Switzer Super Report

Issue 125, 8 October 2012

Hands off!

I don't often give advice to political leaders, but I'm ready for a stoush if the Government makes a cash grab for super. I fill you in on why this is a possibility in today's note.

Also in the *Switzer Super Report*, we give our recommendation on what to do with Woolworths' new property trust. Plus, we have our weekly broker wrap of buys, holds and sells and our chart of the week, which has an updated position on gold. And we bring you up-to-speed with a new interpretation on transferring shares that could cause you to re-think your strategy. Have a great week!

Sincerely,

Peter Switzer

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Keep your hands off our super

by Peter Switzer

I often make suggestions to PMs and Treasurers, but I seldom give advice, but this time is different; I'm advising our top two leaders – keep your hands off super or else you will be decimated at the next election.

The dumbest thing Treasurer Wayne Swan can contemplate is slugging the trustees of self-managed super funds.

The problem

Currently the so-called 'world's greatest finance minister', Wayne Swan, has a number of problems. First, he made a promise to create a budget surplus by June 30 next year to show he is a great financial manager ahead of the next election expected in October.

His second issue is that the Australian economy is slowing down. In the March quarter, the economy was up by 4.4% from a year earlier, but this fell to 3.7% by the June quarter. You might be saying that these yearly changes are above the trend growth rate of 3.25%, but if you annualise the quarterly numbers, you'll get a better picture of what's going on.

The economy grew by 1.4% in the March quarter compared with the previous quarter, and when you multiply this number by four to get a picture of what that sort of growth would look like over the course of a year, you get 5.6%. Not bad. However, June brought quarterly growth of 0.6%, which is about 2.4% when annualised, showing growth more than halved in three months!

The big issue is that the Treasurer needs annual growth of 3.25% to make a surplus happen and so the Reserve Bank of Australia's (RBA) rate cut last week would have been a plus for Mr Swan's dreams, but it also underlines how the economy has slowed.

And this is why Treasury is looking for money and it's why SMSF trustees should be worried.

Why SMSFs?

These numbers show you why Labor is looking at SMSFs:

There are 10,000 SMSFs with $5 million or more in their fund. That means as a minimum, there would be $50 billion in those SMSFs. Meanwhile, there are 45,000 SMSFs with more than $2 million, but less than $5 million, and so let's say there's $90 billion there.

Adding it up, there's $140 billion – and remember, that's a minimum – that Treasury could be running its calculations on.

The big problem for the Government is that if it tries a 'super steal' to fix its budget hole, the Coalition will argue that the Government is targeting SMSFs with $2 million-plus now, but that those with $1 million and later, $500,000, will be next.

Of course, they would need a Mini-Budget to get their hands on the money before June 30 and maybe they wouldn't get the support of the independents on this one, especially with an election looming and a lot of economists, including me, saying a budget surplus is no longer necessary.

Big pressures

One other consideration needs to be highlighted to explain why the Government could be looking at penalising SMSFs; industry funds (which have a been a great success story) are still driven by ex-union heavies and they are worried that their best clients with big balances are leaving to start SMSFs.

Do you think the PM and Treasurer as well as the Super Minister, ex-union boss Bill Shorten, could be interested in this issue?

The bottom line

Historically, I try to maintain balance in my political commentary, but if Labor starts going after SMSFs, then I will be taking off the gloves and will give them the biggest stoush I've ever had with a government.

The SMSF trustees shouldn't have to pick up the tab for the stupid and unfunded policy decisions of a government trying to win friends and influence voters from their heartland, who in recent years have deserted them because of those dumb policy options.

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Our view on Woolworths' new property trust

by Paul Rickard

Woolworths shareholders are about to become unitholders in a new property trust – Shopping Centres Australasia Property (or SCA Property Group) – under a plan to spin-off and sell shares in its properties. Under the plan, shareholders will receive one unit in SCA for every five Woolworths (WOW) shares they own (that is, if you own 1,000 Woolworths shares, you will receive 200 units in the SCA Property Group).

SCA Property Group is being created via the transfer of 69 neighbourhood, sub-regional and freestanding shopping centres from Woolworths, with shareholders receiving an 'in-specie' distribution of units in the new listed property group. The proposal is subject to shareholder approval at the Woolworths annual general meeting (AGM) on 22 November.

SCA is separately seeking to raise around $425 million via an offer to the market and Woolworths shareholders.

Why is Woolworths creating the SCA Property Group?

Woolworths says its core business is retailing, and long-term real estate ownership is not considered to be part of that strategy. The creation of the trust will reduce the real estate held on its balance sheet by $1.27 billion, and generate net cash to Woolworths of around $850 million.

The distribution of SPA units provides Woolworths shareholders with the choice of whether they want to keep their new defensive property portfolio, sell the shares, or top up and increase their exposure.

Not stated of course is the fact that Woolworths has been trying to reduce its property portfolio for some time and following the global financial crisis, it hasn't been swamped with buyers. This proposal is an elegant (though expensive) way of solving part of that problem – the transaction will cost $63.9 million.

The SCA Property Group

The SCA Property Group will comprise 69 shopping centres – 55 in Australia and 14 in New Zealand. The portfolio has been valued at $1.4 billion, with 56 completed properties valued at $1.1 billion and 13 properties under development valued on a completed basis at $0.3 billion.

All centres are anchored by a Woolworths Group business as a tenant. Woolworths Group stores will account for 75% of the gross lettable area and 61% of SCA's gross income, and will have a weighted average lease expiry of 19.8 years. Woolworths is also providing SCA with a rental guarantee to cover vacant specialty tenancies for a period of two years.

Accompanying the unit distribution is an offer by SPA of 337 million new units to raise between $425-$506 million based on an indicative unit price of $1.26 to $1.50 for SPA. This compares with the unit net tangible assets (NTA) of $1.58.

On a forecast basis, the SPA Group is expected to distribute at a yield of between 6.9% and 8.3% for the first full financial year to June 2014, with a tax deferred component of around 35% to 40%. The details are as follows:

	Offer Price $1.26	Offer Price $1.50
Distribution Yield part 2013 (45% to 50% tax deferred)	9.4% pa	7.9% pa
Distribution Yield 2014 (35% to 40% tax deferred)	8.3% pa	6.9% pa

Shareholder implications

For Woolworths shareholders, the SCA units will be treated from a tax perspective as part return of capital (non assessable) and part payment of an assessable fully franked dividend. At a price of $1.40, the capital return will be 50.7% or 71 cents, and the fully franked dividend of 69 cents.

As shareholders are receiving one unit in SCA for every five WOW shares they own, the $0.71 capital return will reduce the cost base of each Woolworth's share by around $0.14. The dividend component is fully franked – so SMSFs will benefit to the extent of the excess imputation credits.

And with the SCA units, you will then have the choice to keep, sell or top up by potentially buying more units in the SCA offer described above. Unfortunately, many shareholders will be left with an unmarketable parcel in SCA (for example, if you own 1,000 WOW shares worth $29,700, you will own 200 SCA units worth just $280). SCA has said it will consider some form of small 'sale facility' to cater for these unitholders.

Our View on the SCA Offer

With the Woolworths Board unanimously recommending the transaction, it is a 'fait accompli' that the distribution and accompanying offer of SCA units will go ahead.

While the forecast distribution yield for the SCA Property Group is relatively attractive, it is difficult to see how the new manager can add substantial value to a portfolio of neighbourhood and sub-regional shopping centres. Sure, it has Woolworths on long-term leases, however it will need to generate "growth" income from the specialty stores that comprise the other 39% of the portfolio's income or by purchasing or developing new centres.

For SMSFs, the tax deferred component is of limited benefit to funds in accumulation, and of no use to funds in pension. This is one of the reasons we maintain an "underweight call" on the listed real estate trust sector.

The bottom line

It is a pass on subscribing for new units in the SCA offer, and probably like many Woolworths' shareholders, we will look to sell our annoyingly small holding. If you do wish to invest, the offer is due to open next Monday (15 October) and a product disclosure statement (PDS) is available at www.scapropertyoffer.com.au.

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Time to change my strategy on gold

by Lance Lai

In recent months, I've recommended investors take up gold at certain levels. Gold has risen 9% in under four months to be at around $1,773, however, I don't think this run is going to continue and I now recommend a different strategy.

In my previous notes on gold on 3 September and 14 of June 2012, I recommended investors enter gold at these three points:

1. 20% of your allocation at $1,616
2. 30% at $1,574
3. 30% at $1,688

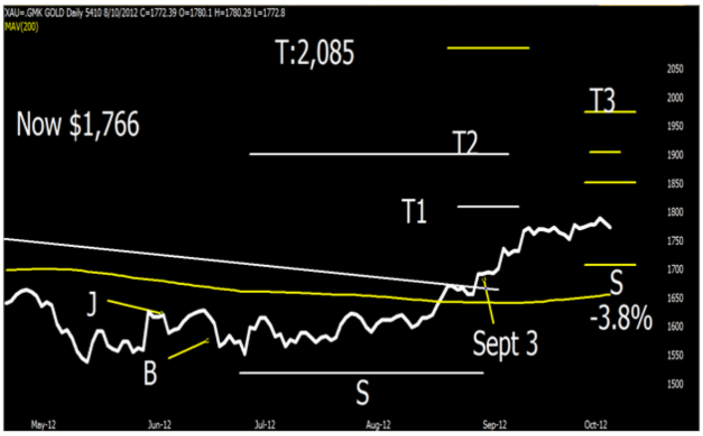
If followed, you would have been 80% filled in your gold allocation at an average price of $1,627.

For me, this is enough and **I recommend locking in profits right now**. For the purposes of this report, one could close out all positions (I declare that I have).

I expect Gold to come off now before resuming its upwards climb. Following a pull-back, you could look to re-enter gold at these support levels:

1. $1,708 buy back 30% of your allocation
2. $1,678 buy back another 30% if it gets there
3. $1,655, buy another 30% if it gets there

Gold $1,773 – Retracement in the Wind. Ultimate Target still $2,085, 17.6% Higher!



Source: Accountancy Invest

What I like about the chart?

1) The 200-day moving average is pointing up.

2) The chart is on track for a long-term target of $2,085.

3) This looks like and feels like the run-up we had from September 2009, and then April 2010. In each case, multiple upside targets were set, and all reached and exceeded.

4) Retracements to $1,708 (3.8% lower), $1,678 (5.7% lower) or even $1,655 (7.1% lower) to the 200-day moving average (yellow line) are possible without doing damage to the upside target.

5) A solid base has been confirmed as created now since my article of 14 June 2012 and then 3 September 2012. A solid bottom has been established from 16 May to 30 August.

6) As in my last article, gold has broken out of resistance of $1,660.

7) Last time I wrote, "Other indicators starting to show we are on the cusp of a new uptrend." Now I

confirm, the uptrend has begun, it is preferable, but not absolutely necessary to see a nice retracement now to consolidate that uptrend.

8) Target 1, of $1,808 has been discarded as not necessary before retracement, now looking for higher T1 at $1,851, the first yellow line on the right of the chart.

9) Target 2, of $1,901 has not been altered.

10) Target 3, of $1,974 has been newly projected.

11) My ultimate target of $2,085 has also not been altered.

What I don't like or what worries me?

1) Nothing.

Please note that my views are not for the long term. My method results in views expressed that relate to an outlook that lasts weeks or at most months. For example, my view on Shanghai's Index has for now been met and completed since 22 March 2012, 11 days later. Currently regards Shanghai, I am in a cautionary observant position. Your utilisation of this information needs to take into account the time frame I set. The stocks recommended as "Steady as She Goes" may be held for the longer term, which for me means months.

The broker wrap: RMD, MQA and CDD

by Rudi Filapek-Vandyck

Changes to stockbroker ratings in the past week

Code	Company	Old Rating	New Rating	Broker
CDD	Cardno Limited	Neutral	Buy	RBS Australia
DTL	Data#3 Limited	Neutral	Buy	RBS Australia
DXS	Dexus Property Group	Sell	Neutral	Deutsche Bank
GPT	GPT	Sell	Neutral	Credit Suisse
MQA	Macquarie Atlas Roads	Neutral	Buy	Macquarie
CPU	Computershare	Buy	Neutral	Deutsche Bank
DML	Discovery Metals	Buy	Neutral	RBS Australia
FKP	FKP Property Group	Neutral	Sell	BA-Merrill Lynch
LYC	Lynas Corporation	Buy	Neutral	UBS
MQA	Macquarie Atlas Roads	Buy	Neutral	RBS Australia
RMD	Resmed Inc	Buy	Neutral	UBS
SRX	Sirtex Medical Limited	Buy	Neutral	UBS

Source: FNArena

A total of seven stocks were downgraded last week, while five enjoyed upgrades. Total Buy ratings in the FNArena database now stand at 44.00% versus 44.76% the week prior.

Upgrades

We'll lead off this week's proceedings with **Cardno (CDD**), which was upgraded to Buy by RBS. The broker noted that the share price has dropped 18% since peaking in August after releasing its full-year result, with current levels now seen offering quite a good buying opportunity. The stock enjoys two Buys and a Neutral in the FNArena Database. Macquarie is the broker sitting on Neutral, saying back in mid-August that shares were too dear. Well, according to RBS, they aren't any more.

Next on our upgrade list is Queensland-based IT services company **Data#3 (DTL)**. Again, the benefactor is RBS, with the broker lifting its call to Buy after noting the share price has dropped nearly 20% in the past two months. The broker thinks the market is being a bit too negative about the company's outlook and not paying enough attention to the 7.2% fully franked yield. The stock is only thinly covered by Australian major brokers, enjoying just one straight Buy in the FNArena database.

Dexus Property (DXS) was lifted to Hold by Deutsche Bank, the broker thinking a rationalisation in the US market is imminent and Dexus will be a definite beneficiary as it looks to dispose of its US portfolio. The stock rates a flat Neutral sentiment in the FNArena database, with one Buy, five Holds and one Sell all nicely balanced. Macquarie is the broker holding the Sell and it does so on valuation grounds, otherwise seeing a chance of increasing earnings opportunities in full-year 2013.

GPT (GPT) was boosted to Hold by Credit Suisse, the broker seeing an increased level of value following a minor sell-down in its shares. The stock is just on the south side of being Neutrally regarded, with one Buy beat by two Sells and four Holds. Even the brokers on Sell see reasonable earnings prospects, with valuation the primary concern of note among brokers our database.

Last in our list of upgrades is **Macquarie Atlas Roads (MQA)**, which was boosted to Buy by analysts from former parent Macquarie. The broker made the move on a rolling forward of its valuation model and a share price drop last week after the announcement of some unfavourable tax deduction rulings by the French Government.

Downgrades

The same news also leads off the downgrade section of out report, as while analysts at Macquarie did little but cut 2012-14 dividend forecasts by 9-12%, RBS downgraded its recommendation on MQA to Hold, also cutting its valuation and earnings/distribution forecasts. The stock is otherwise positively regarded by Australian major brokers, with three Buys and three Holds recorded in the FNArena database.

Investor services and market technology company, **Computershare (CPU)** was cut to Hold by Deutsche Bank, with the broker seeing only limited value on a near-term basis. Earnings per share (EPS) forecasts and the price target were cut and the broker notes that an improvement in its view is now dependent upon improvement in the macro economic outlook and a subsequent increase in corporate activity. The stock remains positively regarded in the FNArena database, boasting five Buys and three Holds.

Discovery Metals (DML) was cut to Hold by RBS, with the broker noting the company is now in play and not trading on fundamentals post a takeover approach from Chinese private equity at $1.70 per share. The broker went on to recommend risk-averse investors to look at trimming their holdings into price strength nearer to $1.70. The stock rates a flat neutral in the FNArena Database, with one Buy, one Sell, one Hold and corporate advisor UBS moving to Restricted (prior Hold) post the news.

FKP Property (FKP) was cut to Sell by BA-Merrill Lynch on the view management's cash before profits push to address an unsustainable build up of unsold inventory will take a bite out of margins and thus short-term profitability. Concerns about balance sheet strength and future business direction were also noted. The stock has slipped to being negatively regarded in the FNArena Database, with four Holds and now one Sell.

UBS also took the knife to **Lynas Corp (LYC)**, downgrading its call to Hold on a less than rosy outlook for the rare earths market and concerns about LAMP commissioning risks given the social, political and legal argy bargy going on in Indonesia. Following the change, the stock enjoys two Buys and three Holds in the FNArena Database.

UBS also cut its recommendation to Hold on **ResMed (RMD)** after a marking to market for foreign exchange assumptions. Forecasts and the price target were also lowered. Despite the downgrade, the stock remains fairly positively regarded on the FNArena Database, boasting four Buys and four Holds.

Lastly, **Sirtex Medical (SRX)** was downgraded to Hold by UBS, the one broker maintaining a recommendation in the FNArena Database. UBS reported that while first quarter volumes were strong and growth was impressive, unfavourable foreign exchange conditions took off a lot of the shine. The broker also notes the shares have run pretty hard this year – 125% to be exact – supporting the inclination to drop the recommendation.

Changes to earnings forecasts (EF) in cents per share

Code	Company	Previous EF	New EF	% Change	No. of brokers
ORI	Orica	182.588	213.075	16.70%	7
TNE	Technology One	7.175	8.225	14.63%	4
IPL	Incitec Pivot	25.263	28.925	14.50%	8
QAN	Qantas	14.388	15.625	8.60%	7
DLX	Dulux	22.071	23.571	6.80%	7
NAB	National Australia Bank	253	261.275	3.27%	8
ANZ	ANZ Bank	219.725	226.563	3.11%	8
WBC	Westpac	205.3	211.088	2.82%	8
CTX	Caltex	136.217	137.883	1.22%	6
STO	Santos	60.938	61.213	0.45%	8
GNC	Graincorp	103.543	79.814	-22.92%	7
MQA	Macquarie Atlas	2.517	2.033	-19.23%	6
GBG	Gindalbie Metals	3.617	3.4	-6.00%	6
CSR	CSR	9.163	8.8	-3.96%	8
EVN	Evolution Mining	18.475	17.82	-3.55%	5
SFR	Sandfire Resources	133	129.214	-2.85%	7
CPU	Computershare	53.354	52.061	-2.42%	8
NCM	Newcrest Mining	141.663	138.663	-2.12%	8
BTT	BT Investment Management	16.18	15.85	-2.04%	4
RRL	Regis Resources	56.286	55.157	-2.01%	7

Source: FNArena

Note: FNArena monitors eight leading stockbrokers on a daily basis. The eight experts are: BA-Merrill Lynch, Citi, Credit Suisse, Deutsche Bank, JP Morgan, Macquarie, RBS and UBS.

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New guidelines for share transfers

by Tony Negline

If you‘re planning to transfer a large number of shares into your self-managed super fund, you may want to tread carefully because a new interpretative decision has shed light on how the Australian Tax Office (ATO) will treat any amounts that exceed your contributions cap.

The ATO interpretative decision (ID 2012/79) states that separate share transfers, even if they occur on the same day, will be counted as separate contributions and this is important because in a situation where your fund breaches its contributions limit, it could mean the difference with being charged excess contributions tax or receiving a refund of the excess amount.

It can often be difficult to know the precise value of a share transfer into super, officially known as an ‘in specie’ contribution, because you won’t know the exact day the transfer may occur and hence the value of those shares. If you are making large and numerous transfers that will, in total, scrape close to the $150,000 non-concessional contributions cap, you run the risk of breaching this limit.

In the past, many SMSFs assumed they could receive a refund of any excess amount, avoiding the tax penalty, but it now looks like this isn’t the case.

Adding up the rules

We’re all familiar with the rule that says SMSFs will be hit with a tax penalty if they break their contributions caps, so your fund shouldn’t accept contributions above the $150,000 non-concessional cap.

There’s another regulation that says if an SMSF receives an amount above the non-concessional cap, then the trustee must refund that excess amount within 30 days of becoming aware that the fund has broken the cap. So far, so good.

There’s an earlier interpretative decision (ID 2007/225) in which the ATO says your SMSF can’t aggregate contributions, either within the super fund or across other super funds.

If we take this interpretation together with the two regulations, the only conclusion we can make is that your SMSF can only refund excess non-concessional contributions when you contribute above the cap in a single contribution.

What’s a single contribution?

The latest interpretation (ID 2012/79), which was released in September, clarifies the ATO’s position on what constitutes a single contribution. The ATO says a single contribution isn’t made by transferring individual parcels of shares on the same day, but rather, each transfer is considered separate. Potentially, this means that no portion of a contribution that causes your fund to breach its non-concessional contribution cap can be returned to you if the contributed amount itself is less than $150,000, therefore the excess contributions will be hit with a penalty tax of 46.5%.

Example

The ATO provides the following example:

A person aged over 65 contributes the following parcels of shares to their SMSF in a single day:

- 2,000 shares in ABC Ltd; total market value $42,000
- 5,500 shares in DEF Ltd; total market value $78,000
- 3,200 shares in XYZ Ltd; total market value $35,000

The total value of these contributions equals $155,000 – breaching the $150,000 non-concessional contributions cap by $5,000. However, as you can see, none of these contributions are above that cap when considered individually.

Since the breach didn't occur in a single transaction, but as a result of multiple transactions, the excess amount can't be refunded and a non-concessional contributions tax assessment will be issued. The end result is that the excess $5,000 will be subject to 46.5% tax equalling $2,325.

The new interpretation says this principle will apply regardless of whether shares are in the same company or different companies (for example, suppose you have shares in the same company, but some are broker sponsored and some are issuer sponsored, causing the transactions to occur separately).

This means your super fund will need to report to the ATO separate contributions made of the same day if the contributions involve different parcels of shares.

If an excess non-concessional contributions tax assessment is issued, there doesn't appear to be many avenues for you to appeal this assessment.

Knowing the exact day your shares will be transferred may be tricky. You super fund trustee can deem that a contribution of shares has been made on the day you give the trustee an Off Market Share Transfer Form in registrable form. This date will apply as long as your administrator correctly records this date. If it's not kept, then the transaction date will be the date that the share registry is officially changed.

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The Week Ahead

Australia
Tuesday 9 October: Speech by RBA Deputy Governor Lowe
Tuesday 9 October: NAB Business survey (September)
Tuesday 9 October: Tourist arrivals (August)
Wednesday 10 October: Consumer sentiment (October)
Thursday 11 October: Employment and unemployment rate (September)
Thursday 11 October: Speech by RBA's Luci Ellis, Head of Financial Stability

Overseas
Monday 8 October: China services gauge (September)
Wednesday 10 October: US Beige Book
Wednesday 10 October: US Wholesale sales (August)
Thursday 11 October: US International trade (August)
Friday 12 October: US Producer prices (September)
Friday 12 October: US Consumer sentiment (October)

Did you know?

Shares in QR National (QRN) have jumped more than 5% on news the Queensland government plans to sell a $1.5 billion stake in the railway operator.

The government says the deal involves the sale of $1 billion in shares via a selective buyback to QR National and a $500 million placement to a small number of cornerstone investors.

The sell-off will reduce the government’s stake in the rail freight operator from 33.9% to 16%.

Treasurer Tim Nicholls says the price the government achieves for the sale will see more funds available to reduce debt.