing to consider with a home loan. Make sure you understand the fees payable, product features/options available and how they work to suit your needs.

Some loan products include redraw facilities, offsets via linked transaction accounts, the ability to split the loan into several accounts on a fixed or variable rate, and greater repayment flexibility.

Be wary of discounted first home buyer specials

Lenders may offer a special discounted introductory rate for first home buyers. Check the terms and conditions carefully as the initial rate may default to a much higher rate at the expiry of the introductory period. These products may also incur higher establishment costs and ongoing fees.

Know the market in your target area

Thoroughly research the property market where you want to buy. Get an understanding of the average prices, supply/demand, local facilities, market activity/trends and recent auction results. This will ensure that your market knowledge will increase, and that your target area has what you need in terms of both lifestyle now and future growth opportunity.

Often the difference between getting value or paying a premium price is the buyer's level of market knowledge.

Get pre-approval

Obtain a pre-approval from your lender. This will ensure that you know your borrowing capacity in advance, and you can negotiate your purchase price.

Typically, there's no cooling-off period at auctions, once you've made an accepted bid that's it. Bidders without finance approval can find themselves in deep water if they sign a sale contract. You cannot make the contract subject to any conditions such as obtaining finance unless the seller agrees to the provision.

Get advice

You can get advice with any stage of the home buying process.

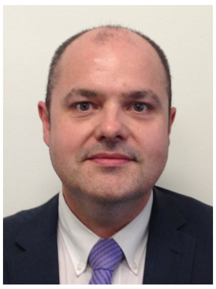
Buyers' agents can assist in locating, evaluating and negotiating the purchase on behalf of the buyer.

A Conveyancer will ensure that the buyer is meeting their legal obligations during the purchase and make certain that the title transfers smoothly.

A Mortgage Broker can review the thousands of products available to source the most appropriate loan solution for your needs, and assist with the finance process from application right through to settlement.

Please contact us today for a confidential, cost and obligation free discussion about your lending needs. We would also be happy for you to refer your family or friends so we can also assist them to locate a cost effective home loan which suits their needs.

Scott Plunkett
Mortgage Broker/Risk Adviser



Why Do I Need A Bookkeeper?

We are not all experts and running a business is a juggling act. Engaging a bookkeeper can take some stress out of your situation. A bookkeeper can help with giving a small business owner back some control and balance to their life.

You shouldn't have to work in your business all day then spend half the night doing the books or stressing about whether your suppliers or employees have been paid on time because there aren't enough hours in the day to do it all. You take your car to a mechanic because they are an expert, why not treat your business the same?

Deciding to have a bookkeeper for your business is one of the most important steps you can take. Ensuring the integrity of your financial records by choosing a professional means less stress and lower costs overall. Having someone else doing your bookkeeping gives you time to work on your business, and to create goals and plans to grow and expand your business. You also have the added bonus that a professional will ensure that your financial records are compliant and all your obligations are met in a timely manner. A bookkeeper can provide reports that will allow you to make crucial decisions regarding the future of your business. These reports and any discussion with someone else gives you a different perspective on the numbers and in turn may offer alternative directions for the future of your business. Having a bookkeeper can give you insight and knowledge you didn't have before.

It is important when choosing a bookkeeper to look at their professional accreditation. Ensure they are a registered BAS Agent with the Tax Practitioners Board and that they have the appropriate qualifications and experience. Research the person you are considering, check their website, ask them about the industries they work in. Check the type of software they use. It's okay to speak with more than one bookkeeper. Ask family and friends for recommendations. Make sure they are compatible with you. It's important that you have a trusted working relationship with your bookkeeper so get to know them and make sure you will be comfortable sharing financial information with them.

Bookkeeping Team

5 Tips to Avoid Scams

Scammers are getting smarter and smarter in the ways they reel people in and they are succeeding because they seem legitimate. You may think that you won't get caught, however, many people with this attitude still get caught out.

Here are some tips to help avoid being scammed:

1. Be alert, understand there are a lot of scams and scammers who are very good at what they do.
2. Don't get intimidated by threatening emails or phone calls. If you receive a phone call, let the caller know you will verify the information and call them back. Legitimate organisations will not have a problem with this.
3. Know who you are talking to. Do some research via Google or look the organisation up in the phone book and call them on the published phone number, NOT the one they have provided and verify what you have been advised independently.
4. If there is a legitimate debt only provide payment details to someone you have contacted via the official published phone number.
5. If someone is asking for payment via gift cards, hang up! If someone calls you regarding your computer or phone service and requests remote access, hang up! These will be scams.

We are all at risk so be careful and never assume that a call is legitimate.

Information for this article has been sourced from Scamwatch, a site developed by the Australian Competition and Consumer Commission (ACCC) with information and tips to avoid becoming a victim. For more information on ways you can protect yourself please review the following site.

https://www.scamwatch.gov.au/get-help/protect-yourself-from-scams

Sharon Pollock
Client Services Manager

Best Interest Duty

In this newsletter I'm going to dig a bit deeper into a phrase that we hear a lot in financial services – 'best interest duty'. This phrase, and its cousin, 'act in the client's best interest', has been heard a lot in the past year, particularly at the Royal Commission, where instances of not acting in the client's best interest were highlighted.

So, what is 'best interest duty'? You would think that three simple words would amount to a pretty simple concept? Well, sort of. 'Best interest duty', means what it says. That is, that in any interaction between a client and a financial adviser, the adviser must always act in the client's best interests. Pretty simple so far.

Best interest duty became law in 2013 when the Corporations Act 2001 was amended to include section 961B, which says "(1) The provider must act in the best interests of the client in relation to the advice." The next sub-section then goes on to list seven steps that the provider can use to satisfy the requirement. This is often called the 'safe harbour'.

Safe harbour is a legal term that means if certain conduct is followed, then the law has not been broken. I won't go into detail of the full components of the safe harbour here, but will look at just two aspects.

Part (c) of the safe harbour states "where it was reasonably apparent that information relating to the client's relevant circumstances was incomplete or inaccurate, made reasonable inquiries to obtain complete and accurate information;" This provision puts the onus on your adviser to ensure that the information that you have provided is complete and accurate. For example, if you have stated your annual cost of living expenses as $40,000 and you have two car loans, three children at private schools and a boat in the driveway, it would be 'reasonably apparent' to the adviser that your relevant circumstances were inaccurately stated as these items alone would cost more than $40,000. The adviser is then bound by law to make further inquiries to obtain complete and accurate information about your cost of living expenses.

Part (g) of the safe harbour clause is a catch-all that states "taken any other step that, at the time the advice is provided, would reasonably be regarded as being in the best interests of the client, given the client's relevant circumstances." As you can see, this part contains some pretty onerous provisions. 'Any other step' is very broad and the word 'reasonably' is open to interpretation. An example where this might be relevant is where a client comes to an adviser and wants to add a particular share to their portfolio. The adviser analyses the request and decides that this would not be in the client's best interest and advises the client accordingly. In other walks of life, customer service would dictate that the adviser provides the client with exactly what they have asked for. In financial services, the law requires that the adviser do the opposite to what the customer has asked for, if it is not in the client's best interest.

Finally, an advice provider must be able to show that all of the elements of the safe harbour have been met in relying on the safe harbour to be compliant. If you have a hankering to learn more about best interest duty, Australian Securities and Investments Commission (ASIC) Regulatory Guide 175 is a good start and of course the World Wide Web is awash with articles on best interest duty. Enjoy the reading!

John Phelan
Compliance Manager

Protection From Potential Financial Mistreatment

What I really enjoy about being an adviser is the opportunity to resolve client puzzles. Each situation is unique and the solutions are an opportunity to make a real difference to a family's life.

Recently, I was asked by a client how to protect their child with special needs from potential future financial mistreatment. This was an opportunity for me to dust off my knowledge of trusts and more specifically, special disability trusts.

The purpose of a special disability trust

A trust is a legal obligation that details how you want property or assets held for the benefit of a beneficiary administered and managed.

Special disability trusts are primarily established to assist succession planning by parents and family members, for the care and accommodation needs of a child or adult with a severe disability. The name "special disability trust" relates to the social security treatment of the trust, not the actual disability.

The legal requirements for setting up a special disability trust

The first step is to make sure that the special needs person qualifies for a special disability trust. They need to meet the definition of severe disability as detailed in the Social Security Act 1991. The individual will have to go through a process where they are interviewed and assessed by social security. Centrelink has a special division that makes an assessment regarding whether they meet the criteria under section 1209M of the Social Security Act.

The Social Security Act recognises that people with special needs work and positively contribute to our society. If the special needs person is working, the act states that a condition of a disability restricts them from working more than 7 hours a week for a wage that is at or above the relevant minimum wage.

The trust deed must comply with certain conditions, and incorporate compulsory clauses as defined in the model trust deed as laid out by the Department of Social Services.

Anyone except the special needs person or the settlor can be a trustee of a special disability trust. There are two types of trustees and they both must be Australian residents (must be assessed by the Department of Social Services).

1. Independent (corporate) trustee – does not have any relationship with the special needs individual and has to be a professional person or a lawyer.
2. Individual trustee – A minimum of two trustees are required to ensure the special needs individual's interests are protected.

The trust can either be activated while you are alive - this gives the special needs individual more independence or set up as part of a will - to protect the special needs individual.

The special disability trust can only have one beneficiary (the special needs individual) and the beneficiary can only have one trust. There are two main restrictions placed on the beneficiary, their living situation and gifting.

The Social Security Act stipulates that the beneficiary is not able to reside permanently outside of Australia - the reasonable primary care and needs for the beneficiary must be met in Australia. There is also a gifting concession available and the contribution made must be unconditional (you can't get it back), and without the expectation of receiving any payment or benefit in return (if gifted by you). The beneficiary is only able to give money that they received as an inheritance within 3 years of receipt into the trust. Also, a gifting concession, that does not impact any Centrelink benefits is available for the first $500,000 of gifts contributed to the trust.

The social security implications of a special disability trust

There is no limit to the dollar value of assets that can be held in a special disability trust, however, there is an asset test exemption (for Centrelink benefits) of up to $669,750 (indexed 1 July each year) available to the beneficiary. Another advantage is no income is assessed under the social security income test for the beneficiary. The special needs individual can also have their primary residence in the special disability trust, which is also exempt.

Centrelink has also added a limit of $11,750 to 'discretionary expenses' for beneficiaries to improve their level of health, wellbeing, recreation and independence.

Further information can be found at these sites:

https://www.dva.gov.au/factsheet-is163-special-disability-trust

https://www.dss.gov.au/our-responsibilities/disability-and-carers/publications-articles/model-trust-deed-for-special-disability-trusts

In conclusion, the aim of establishing a special disability trust is to provide protection and to ensure that those we love have a secure financial future.

Stephen Coniglione
Financial Adviser

APA Group takeover offer rejected by the Australian Government

Even though the Australian Competition and Consumer Commission (ACCC) didn't have a problem with the deal, the Treasurer, Josh Frydenberg, wasn't comfortable with CK Infrastructure (CKI) taking over one of our world class infrastructure companies. As a result of the treasurer's decision, APA's share price has fallen well below the takeover offer price of $11 per share. At the current levels, we are no longer happy to sell as this is a world class infrastructure company.

At this stage there are no other suiters that have come forward but in the event that another offer materialises, the offer will be assessed and further recommendations may be made.

Ian Maloney
Manager - Share Trading

Do You Know What You're Really Covered For?

If I had a dollar for every time someone told me, 'yes, I have insurance, it's in my super fund', I'd be one rich lady! Whilst I'm not disagreeing that you may indeed have cover, my problem lies with the quality of cover.

Industry and retail funds are required by law to offer default insurance within your superannuation account. However, there are no rules around the benefits they offer within these policies and what most people don't realise is they may not be covered at all.

Here's a few fun facts you should know about insurance held inside your super:

Policy indexation

Most policies within these funds decrease as you get older. They usually start tapering off at around age 40. This is usually the time when you need cover most because you have a mortgage to repay and kids to put through school. Policy indexation is important to ensure cover keeps inline with the time value of money.

Guaranteed renewability

Industry and retail fund policies are not guaranteed to renew. Most policies have a hidden clause which states that the cover can be cancelled at the decision of the trustees for any reason at any time. You could think you're fully protected, then the unthinkable happens and you find out you weren't protected.

Tax on benefits

Regardless of the superannuation fund, you will always pay tax on Total & Permanent Disablement (TPD) benefits. The implication of this means you may think you're going to receive a $500,000 benefit but what you actually receive will be far less.

Underwriting on claim

When you opened your superannuation account, you are offered default cover, meaning you never have to answer a long list of personal medical questions. You may not realise there are serious implications to not doing this. Say for instance you're diagnosed with diabetes at age 25. Then two years later you change superannuation providers and you're offered default cover within that fund. Fast forward to another two years and you've had to take an extended time off work due to complications of your diabetes. You try to claim on your income protection/salary continuance only to be denied the claim. This is because two years prior to you taking out this new policy, you had already been diagnosed and this is technically a "pre-existing condition" in the eyes of the claims assessor.

There are many more reasons why you shouldn't rely on default cover within your superannuation. To be certain you know what you're covered for, be sure to come and see us for a full insurance review. We'll prepare a detailed analysis of your current cover compared to other policies on the market you'll know exactly what you're covered for.

Amy Gill
Risk Adviser

Investment Update

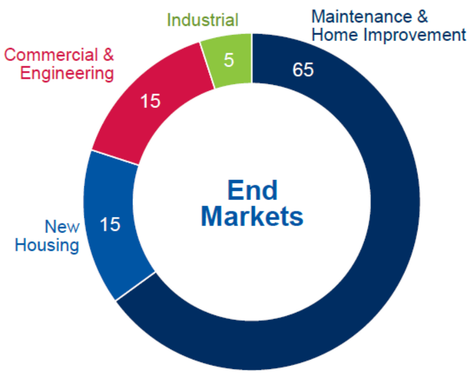
Dulux

We have been investing clients' money in Dulux for several years and the latest results announced in December once again demonstrates how consistent this company is:

- Revenue grew 3.3%
- Earnings Before Interest and Tax (EBIT) grew by 4.2%
- EBIT margins increased by 0.1% to 12.1%

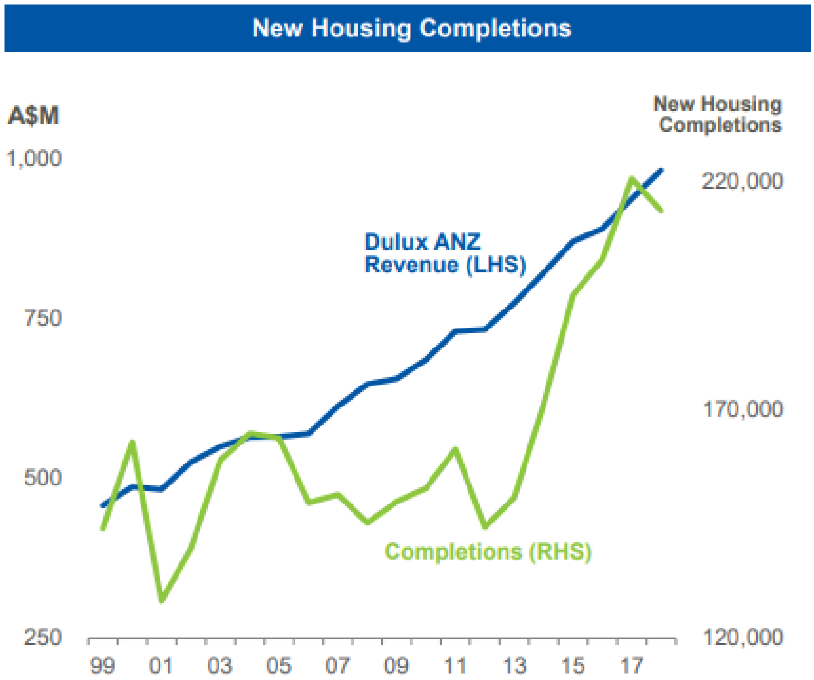
However, one of the questions that is most asked by clients is, ''How will this stock fair in the midst of a housing downturn?'' - An excellent point to raise about a paint, coatings and adhesives business.

Well, it is appropriate for us to first identify how exposed Dulux's revenue is to existing housing and new builds. Straight from the annual investor presentation, the pie chart below shows 65% of Dulux's revenues are tied to existing housing and 15% to new housing.

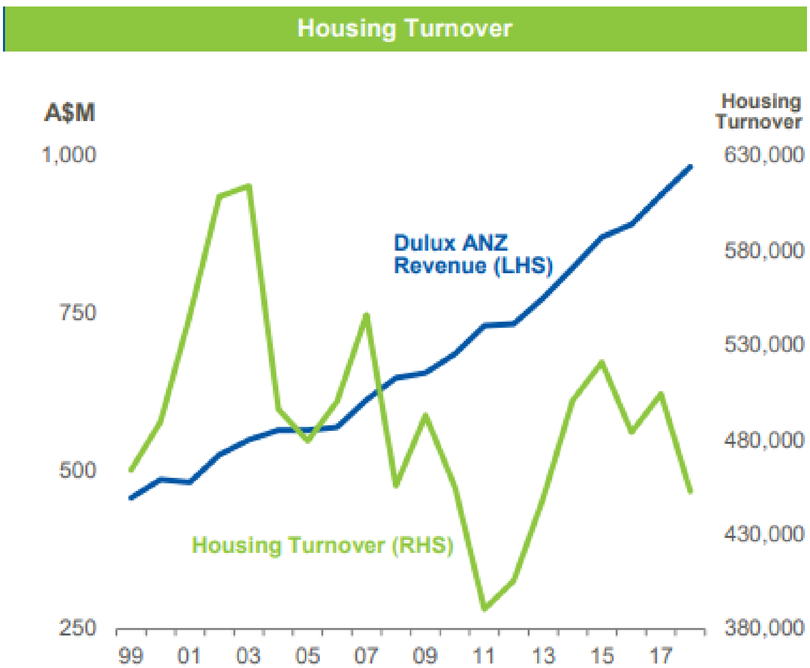


The figures above may seem like a housing downturn would be a catastrophe for shareholders but, there is more to it than that.

In Dulux's annual report, some interesting graphs illustrate very clearly that the number of houses that are bought and sold every year (housing turnover) and the number of new homes built have very little impact on Dulux's revenue and profit. Sounds surprising, but for the most part new homes are built with the developers' profit margins front and centre – sometimes a developer may skimp on quality to lower the construction costs. However, once these houses are sold and the new owners move in, the first thing they want to do is decorate the house. For most people their house is their most valuable asset and they want nothing but the best for it, inevitably Dulux is their preferred brand of paint.



Furthermore, the next graph plots revenue against housing turnover. The property boom led to an increase in housing sales that started in 2011 and while the boom has definitely fizzled out, revenue continues to climb.



Lastly, as another sweetener to allow investors to sleep at night, it is worth remembering that in Australia, there are approximately 10 million detached homes and 70% of those are over 20 years old. They need a paint job!

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