Switzer Super Report

Issue 359, 29 January, 2015

Batter up!

The news out of the US overnight was relatively good, with the Fed promising patience on interest rates, although the Dow Jones ended lower. But the key themes for local investors remain, and one of the biggest ones - which we've been talking about for ages in the *Switzer Super Report* - is US dollar exposure.

Today Charlie Aitken explains why this will remain a key theme for 2015 and why you might want to consider adding companies like Macquarie Group to your portfolio.

Tony Featherstone has got a great article for you on the 14 curveballs that could hit you from left field in 2015 and how to play them.

David Buckland, chief executive officer of Montgomery Investment Management, talks about the lessons investors should learn from Arrium in a *Fundie's not-so-favourite* and Tony Negline explains the proposed relief for excess super contributions.

Sincerely,

Peter Switzer

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switzersuperreport.com.au

Switzer Super Report is published by Switzer Financial Group Pty Ltd AFSL No. 286 531
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High conviction picks and upgrade for Macquarie Group

by Charlie Aitken

Key points

- *The key themes of US dollar leverage, major banks, non-bank dividend growth and inbound tourism remain.*
- *Macquarie Group, along with Westfield Corporation (WFD), Servcorp (SRV), CSL (CSL), Resmed (RMD), Brambles (BXB), Platinum Asset Management (PTM), and Magellan Financial Group (MFG), are leveraged to the US dollar.*
- *Macquarie Group's earnings per share (EPS) is only set to grow, which means it deserves a new 12-month target of $70.*

In terms of Australian equity strategy, I am attempting to position for globally-driven yield compression meeting domestically-driven yield compression as the Reserve Bank (RBA) cuts the cash rate. I have a feeling we are all going to be surprised by how much money attempts to move down a reasonable narrow street and that is why my entire focus this year has been on dividend growth stocks (and currency-translated winners).

In an Australian context, these global growth downgrades mean ASX200 earnings growth will be harder to find. That is why I am looking for industrial ideas that can most likely grind out 6% EPS growth and generate a 6% plus pre-tax dividend yield. A 12% pre-tax total return may well look extremely attractive by the end of 2015 if bond yields are to be believed. That is why I recently upgraded Telstra and the big four banks.

High conviction ideas

I have attempted to move quickly at the Australian equity strategy level in three ways. Firstly, upgrading Telstra ($7.00 target) and the major banks (5% fully franked FY15 yield targets), secondly, reaffirming high conviction non-bank yield growth ideas, and thirdly, reiterating US dollar leverage and inbound tourism exposures as the Australian dollar heads towards 75 US cents. I have tried to get the message across in the big liquid stuff first. My high conviction ideas are listed below.

• Major banks

ANZ (ANZ), National Australia Bank (NAB), Westpac (WBC)

• Non-bank dividend growth

AMP (AMP), APA Group (APA), Challenger (CGF), Goodman Group (GMG), GPT (GPT), IAG (IAG), Transurban (TCL), Sydney Airport (SYD), Suncorp (SUN), Tabcorp (TAH), Telstra (TLS) Wesfarmers (WES) and Spark New Zealand (SPK).

• US dollar leverage

Westfield Corporation (WFD), Servcorp (SRV), CSL (CSL), Resmed (RMD), Brambles (BXB), Macquarie Group (MQG), Platinum Asset Management (PTM), and Magellan Financial Group (MFG). In the banks, ANZ (ANZ) generates the greatest proportion of USD earnings.

• Inbound tourism

Crown Resorts (CWN), Sydney Airport (SYD), Auckland Airport (AIA), Qantas (QAN), Air New Zealand (AIR.NZ), Village Roadshow (VRL), Ardent Leisure Group (AAD) and Sealink Travel Group (SLK). For the highly risk tolerant, Virgin Australia (VAH) is arguably worth a punt.

Macquarie Bank

I have consistently written, *"currency translated EPS growth is EPS growth"* and that key *"US dollar earning stocks were cum consensus upgrades"*. We got evidence of that earlier last week when **Macquarie Group (MQG),** who generates 65% of revenue outside of Australia, revised up their earnings guidance.

Macquarie Group is a member of my key high conviction US dollar earning ideas list alongside **Westfield Corporation (WFD), Servcorp (SRV), CSL (CSL), Resmed (RMD), Brambles (BXB), Platinum Asset Management (PTM), and Magellan Financial Group (MFG). In the banks, ANZ (ANZ) generates the greatest proportion of USD earnings.**

Macquarie Bank (MQG)

Source: Yahoo!7 Finance, 29 January 2015

Macquarie Group is now more of a fund manager than investment bank. I tend to think comparisons to US investment banks, and their cyclical profitability, are out of date. Macquarie has a lot more in terms of better quality, higher return on equity (ROE), and lower volatility income than its US-based peers.

With 62% of operating income now generated from "annuity-style" businesses that generate an ROE of 24%, and as I said above, 65% of revenue generated from offshore, I suspect Macquarie's price to earnings ratio (P/E) is about to rise a few points to reflect the greater forecastability of EPS and dividend per share (DPS).

Macquarie didn't give details of the drivers of the profit guidance upgrade but it's fair to assume currency and advisory fees played a role. I also keep hearing market rumours they had a big win in oil trading, but that is yet to be confirmed.

Either way, I'm not too interested in the minutia, more that Macquarie has confirmed they have earnings leverage to our key macro theme: the US dollar.

The numbers

I have upgraded my FY15 net profit after tax (NPAT) estimate to $1,455 million and I now forecast MQG to generate 20% EPS growth in FY15 and 16% DPS growth.

Despite the share price bounce from recent lows, Macquarie remains a cheap US dollar leverage stock with the ability to deliver total returns above most ASX200 members. Again, that should lead to P/E expansion as growth becomes harder to find.

Based off a MQG share price of $60.00, below are my forecasts and multiples.

	FY15	FY16	FY17
NPAT	$1,445m	$1,550m	$1,635m
EPS	460c	492c	521c
EPS Growth	+20%	+7%	+6%
PE	13.04x	12.19x	11.51x
P/book	1.4x	1.4x	1.3x
ROE	13.2%	13.4%	13.5%
DPS	302c	334c	366c
DPS growth	+16%	+10.5%	+9.5%
Dividend Yield	5.03%	5.56%	6.10%

The only slight negative with Macquarie is that dividends are only 40% franked. However, this is the trade-off. If you want earnings growth driven via offshore revenue exposure, you are going to have to tolerate a lower level of franking.

Interestingly though, and this is a positive, shareholders are now getting a greater share of the growing revenue pie with the *"compensation ratio"* down to 43% in FY15 from 45% in FY14.

Macquarie remains a high conviction buy. The EPS/DPS forecasts are in an upgrade cycle. That cycle will be underestimated if I am right about my 75 US cents Aussie dollar target.

New target

By the time we get to the end of FY16 (March 2016) I expect Macquarie consensus EPS to be 500 cents. **I expect the market will pay 14 times for that 500 cents EPS and therefore set a 12-month price target for Macquarie at $70.00.**

That would equate to a 16.6% capital gain and 5.03% yield, taking potential total 12-month return above 20% even from today's $60.00 share price.

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14 potential 'curveballs' and how to play them

by Tony Featherstone

Key points

- *The oil price collapse was a curveball in 2014, which nobody publicly predicted, and highlighted why it's so important to look out for the unexpected.*
- *If markets lost faith in central banks, that would be the mother of all curveballs in 2015.*
- *Others could be a new prime minister, a hard landing in China and more interest rate cuts this year.*

A curveball, X Factor or Black Swan event… call it what you will. The oil price collapse was the shock nobody publicly predicted last year and a no-brainer for *"Unexpected Event of 2014"*, given its profound effect on financial markets and the global economy.

The tumbling oil price was also a timely reminder that trying to pick financial shocks is a mug's game. Purists argue that a true X Factor cannot be predicted, so it's pointless to try. Realists argue that profiting from such events is a struggle for even gifted traders.

A better approach is identifying long-term themes and positioning portfolios to benefit. That is especially important for self-managed superannuation funds (SMSF) with a multi-year or decade focus. Financial shocks, often presented as "left field events", are usually the culmination of powerful long-term themes that were well-known and underestimated for several years.

Still, it pays to think about curveballs that can disrupt markets and your portfolio – and have a plan to capitalise on buying opportunities that emerge. Patiently buying high-quality companies during big market dips can be an immensely rewarding long-term strategy.

Here are 14 curveballs, positive or negative, that could disrupt the Australian sharemarket and economy in 2015. By definition, these curveballs have a low probability of occurring – a less than one in five chance – but still warrant consideration.

1. A new prime minister

Granted, the odds of leadership change are slim, despite Coalition backbenchers leaking their grumbles about the Government's performance over the summer, and the Prime Minister's blunder this week in knighting Prince Phillip. The Federal Government can scarcely afford another poor year after a lacklustre start. If its weak polling continues, watch for leadership speculation to have more credibility in the second half of 2015. Such change, currently unlikely, would further stall regulatory reform and further crunch business and consumer confidence.

2. A cyber-led GFC in 2015

Picture this: a rogue State hacks into the mainframes of the world's largest stock exchanges, rendering them inoperable. Or a local group hacks into the four biggest banks, shutting down electronic-banking platforms and ATMs nationwide. Fantasy? Media reports say cyber-terrorism threats to Australia are rising rapidly and overseas events – notably Sony being hacked by North Korea sympathisers – show the threat is more dangerous than widely realised.

3. A hard landing in China

Although there are plenty of doomsayers about China, the consensus view for its economy was 7.2% growth in 2014, in line with Government efforts to

engineer more sustainable growth. But what if China reports sharply lower-than-expected growth in 2015, amid a rapid slowdown in its property market? In January, Blackstone Advisory Partners' Byron Wien named a hard landing in China as one of his top 10 potential surprises in 2015. The Government, he surmised, could announce more financial and monetary policy stimulus needed to maintain a 5% growth rate, let alone 7%. If that happened, commodities prices would find new lows, triggering the final washout in Australian resource stocks, and perhaps signalling a buying opportunity in resource stocks for contrarians.

4. Four interest-rate cuts in Australia

Most economists expect one or two interest rate cuts in 2015 as the Reserve Bank responds to a stubbornly high Australian currency and slower economy. But an intensifying global currency war could force its hand; the official cash rate cut to 1.5%, from 2.5%, in four instalments, to lower the Australian dollar. Imagine the effect on property prices, bank term-deposit rates, and popular income stocks. More likely is a 2% cash rate by late 2015, possibly higher, as the easing Australian dollar heads towards US 75 cents, keeping the RBA happy. But further rate cuts cannot be ruled out if the global currency war escalates and the Australian dollar rises.

5. CBA cracks $100

A three-digit share price for the Commonwealth Bank would imply a total 12-month shareholder return (including grossed-up dividends) of about 24% from Australia's best bank, from its $86 share price. The catalyst? Lower interest rates driving more income investors into high-yield stocks such as the big-four banks, Telstra Corporation and other utilities.

Many strategists believe the bull market in popular yield stocks has run its course, and that the banks are fully valued and face greater regulatory risk. But don't discount an army of income investors paying even higher prices for reliable, fully-franked dividend yield. Or the effect of a continued bull market in bank stocks on the broader share market. Another huge year for yield stocks would be a curveball for those too quick to take profits.

6. Central banks lose credibility

The Swiss National Bank's credibility took a hit after its shock move in January to abandon the cap on the franc's exchange rate. What happens if more central banks surprise global financial markets as they seek to protect their national currency? And what if markets struggle to understand central bank rate intentions, and incorporate them into asset prices? Nobody knows how the great global experiment of quantitative easing – taken to new extremes by the European Central Bank's massive new bond-buying program – will end. Heaven help us if markets start to lose faith in central banks; that would be the mother of all curveballs in 2015.

7. Gold rallies

After a stunning rally in 2006 to 2011, gold has had fewer friends. The US dollar gold price fell from above US$1,800 an ounce to US$1,294 amid expectations of declining inflation and after a year of lower volatility. But higher financial-market volatility in 2015 could see the yellow metal return to favour as traders buy it for its safe-haven qualities. More likely is gold moving sideways, but it's one commodity that could surprise on the upside in 2015.

8. Russian roulette

The falling oil price is great news for consumers and terrible news for large energy producers such as Russia. Those with longer memories will recall the Russian debt default of 1998 killing once-feted hedge fund Long-Term Capital Management, and threatening Wall Street banks that traded with LTCM. Could there be a re-run of a Russian debt default sending shivers through global bond markets in 2015? It's unlikely: Russia's public debt relative to its GDP is much lower than in 1998 and foreign-exchange reserves are higher. But so much depends on the oil price. If it keeps falling, oil-revenue-dependent Russia will be increasingly vulnerable.

9. The US bull market finds new steam

It is hard to find fund managers who believe US shares are undervalued and that its mighty bull market will continue in 2015. Huge tailwinds for US

shares in recent years – quantitative easing, low interest rates and a lower US dollar – have reversed and become headwinds. Many strategists prefer Asian or even European markets over the US in 2015. But what if the US equities market rally advances, driven by the housing recovery and stronger-than-expected productivity gains from technology? That would catch out asset allocators who have reduced US portfolio weightings, and boost our market. It's arguably one of the better bets on this list.

10. India rises

Hype is growing about India's potential to overtake China as the star of the BRIC economies, thanks to its new pro-business government, led by Prime Minister Narendra Modi. Although its share market looks fully valued after strong gains, expect more investors to increase portfolio weightings to India as its economic growth quickens. They might be a bit late to the party, but that has never stopped emerging-market booms – and busts – in the past. Another big year for Indian equities, driven more by sentiment than fundamentals, could be a curveball for emerging market asset allocators.

13. The dining boom

For years, commentators have predicted a soft commodities boom as rapid growth in middle-class Asian consumers spurs demand for agriculture. Yet soft commodity prices have mostly disappointed in the past few years: the Betashares Agriculture ETF, which tracks a basket of corn, wheat, sugar and soybean prices (and is hedged for currency exposure), has an annualised loss of almost 6% over three years to December 2014.

Now picture tens of millions of extra middle-class consumers in Asia and a lower oil price eventually boosting South East Asian countries that are heavily into manufacturing. And a lower Australian dollar, and hopefully higher rainfall, boosting Australian agriculture exports. Although some agriculture stocks have already gained, the boom has been tame compared with the potential of feeding billions of Asia's middle-class consumers in coming decades.

14. Double-digit property price gains

Property commentators mostly expect single-digit residential price gains in Australia and a year of consolidation after the property boom. But two or more interest rate cuts and higher demand from foreign buyers after the Australian dollar falls would inject new strength into the market.

That would further stretch new home buyers, make the banks more vulnerable to a property correction, and intensify pressure on the Government to improve housing affordability. A bigger debate on negative gearing's role in property-market speculation could feature as part of broader tax reform debate in 2015. My base case is low single-digit gains for property in 2015 – how far can prices rise relative to income? But bigger gains would not surprise if rates stay low, or lower, and unemployment flattens.

• *Tony Featherstone is a former managing editor of BRW and Shares magazines.. All prices and analysis at January 28, 2015*

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Buy, Sell, Hold – what the brokers say

by Staff Reporter

In the good books

Citi upgraded Arrium (ARI) to Neutral from Sell. Citi analysts have updated their modeling for the latest changes in commodity prices and foreign exchange forecasts, as well as the company's announced restructuring of its iron ore operations. Citi observes its non-consensus forecasts of the Aussie dollar for US 72 cents and iron at US$58/tonne keep the pressure high for Arrium, with the latter more than outweighing the tailwind benefits from the weaker currency. (See downgrade).

UBS upgraded Myer Holdings (MYR) to Neutral from Sell following a share price decline of around 30% since September. The broker is increasingly confident in management's ability to meet or exceed forecasts for the first half. UBS considers the valuation attractive and outlook is improving despite the long-term structural risks, which remain.

UBS upgraded Santos (STO) to Buy from Neutral after incorporating lower oil price assumptions. While prices are expected to stay volatile, the broker considers the share price decline of 47% since early September more than adequately compensates for the fall in the oil price and the chance of an equity raising. The company posted a better-than-expected end to 2014 with December quarter production surprising on the upside.

In the not-so-good books

Credit Suisse downgraded Arrium (ARI) to Neutral from Outperform. The company has signaled the closure of its Southern Iron operations, which did not surprise Credit Suisse. The iron ore impairment of $1.17 billion is in line with expectations. While the iron ore asset is taken from the balance sheet the broker expects the debt liability will continue to challenge the company for many years. (see upgrade).

UBS downgraded GrainCorp (GNC) to Sell from Neutral. Recent rainfall in parts of the east coast is too late for the winter crop harvest and unlikely to materially affect the summer crop but could improve winter planting in May if sustained. A falling Australian dollar also improves GrainCorp's outlook, as UBS notes it translates positively for offshore earnings as well as making Australian grain relatively cheaper. UBS downgraded its rating to Sell from Neutral after strong share price performance and now forecasts negative total shareholder returns.

UBS downgraded The Reject Shop (TRS) to Sell from Neutral. The company has announced that first-half earnings will be down 14%. UBS observes cash flows appear to have been reasonable and sales were noted to have stabilised in January. The tough decisions on store closures are still to come and UBS also believes the weakening Australian dollar looks ominous.

Citi has downgraded Westpac (WBC) to Sell from Neutral. Citi analysts believe Westpac post-Gail Kelly will have to face more significant challenges than opportunities for its key Australian operations. Amongst the challenges that need to be tackled are the risk of an "overdose" on mortgage lending, high costs for running a multi-brand strategy and a challenging revenue outlook for the wholesale and institutional divisions.

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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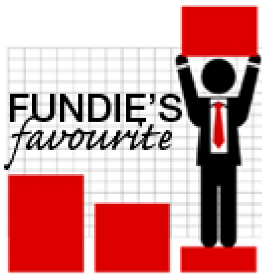

Fundie's not-so-favourite – lessons to learn from Arrium

by David Buckland

The history of Arrium

The demerger of OneSteel Limited, the manufacturer and distributor of steel products throughout Australia and New Zealand, from BHP occurred in 2000. Five years later the Whyalla Steelworks were converted to magnetite iron ore feed, thereby creating a new revenue stream for the company by freeing up the hematite iron ore reserves for export sales. OneSteel was soon exporting 6 million tonnes per annum and with the appreciating iron ore price, the strategy appeared well founded. The acquisition of WPG Resources in 2011 lead to a doubling of iron ore exports to 12 million tonnes per annum and the Whyalla port capacity was also doubled to 13 million tonnes per annum.

In 2007, OneSteel acquired the Smorgon Steel Group, and activities were broadened to include some domestic mining consumables. In 2010, this division was expanded by the acquisition of the Moly-Cop Group mining consumables business from Anglo American, making the re-named Arrium the global leader in grinding media.

On the surface, Arrium's diversification from steelmaking into mining and consumables appeared logical, particularly given the threat of low-cost Asian steel imports into Australia and the strongly rising commodity prices. The financials, however, tell a different story, and this is why it is important for investors to fundamentally assess a company's progress, or lack thereof, over time.

Back in September 2014, on the back of five-year low iron ore prices, Arrium announced a deeply discounted $756 million equity raising. Underwritten by UBS at $0.48 per share, the company said $732 million would be used to reduce debt, which stood at $1,708 million at 30 June 2014. This was more than triple the earnings before interest and tax (EBIT), from continuing operations, in fiscal 2014 of $530 million. Pro-forma net debt would therefore be cut to $976 million, assuming the operating environment didn't get worse.

Worst-case scenario

Unfortunately for Arrium, that is exactly what has happened, and in recent months the iron ore price has declined a further 20% from US$80/tonne to US$64/tonne. Before we analyse the rights or wrongs of supporting the deeply discounted rights issue at $0.48 per share (the prevailing price was $0.72 per share) I think it is important for investors (rather than speculators) to take a forensic look at some of the numbers in the period since 2007, and I'll ask you to be the judge on whether this is a company you want to invest in.

1. The number of shares on issue have increased by more than four-fold from 723.8 million to the current 2937.3 million;

2. Shareholders' funds have increased from $1.6 billion to an estimated $2.9 billion, meaning shareholders' funds per share on issue decreased from $2.20 to sub $1.00;

3. Net debt has increased from $770 million to an estimated $1,300 million;

4. Return on shareholders' funds, or normalized net profit after tax (NPAT) to shareholders' funds, has generally trended downward from a peak of 13.5% and this will likely be negative in fiscal 2015, and negligible in fiscal 2016;

5. Cash flow generated from operations and negative cash flow from investing activities were almost identical, in that they both aggregated to around $3.86 billion over the eight-year period 2007-2014.

This is an unhealthy situation, in that some additional debt and capital raisings were required to assist with the payment of dividends.

6. The announcement of asset impairments has become the rule rather than the exception with an aggregate $2.24 billion reported over the past three years, including this week's announcement of the impairment of $1.17 billion from the closure of the Southern Iron operation and $130 million from the steel and recycling division.

I would argue that despite the excitement behind the company's diversification strategy from steelmaking into mining and consumables, the fundamental numbers I have presented generally represent a business in relatively poor health.

To that end, the serious downturn in the price of iron ore, the difficult outlook for the steel division and the relatively high indebtedness have all conspired to send the Arrium share price, which peaked in mid-2008 at above $6.00 per share, down to the current $0.20.

Arrium (ARI)

Source: Yahoo!7 Finance, 29 January 2015

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Relief for excess super contributions

by Tony Negline

Key points

- *In scheduled changes, the tax on excess non-concessional contributions will now be the maximum marginal tax rate plus medicare levy and the budget repair levy.*
- *You can choose to leave excess non-concessional contributions in your super (if you're on the highest marginal rate) or remove it.*
- *The ATO will send you a notification.*

Good news if you've made excess non-concessional contributions after June 2013!

Late last year the Government introduced legislation into Parliament that will enable you to have those contributions returned to you.

Excess non-concessional contributions can be left in the super system and will be taxed at the highest marginal tax rate plus the Medicare Levy and the Temporary Budget Repair Levy for a few financial years.

If you don't pay the highest marginal tax rate then, you could take the excess non-concessional contributions out of the system and not face a tax penalty on those contributions.

The new system

Once you have submitted your personal income tax return and your super fund has submitted its contribution data to the Tax Office, the ATO will determine if you have any excess non-concessional contributions (excess NCCs). This year the NCC cap is $180,000. Some super investors can make use of the three bring forward NCC cap of $540,000.

If you have excess NCCs, then the ATO will write to you and give you two options:

1. You can ask that all of the excess NCCs be paid to you
2. Decide that the contributions should remain in the super system

The ATO's notice will detail an amount of earnings that the excess NCCs will be assumed to have earned while in the super system from 1 July in the year the contributions are made until the date when the ATO issues a determination.

Once the ATO has written to you about your excess NCC options, you will have 60 days to make up your mind and tell it what your preference is. Under the draft legislation the ATO can give you more time if there are legitimate reasons as to why you didn't respond in the required timeframe. For example, you were overseas and not contactable for an extended period.

Note that under this proposed policy, your excess NCCs must be dealt with as a whole amount. This means that all of your excess NCCs will have to remain in or be taken out of the super system.

The options

If you want your money left in your super fund and you're happy to pay excess NCC tax at the highest marginal tax rate, then you won't need to do anything. The assumed earnings that the ATO have calculated will be disregarded in these cases.

If you want your excess NCCs to be taken out of the super system to avoid paying the excess NCC penalty tax (if your tax rate is lower than the highest

marginal tax rate) then you must tell the Tax Office the names of the super funds that hold your super investments. The Tax Office will then communicate with these super funds, which will have seven days to pay back the maximum possible and to tell you and the ATO how much they've paid. They will initially take money from the taxable component. Once that is exhausted, they'll then take money from your tax-free component.

When you select this option, the assumed earnings that the ATO have determined is included in your personal tax return and taxed at your marginal tax rate, but a 15% tax offset will be available. This assumed earnings will apply even when the value of your investments have gone down because the market value of the contribution's underlying investments have gone down.

What happens if your super fund can't pay the amount determined by the ATO? It will notify the ATO, which will then ask you to nominate another super fund. It may be that you've taken all your money out of the super system. In these cases excess NCC tax will be waived but you will pay tax at your marginal rate on the assumed earnings amount calculated by the ATO.

As you can see, these rules are quite complicated and I expect it'll take sometime for their operation to run smoothly.

One final point – these rules are not formally in place. Hopefully the Government will be able to negotiate their passage through the Senate in the near future. Once that happens the ATO will get cracking on finalising their IT systems.

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Carsales.com and ETFs

by Questions of the Week

Question: Am thinking of adding carsales.com (CRZ) to my super portfolio at $10.50. What do you think of the stock and that price? Am also thinking of adding to my Bendigo and Adelaide Bank (BEN) holding but am concerned that the price is too high at the moment. Should I be waiting for a drop in market?

Answer (By Paul Rickard): I think carsales.com looks ok value around $10.50. There is a little bit of concern at the moment that industry sales are down – and this may impact carsales.com's revenue.

The brokers still seem to like it. According to FN Arena, the current consensus price target is $11.41 and the sentiment rating is +0.6 (scale -1.0 most negative, +1.0 most positive).

On Bendigo (which is trading at a 52-week high), I am with you. I prefer the major banks to the regional banks.

Question 2: Do you recommend investing in ETFs for retirees? How do you rate ETFs in terms of risk compared to direct shares or managed funds?

Answer 2 (By Paul Rickard): ETFs in general are fine for retirees.

Whether they are suitable for you will depend on your own particular situation.

ETFs that track broad-based indices are, in general, less risky than individual shares. With an ETF, you should get the return of the index, less a tiny management percentage. For example, if you invest in SPDRs ETF that tracks the S&P/ASX 200 (ASX Code STW), then if the sharemarket goes up by 2%, the value of your ETF should go up by 2%. They are passively managed.

On the other hand, managed funds are actively managed. Strong managers will perform ahead of the index, others will do worse than the index.

With individual shares, it will depend on your skills in portfolio construction, and hence they are arguably higher risk than an ETF that tracks a broad based index.

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