Switzer Super Report

Issue 347, 11 December 2014

Jingle bells

It's starting to look a lot like Christmas, and for your portfolio stocking today we've got a bunch of ideas around companies that will do well next year.

Geoff Wilson outlines his best picks for 2015 as Tony Featherstone provides 10 steps for making money out of IPOs. Sometimes the better ideas are after the float itself.

Also in the *Switzer Super Report,* Charlie talks about his best idea all year. Airlines might not be a favourite of fellow *Switzer Super Report* expert Paul Rickard, but Qantas has certainly delivered for Charlie.

Tony Negline looks at all the regulation changes for next year and in *Buy, Sell, Hold – what the brokers say,* CBA and Qantas get upgrades.

Sincerely,

Peter Switzer

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My small cap picks for 2015 – finding growth

by Geoff Wilson

Key points

- *In the absence of strong economic growth, look for stocks that have their own growth drivers.*
- *IPH Limited, better known as Spruson & Ferguson, listed on the ASX in November and has been a great performer.*
- *Slater & Gordon could also see some upside from the weaker Australian dollar.*

I expect the Australian equity market to be lower at the end of 2015 than at the start. My guess is that it will close the year down about 5%. Take this with a pinch of salt as always with the stock market, because – quoting from Ellie Goulding's pop lyrics – "anything could happen".

My expectation of slow Australian economic growth and inflated valuations due to excess global liquidity lies at the core of this prediction. In the last six years, a significant factor that has driven global equity markets has been the excessive liquidity injected in the system by world monetary authorities. Even though the US has halted its QE (Quantitative Easing) policy, excess liquidity is still being pumped into the system via Japan and Europe. My main concern is what will happen to equity markets when the easy money policy finishes. Given the high valuations that have resulted from the excessive global liquidity, I believe world equity markets are vulnerable.

Over the past few years, corporate Australia has significantly reduced its costs in an effort to boost profitability. Lower interest rates have not yet led to a pick-up in general economic activity, as shown by the recent release of third quarter domestic GDP. The growth figures released at the start of the month came in at 0.3%, well below expectations of 0.7% and down from 0.5% in the previous quarter. We are expecting that interest rates will be cut in the first half of calendar year 2015.

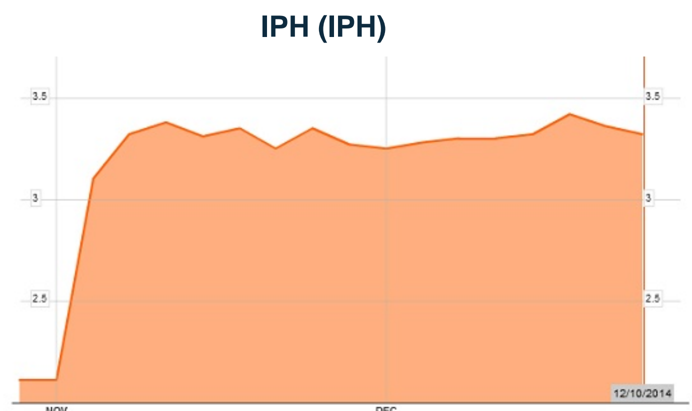
When the broader economy eventually delivers stronger growth from lower interest rates, the impact on corporate profitability is likely to be significant. Simply put, revenue growth of 5% would lead to a 25% increase in profitability for any company that can maintain costs with a 20% profit margin. The key remains the ability to predict when this will happen.

In the absence of strong economic growth in the near future, we look for stock picks that have their own growth drivers.

The following two stocks demonstrate this potential for growth.

Intellectual property services firm, **IPH Limited (ASX: IPH)**, better known as Spruson & Ferguson, listed on the ASX in November and has been a great performer. This company is one of the better quality IPOs we have seen in recent years with highly predictable revenue streams and strong cash flows emanating from its capital light structure. We like the longer-term fundamentals of IPH and think that it is well placed to grow through acquisitions in the coming years.

IPH (IPH)



Source: Bloomberg, 11 December 2014

Slater & Gordon (ASX: SGH) is based in Australia and the UK. The law firm specialises in insurance litigation, commercial and family law. Over the past two years, its share price has increased from $2.00 to $6.00, driven by strong earnings growth, while successfully expanding overseas. We are forecasting 15% annual growth over the next two years, as the law firm continues to grow organically and via acquisitions. With 50% of its earnings this financial year forecast to come from its UK-based operations, we expect Slater & Gordon to also see some upside from the weaker Australian dollar.

Slater & Gordon (SGH)

Source: Yahoo!7 Finance, 11 December 2014

I also like to look at companies in the listed investment company sector trading at a discount to NTA (Net Tangible Assets). **Hunter Hall Global Value (ASX: HHV)** fits the bill. At the time of writing, it is trading at a 10% discount to its asset value. It has two main drivers of growth. First, it is exposed to international stocks, with 52% of its assets listed outside of Australia, where we see stronger drivers of economic growth in the main. Second, its largest holding, medical device group **Sirtex (ASX: SRX)** is currently undergoing trials for its major product,

SIR-Sphere, to be used at an earlier stage of liver cancer upon diagnosis, with results expected mid-2015. This could provide a strong fillip for the shares, were the trials to come out with a positive result.

Hunter Hall Global Value (HHV)

Source: Yahoo!7 Finance, 11 December 2014

Sirtex (SRX)

Source: Yahoo!7 Finance, 11 December 2014

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Qantas delivers

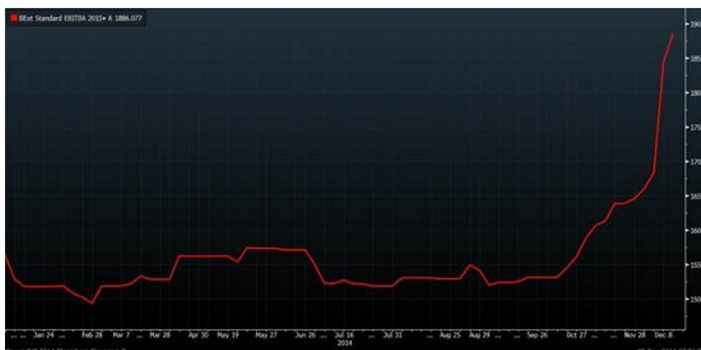
by Charlie Aitken

Believe it or not, Qantas (QAN) has been my single best returning idea of the year, 140% and still climbing. Unfortunately, not many people internally or externally thought that would be the case and very few domestic investors have benefitted from the QAN re-rating.

Airlines are trading stocks, and for the first time in a decade, everything is going right for QAN. On that basis, rather than taking trading profits, I am going to let this winner run and UPGRADE my price target to $3.00 from my long-held $2.00 price target (set when QAN was 97c).

While most of the market was over-analysing the Murray Report earlier this week, Qantas snuck in its first profit upgrade in living memory. The result was a 14% share price gain on the day.

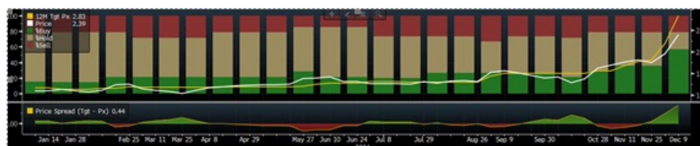
I feel this is the infancy of an earnings UPGRADE cycle from QAN and that is why I am sticking with the stock despite my original price target being exceeded. Below is the FY15 consensus EBITDA forecast for QAN on Tuesday. It is approaching the $2 billion forecast I made back in May.



The Aussie dollar and oil price fall has happened faster than expected, the domestic capacity war has ceased and airfares are rising, while the oil price fall is reducing the structural cost advantage of the subsidised Middle Eastern airlines. This is all good news for Qantas.

Globally, airline equities are being re-rated and Qantas is going up with them.

Qantas consensus earnings are being revised up and unsurprisingly the analysts are chasing the share price with recommendations and price targets. This becomes somewhat self-fulfilling now as momentum funds enter the QAN register.



Click here to view larger image

I am simply going to reiterate my updated "trading buy" thesis on QAN from 2 September when QAN was $1.45. The two big macro events since then are the AUD (-11%) and Oil price (-35%) collapse. That is the key reason for my price target upgrade to $3.00.

Let winners run…

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10 things you must know about IPOs to make money

by Tony Featherstone

Key points

- *Don't give up on an IPO just because you miss out on an allocation. Try buying it in the aftermarket.*
- *Find out whether sellers still have "skin in the game", or if they making a quick dash for the exits via an IPO*
- *Like any share investment, it pays to examine management and the board and basic metrics like valuation.*

Having written about hundreds of floats over the years, I have come across many terrific companies that have used the IPO market for its true purpose: to raise capital to grow faster, not as a quick exit for vendors.

Of course there are reasons to avoid IPOs, particularly the ones which are purely money making ventures, but generalising about the IPO market, or any sector for that matter, is dumb.

Every company must be treated on its merits. For example, fund managers who moaned about private-equity vended floats after the disappointing Myer Holdings float in 2009 and Collins Foods float in 2011 missed stellar private-equity IPOs such as In Vitro Fertilisation provider Virtus Health.

Another IPO benefit, especially in this market, is portfolio diversity. A feature of 2014's record-breaking IPO market is the emergence of companies from new sectors or those poorly represented on ASX: healthcare, education, software and service companies are examples.

Every now and then, a different offering comes along:

Genworth Mortgage Insurance Australia provided the first specialist exposure to mortgage origination; IPH Ltd gave the first exposure to intellectual property law; and iSentia Group to media-monitoring software. Each added different industry exposure to portfolios and soared after listing.

Also, successful IPO investing can boost returns for self managed superannuation funds and other long-term investors, improve portfolio diversification, and give DIY investors great satisfaction from backing high-growth companies at the next stage of the growth journey.

But there are plenty of tricks and traps and other IPO traits that rarely get covered in mainstream commentary. Here are 10 IPO considerations for retail investors:

1. Know the odds

Cadence Capital founder Karl Siegling says one in every 10 IPOs are worthy investments. Assuming 80 IPOs in a good year, investors will have eight floats on their radar, but perhaps only get their desired stock allocation in two or three. Getting stock in the best floats is beyond most retail investors, especially those who do not have a relationship with big investment banks.

2. Know the IPO cycle

Good and bad companies can be found in all parts of the IPO cycle. As a rule of thumb, better-quality, better-priced floats typically come to market earlier in the IPO cycle, which began in earnest last year. Professional investors usually dominate the early part of the cycle: nimble private-equity firms vending assets to fund managers. Retail investors are often harder to find in the early stages of an IPO market recovery.

Lower-quality, more aggressively priced IPOs typically emerge in the later stages of a bull market, when some corporate advisers will "float a cork" if it means advisory fees. By then, retail investors are back in the IPO market in force and, sadly, loading up on too many bad ones.

The cycle is not always clear-cut, but it pays to think about broader IPO trends. This cycle looks like it is about halfway: retail investors are starting to return to the IPO market, largely because of the Medibank Private IPO and the success of the larger IPOs such as Healthscope.

But IPO "fatigue" is emerging. More floats were abandoned, repriced or delayed in the fourth quarter because of the sheer rush of float activity. The best of the IPO market was probably in 2013 and 2014, although there will always be opportunities for value hunters.

3. IPO or aftermarket?

Too many investors give up on IPOs when they cannot get stock, even though the best opportunities are often in the aftermarket, six to 12 months after the company lists.

By then, the IPO has more history as a listed company, greater compliance with ASX Listing Rules, and time under the market's gaze. Investors can better judge whether the prospectus was fact or fiction and if the company is doing what it said it would. The best floats rally long after listing; giving up some early price gains and reducing risk, by buying in the aftermarket, often makes sense.

4. The debut

In years past, investors expected the mandatory 10% "stag" on debut, as the vendor underpriced the stock to leave something on the table for others. These days, hedge funds and high-frequency traders are creating different IPO dynamics.

There is talk of US hedge funds dumping IPO stock on debut if it drops below the issue price and momentum traders selling if the early share-price trend is down. There seems to be a lot more turnover in IPOs on debut as traders get in and out, and then a quieter aftermarket in some floats.

The upshot is good IPOs can be dumped on debut for no other reason than the price quickly breaching some technical level determined on an offshore computer program. That creates opportunities for patient capital to move in when short-term owners have left the register.

5. IPO or listed peer?

Investors can put all their focus into an IPO, overlook its nearest listed peer, and miss opportunities. For example, those who bought Steadfast Group might have overlooked Austbrokers Holdings, a more established, successful listed company. Those who clamoured for Healthscope might have paid less attention to Ramsay Health Care.

Always compare an IPO with its nearest listed peer – in most cases it should trade at a discount, although in this market many IPOs get away on Price/Earnings multiples similar to those of their nearest listed rivals, or in some cases even higher.

Moreover, watch how the listed peer trades in the lead-up to its rival's IPO. Fund managers that have to be fully invested in equities will sometimes take profits in an established company to free up portfolio funds to invest in the IPO. The IPO's listed rival could be the better investment.

6. Know who is selling

The single most important piece of information in any float: who is selling, why, and what are IPO funds being used for? Do the vendors still have "skin in the game" or are they making a quick dash for the exits, via an IPO? How aligned are the vendors with new shareholders after listing? Are IPO funds being reinvested in the business or mostly going back to the vendors?

After a few private-equity IPO fiascos (Myer, Collins Food etc), the market generally required vendors to hold more stock after listing, and sell down less through the float. That cuts both ways: the vendor has more to lose, but equally more stock to sell at some point, as is the case with several floats from 2013 where private equity still has a big stake that has to be sold.

Billions of dollars of "block trades" will need to be absorbed in 2015 as private equity in floats such as Nine Entertainment Co. Holdings look to exit.

7. Know who is buying

Waiting to see who bought into the IPO is another reason why it often pays to buy in the aftermarket. Examine the top 20 shareholders after listing; the better-performing funds, especially specialist small-fund investors, often get stock in better-quality IPOs as vendors try to build a strong share register of long-term institutional capital. Or there might be prominent cornerstone investors who get access to better deals.

It's not foolproof, of course. But investing in an IPO that has high-calibre institutional investors on its share register means there has been serious due diligence and that there is a base of investors that will subscribe to future equity capital raisings if the company performs.

8. People

Like any share investment, it pays to examine management and the board. Don't fall for the glossy bios in the prospectus: nothing tells you more about the executive team's calibre and ethics than the capital structure. Companies with excessive options issuance and easier hurdles for options to vest (usually based on the flimsy metric of share-price target) provide clues that the management and board are potentially gouging investors.

Challenging performance targets for executives based on profitability measures rather than share-price targets are a good sign. So is a board with a high proportion of independent directors who are there for their skills rather than their profile, and capable of holding management to account, rather than being captured by it.

9. Future share issuance

Study the capital structure carefully to understand how many shares could be issued if all options or performance shares are granted. Shareholdings can be badly diluted if a wall of new share issuance emerges a year or two after listing, which weighs on return on equity.

With smaller floats, pay particular attention to restricted securities that ASX deems cannot be sold until a certain time has elapsed (the escrow period).

Escrow dates, usually a year or two after listing, can be accompanied by a wave of selling as original investors are allowed to sell their shares. That's fine if there is sufficient buying to absorb the selling, but too many early investors heading for the exit at the same time can crunch the share price.

Voluntary escrowing of shares, sometimes by company founders, cornerstone investors or directors, is usually a good sign. It shows the company's backers are willing to hold their shares longer than they have to, thus better aligning their interests with new shareholders.

10. Usual rules apply

Focus on IPOs in faster-growing, attractive industries: healthcare, education, software and service floats have been popular this year because they have the potential to outperform in a weakening economy. Choose companies with a clear, sustainable competitive advantage or "economic moat" that makes it harder for rivals to compete against.

Favour IPOs that have a strong business model, are profitable, have potential for a high return on equity (above 15%), strong cash-flow growth and low debt. Seek small-cap companies with, or potential to have, a global footprint, as their growth prospects in a limited Australian market can be quickly exhausted.

On valuation, assess how their forecast PE compares with similar listed peers here or overseas. In theory, the IPO should trade at a reasonable discount to larger, more established listed peers.

Top ten IPOS

These IPOs caught my eye in 2014. Several have rallied sharply since listing and look fully valued, but are worth considering on any share-price weakness or broader market sell-off. Others make the list on

valuation grounds after post-listing share-price weakness.

- Genworth Mortgage Insurance Australia
- Intellectual property lawyer IPH Ltd
- Media-monitoring technology provider iSentia Group
- Labour hire firm Ashley Services Group
- Monash IVF Group
- Intueri Education Group
- Car-parts distributor Burson Group
- Japara Healthcare
- Beacon Lighting Group
- Dental provider Pacific Smiles Group

Tony Featherstone is a former managing editor of BRW and Shares magazines. All prices and analysis at December 10, 2014

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Buy, Sell, Hold – what the brokers say

by Staff Reporter

The banks got an overhaul this week from the brokers following the release of David Murray's Financial System Inquiry report. However their opinions were quite different with Credit Suisse believing it would be the regionals that would be the winners from the report and Macquarie believing the opposite.

Credit Suisse upgraded Bendigo and Adelaide Bank (BEN) to Outperform from Neutral. Following the Murray Financial System Inquiry Credit Suisse considers the regional banks are the winners, with a clearer path to advanced accreditation, greater regulatory capital neutrality and a margin and profitability opportunity to follow the majors on product re-pricing. (see downgrade)

Credit Suisse upgraded Commonwealth Bank (CBA) to Neutral from Underperform. Despite its overall view on the big banks, Credit Suisse believes CBA has an advantage in organic capital generation from its franchise. Credit Suisse expects some form of share issuance; DRP or placement will be forthcoming.

Morgan Stanley upgraded Qantas to Overweight from Equal-weight. Morgan Stanley considers Qantas has shown capacity discipline over the last six months. The broker concedes, with yield recovery and fuel upside, it may have underestimated the company's rebound potential. With few foreseeable hurdles over the near term, the broker moved to Overweight from Equal-weight, retaining an attractive sector view.

In the not-so-good books

Credit Suisse downgraded ANZ to Neutral from Outperform. Following the Murray financial system review Credit Suisse considers the major banks are the immediate losers. ANZ will need to raise equity to address what the broker suspects is a substantial tier 1 capital requirement. Credit Suisse remains supportive of the bank's business strategy and would look to review the rating if ANZ were to quickly address its capital position.

Macquarie downgraded Bank of Queensland to Underperform from Neutral and Bendigo and Adelaide Bank to Neutral from Outperform. Macquarie believes, contrary to Credit Suisse, that the regional banks and business banks appear to be the losers in the Murray Financial System Inquiry. Capital targets are in the same quartile measure as the major banks and this is viewed as a constraint. In Macquarie's analysis, the regional banks would need to raise $300-800 million, diluting by 9-12%.

Credit Suisse downgraded Coca Cola Amatil to Underperform from Neutral. The company provided a subdued trading update, prompting Credit Suisse to nudge its forecasts to the lower end of guidance. Australia is yet to realise improvements in the company's grocery accounts while Indonesian profitability is being affected by competition and rising costs.

Macquarie downgraded Myer Holdings (MYR) to Underperform from Outperform. Sephora, a large, global, vertically integrated player with a strong brand, low costs and a well-developed online offering has just opened a store in Pitt St Mall, right between the Myer and David Jones' Sydney CBD flagship stores. Cosmetics are critical to Myer's comparable sales numbers, particularly at the Sydney CBD store, the broker notes. Sephora's entry will "comprehensively" impact, the broker warns.

The above was compiled from reports on FNArena, which tabulates the views of eight major Australian and international stock brokers: BA-Merrill Lynch, CIMB, Citi, Credit Suisse, Deutsche Bank, JP Morgan, Macquarie and UBS.

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My SMSF - successful transition, strong returns

by My SMSF

Just over 12 months ago, in September 2013, we spoke to head of policy, technical and educational services at AMP SMSF, Peter Burgess, for a *My SMSF* just as he was transitioning from a small Australian Prudential Regulation Authority (APRA) fund into a self managed superannuation fund.

We caught up with Peter recently to find out how the transition went and what the whole experience taught him about SMSFs.

How has the switch worked out for you?

It has worked out well for me. Even though it was a relatively unusual transaction (i.e. converting from a small APRA fund to an SMSF), the conversion went pretty smoothly. For me the decision to convert my fund to SMSF was mainly driven by cost and a desire to have more control over corporate actions. I really enjoy the interaction I can now have with my advisers around things like corporate actions for example.

How has it performed?

It has been pretty strong. I've got a fair weighting to Australian equities so obviously it goes up and down with movements in the ASX but its been pretty good. It has outperformed the market since I made the transition.

Have you changed your investment strategy at all?

No. As a small APRA fund, I already had an investment strategy in place for my fund. As my circumstances had not materially changed since the strategy was first put in place, my adviser and I did not see any need to change the investment strategy when my fund was converted to an SMSF.

What are some of your holdings?

I have some blue-chip stocks, like BHP, the big four banks, Telstra, Coca Cola Amatil, AGL in there, but also some Sonic Health Care, Ansell and Platinum Asset Management.

Did you use a corporate or individual trustee structure?

I used a corporate trustee. Although it was more expensive to establish than an individual structure, the benefits of having a corporate trustee versus an individual trustee are very significant and it is definitely worth paying for.

Is there anything easier/harder about having an SMSF rather than a small APRA fund?

It's harder in terms of having to devote more time to some compliance type activities such as making sure all the paperwork is in order. I also nominated my home address as the mailbox for my fund, which means I get more mail than before. Things like share-holding statements, dividend statements, annual general meeting notifications and corporate action notifications. The Cavendish SMSF administration service has certainly helped from an administration and compliance perspective. The dashboard is a great tool as it alerts me to upcoming compliance events and missing or incomplete

documentation. For me the biggest change has been a mindset change. When my fund was a small APRA fund, it was still my fund but I was not the trustee of the fund so I could afford to be a little more relaxed about the administration and compliance issues. However, now that I am a director of the corporate trustee of my fund, I am legally responsible for ensuring everything gets done which means administration and compliance issues are now more front of mind for me.

Are you glad you made the switch?

Yes I am. For me an SMSF is a much more cost effective option compared to an small APRA fund and using a professional SMSF administrator has enabled me to minimise the time I need to devote to administration and compliance type activities. Having worked in the sector for 10 years or so, there were certainly some things that I learnt setting one up myself. Yes the extra mail and notifications I now receive can take a bit of time to sort through each week, but for me the benefits of converting to an SMSF certainly outweigh this inconvenience.

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Murray in waiting

by Barrie Dunstan

Key points

- *Reasons for 'sticky' fees in super are rarely acknowledged or understood by politicians.*
- *The free market theory that competition reduces costs doesn't work very well in superannuation.*
- *Some members may decide they prefer cheaper costs over 'independent' directors.*

The stock market's immediate reaction to the Murray report suggests there's not a lot to worry about the shares of the big banks, which are stuffed into most SMSF portfolios. And the "not to worry" reaction probably will also apply to its superannuation recommendations.

Many of the super recommendations appear to be several years away. This applies particularly to the suggested changes to introduce more formal competition over fees and default funds. The idea of pushing more people into a formal income product in retirement also will require a lot more reforms for example, on annuities. Recent governments have shown little enthusiasm in this area and, in general, it seems the government will leave the tough decisions and work to the regulators, APRA and the ATO.

Promises, promises

Almost every review of superannuation – and there have been plenty – has tackled the question of fees, leading to regular promises of reduced fees and higher account balances at retirement. But fees haven't fallen much, though MySuper lower-cost model funds now seem to be making some very modest progress. Anyway, it seems any formal action on the Murray recommendations won't begin until 2020.

There are several obvious reasons why fees are "sticky", which are rarely acknowledged by the politicians who designed the system. The first reason is that by offering a bewildering range of fund choices, the Liberals imposed high cost structures, all in the name of giving some members unlimited choice of investment. The choice regime also imposed restrictions on many funds, which had to retain liquidity to handle members switching.

Second, politicians still haven't twigged that the free market theory that competition reduces costs doesn't work very well in superannuation. This is largely because the majority of super fund members are still disengaged from their super accounts. In addition, the continual tinkering with super has meant funds have had to spend millions to update systems over the last decade.

Harmony required

The chance of any effective government action depends in part, as the Murray report notes, on the need for "broad political agreement" on the objectives for super. But it's clear that the deep ideological divide in the industry hasn't lessened after more than 25 years of squabbling. And now this report has re-ignited the anti-union arguments about industry funds, with the predictable reaction from the industry funds.

The Murray report's argument against representatives of employers and unions sharing board seats (with an independent chairman) appears to elevate a desire for "governance" over actual member returns. Given the recent scandals in the CBA and other financial planners, this seems ironic timing.

Industry fund members might prefer better returns rather than independent trustees. Indeed, the long history of outperformance of industry funds over retail funds, suggests there could well be an argument to change the boards of retail funds – and adopt the low-cost business model (as is happening with the new MySuper funds).

A long time coming

As for current SMSF fund members, there's probably a likely time gap between David Murray's recommendations and any future Federal Government action. Current political reality is that the government is scrambling just to regain momentum in its May Budget measures, let alone take on a new round of reforms involving a fight with the banks.

With a major discussion paper and then a debate on tax reform to come, it's unlikely that any decision on prohibiting borrowing by SMSFs for direct property investment is on the immediate horizon – assuming the government had the stomach to act.

Existing arrangements would have to be grandfathered – which will be an invitation to property floggers to push more SMSFs into borrowing at what might be an inopportune time in the property market. More likely, any limit on borrowing seems likely to be enforced by the regulator leaning on lenders to limit their loans for property.

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What will change on January 1

by Tony Negline

Key points

- *Income from account-based pensions will be deemed for both pension and Commonwealth Senior Health Card purposes.*
- *FBT will increase from 47% to 49%.*
- *You need to lobby your local representatives if you don't want borrowing in super to be banned.*

As we brace ourselves for a new year, we need to be on top of all the changes to policy and regulations. The following is a quick round-up of some of the tax, super and Social Security changes that will take place sometime in 2015.

1. Deeming of Account Based Pensions for the Aged Pension and the Commonwealth Seniors Health Care Card

These are two very important changes. Both changes involve grandfathering which means there is a before and after situation. The two changes are as follows:

- Aged Pension – Income from account based pensions (ABPs) that commence after 2014 will be deemed for aged pension purposes – this change has been legislated
- Commonwealth Seniors Health Care Card (CSHC) – Income from ABPs that commence after 2014 will be deemed for the purposes of the CSHC income test – this change hasn't been legislated

Over the last six months we have written about these two changes quite extensively. The most recent articles were published in October, which you can read here and here.

If you want to take advantage of the pre-January 2015 rules then you're fast running out of time. (If you need to transfer money from one super fund to another, then there is a high likelihood that you have run out of time given the time it often takes to move money between super funds.)

2. Fringe Benefits Tax – this will increase from 47% to 49% on 1 April 2015 to cover for the Temporary Budget Repair Levy.

3. First Home Owners Savers Account – the government announced that new accounts wouldn't be allowed after mid-May 2014 and existing accounts would be abolished from 1 July 2015, however the necessary legislation hasn't been passed by Parliament so it's business as usual for these accounts until that occurs.

4. Paid Parental Leave – the policy that the government took to the election was expected to commence on 1 July 2015, however that policy will be adjusted and may have a new commencement date (all dependant on the ability of the government to get this legislation through the Parliament). At this stage it appears that the government will reduce the maximum that can be paid under its proposed scheme and also allow it to be a little more flexible.

5. Family Tax Benefit A & B – there are a number of changes that will occur on 1 July 2015:

- Cessation of the indexation of the end of year supplement for FTB A & B
- FTB A – the $3,796 add-on to the income threshold for each child after the first will no longer be applied.
- FTB A – the Large Family Supplement will only be paid for families with four or more children.
- FTB B – Primary income earner limit will be reduced to $100,000

6. Asset test thresholds for Centrelink/DVA pensions – the indexation of these thresholds will cease for two years commencing on 1 July 2015.

Will super gearing be banned?

Finally as you've no doubt heard the Financial System Inquiry headed by David Murray recommended to the government that super funds shouldn't be allowed to borrow money.

For all of the FSI's recommendations, the government is now considering what it should accept or reject. It has asked interested parties to make submissions to the government over the next three months.

In my mind, no evidence has been presented with exposes the potential weakness in SMSFs borrowing money.

Writing in The Australian on 8 December 2014, company director and economist Judith Sloan said, without any elaboration, that, "the SMSF sector would probably be well-advised to quietly accept" the proposal to ban super funds from borrowing money.

With respect I disagree. I do however think that some restrictions on the amount that can be borrowed should be put in place. Unfortunately a subtle change like this may be beyond the ability of our political masters.

Strong and loud voices to your political representatives are needed if you agree with my view that a ban in this area is unnecessary.

However it has to be said that the Government may accept this recommendation but will probably do so prospectively. That is, any arrangement in place when a ban commences will be allowed to continue.

Therefore if you're attracted to borrowing money in your super fund, you should probably not allow the grass to grow under your feet for too long.

***Important:** This content has been prepared without taking account of the objectives, financial situation or needs of any particular individual. It does not constitute formal advice. Consider the appropriateness of the information in regards to your circumstances.*

Big on banks and more international exposure

by Questions of the Week

Question: I have a SMSF and I am in pension phase and 70% of the portfolio is in the banks. Do you think this is a good idea?

Answer (By Paul Rickard): Notwithstanding that I am a huge fan of bank shares for tax advantaged income, my sense is that a 70% weighting to banks is too much. The ‘financials’ index in total makes up about 46.5% of the ASX. Of this, banks and insurance companies are 40%, with property trusts accounting for the balance of 6.5%. Effectively, you are almost 100% overweight.

My suggestion is that you consider de-weighting over time. Our income portfolio could be a guide if you are looking for potential sector weightings and/or stocks.

Question 2: I have an account-based SMSF, concentrating mainly on dividends. Recently there have been several articles about exposure to the US market. What ETFs could I get for the US market or would direct shares like QBE be better? I’ve also been looking at the EFT for IJP, but wondering if it has got too expensive?

Answer 2 (By Paul Rickard): Probably, the easiest way to get exposure to the US market is through Exchange Traded Funds (ETFs). There are three ETFs that track broad-based indices:

1. iShares IVV, which tracks the S&P 500
2. iShares ISR which tracks the Russell 2000
3. Vanguard’s VTS, which tracks a US total shares index (CRPS US Total Market Index)

Less directly, you can weigh your portfolio to shares that have a major part of their revenue in US dollars and/or report in US dollars. Companies such as CSL, Brambles, Resmed, Computershare, QBE etc.

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