Switzer Super Report

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Buffett's buying

The data continues to show that investors are flocking to fixed-interest investments. But not legendary investor Warren Buffett. He buys! But in today's see-sawing market, SMSFs need to be smart about which companies they sink their money into, so today I've got 18 high yielding dividend stocks for you to consider.

Also in the Switzer Super Report, Paul Rickard has some advice on whether you should buy Origin Energy's new hybrid notes, Charlie Aitken names two hot stocks to buy right now, we pick the best Australian high-income generating ETF, look at whether you should invest in property or contribute to super, and our new expert Andrew Bloore runs over your obligations as an SMSF trustee. Enjoy this bumper edition!

Sincerely,

Peter Switzer

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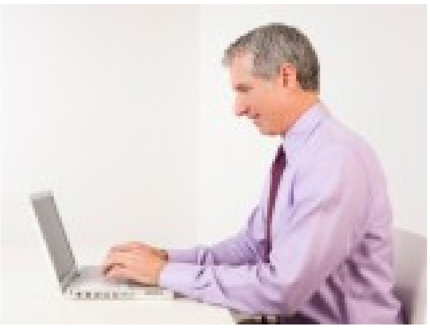

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Warren Buffett and 18 high yielding stocks to buy

by Peter Switzer

Let's get real; if you had a Warren Buffett approach to investing you would sell all of your stocks and go to term deposits and wait. The 'Oracle of Omaha' maintains that if you don't understand it, don't invest in it and, at the moment, if you can't understand Europe and its potential to hurt or help your portfolio, then you should head for the safety of fixed interest with a bank.

Right now the stock market is trying to fight the forces of gravity powered by the uncertainty of Europe and now there's the potential negative input from the so-called Super Committee in the US that has to come up with a fiscal austerity plan or else a program of automatic cuts will be implemented in 2013. If you can recall early August, it was the combination of the Congressional impasse on austerity measures and Greek debt concerns that sent the market hurtling down.

On 8 August, our stock market gave up $35 billion of share value with stocks diving 2.9%. The next day we endured a 5.5% slump at one stage before we got that weird 269-point gain by day's end! We are in strange, inexplicable days and it makes me think of the Buffett advice: "If you don't understand it, then don't invest in it".

However, just this week the US billionaire revealed on CNBC that his listed Berkshire Hathaway investment company has plonked $US10.7 billion into IBM shares since March. Clearly, as I have been suggesting to my brave-hearted clients, viewers, listeners and readers, he has been buying the dips. He has been true to his other pearls of advisory wisdom: "Be fearful when others are greedy and be greedy only when others are fearful," and buy good quality companies that you want to "go into business with".

And how worried is he? Well, not enough to stop him about buying some 64 million shares in IBM, which means he now holds 5.5% of this IT giant!

Right now there are so many issues that could hurt our wealth building goals and they include: rising bond yields for Italy and now Spain; the November deadline for the Super Committee; recession news out of Europe; and political tomfoolery from the 17 countries in the eurozone.

Against that, the US and China are growing better than expected while even Japan revealed this week that its growing at an annualised rate of 6%. At home, the Reserve Bank of Australia (RBA) has woken up and is cutting interest rates that should help those stocks beaten up by both high interest rates and a very strong dollar.

Obviously, if you can't take the heat of the stock market, get out of the boiler room and wait until someone like me says that the worst is over. You could miss the bounce, but on the other hand, this newsletter might just give you the heads up so you don't miss all of it!

I'm telling my clients that if they can wait for the capital gain from stocks to eventually kick in — and it will — let's hold good dividend paying stocks and recognize that as long as you can cope with possible capital loss in the short-term, the yield benefits each year will soften the blow. Eventually capital gain will roar back and the losses will be wiped from your bottom line and even your memory.

Finally, recently on my *SWITZER* program on the Sky News Business Channel, Tom Elliott the CIO of Beulah Capital gave us 18 good dividend stocks and here they are:

1. Telstra (TLS)
2. Westpac (WBC)
3. National Australia Bank (NAB)

4. ANZ Banking Group (ANZ)
5. Commonwealth Bank (CBA)
6. QBE Insurance (QBE)
7. AMP (AMP)
8. ASX (ASX)
9. Woolworths (WOW)
10. Wesfarmers (WES)
11. Coca-Cola Amatil (CCL)
12. Sonic Healthcare (SHL)
13. Orica (ORI)
14. Transurban (TCL)
15. Woodside Petroleum (WPL)
16. Santos (STO)
17. Computershare (CPU)
18. Brambles (BXB)

You can listed to what Elliott had to say about these companies on Super TV.

Important information: *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. For this reason, any individual should, before acting, consider the appropriateness of the information, having regard to the individual's objectives, financial situation and needs and, if necessary, seek appropriate professional advice.*

Should you buy Origin Energy's hybrid notes?

by Paul Rickard

The rush of new hybrid issues continues, with Origin Energy being the latest to announce an offer with a headline grabbing interest rate of around 8.7%. As we have noted in previous issues of the Switzer Super Report, there are more hybrid issues to come – although with Christmas fast approaching, this may be the last before February.

Origin is a leading integrated energy company. It supplies gas and other fuels to wholesale and retail customers, generates electrical power and it is also the largest energy retailer in Australia. On a market capitalisation basis, it ranks 15th on the ASX at around $15.6 billion.

Origin is seeking to raise $500 million through the issue of 'Origin Energy Notes' and will use the money in part to fund its contribution to the Australian Pacific LNG Project. Further, these notes will be classified as 'equity credit' by the Ratings Agencies, which will support Origin in maintaining its corporate credit rating.

The Notes will pay interest at a rate of between 4% and 4.5% above the 90-day bank bill rate. The institutional book-build on Tuesday will set the final margin. At the lower end of 4%, this implies an interest rate of around 8.7% for the first quarter. At the higher end of 4.5%, the interest rate would be 9.2%. On paper at least, this looks pretty attractive.

Details of the issue are as follows:

Origin Energy's hybrid notes

Issue Size	$500m, with right to accept over subscriptions
Security Type	Dated, unsecured, subordinated, cumulative notes issued by Origin Energy Ltd
Listing	ASX, stock code ORGHA, expected 21/12/11
Issue Price	$100 per Note
Term	20 December, 2071
Expected Redemption	20 December, 2016
Interest	Paid quarterly, 20 Mar, 20 Jun, 20 Sept and 20 Dec
Interest Rate	90 Day Bank Bill rate + Margin
Margin	Range of 4.00% to 4.50% (set in book build)
Ranking	Behind all senior debt, creditors and NZ$ Preference Shares, ahead of ordinary shareholders
Offer Opens	23 November, 2011
Offer Closes (scheduled)	5.00pm, 12 December 2011
Issue Date	20 December, 2011
Minimum Subscription	$5,000 or 50 Notes, then in multiples of $1,000 or 10 Notes

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Origin Energy as a corporate entity is rated BBB+ by Standard & Poor's, and Baa1 by Moodys. This is classified as 'investment grade', but well down on the rating achieved by Woolworths, whose recent hybrid issue was priced at a margin of 3.25% over the 90-day bank bill rate. In overseas markets, some other note issues by Origin are effectively being priced by the market at a margin of around 7%. That said, retail investors can't access these wholesale issues.

Origin's diversified portfolio of energy businesses and generally sound financial ratios should provide comfort to investors. The company's interest coverage ratio (which is its ability to cover its interest payments) at 30 June was 6.6 times, and the adjusted gearing ratio was 23.9%.

An important feature of these Notes is that Origin Energy must defer payment of all interest if its corporate credit rating falls below 'investment grade'. If this happens, Origin can only resume paying interest if it regains its investment-grade rating, or assuming it has the capacity to pay, after five years have elapsed.

Non investment grade (or junk status) under the Standard and Poor's methodology is a rating of BB+ or lower. I should point out that this is three notches below Origin's current corporate credit rating of BBB-.

Further, investors can probably take some comfort from Origin's statement in the prospectus that if "Origin's financial profile materially deteriorates and it believes one of its corporate credit ratings risks being below investment grade, Origin intends to take measures to avoid this, including asset sales, further equity issuance, discontinuation of certain businesses, suspension or ordinary dividends, etc.".

So, where does this issue fit?

While definitely being in the higher risk category, it is pretty hard for retail investors and SMSFs to find comparable investment margins. I think this issue will be swallowed up. However, I caution that there are more issues to come, so keep some powder dry. Given the risk profile of these notes, they should be part, but not a major component, of a diversified portfolio of fixed income securities. The old adage "don't put all your eggs in the one basket" applies.

Two stocks to buy today

by Charlie Aitken

The most under-reported story in global finance remains the growth of the US economy, US corporate earnings, and Wall Street's year-to-date performance. I realise good news doesn't generate press ratings or web hits, but on Tuesday night there was again further evidence of the US economic recovery and Wall Street rightly reversed its opening European sentiment-driven losses.

With 70% of US gross domestic product (GDP) being consumer spending, it's very encouraging to see October retail sales up 0.5% (above the market estimate of 0.3%) on the back of September's retail sales that rose 1.1%. Interestingly, electronics sales rose 3.7%, which is intriguing because huge short positions remain in US and Australian electronics retailers, including JB Hi-Fi and Harvey Norman.

Also worth noting was the Empire State manufacturing index, which rose for the first time in five months. I continue to believe US GDP forecasts are too pessimistic. Don't make the mistake of underestimating how important economic recovery momentum in the biggest economy in the world is. The S&P500 is up 0.3% for 2011, but where do you see that written in the financial press or doomsday blogs? **Westfield** (ASX:WDC) remains my top recommended way of playing this US economic recovery.

Commodities liked the US data, with copper and oil rising. The Aussie dollar again underperformed commodities, which is good for Australian commodity producers. But the biggest move following the US data was the spot price of iron ore, which rose by 5.8% to $146.30t.

I have seen all sorts of excuses from global broker hedge fund desks (who had iron ore targets of $90t) about why the rally in spot iron ore is unconvincing. The simple fact is spot iron ore bounced off the marginal cost of Chinese production ($120t) and is headed back to $145-$150t. The Chinese started restocking low steel mill inventories two weeks ago. There are MASSIVE short positions in pure play iron ore equities and the risks of a violent short squeeze increases daily. **Fortescue** (FMG), **Rio Tinto** (RIO) and **Atlas Iron** (AGO) remain the most leveraged and shorted stocks to rebounding spot iron ore prices. They all remain trading and fundamental 'buys', as does **BHP Billiton** (BHP).

But if there are two stocks you should add to your portfolio right now, it's these:

Telstra Corporation (ASX:TLS) – Buy

The market remains too bearish on Telstra. Foreign investors continue to increase their weightings in Telstra and the stock also continues to relatively outperform the ASX 200. To me this looks structural and likely to accelerate when Telstra talk to investors and analysts this Friday. I think there is significantly more to come from this stock. The key uncertainties are improving – the NBN Deal, operating trends, dividend, Future Fund overhang cleared. With greater confidence that these uncertainties are improving, coupled with an earnings upgrade cycle, we believe that strong value exists. On this basis we reinforce our strong 'buy' rating

Target price: $3.55

Wednesday's close: $3.17

Commonwealth Bank (ASX:CBA) – Accumulate

Commonwealth Bank of Australia reported a quarterly profit of $1.75 billion this week. At that run rate CBA will either match or most likely exceed fiscal 2011's record profit, which in turn means CBA's dividend payout this year will either match or most likely exceed last year's record payout of 320 cents fully franked. Of course the bank analyst nitpickers can always find some fault with every result, but this result from CBA would be the envy of every bank in the universe right now. CBA is on track to generate a $7 billion profit, has tier-one regulatory capital of 9.85%, and liquid assets of $108 billion. To compare CBA to any European or US bank is simply unfair. This is like comparing a fillet steak to reheated takeaway. I'd be accumulating CBA shares into any further weakness, feeling the $50 technical resistance level will be taken out when the stock goes cum the interim dividend in February.

Target price: $50.80

Wednesday close: $48.62

Another company we have a buy recommendation on is:

Emeco Holdings (ASX:EHL) – Buy

The turnaround at Emeco is now largely complete and the business is positioned to benefit from the growth in demand for rental equipment. Emeco has the scope to recycle $100-150mpa of surplus cash flow into the business for growth and there are clear signs this is occurring. The trajectory in Emeco is clear, with an improving return on equity, strong cash realisation, high levels of production based revenues and further investment in fleet underwriting growth in net tangible assets. We retain our Buy rating on this stock.

Target price: $1.39

Wednesday's close: $1.005

JP Goldman

Which high-income ETF is best for your SMSF?

by JP Goldman

Given growing demand for steadier income returns from those approaching or in retirement, a suite of high-income exchange traded funds (ETFs) have hit the market over the past year.

Using their own proprietary stock selection methodology, these ETFs attach a higher weight to stocks with relatively large and steady dividends – such that each ETF provider aims to match the overall market's piece returns over time, though with a higher and steadier than average dividend yield.

That compares with the typical capitalisation-weighted ETF – such as State Street's S&P/ASX 200 SPDR fund (ASX:STW) – that attaches the highest weight to stocks with the highest market capitalisation.

All three of Australia's major ETF providers, State Street, Vanguard, and iShares have launched their own version of a high-income ETF – with the respective ASX codes of SYI, VHY, and IHD. Russell Investments was in fact the first into this space with its own high income ETF (ASX: RDY) launched in May last year.

So how can we assess these ETFs? There are a number of criteria.

In terms of cost and liquidity, Russell's RDV is the most expensive with a management expense ratio of 0.46%. That's almost a quarter of a percentage point higher than the cheapest ETF, provided by Vanguard. In terms of market depth and bid-offer spreads, the four are fairly close according to the latest monthly survey by the Australian Securities Exchange.

Of course, Russell's ETF has the benefit of being the first to market, and has so far attracted $160 million in funds under management, while Vanguard's VHY – as the next ETF to hit the ASX – had only $15 million under management at end-October. That said, Vanguard's ETF is backed by a far larger unlisted managed fund founded in 2000, with $340 million under management.

ETF Costs and Liquidity

ETF Provider	Listing Date	ASX Code	MER (1)	FUM ($Am) (2)	Av. Bid/Offer (3)	Depth ($Am) (4)
ishares	09-Dec-10	IHD	0.30%	$31	0.17%	$1,045
Russell	14-May-10	RDV	0.46%	$160	0.26%	$840
State Street	24-Sep-10	SYI	0.35%	$44	0.28%	$417
Vanguard	26-May-11	VHY	0.25%	$15	0.23%	$810

(1) management expense ratio (2) funds under management in Australia (3) average % spread between best bid & offer price

(4) average dollar value of 5 best bids & offers (5) 12 months to August for STW and VAS, year to date for IOZ

Source: ASX ETF Monthly Report October 2011, ETF Provider websites.

So far at least, these ETFs have achieved their goal of providing relatively high dividends. While some ETFs are too new to provide full-year results, over the past year Russell's RDV provided $1.23 in dividends that equated to a 5.3% yield based on the closing price on Tuesday 15 November. State Street's SYI provided $1.76 per share in dividends, implying a yield also around 5.3% based on Tuesday closing price.

That compares with a yield of 4.2% over the past year for State Street's S&P/ASX 200 market capitalisation weighted ETF, (ASX: STW).

It should be noted that by chasing yield, these ETFs often end up with sector exposures different to that of the overall market – typically more in financials and consumer staples, which tend of have higher yields. But each provider also differs in the risk limits placed on each sector. These sector differences may be important, depending on the extent of nature of other exposures in your portfolio.

As seen in the table below, the overweight to financials is most evident for State Street's SYI, while iShares' IHD uses a methodology that under weights financials, while increasing exposure to industrials. Note also that only Russell Investment (not included in the table below) includes listed property trusts in its higher yield ETF.

Sector Break Down

ETF Provider	ASX Code	Financial ex-A REITs	Industrials	Consumer Staples	A-REITs
ishares	IHD	20%	20%	14%	0%
State Street	SYI	53%	11%	10%	0%
Vanguard	VHY	40%	13%	17%	0%
S&P/ASX 200		**31%**	**7%**	**9%**	**6%**

Source: ETF Provider websites.

In terms of price performance over a comparable period, Vanguard's VHY has fallen the least in the market correction since mid-year, while Russell's has fallen the most.

Recent Price Performance

ETF Provider	ASX Code	% change Jun-Nov'11
ishares	IHD	-5.3%
Russell	RDV	-7.1%
State Street	SYI	-5.1%
Vanguard	VHY	-3.3%
S&P/ASX 200		-8.7%

Which one should you buy?

Overall, my choice of ETF for relatively conservative and income needy investors would be Vanguard's ETF. While this is the newest ETF, it's backed by a fund that has been operating for the past ten years and achieved an annualised yield of 5.2%. It's also the cheapest high-income ETF and has relatively greater defensive qualities given its higher weight to consumer staples rather than financials.

Of course, that may also mean this ETF may underperform the overall market during strong bull market periods. But price conservative investors may be willing to pay for steadier yields and greater defensive protection.

Should I buy property or contribute to super?

by Tony Negline

Shane, a 34 year-old self-employed tradesman, asked me an interesting question the other day on Peter Switzer's *The Super Show* on 2GB and MTR.

During the GFC, Shane and his wife watched their super lose a lot of money and they decided they would be better off ignoring the super system. Instead, they bought several residential investment properties with which they plan to fund their long-term wealth-creation needs. The properties are geared, but the rent is paying down some of this debt as well as meeting their other costs.

"There's nothing as safe as houses," Shane said. Nevertheless, he wanted to know if their strategy was a good idea.

On the surface Shane's question strikes at the heart of many an emotional view about where to invest our money. Some of us will passionately believe, perhaps through positive personal or family experience, that Australian property is a sure fire way of building wealth.

Other investors will think that other investment sectors such as equities are the way to go because property can only be traded in large lumps and is difficult to manage.

Personally, I have no strong opinion either way. All investments have their pros and cons.

The reality, however, is that it's inappropriate to compare property and super. I know it's a common point of discussion, but it's not a reasonable comparison.

Why? Property is an asset class much the same as shares are an asset class. On the other hand superannuation is an investment structure that holds asset classes. Your super fund can invest in property if it wishes to do so.

So how can I help Shane make an informed decision? Well an important issue with all investments is to know the costs of buying, holding and selling those investments, especially when it comes to the tax implications.

Property

Typically residential property is expensive to buy and sell. There are many transaction costs, like legal fees, agent costs, architectural inspections, stamp duty and so on.

The tax system potentially provides a range of tax concessions for investing in residential property – building and depreciation allowances as well as the ability to claim various costs as tax deductions. Typical examples may include repairs and maintenance, but not improvements, as well as interest costs on any borrowings.

Importantly, there is no limit to the size of the tax concessions. For example, your interest tax deduction is unlimited and this in itself creates a risk for some enthusiastic investors. Many property investors rely on these tax concessions to make the investment work from a cash flow perspective. That is, if they didn't get the tax breaks, the investment wouldn't work for them.

Another risk is that you might borrow too much. If there is a sharp spike in interest rates or a tenant can't be replaced, then many residential property strategies unravel.

When a property is sold, if it's been held for more than 12 months then only 50% of the net capital gain is subject to capital gains tax (CGT). If your marginal tax rate is 46.5% then this means you would be paying

23.35% CGT.

Super

There are a number of tax concessions for making super contributions, typically tax deductions, but there are tight restrictions on these. The Government Co-contribution is also available.

Super is subject to a flat tax of 15% for non-pension assets and 0% for assets supporting a pension, and after age 60, super becomes fully tax-free inside and outside the super fund. Realised capital gains in the 15% tax part of a fund are taxed at 10%.

Even so, super can be very expensive because many costs are hidden through percentage of asset fees.

As you'll all be aware, super is locked away until retirement, whereas property investments held directly can be liquidated. Access to you investments prior to retirement may be an important consideration for you when determining what to put in or keep out of super.

But what is often not known is that most property concessions mentioned are available to a self-managed super fund and it's possible to borrow money in a super fund and buy a property (read, How to use super gearing to buy property and Top 5 super gearing traps.

If you're interested in holding property in your super fund, remember to consider your fund's investment strategy. Property investments often don't work for super pensions without very careful planning. This is because pensions demand income be paid and this means that ultimately the asset will have to sold, so your investment time frame needs to be considered.

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Your responsibilities as an SMSF trustee

by Andrew Bloore

The choice to set up a self-managed super fund is becoming an increasingly popular one for many Australians who want to take control of their investments.

The major attraction of an SMSF is that you become, as a trustee, your own fund manager, which means you are ultimately responsible for the both the investment decision making and the administration of the fund. There are significant penalties imposed on those who fail to perform their duties properly.

There are many benefits to having an SMSF, such as the opportunity to actively decide upon the fund's investment strategy and to select appropriate asset classes. An SMSF structure therefore means that trustees have a number of responsibilities and duties, so the role of a trustee should not be taken lightly.

Trustees should familiarise themselves with the legislative requirements and administrative responsibilities of running a fund. These rules exist to ensure a super fund's assets are protected until they are needed at retirement.

Here's a list of some of the responsibilities you take on when you start a DIY super fund:

Save for retirement

SMSFs must meet the sole purpose test under superannuation law. The sole purpose test means that a SMSF must be maintained for the sole purpose of providing benefits to members upon their retirement, or to their dependants if a member dies before retirement.

Prepare and implement and investment strategy

Trustees of SMSFs are required to prepare and implement an investment strategy for their fund, and regularly review the strategy. The investment strategy must reflect the purpose and circumstances of the fund and consider the risk, return and liquidity of each investment made.

Record keeping requirements

Trustees must keep some records for a minimum of five years and other records for a minimum of 10 years. This is to ensure that they can verify their decision-making processes and an accurate history of the fund can be established.

Super assets must be kept separately

Trustees of SMSFs must keep money and other assets of the super fund separate from their personal assets and the assets held by employers who contribute to the fund.

Money must not be lent to members or relatives

Trustees must not lend money, or provide direct or indirect financial assistance from the fund, to a member or a member's relative.

Don't borrow money

SMSFs are prohibited from borrowing money, except in some limited circumstances, such as to gear investments. This is to ensure that there is money available to pay out all member benefits when members retire.

Buying assets from a related party

Trustees are prohibited from acquiring assets for their fund from a related party of the fund.

Limited exceptions to this rule include where:

- The asset is a listed security
- The asset is business real property
- The asset is money contributed to the fund
- The asset is an in-house asset and the acquisition would not result in the in-house assets of the fund exceeding 5% of the fund's total assets.

Assets must be bought and sold at market value

The purchase and sale price of SMSF assets should always reflect a true market value for the asset. Income from assets held by the Fund should always reflect a true market rate of return.

Early access to benefits

Trustees must not take money out of their SMSF earlier than legally permitted as it is meant for retirement.

Early access or release of preserved benefits is permitted only in cases of severe financial hardship or on tightly restricted compassionate grounds. These situations occur only in very limited circumstances.

Reporting and administration obligations

All SMSFs need to lodge an annual return with the ATO each year to:

- Report income tax
- Report super regulatory information
- Report member contributions
- Pay the supervisory levy.

Consequences of breaches by trustees can include:

- The ATO issuing fines and penalties and freezing the assets of the fund
- Trustees being disqualified and suspended
- The fund losing its compliance status
- The ATO seeking civil and/or criminal penalties through the courts.

An SMSF trustee should receive professional advice from a financial adviser and proper assistance from the fund's administrator so that they are aware of their roles and responsibilities as trustees and avoid any regulatory penalties.

Did you know?

It's important your SMSF has a clear investment strategy. Find out how to create one through the Switzer Super Report's resource centre. Read, Creating an investment strategy and A sample investment strategy.

Don't miss this!

A Friday lunch you will never forget! Former Prime Minister John Howard, rugby great Ewen McKenzie and media man Harold Mitchell, take the stage in an exclusive national leadership series hosted by Peter Switzer. This is a must-see for anyone in business. Click here for more information.