Five IPOs to watch

by Tony Featherstone

Key points

- *2014 was a record-breaking year, with $18.6 billion in new listings.*
- *This year could be tamer, potential floats include MYOB, Link Market Services and Fleet Partners.*
- *The smart money is on new listings like Genworth, iSentia and Monash IVF.*

After a record-breaking year with $18.6 billion in listings, the 2015 initial public offerings (IPOs) market could be tamer. Potential floats for 2015 include accounting software provider MYOB, share registry Link Market Services, dairy processor Murray Goulburn Co-operative, software developer Wise Tech Global (in late 2015), fleet-management provider Fleet Partners, and South-East Asia-focused Property Guru.

Smaller touted IPOs include software developer Readify, homeware provider Adair Retail Group, QMS's digital outdoor advertising spin-off, chemotherapy provider Icon Cancer Care, and foreign-currency broker FXPrimus.

But as investors look for the next IPOs, the smart money might focus on recent listings rather than upcoming ones. High-quality small and mid-cap floats can be overlooked in boom IPO years, as investors scramble for a piece of the largest offers.

Below are five interesting IPOs from 2014. Some have already rallied and have further to run in the next few years, albeit at a slower pace. Others are wallowing below their issue price and make the grade on valuation grounds.

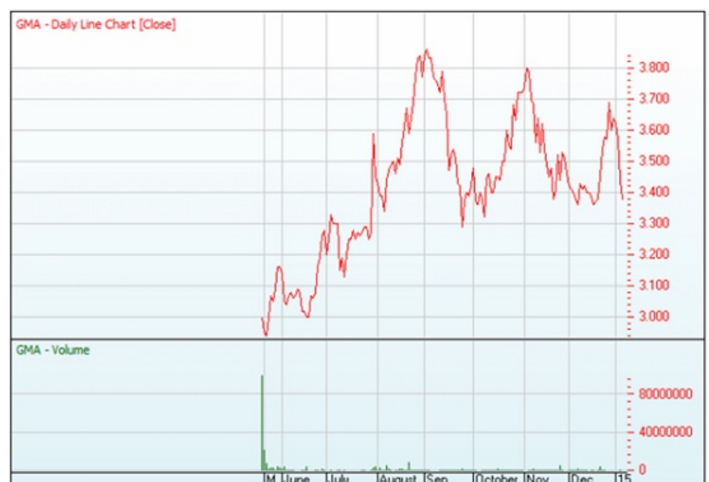
Always remember that IPOs have extra risks because far less is known about them compared to listed companies.

1. Genworth Mortgage Insurance Australia

After being delayed for almost three years, Genworth's IPO had impeccable timing. It listed in May 2014 – in the middle of a residential property boom – after raising $583 million. The $2.65 issued shares peaked at $3.90 after strong earnings guidance, before retreating to $3.38.

Genworth would be a terrible stock to own during a property downturn, characterised by sharply higher mortgage arrears and loan defaults. But it is hard to see residential property tanking, with another interest rate cut a possibility in 2015, lower petrol prices helping homeowners, and unemployment remaining elevated although manageable. FN Arena's consensus target price for Genworth is $3.87.

Genworth Mortgage Insurance Australia (GNW)



Source: ASX

2. iSentia Group

The media-monitoring group was among the more impressive floats of 2014. After raising $284 million in an oversubscribed offer and listing in June, iSentia rallied from a $2.04 offer price to $2.65. Fund managers liked its business model and Asia growth prospects.

iSentia provides media monitoring, social-media monitoring and analysis, media management and analysis, contract management services around communication strategies, and media-release distribution. It is superbly positioned as companies use advanced software to understand what is said about them online and tailor messages in real-time.

Like all good software companies, iSentia's business model is highly scaleable and can be expanded to new market segments without huge capital investment. As the clear market leader in its industry, iSentia also enjoys high barriers to entry, a valuable competitive advantage, and pricing power. It's a stock to watch over the next few years. FN Arena's consensus target price for iSentia is $3.07

iSentia Group (ISD)

Source: ASX

3. Monash IVF Group

The in-vitro fertilisation (IVF) group was one of last year's big IPO disappointments. After raising $315.9 million and listing in June, Monash's $1.85 issued shares have slumped to $1.39. Signs of slowing IVF demand and greater IVF competition in Australia have weighed on the stock.

The market had high hopes for Monash after its close rival, Virtus Health, soared on listing in 2013. Virtus has a better industry position, but Monash has plenty of attractions, notably a fantastic brand, deep intellectual property and strong potential to expand in Malaysia, which has much lower rates of IVF penetration than Australia. IVF is a solid, reliable industry with high barriers to entry and good long-term prospects

FN Arena's consensus target price for Monash IVF is $2.07. Monash has the potential to grow by acquisition in New South Wales, a market where it is under-represented. Like many IPOs, it was overpriced at listing and looks a lot more interesting after listing.

Monash IVF Group (MVF)

Source: ASX

4. 3P Learning

The education software provider raised $282 million in an IPO, attracted several prominent small-cap fund managers, and listed in July 2014. It briefly traded above the $2.50 issue price before slumping to as low as $1.94 in one of the year's more disappointing floats.

But every stock has its price and 3P has a fantastic global business in online learning through its popular programs: Mathletics, Reading Eggs, Spellodrome and the newer IntoScience. About 4.7 million students

and 17,000 schools use its software, according to the company.

3P slightly beat revenue and underlying earnings projections in the prospectus, confirmed it was on track to meet 2014-15 guidance, and has plenty of operational momentum with product releases. The market may have been too harsh on 3P given its potential to expand in the United States, its pricing power and a unique product offering online education in Australia.

Online education is a lucrative global business, and 3P clearly has good products and is well run. The only broker to rate the company on FN Arena's database – Macquarie – has a $3 target on the company.

3P Learning (3PL)

Source: ASX

5. Orion Health Group

With several billion-dollar healthcare floats in 2014, it was easy to overlook the $112-million IPO of the health software provider. Listed in November, Orion rallied from a $5.11 offer price to as high as $6.05 before easing to $5.50, making it one the best health-related IPOs in 2014.

Orion has three key products: Intelligent Integration, an enabler of healthcare information exchange; Smart Hospitals, which manages the clinical and administrative information flows within hospitals; and Healthier Populations, which provides care, co-ordination and analytic tools to manage healthcare needs beyond hospitals.

True believers in technology's potential to revolutionise healthcare will find much to like in Orion. It says the key to the health data revolution is software that captures and analyses healthcare information for populations, to help clinicians create individual healthcare plans.

Orion looks like another New Zealand company that should benefit from a secondary listing on the ASX. Established 21 years ago, it has a good long-term record and 450 healthcare customers across 25 countries. With governments worldwide under pressure on healthcare spending, Orion's software should enjoy stronger demand in the next five years.

Orion Health Group (OHE)

Source: ASX

• Tony Featherstone is a former managing editor of BRW and Shares magazines.

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My SMSF – half-yearly check-up

by Barrie Dunstan

Key points

- *Beginning of the year is a good time for a once over.*
- *The most important thing is asset allocation: is it tracking original targets?*
- *Review decisions to invest, or not invest, in particular asset classes.*

What does this time of year mean for your SMSF?

It's that time of the year when the media gives us New Year resolutions, predictions and share market tips. As a former daily newspaper journalist, I once merrily joined the game to fill those empty pages – unaware whether anyone was heeding the advice. Now, this season is simply a reminder to check my super fund's investment strategy.

It's usually only a check rather than a full-blooded review or renovation. The financial year-end is the more natural time for that, when accounts are finished, reports are completed and the annual figures provide the necessary measure of a year's performance.

What checks have you done?

I've just completed my half-yearly check, beginning with the most important thing – my fund's overall asset allocations. I regard this as the key to my investment strategy (and it also fulfils that pesky requirement on which the regulator insists).

What's your asset allocation?

My fund has run on a rough split of 60% of assets in equities and 40% in cash and fixed interest for about five years. There's no science in that ratio: it just seems to work for my needs. Over the past couple of years, it's managed to balance a need for dividend income (when interest rates are low), against the need to hold a buffer of safe money to ensure pension distributions if tough times hit the stock market.

Over the past 12 months, the equities percentage has risen from 59% to 62%, largely because of a slight improvement in the stock market and slight cutback in the holding of bank hybrids. I'm not looking to move any more money into shares unless the climate changes and I think I've de-risked the share portfolio with some adjustments in 2014.

What investments do you like?

Some SMSFs like to pick stocks. I like to pick the best stocks – after assessing the big issues. My list of big issues includes: China and commodity prices; a softening local economy; interest rates and a weakening Australian dollar. That has led the fund to hold the lowest cost resource stocks (BHP fills that bill); higher yielding, defensive local stocks; short-term bank term deposits and to buy more US stocks.

What have you changed?

The major change has been an increase in the overseas share component from under 6% to more than 10%, by adding to the fund's holding in the S&P 500 ETF (IVV) and maintaining another global equity ETF (the SPDR WXOZ).

The bank component (including hybrids) has declined from 31% to 25%, reflecting some hybrids maturing and sale of Bank of Queensland. Maybe the Murray Report might slow the banks' growth but the market

seems to be comfortable with the current valuations of the Big Four – and bank dividends produce about 27% of my fund's total current projected income.

The wish for defensive stocks has seen an increase in the health and infrastructure sectors. A modest holding in Medibank Private and growth by CSL has seen the health sector increase to 8.6%, hopefully providing a defensive element. I take a similar view on infrastructure (11.6% of assets), adding to the existing Transurban holding (now the second biggest individual holding) and increasing the APA holding through its new issue. The fund also bought Sydney Airport in 2014.

In resources and energy (7.7%), the fund is a firm holder of Woodside (despite some market sceptics) and is sitting on its largest paper loss with BHP. So far, it has resisted the temptation to try and pick a turning point in resources prices or stocks. Any bargain hunting will probably reflect any revival in oil prices, with Oil Search the likely target.

Like many SMSFs, Telstra has been a mainstay for capital growth and income and it has been tempting to chase the stock as it rises. But it now comprises almost 10% of the portfolio, approaching my unofficial limit for an individual stock.

Stock selection is a compromise between seeking some potential growth stocks and the need to fund pensions, hopefully from current dividend income.

How is its performance?

Total income rose over 11% in 2012-13 and projected 2014-15 income (from our helpful stockbroker's analysis) could rise another 12-13%. This has been achieved despite holding only about 4% in higher-yielding property trusts – Novion (the successful Chadstone centre) and an ETF which replicates the listed property sector.

What are other considerations?

The fund has stood aside from borrowing to invest in direct property. This is because of a general dislike of gearing; a suspicion that apartment (and other) property values could be affected by potential over-supply; the risk of higher interest rates; adequate exposure to property via the family home and a history of generally miserable net returns from rental properties.

The fund's biggest punt is on the Wall Street market via ETFs. This is based on a view that the US economy and stock market are the most robust in the world and that, if the Australian dollar remains under downward pressure, this is the most straightforward way to profit on the exchange rate.

Thoughts on the year ahead?

So 2015 will probably see the portfolio stay on cruise control, absent any major incidents. As structured, the portfolio is set to provide modest income growth, with a conservative approach to capital preservation. There are possible worries with the economy (and perhaps the share market) though there's probably more risk from legislative change in superannuation and tax (keep an eye on the debate on imputation).

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All in the family – why loaning money to the in-laws is never a good idea

by Tony Negline

Key points

- *A court case last year reinforced why it's important to understand the in-house asset rules.*
- *The Lyons Family Superannuation Fund loaned more than 97% of its fund to a member's brother-in-law who loaned it back to the Lyons' family business.*
- *The auditor of the fund reported what they thought was a breach to the ATO who declared the fund non-complying.*

Loaning money in a self managed super fund to the spouse of your sister, who then loans this money to your business, is likely to lead to trouble.

This is one key lesson from a Federal Court case handed down in December 2014 involving Anthony Lyons. The other key lesson is that a few days can make a substantial difference to the penalties you might face if the ATO takes action against your super fund.

The details

The Lyons Family Superannuation Fund was set up in June 2008. It had two members, Anthony and his former wife Julianne. The fund was capitalised in July 2008 with almost $200,000 in transfers from the Queensland Government Employees super fund (Q Super) and another employer-sponsored super fund.

Between July 2008 and May 2009, the fund loaned $190,000 to Paul Ellis, the spouse of Anthony Lyon's sister. Under the super laws, Mr Ellis is deemed to be a relative of Mr Lyon.

Mr Ellis then loaned this money to the Lyons' struggling business. It appears that this money was lost because the business failed in March 2010. Its failure also pushed the Lyons into bankruptcy.

This rather unusual loan process was suggested to the Lyons by a financial adviser. The adviser is said to have suggested that the loan from the trustee to Ellis should be documented as a "Debtors Factoring Agreement" so the true purpose of the loans was disguised. None of this information appears to have been tested in court.

Auditor's report

The fund's external auditor, as required by the super laws, told the ATO about the loans and that, in his opinion, they were a breach of various super laws. In particular the following problems identified were:

- Sole purpose test – a fund must be run to satisfy certain statutory purposes and the loans breached this requirement.
- In house assets: the loans to Ellis were to a fund member's relative and as such these loans are deemed to be in-house assets. The maximum in-house assets allowed is 5% of the fund's total assets using a prevailing market value for all super fund assets. The Lyons had loaned Ellis over 97% of the fund's assets – a clear breach. When this 5%is exceeded, a super fund's trustee has to prepare a written plan within a specific timeframe about how they will bring the fund back into compliance with this requirement. Once this document has been prepared, the trustee has until the end of the next financial year to implement it. Super law breaches arise for not preparing the written plan or implementing it in the required timeframe. None of this rectification process had been

conducted.

- Arm's length dealing: the loans were made in the full expectation that they were never going to be repaid. Ordinarily, the arm's length rule demands that the other party to a transaction must not obtain any monetary benefit greater than that which would ordinarily be available when two parties are operating at arm's length.

The ATO then looked at the super fund and its records and, after interviewing Anthony Lyons on three separate occasions, came to the same conclusion as the external auditor.

The ATO's reaction

The Tax Office's first action was to make the fund non-complying in the 2009 financial year. In the year a super fund is deemed to be non-complying, the tax rate is 45% and charged on the market value of the net assets of the fund, less non-concessional contributions at the start of the financial year. At the time, the fund had assets of less than $2,500.

If the transfers from the corporate super funds had occurred just before the end of the financial year, several days earlier in 2008, then the fines would have been significantly higher. It's amazing the difference a few days can make!

As the ATO had declared the fund to be non-complying, it was unable to apply tax penalties on the illegal withdrawal of money from a super fund.

The ATO's next step was to seek Court imposed fines against the Lyons as super fund trustees. Before the Court hearing, the ATO and the Lyons had agreed that they would jointly propose that only Mr Lyons should be penalised because he was primarily responsible for the fund not complying with the super laws.

However, the ATO told the Court that Lyons had fully co-operated with the ATO's investigation and had made full admissions and this should be considered in the penalties imposed by the Court.

The Court accepted this view and imposed a modest fine of $37,500, which included a small amount for the Tax Office's legal costs.

Under rules put in place from 1 July 2014, the ATO would have been able to impose other, overall much higher, specific penalties for breaching the three specific super laws mentioned above.

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Crown falls, transferring property and short selling

by Questions of the Week

Question: I am rather concerned about the fall in Crown's share price and have had difficulty finding out the reason. Are there problems with Macau? Would be glad of advice on whether or not to sell out.

Answer (By Paul Rickard): There are clearly some issues with Macau, which is impacting Crown. Crown owns approximately 33.8% of Melco Crown Entertainment, one of the casino operators in Macau.

The Financial Times reported that total gaming revenue in Macau declined by 2.6% in 2014 (the first year-on-year decline), with steeper declines at the back end of the year. An expectation of a further revenue decline is one of the factors currently impacting Crown.

Despite the issues in Macau, the brokers remain largely positive on Crown based on the strength of its domestic business and prospects. According to FN Arena, broker sentiment is currently +0.6 (scale -1.0 most negative, +1.0 most positive), with a consensus target price of $16.44.

Given the fall in price, my inclination is to hang on to Crown at these levels.

Question 2: In relation to your recent article "Super at every stage – 55 plus", you mentioned transferring personally held assets into super CGT free.

What are the annual limits for such contributions and can property be transferred? If property is allowed, I imagine that a portion could be transferred by a percentage of ownership (say 20%) deducted from a current property valuation.

Answer 2 (By Tony Negline): If by property you mean residential real estate, then in most cases the answer is no because super funds aren't allowed to acquire this type of real estate from members or their relatives.

The concessional and non-concessional contribution caps are important for moving assets into your super fund prior to retirement.

All of this can get tricky so I encourage you to take some advice.

Question 3: Could you explain "short selling" to me?

Answer 3 (By Paul Rickard): "Short selling" is the opposite of buying.

If you buy a stock, hopefully at some stage you can sell it at a higher price to make a profit. With short selling, you sell the stock first with the intention of buying it back at a lower price to make a profit.

As you can't sell something that you don't own, a short seller needs to be able to borrow the stock from another party. Typically, a short seller borrows the stock from a financial institution and secures the loan of the stock with cash.

The stock is then sold into the market, with the short seller receiving cash, and delivering the borrowed stock to the buyer. When it comes time to close the short position, the transaction is reversed. The short seller buys the stock back in the market, and then delivers that stock to the institution that he borrowed it from.

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Don't miss!

The beginning of the year is a great time to get your superannuation in order. Check out our eBook on *Super at every stage.* It has something for every member of the family, no matter their age.