

# the INVESTORSvoice

Newsletter of the Australian Investors Association - *Investors helping Investors*

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# THE SAFE INCOME BOOM

Marcus Padley

The banks on an all time high. Safe income stocks flying. What is going on and can it continue? This is the question for almost every long-term investor/retiree, can you still buy or are you buying at the top? It is the debate du jour.

Let's give one side of the argument, the argument for the safe income stocks continuing to rally for years to come, the glass half full argument, at the risk of getting you all in at the top. There are a number of factors driving the appetite for safe income stocks and you have to decide if they will last. They include:

- Low interest rates - Low interest rates are core to the interest in safe equities as bonds and term deposit returns fail to deliver on the income expectations of superannuation funds and in particular retirees. You can't live off bonds. The safe equities rally relies on global interest rates remaining at record lows. Will they? You choose.

- The growth in the superannuation industry. The government forecasts superannuation assets to rise from \$1.5 trillion to \$7 trillion by 2030. In other words Super assets will grow by 470% in 17 years, 12.5% compound per annum and they will buy equities. Is that true?

- Baby boomers moving into pension phase. The first baby boomer is now 67. There are 5.5m of them in Australia. 39% are over 60 with another 61% (around 3.35m) yet to hit retirement age. This really is the huge driver for "safe equities", millions of people moving into retirement whose focus goes from accumulation (looking for capital gains) to preserving capital and earning a return on it in order to live. That transformation in focus is driving money from growth and risk to safe income stocks. The growth in retirees is key to safe income stocks and this one is certain, it is happening.

- Growth in SMSF usage. The number of SMSF's grew 8% last year. This is still a transition and it matters because as funds move from managed funds to SMSF the nature of where the money is invested changes to focus more on domestic equities and cash rather than international equities and no cash.

- Risk aversion - As the number of retirees in pension phase grows the risk appetite of the average investor falls away and as it does the priority moves to preserving your capital not risking it. As it does everyone learns that it will not be enough to simply focus on dividends and the size of the yield (the yield trap) but will be a lot smarter than that because they know that a big dividend doesn't mean a safe stock, in fact it can mean the opposite. What they are now looking for is safety before income which means the focus goes to high quality stocks rather than high income stocks. In other words it's no good BHP, RIO and WPL becoming income stocks unless they can afford to. Although all three stocks currently have returns on equity of 15% to 30% retiree investors are going to steer clear of them if those returns on equity are falling (which they are). Its about risk first, not yield.

- Stocks like bonds - What retirees really want are bonds with a high return, but they don't exist, so what they are buying are equities that look like bonds. In other words stocks that provide reliable, safe earnings streams from which they pay reliable, sustainable, safe, affordable dividends which return more than bonds. No wonder hybrids walk off the shelf, they look low risk and offer a higher return. If bonds are priced according to their credit ratings then this is exactly how equities will be valued/differentiated from now on, on risk. Low risk equals higher PEs. You should also note on this basis that volatile, risky equities with unreliable earnings streams (resources) are going to be discounted (they already have been).

I can't help feeling the above arguments are being used to justify past performance rather than predict future performance, it would be typical of 99% of stock market commentary. But it does provide the elements for an interesting debate and explains why it might still be OK to buy at the top, because we are possibly still in the very early stages of this safe equity appetite and it could run for years. Either that or we'll be looking back at this article and saying "When Marcus wrote about it, that was the top!"

“The banks on an all time high. Safe income stocks flying. What is going on and can it continue?”

I was also asked recently "What do you buy when all the safe income stocks look expensive". My answer was "Safe Growth stocks" because as you could doubtless read a hundred times in "Value investing for Dummies" if it existed, ultimately what really matters is not the dividend but how much money a company earns on a dollar (ROE). Whether a company chooses to pay earnings to shareholders as a dividend is a bit irrelevant because if they have a high ROE and are reinvesting cash at a higher rate than the shareholder can achieve then the appreciation in capital value of the company (and the share price) will far outweigh the returns from a dividend yield.

A stock that earns 20% per annum and reinvests will grow by 150% in five years. What would you prefer, a 10% yield per annum and a 60% increase in value over five years or a zero yield and a 150% increase in value over five years. Investors in the pension phase shouldn't care whether a dollar arrives through capital or income, a dollar is a dollar, and as soon as they get their head around the idea that some growth stocks are safe even though they don't yield a lot, then the "Safe Growth" theme will begin (it already has). When it does a lot of growth stocks will come onto the radar of conservative investors. Growth does not necessarily mean risk in which case even conservative investors concerned with capital preservation could buy quality growth stocks in addition to quality income stocks. As they do they will start (already have) to push safe growth stocks in the same way as they have pushed safe income stocks. What that will mean is that quality stocks, emphasis on quality (quality = safe), are going to be driven even harder. As we've written above, as 5.5m Baby Boomers move into pension phase in the next 18 years what they will want are stocks like bonds and the emphasis is not on bond yields but on bond safety.

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## President's Message By Bill Shirley



As winter begins, I hope your expectations in relation to overall investment returns are being achieved in a satisfactory manner.

### Investing in Property

Background – There has been a recent trend for a number of SMSF investors to allocate a large amount of their fund's holdings to the property sector. This approach is further made complex by the large dollar holding required to acquire an investment property and in a number of cases a loan of some type is contracted. This results in a large portfolio allocation towards one type of asset, plus a level debt is included.

I believe we should make you aware that in some cases the above outlined approach could leave some investors in difficult circumstances. Some of the possible issues are briefly outlined below.

**Gearing** - The amount of gearing to be used and set-up costs, if any.

**Interest** – The gearing interest component, also needs to be factored into the Net Return of the property, and funded.

**Legal Documents** - The complex Title, Hands Off & Usage Rules need to be considered, as well as the asset holding costs associated with this structure. (ie: a "bare trust" is used during the loan period.)

**Government Monitoring** – ASIC has signalled its growing concern in relation to possible rogue operators who could be rorting the process. ASIC has singled its intention that it will monitor this trend & fund usage.

**Lack of Asset Diversification** – For the smaller sized fund the possible high property component held within the structure could cause future issues, mainly in the cash flow and allocation areas. (NB. The Median house price in Melbourne is around \$525,000.)

**Cash Flow** - Yearly Yield returns need to be considered, as these could be around 4.50%.

**Pension Mode** – If in pension mode you must have enough cash flow each year for pensions and to maintain SMSF status. (It's a bit hard to sell one bedroom to cover your payment.)

**Property Liquidity** – Due to the cyclical nature of property values the sell cycle may be a very protracted, before a profitable sale can be completed. This matter is a further holding risk that needs to be considered.

**Existing Property** – Most of us live in an owned family home and these assets, plus our SMSF holdings form part of our future estate assets. This total asset picture needs to be considered when purchasing additional property.

**Conclusion** – For example those that have a SMSF holding in the region of half to one million dollars in value, need very careful consideration and review when undertaking a property purchase. The main points could be available yearly cash flow, as well as sector allocation, particularly when purchasing an investment property that will be included within the fund structure. It is understood that each investor has different risk profiles and objectives, however due consideration should be given in reference to a suitable investment direction for each fund or member. This review should enable you to proceed down a path that is suitable to your SMSF investment objectives.



# LONGEVITY

## *The Road Ahead*

David Williams

Over half the women currently aged 50 can expect to live to beyond age 90. More than a third of men aged 50 will also achieve this. After living that long, at least half these 90 year olds could expect to live another four years or so.

Will you be in this half of your age group who are the longer term survivors? What will it be like? What can you do about it?

My Longevity Pty Ltd was developed to help answer these and many other questions about longevity so that informed decisions can be made about the future. Our website at [www.mylongevity.com.au](http://www.mylongevity.com.au) has already provided guidance to more than 30,000 inquiries.

### The dangers of ignorance

Recently a well-known fund manager said "I don't want to live until my eighties – I don't want to be living like a vegetable with a sick body and no mind to speak of".

His ignorance of ageing was typical. Whether he likes it or not, there is a good chance he will live well into his nineties. Furthermore, he has a good chance of being neither sick nor mindless. Whether he sees that as an opportunity or a threat is up to him. Either way, there is plenty he can do in response.

This is a key message – there is plenty we can do. Why are we so confident about that?

### How things have changed

One hundred years ago in Australia, the average baby survived less than sixty years. Today the average survival age from birth is around eighty.

The difference is due to improvements in our standard of living – supported by medical science, economic and social changes and many other human-driven developments. Not all progress has been good, but the overall impact on longevity has been massive. It represents an increase of one third of a lifetime. Even more impressively, the evidence is that this trend in increased life expectancy is continuing.

The really good news is that there is much you can do personally to make this time productive and satisfying. People who understand and respond to the drivers of longevity can make a difference to their lives. The sooner they start, the more likely they are to achieve the outcomes they want.

Our research suggests that about one in five baby boomers don't engage with the idea of longevity. Ignorance-based fear appears to be the main cause. Addressing this ignorance has been a primary goal of My Longevity.

Information about longevity is growing. Even five years ago the word 'longevity' was rarely heard or seen. Today that early trickle has become a torrent of information that washes over us and is difficult to manage.

The real longevity awareness began about ten years ago. Research began in earnest in the 1980's and 90's into the reasons behind increasing community longevity. However it took 20 years for this to be published more widely. Why? Because it takes that length of time for a long term study into people's health and behaviour to produce valid statistics on possible causes of their death or current disabilities.

### Why bother?

A typical person at age 65 would – if they follow the Government Actuary's Australian Life Tables - expect to live for around 20 years.

However, for practical purposes actuaries know that on average this understates the likely remaining life expectancy (which we call longevity) by about three years.

Taking account of the evidence of socio-economic circumstances suggests the members of the AIA should add roughly another two more years. This is because AIA members are likely to be wealthier and better educated than average.

In simple terms, this amounts to an 'error' of five years or 25%. People who plan using the Life Table numbers are potentially significantly underestimating the likely demand on their finances.

Clearly this kind of mis-information has major implications for our community and for our personal planning. So what could be done about this?

### Next Steps

We realised that individuals are not average. We knew that a mountain of excellent longevity research had already been completed. Most of it was not reaching the community in a useful way. So we systematically culled masses of published and unpublished material and categorized it into five major elements.

These are:

**Surroundings** – external physical and social factors

**Health** – the condition of our body and how we manage it

**Attitude** – how we see the present and future

**Parents** – our genetic makeup

**Eating** – everything we put into our bodies

Usefully, the first letters of these elements form the word SHAPE – and so our SHAPE Analyser was born! Based on the five SHAPE elements and some other basic data, the Analyser provides a useful way of showing not only how long a person might live but why this could be so.

I'll be explaining more about our longevity work at the Annual Conference in July. In the meantime, I invite you to visit [www.mylongevity.com.au](http://www.mylongevity.com.au) and, if you are interested, learn more about your own potential longevity. The site is free and sponsor free.

## The access you need

We provide investors with access to a wide range of ASX listed bluechip shares and exchange traded funds through an instalment warrant structure (which can be suitable for SMSFs).

### RBS Investor Products

Instalment warrants are one of the few products that allow investors who are SMSFs to obtain the benefits of gearing. This is due to the limited recourse nature of the borrowing associated with instalment warrants.

Apart from the benefits associated with gearing, interest deductions and enhanced franking credits generated by instalment warrants can be used to reduce earnings and contributions tax liabilities payable by SMSFs. SMSFs can also potentially enhance returns using instalment warrants due to the high level of franking credits generated by geared shares in a low tax vehicle\*.

### Multiple Solutions

RBS Investor Products Platform covers 2000 products/warrants listed on the ASX with different underlying assets giving access to Australian shares, international shares and managed funds.



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# Me & My Portfolio

## Can you beat the Index?

Brian Mc Erlean - AIA Member WA

Index investing.

Here is a challenge. Pick any time in the last century. You are going to inherit a business to last a lifetime. Which business in the world would you chose?

This calls into question longevity, profitability and obsolescence. You don't want the family tree squabbling over diminishing returns. Before responding, let me tell you that a US stock, Pennsylvania Railway, founded in 1846, still holds the record for paying the longest continuous dividend. It paid out every year for 100 years. After a merger in 1970 it went bankrupt!

My choice would be Walmart. It frequents surveys as the best business ever. The imperative is to be in the right industry at the right time. Around 1900 if you had inherited a NSW sheep station you would have done very well, albeit temporarily.

In the early 1980's I visited a stock-broking office in Perth. The elderly stockbroker was kind. He pitied all that financial innocence and determination. He ushered me into the research room which seemed to be wall papered with charts. Being of a scientific rather than economic background, I was captivated. There were charts of individual commodities and some large capitalised stocks stretching back to the early 1900's. It was clear that at different times in the last century if you inherited a sheep farm or a gold mine, an iron ore mine, a nickel mine, cattle station, oil well, sugar plantation or stock in a company with a large capitalisation, you were poorly insulated from the ravages of time, war and commodity cycles.

The bestowed wisdom of the stockbroker is long gone but what I saw on the walls left an indelible impression. Those charts screamed out not to stay too long at the party, be it at the gold mine or cattle station or any of the other commodity driven businesses. They spoke of unpredictability and the need to spread risk.

This wisdom is borne out by the fact that 2/3 of US fund managers can't beat an index fund. An index fund held over 25 years will just about iron out all the ups and downs that make the rest of us insomniacs. A US study found it will average around 10% a year and you can do slightly better at 11-12% with a small cap fund. There is no active management so fees of 0.2% or less are commonplace.

The poor old fund manager on a 1-2% management fee has to beat the index by that margin of agony annually.

Investors that have beaten the index over 15-20 years are legendary and you are probably aware of who they are; Graham, Buffet, Lynch, Neff and so on. Graham lost everything in 1929 and thankfully did not end up in an ICU as his later investing record was outstanding.

**“ There is another way to try to beat the index and that is to assume more risk or attempt to time the market.”**

There is another way to try to beat the index and that is to assume more risk or attempt to time the market.

What is the index fund doing? It is procuring companies as their capitalisation reaches a threshold and chucking them out as they fall below it. So it evacuates the wool company and the newspaper business and it welcomes the communications and mining companies. It eventually evicts them too and introduces new shining stars. ETFs are the Australian equivalent of Index funds and you can check them out on the ASX website where there is a product list with Management Expense Ratios (MER) quoted.

One of my favourite books is written by a Professor of Economics from Princeton University USA.

“A Random Walk Down Wall Street” by Burton Malkiel. Burton was the original proponent of Index funds. Wall St. had no choice but to create them and lose fees in response to his undeniable statistics. DIY investing.

If index funds are not for you there is always value investing. Buy low, circle companies with lots of potential, great ROE and low debt and ride them like a bucking bronco. Then cleverly bail out for huge capital profits and a low CGT in the superfund.

In the early 90's a lot of stocks were trading on high P/Es and low dividends. Many value investors sold. They missed the rest of the decade which delivered some of the best results ever abetted by low interest rates. Value investing can hurt if you bail out at the wrong time.

The best stock is the one you never have to sell. In that way you avoid insomnia, frictional costs and CGT. Such stocks are very rare.

The long term trend is up. Most of my modest gains come from time in the market, adding equity in the dips and allowing compounding to do its fabulous work. I have never sold completely out of the market in the last 25 years. Most losses have come from speculation or staying too long at the party with a stock or sector.

If you elect, like me to do your own stock investing it is beneficial to know what actually works. Index funds held over long intervals offer a clue. Here are a few principals that should improve the odds.

- Time in the market. Ask Warren Buffet about See's Candy, Coca Cola and Gillette. Charlie Munger admitted that most of the fortune was made in a few stocks held over decades.

- Stocks regarded as essential services often do very well thanks to compounding. They are attractive if they can do the distance with high ROE and low debt. Just think of CBA and WOW.

- Topping up in the dips is very beneficial especially when the general market P/E is very low and dividends look good. Fear reared its head in Australia from 2008 – 2009 creating excellent years for buyers. Buffet made huge long term gains by buying after the 1974 and 2008 crashes.

- Never pay too much. Many stock prices will be volatile on an annual basis with a 10-30% spread. I often top up when a stock in my portfolio appears ill e.g. BHP under \$32.

- Watch interest rates. The market has an aversion to high interest rates.

- Investing through a Superannuation Fund is great but don't get locked into an allocated pension by a rule change.

- Consider selling when P/E's are stratospheric or the company is maturing and ROE is dropping. Calculate the CGT consequences. I rely on Robert Vagg's charts to know where the general market is at from an historical perspective. Robert is an AIA member and contributor. A median line of the Australian stockmarket index drawn from early in the last century featuring the 50th and 90th percentiles above and below that line is my favourite.

Only twice in recent history has the market been below the 90th percentile on the low side.

That occurred in 1974 (oil crisis) and it is there now with the All Ords around 5000.

I have a great affinity for the advice of ancient wealthy investors:

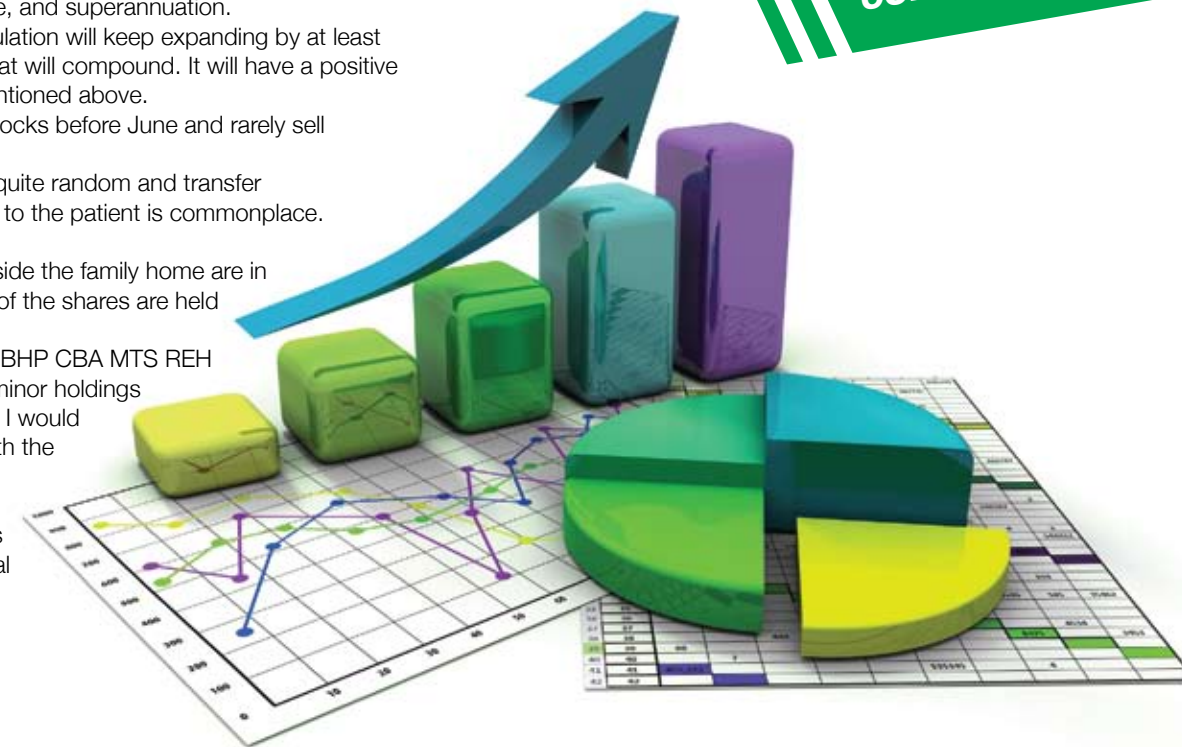
- Don't risk your capital. Preserve it at every turn.
- Don't churn stocks. Buy the right ones in the first place.
- Think about businesses and services that will be in demand forever and that are virtually compulsory to use e.g. food, banking, pharmaceuticals, health care, and superannuation.
- Look for growth. Our population will keep expanding by at least 0.5million per annum and that will compound. It will have a positive influence on the sectors mentioned above.
- Quit the non performing stocks before June and rarely sell the performing stocks.
- Be patient. The market is quite random and transfer of wealth from the impatient to the patient is commonplace.

75% of my investments outside the family home are in Australian Shares and 20% of the shares are held in a Wrap Super Fund.

The share portfolio includes BHP CBA MTS REH ORL FWD WOW BKL with minor holdings in ANG JBH ARP. Presently I would

not buy any of the above with the exception of BHP at \$32. ORL is my only concern.

Please do not accept this as advice. Consult your financial advisor before making financial decisions.



**Me & My Portfolio**  
*continued...*



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## A source of information from experienced investors to help you make informed financial decisions!

While the focus for many investors has been on generating income in a low yield environment, lurking in the background is the ever-present inflation and the need to have some growth in the portfolio to counter this threat.

Asia has almost half the world's population and is expected to provide over half of the world's economic growth for the foreseeable future. A CLSA report estimated Asia's middle class consumers will increase by 370 million this decade, adding another US\$ 2 trillion to spending. Urbanisation is adding over 2 million people to Asian cities every month, with Asian governments responding with unprecedented investment in infrastructure.

According to the World Federation of Exchanges nearly 50% of all the listed companies are Asian, providing 30% of the world's share market value. Yet the MSCI World All Countries Index total exposure to Asia is only 19%, with Japan making up 9%.

We think portfolios are generally under-invested in the world's best growth engine and at Asian Investment Forum we discuss what to do about it, including making specific investment recommendations with no entry or exit fees and no ongoing commissions.

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[www.asianinvestmentforum.com.au](http://www.asianinvestmentforum.com.au)



# WHERE TO for Small & MicroCaps?

Boyd Peters ~ Contango MicroCap Limited



In the February issue of Investors Voice I drew attention to the difference in share price performance between Resources and Industrials stocks, and how the gap between the Large and Small company stocks was similarly extreme.

Following the February earnings season, where revenues were generally in line with expectations, Contango's market view was positive overall. Generally from Large to Small to Microcap stocks there was good value to be found with attractive PE's, EPS and ROEs across the spectrum.

We were quietly positive but cautious overall as we were unable to see then the catalyst that would translate fundamentals into rising prices for small and microcap stocks. In the meantime we continued to observe the market's attraction to yield and the retreat to the safety of large cap household names stocks.

As we come up to the AIA National Conference where my presentation will explore the Value in Small and MicroCap stocks, this article provides the opportunity to see how the 10 weeks since the last article transpired. Did markets rally into Small stocks? Was the "accumulated value" realised? Is there still upside for investors in the Small and Micro part of the market?

The short answer is that April was a horrendous month for Small and Resource stocks. Gold attracted many headlines in April as it suffered its biggest daily fall in 30 years and all commodity groups fared poorly along with gold (-28.1% on average), copper (-21.3% on average), nickel (-22.4%) and iron ore (-17.0%).

At the same time, the S&P ASX 100 accumulation index (+5.1%) notably outperformed the Small cap index (-4.7%) and the differential between Small Industrials and Small Resources shows no sign of ending. The Small Resources sector had the worst monthly returns since October 2008, posting a fall of -20.4%.

The performance of the Large, Small and MicroCap indices can be seen in Table 1.

As at 30.04.13	1m	3m	6m	1 year	3 years pa	5 years pa
ASX Emerging Companies	-10.9%	-18.8%	-20.8%	-31.7%	-8.3%	-6.7%
ASX Small Ords	-4.7%	-7.0%	-2.4%	-9.4%	-2.3%	-5.1%
ASX100	5.1%	8.6%	18.7%	26.0%	7.9%	3.7%

Table 1: Accumulation Indices. Source Contango

While a 12-month return differential of 57.7% between ASX100 and Micro Cap stocks is extreme in itself, this difference is even more pronounced when the Small Ordinaries (ie stocks ASX101 to stock ASX300) is broken into Industrial and Resource performance, as per Chart 1.

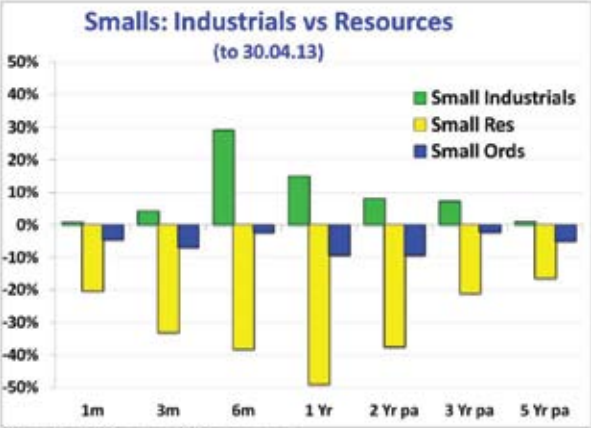


Chart 1: Source Contango

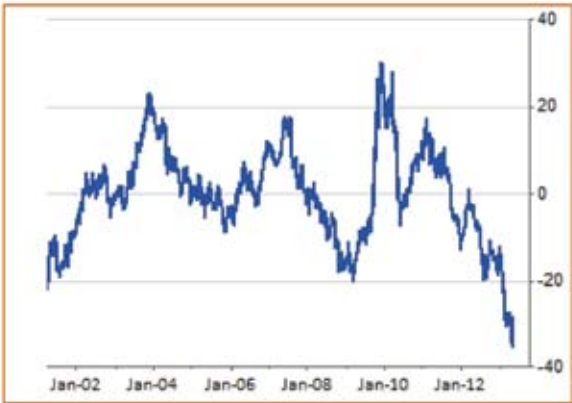
Some investors are asking whether the top 100 stocks will ever come down. The market apparently does not believe so. Equity markets have rallied strongly over the past six months on the back of easy monetary conditions and a more benign risk environment.

The US Fed has made it clear that interest rates will be kept low for an extended period of time. Similarly, recent announcements by the Bank of Japan have added to the abundance of global liquidity. With interest rates at historical lows, investors will continue to seek out higher yielding risk assets, including equities.

For "yield stocks" to reverse it will require a catalyst for their prices to fall in favour of growth stocks. It may be cuts to dividends, earnings downgrades, recommendations for growth stocks, analysts downgrades due to share prices being too high to justify buying more or they could simply stop rising and simply stay where they are and cheaper growth stocks may start to rise. Only time will tell.

## Opportunity in Australian small companies

As we have seen Small Companies are currently out of favour with investors. Chart 2 tracks the difference between the performance of the Small Companies Index and the ASX100 (Total Returns). It is clear that the underperformance of small companies compared to the ASX 100 is historically extreme. What is also visible is that over the past 10 years when small caps have "caught up" their relative underperformance to large caps, they have usually gone on to outperform the large cap index in a relative sense.



Tactically, the market has largely ignored smaller companies while pushing some of our large caps to all-time highs. History suggests that divergence of performance cannot be maintained for the long-term.

While going against the investment tide can feel difficult, for investors with a reasonable time horizon, history tells us there is presently an opportunity in Small Cap stocks. Understandably many investors are looking closer at these smaller companies and asking when, and how much could they go up?

A cursory look at consensus valuations in Table 2 (ie- valuations taken from many brokers and providers of research\*) helps identify whether, based on fundamentals, any particular sector is poised for a positive market return.

This table updates the Consensus valuations shown in the February article to the position 10 weeks subsequent. We also identify the market return in that sector through that time.

Sector Fundamentals	S&P/ ASX 100		Small Ordinaries		Small Resources		Small Industrials	
	25/2	13/5	25/2	13/5	25/2	13/5	25/2	13/5
Index Return in Period (Accum)	+4.2%		-4.5%		-31.7%		+14.4%	
Price/ Earnings	13.6 x	14.4 x	10.5 x	12.9 x	7.0 x	7.0 x	12.4 x	14.6 x
EPS growth	12.4%	12.1%	24.7%	22.1%	96.4%	136.5%	13.0%	12.3%
Dividend Yield	4.7%	4.6%	3.8%	3.9%	1.1%	1.1%	4.7%	4.4%
Return on Equity	14.3%	14.1%	12.0%	11.4%	9.9%	7.5%	12.8%	12.6%

Table 2: Source Contango

While only as good as the data provided, the information in Table 2 identifies that, across Micro, Small and even Large cap stocks there is value to be found, with attractive PE's, EPS and ROEs across the spectrum. Small stocks in particular suggest a positive outlook in FY14.

Boyd Peters ~ Contango MicroCap Limited continued...

This table highlights the conundrum for investors who fear entering the market on the back of compelling valuations, only to see forward earnings growth projections deteriorate. Notwithstanding that risk, investing in quality, well-run businesses, with earnings and sales growth potential in industries that provide quantifiable upside opportunity is rarely a bad investment strategy, irrespective of short-term market returns.

At present, the market is obsessed with yield. Barring global shocks to the economic system, at some point in the near future, investors may decide that earnings are indeed sustainable and that prices are compelling enough to forge their re-entry to the smaller part of the market. At that point considerable pent up value may finally be realised for long-suffering investors.

My presentation at the 2013 AIA National Conference will focus on Small cap earnings and valuations, and how the second half of 2013 is looking, and if/when the pay-day finally comes, how much upside still remains. I look forward to seeing you there.

Notes and Disclaimer:  
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## INVESTOR or TRADER?

Alan Hull

This article is an extract from Alan Hull's latest bestselling book, 'Invest My Way'.

The word 'Invest' actually means to, 'Apply or use money for profit' which includes any money making endeavor which requires money. So to describe yourself as an investor could mean that you've had to spend money to start your own business, you're a property investor or even a Tradesman who owns his own tools. Hence the tag, 'Investor' is not a very useful definition.

However the word 'Trade' means, 'Buying and selling for profit' which does make for a useful definition. If I say I am a share trader then I am stating that I buy and sell shares for a profit which sounds ridiculously simple but there are deeper implications to this statement. For instance, if I am buying shares with the intention to sell them at a future date for a profit then they must be rising in value. The funds management industry refer to this type of share as a 'Growth stock' because, hopefully, the share price will grow over time.

A share trader qualifies as a type of investor because they are applying money to the Stockmarket in order to generate a profit. Contrary to popular belief, a person who deals in shares is not defined as a 'Trader' by the number of trades they perform each year. This definition was created by a certain Government department and, whilst it may serve their purposes well, it is very misleading for the rest of us. If you purchase a share with the intention to sell it at anytime in the future for a profit then you are a share trader. The value of the share must go up over time and you could sell it after 1 week, 1 year, 10 years or even longer.

If we define a share investor as someone other than a share trader then I think it would be fairly sensible to view investors as 'Asset managers'. So unlike a share trader who will sell shares that start to fall in value, investors will buy more shares because they represent a cheaper income stream. So a share trader wants to buy a rising share price and an Investor (read asset manager) wants to buy a high income yield which occurs when the share price falls...perfectly opposed objectives!

Furthermore as investors have no intention of selling, unless the income yield becomes unacceptable, one can safely assume that their preferred holding time is forever. And 'forever' just happens to be Warren Buffett's favourite holding time as well...not really surprising as he's very much an investor and not a trader.

Numeric Example

- Assume that a company pays an annual dividend of \$1.00 and the share price is \$10.00
- Hence the dividend yield or income yield =  $\$1.00 / \$10.00 = 10\%$  per annum.
- Now assume the share price drops to \$8.00 but the dividend is unchanged, a not unlikely scenario given that a company's profitability isn't directly linked to its share price.
- Therefore the dividend yield would increase to =  $\$1.00 / \$8.00 = 12.5\%$  per annum

So if you want to buy a high yielding stock, referred to by Fund Managers as an, 'Income Stock', then the direction of the share price is largely irrelevant because you don't really have any

intention of selling the share at a later date. In fact if the share price was to halve during a Stockmarket crash you would buy more shares because the yield will have doubled.

This is where 'Dollar cost averaging' is used very effectively because you keep buying more shares as the share price drops and the dividend yield keeps rising, thus averaging up your income. Hence dollar cost averaging is a very effective technique for investors...but not traders.

Thus, given the opposed objectives of traders and investors, you can appreciate the importance of knowing which category you belong to. Too often I see investors using trading tactics and traders using investing techniques. So next time you buy a share, ask yourself first; am I an investor or a trader?

“ The word **INVEST** actually means to **APPLY** or **USE** money for **PROFIT** ”

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# It's A New World For Commodities

By Rudi Filapek-Vandyck, Editor FNArena

Another oft repeated prediction amongst those same strategists, commentators and economists has been that commodity prices will "remain at elevated levels". This is not so much a prediction (even though it has been dressed up as such) as an observation of today's high-cost reality that it takes a lot more effort, time, technology and capital to dig up stuff from deep underground and that is why prices for energy and base materials can never go back to where they were during the nineties.

The words are correct, but the implication is dead wrong. A third "misunderstanding" I'd like to nominate is that we're now entering the phase of increased output volumes after years of multi-billion investments the world around. Again, this is strictly correct but is misleading for equity investors and their advisors who think this will translate into strong earnings growth for the companies involved.

It may lead to earnings growth, but only if the projected growth is both substantial and achievable. Newcrest, for example, still has substantial growth potential up its sleeve but right now too many disappointments have cost shareholders too much money, so the market's focus has shifted to management's credibility which, by now, must be at an all-time low.

Deutsche Bank analysts recently concluded both BHP Billiton and Rio Tinto should be able to achieve significant growth numbers in the years ahead as both sector juggernauts enter their "fastest volume growth phase ever". But investors should note the ability to do so depends on two key components: achieving targeted production increases AND substantially lower operational costs.

Many smaller players in the industry don't necessarily have that second option at their disposal.

Even then, a closer look into the details of Deutsche Bank's projections, all the way up until 2020, shows a remarkable shift in underlying dynamics for these "fastest volume growth phase ever"-companies: gone are the days of 20%, 30%, 40% or higher growth years. Instead, Deutsche Bank's projections show one single high growth number (FY14 for BHP Billiton after two consecutive years of sharply declining EPS growth) but apparently the overall coming decade will be one characterized by only low to medium single digit growth years. Similarly, Deutsche Bank is projecting two years of negative growth for Rio Tinto out of the next seven.

This is what "substantial volume growth" looks like in an environment of weaker prices.

In today's 24 hour media world that is increasingly centred around extreme outcomes and potential possibilities, such as: "China - hard landing or not?", surely the biggest surprise of the past two years has been the relentless underperformance of mining and energy stocks.

This underperformance makes it a bit odd when strategists, market commentators and economists try to reinstate their credentials by reminding everyone they predicted China would not experience a hard landing, don't you remember? Well, ermmm, yes, but Rio Tinto shares are now back in the mid-\$50s and they were a lot lower not that long ago. Atlas Iron shares are significantly below \$1 and have been a lot lower too. It's probably best that I do not even mention the current share prices for the likes of Newcrest, Alacer, OZ Minerals, et cetera. As many among you know from firsthand experience, many stocks further up the risk scale have tales of absolute horror to tell.

No surprise then that many analysts believe the boards at both companies will increasingly play their dividend cards. Both BHP Billiton and Rio Tinto are projected to have billions in free cash flow between 2015 and 2020. For BHP in particular there should be enough room to combine financing further expansions with pleasing shareholders through extra dividends and other forms of capital management.

On Deutsche Bank's projections, Rio Tinto's annual dividends will steadily increase by 50% between 2012 - 2020. BHP's projected increase is smaller, but that's because it is the better dividend payer of the two, right now.

Investors should note it is not that unusual for dividends to make up an important part of shareholder rewards at BHP Billiton and Rio Tinto. Throughout the nineties dividends were responsible for 50% of total returns for the ten years leading up to the new millennium. Since 2006, dividends have made up close to 100% of total return.

Yes, I know, nobody ever buys resources companies for their dividends...

Analysts at Goldman Sachs recently lined up the key characteristics for the sector during the era that has now been relegated to history, plus they nominated what they believe are likely to become the new characteristics for the era that lies ahead.

In their terminology, such were the ten key characteristics of the past ten years:

- The BRICs (Brazil, Russia, India and China) phenomenon
  - Short aluminium and long iron ore
  - UK the new home of mining finance
  - The A\$200k truck driver - cost inflation
  - Emergence of the commodities ETF
  - Spot pricing for the bulks
  - Focus on capex, not dividends
  - Contracting P/Es
  - Super Cycle = Super M&A Cycle
  - Bye bye hedging
- And these will be important issues for the years ahead:
- Growing environmental awareness
  - Mining in a carbon constrained world
  - Potash
  - Resource nationalism
  - Recycling and the threat of alternate supply
  - Mining's technology revolution
  - The need to mine in more 'exotic' locations
  - The rise of the mega project
  - The return of high interest rates
  - Can N11 become the new China?

The cycle is not over, the analysts assure us confidently, it's just evolving. That may well be the case, but it surely looks like the years ahead will be very different from the years in the past. Seven out of the ten items lined up for the years ahead imply either upward cost pressures, elevated risks or downward pressures on product prices. This equates to seven more reasons why large cap miners look better equipped to deal with the sector's challenges as industry dynamics change, and Goldman Sachs analysts agree wholeheartedly.

While the BRICs have been solely responsible for starting this Super Cycle, Goldman analysts note the past decade also saw very, very loose monetary policies. This may well change in the years ahead. Equally important is that

## It's A New World For Commodities continued...



the BRICs will now pass on the baton to N11, which stands for Next 11, comprising of countries Bangladesh, Egypt, Indonesia, Iran, Mexico, Nigeria, Pakistan, Philippines, Turkey, South Korea and Vietnam. It is Goldman's view these 11 will keep demand for commodities high, but they will not trigger a repeat of the impact Chinese demand has had since 2003.

The analysts are tipping that potash might become the new iron ore. Please note also: shale oil and gas didn't even make the list. FNArena provides unique tools, data and analysis that assist investors who do their own research. [www.fnarena.com](http://www.fnarena.com)

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## INVESTING SYSTEMS PART II - KEY COMPONENTS

LEE M. SPANO  
Private Investor & Creatness CEO



In our earlier article, Investing Systems Part I - Introduction, you might recall, we explained the importance and use of systems for investors and traders. We also identified five key principles to assist you to develop your own system or systematised approach. In this article we will explain succinctly the often overlooked system components, which are covered by the term, expectancy, or more precisely Mathematical Expectancy (ME).

### The Concept of Expectancy

So many people speak of an 'edge' to your trading or investing approach, an expectancy, or something which ensures long term success. We are usually presented with a myriad of fundamental or technical factors or indicators, which often conflict and vary widely. This leaves us confused, frustrated and often left alone to try to find a sustainable and personalised approach. This might explain, in part at least, why most still fail in the long term. The key question which so often eludes us is: precisely what is a positive edge or expectancy, how do we find it and then integrate it into our system or approach to the financial markets? The concept of expectancy as defined through Mathematical Expectancy (ME) will assist us in this regard.

### Defining Mathematical Expectancy (ME)?

Mathematical Expectancy involves designing an approach or system which can, as a matter of probability, provide to us profitable returns over the longer term. The formula commonly used is:

$$ME = ((1 + AW / AL) \times SR) - 1$$

We want ME to be > 0.2

Where: AW = Average Win, AL = Average Loss; SR = Success Rate.

Let's explain ME in words. ME is about comparing average wins to average losses, ensuring that the average win amount is larger than the average loss amount, and then also ensuring our average number of successes is maximised. An example will assist.

Suppose, over the last 12m or so, your approach to stocks for instance produced an average win of \$1,000, and an average loss of \$500. You had a simple success rate of 50%. Then the ME of your approach or system would be:

$$AW = \$1000, AL = \$500, SR = 50\%$$

$$ME = ((1 + 1000/500) \times 50\%) - 1$$

$$= ((1 + 2) \times 50\%) - 1$$

$$= (3 \times 50\%) - 1$$

$$= 1.5 - 1$$

$$= 0.5$$

An ME of 0.5 is greater than the threshold of 0.2, so you have an approach or system with a positive expectancy. So, over time, there is a good probability you will be successful with this particular approach or system.

### Maximising ME

It is important to note that we must focus on the average win amount and compare it to the average loss amount. The individual amount of each successful trade or investment is not so important over the long term. This leads us to two important insights.

First, we should shift our focus away from each individual trade or investment. Instead we should focus on a series of trades or investments over the longer term. This will help us with psychological vagrancies, such as trying to find the 'big winner' or finding it hard to deal with losses, even several small losses. Second, it forces us to look at maximising our average wins and minimising our average losses. You will see from the ME formula, that if we maximise the numerator (AW) and minimise the denominator (AL), then we can still have a positive ME, even if we have a low success rate, say below 50%.

This is a simple proof of the common adage: 'let your profits run and cut your losses.'

### Which Approach or System?

If we now clearly understand Mathematical Expectancy and how to maximise its variables, this begs the question: what approach or type of system will help us achieve a sound ME?

We do not have the space here to explore the many methodologies used in the financial markets, but let us examine perhaps the most popular one- a Trend based system or approach.

Simply stated, a Trend based system involves: (a) finding and defining a valid trend; (b) finding a sound entry point in that trend- usually a point of weakness; (c) entering with one or more trade or investing lines; (d) then holding onto that trend as long as it is still valid, and usually compounding profits.

The key question for all Trend systems is: what constitutes a valid trend? Again, we do not have the space to examine this question in detail, suffice to say combining tested technical (chart based) signals and then combining them with sound fundamental principles, is a good start point.

So, if we embark on a Trend based approach will this move us towards a sound Mathematical Expectancy? The answer is clearly yes because Trend based systems inherently do the following. First, they maximise the Average Win (AW) variable by letting profits run. Second, they minimise the Average Loss (AL) variable by cutting losses short usually through stops. Third, if soundly built, a Trend based system will have a good Success Rate (SR), usually between 30% to 60%. The other important benefit of longer term Trend based systems is that they allow you to easily compound profits, for instance through multiple lines of trades or investments. Importantly, you will observe solid risk and trade management is the key for Trend based systems to maximise ME and its variables. For instance, a sound risk to reward ratio (RRR) of usually more than 2.0 will mean the Average Win (AW) is greater than the Average Losses (AL) over the longer term.

### Summary - 5 Steps

In our two part series we have hopefully given to you some valuable insights into how to ensure or start to build a robust trading or investing system for the financial markets. We will summarise things in the following steps:

- Understand how systems or a systematised approach can greatly assist with discipline and consistency. Putting your approach into a written trading or investing plan is a crucial starting point.
- Apply the five principles relating to how to build a system or approach personalised to you and your objectives.
- Understand Mathematical Expectancy and apply it to your current or new system.
- Maximise the ME variables, especially the Average Win (AW) / Average Loss (AL) ratio.
- Finding a trading or investing methodology which can maximise ME, such as a sound Trend based system.

If you move through these steps diligently, you will be armed with key insights and have practical parameters which will assist you to become a successful and independent trader or investor in the long term.



# SUPER is your future!

Josh Vrsaljko - CEO ZAC Investments

In these current days of financial volatility, a greater number of investors are finding investment in property a good hedge on inflation and also a provider of positive cash flow to help them build and ready their portfolios for retirement. Because of its ability to perform financially over time, as well as its tangibility, property investment has become a favourite with many investors. As more and more Australian's are looking for greater control and value from their superannuation, a Self-Managed Super Fund (SMSF) appears to be the retirement investment vehicle of choice. In 2012 there was a net increase of 37,174 SMSF's for the year, or 3,097 per month, making over 470,000 Superfund members to date. A self-managed super fund is your own personal Superannuation Fund that gives you total control over how your super benefits are invested.

Residential property is one of the fastest-growing investment assets of self-managed superannuation funds, as Australians combine a love of property with the need to fund their retirement. Share market losses during the global financial crisis and a familiarity with property have aided the trend. We all live in a home and so we believe we understand property, but the biggest driver of this growth has been the change to borrowing rules, introduced by the Federal Government five years ago, that allow leveraging in property inside a SMSF.

The change allows self-managed super fund structure to take out a loan to buy an investment property asset. Why should you consider a self-managed super fund?

It allows you to manage and grow your future superannuation and gives you control of your superannuation funds. As superannuation is the one of the better tax structures around if you are looking at a pure net return from your asset, property held within a SMSF can be a good option.

## What are the benefits of borrowing for property through your SMSF?

While advantages will differ from person to person, the advantages include:

- The ability to leverage an asset
- Tax savings and benefits
- It provides diversification of investment from shares or managed funds
- 10% capital gains tax if the property is held for more than 12 months and potentially nil tax if the property is sold when the fund is in pension phase.
- Tax deductible interest costs
- The bank or lender has no recall to other assets in your SMSF in the case of default
- Depreciation on the property is a huge advantage
- Rent generated from the property does not count as a taxable contribution.

Investing in property is especially helpful to consumers who are not particularly happy with inconsistent or negative returns from their particular industry Super Fund.

Do you know how much your current superannuation is paying in fees and charges?

Last year alone, \$17 Billion worth of fees and charges were generated from managed industry super funds. Superannuation Retail Funds that invest in managed funds charge an average fee of minimum 2% pa and growing. The only reason this sort has been allowed to go on for so long, is that the fee is usually taken out of the balance before the net amount is credited to your account. So you never actually "pay it" and therefore you never notice what you are actually paying.

Buying an investment property inside super compared to outside super is beginning to look better and better. The advantages provided by super are important questions for investors to consider.

So, just what are the advantages and tax benefits?

All expenses related to the property are tax deductible. For pension mode, when the property is maybe sold, there won't be any capital gains tax as it would be charged if held outside a SMSF. Alternatively, in pension phase you can choose to keep the property investment which will make the income earned tax free. This also does not happen on a property sold outside your SMSF.

There are a few restrictions regarding buying an investment property inside super versus outside super. The main restriction is that neither the purchaser nor anyone related to the purchaser can live in a property owned by the super fund. Unfortunately, this restriction applies to holiday properties as well. The property must function purely as an investment property only.

Can you borrow to invest in property?

Yes you can, but there are some things you need to take into account.

Does your super fund assets have the cash flow and capacity to service the loan? The bank will value the property and decide whether the rental income and any additional super contributions you make can service the loan.

Property may be purchased as an income-producing investment asset. Investment property can be held directly through the direct purchase of real estate, or indirectly; purchased through a self-managed super fund.

Returns from property investment can be in the form of income and capital growth and depreciation. Over the years property has demonstrated an ability to generate a reasonable and reliable income that grows at least in line with inflation, together with steady capital gains. Rental income generated from the property can be off-set by tax deductions and depreciation on a new home.

Indirect ownership through units purchased in a self-managed fund is especially useful for those investors who are unable to gain access to investment in real estate in any other way. Borrowing money is a great way to create wealth through property using a self-managed superannuation vehicle. It means you are able to borrow up to 80% of the dwelling, so you potentially can own a \$400,000 asset with an investment (deposit) of only \$80,000.

So, for all investors considering buying a residential investment property, buying an investment property, inside a SMSF would appear to be a win-win situation. The tax benefits are considerable and recent legislation changes seem to favour these investments more every year.

Industry funds are getting more involved with SMSFs and designing products for this huge market. Its popularity is not only with the Australian public, but also now with the trend evident with industry funds. It shows that a SMSF can be a great investment choice.

# INVESTING with MOMENTUM

with Nick Radge

It's little wonder that some investors are confused when it comes to the path of stock prices. If we use two common dictums of Isaac Newton we can see the contradiction: an object in motion tends to stay in motion, yet what goes up must come down. So will a share price keep going up or will it go up then come down? And if it comes down will it go back up again?

Understanding the journey is an important factor for successful stock market investing. For example, we can ask a non-biased computer, programmed with our research, a simple question, "If I buy a stock going up will it keep going up?" The answer is that, "Yes, buying a stock already exhibiting strength has a 63% chance of continuing to go higher over the following year". On the flip side, if we buy a stock exhibiting weakness (a stock with a falling share price) there is only a 48% chance of the stock price being higher after a year. In other words, a statistical edge is achieved by buying stocks already travelling up rather than buying stocks travelling down.

However most people believe they are buying a bargain when purchasing a stock that has fallen in price. Under general market conditions buying a quality company exhibiting weakness can result in an eventual profitable outcome. However, this concept only works well until it doesn't. As we saw in 2008, most stocks just kept falling, some as much as 70%, and others that fell into the abyss never to be heard of again.

A fact not readily recognised by most investors is that stocks that fall into the abyss all exhibit the exact same trait, namely, they decline for an extended period of time. In other words, they don't just disappear one day without warning but trend down over many months if not years. HIH, OneTel, ABC Learning and even Hastie Group, all had the same long term downward trend before declaring bankruptcy. Have you looked at the Billabong stock chart lately?

An investor can gain a statistical edge by hitching a ride on a stock that is trending up and jumping off that ride when the stock price starts to reverse.

“Understanding the journey is an important factor for successful stock market investing.”

Momentum investing has been well documented over the last 10-years and successfully used by a fringe group of investors for the last 40-years. Momentum refers to the ability of a stock to outperform other stocks or the market in general. For example, since the dire lows of March 2009 Commonwealth Bank (CBA) has risen some 160% whereas BHP Billiton has risen just 86%. Commonwealth Bank has shown substantially more momentum than BHP and has therefore been the better investment over the last 3-years.

Momentum exists purely because of investor's expectations that the share price will rise for some reason. This expectation can be based on valid or invalid reasoning which is why it is difficult for fundamental investors to capture. Momentum reflects investor sentiment and is only quantifiable after the fact. It cannot be scientifically calculated, meaning it can't be predicted ahead of time. Some investors wait many years for a fundamental shift to occur and to be reflected in the share price. How often have we heard what a stock should be worth, or should be doing, yet it is failing to actually do so? We only need to look back to 2007 with so many high company valuations yet here we are 5-years later still waiting for stock prices to rise.

So how do we know which stocks to buy? We can never be certain, but research shows that future leaders, a CBA versus a BHP, exhibit higher momentum traits earlier. They rise at a faster rate and earlier. As an investor, rather than focus on why certain stocks should rise (a normal human trait) we simply need to be cognizant of which stocks are moving faster than others and hitch a ride on those stocks.

Back in mid-2010 Iluka Resources (ASX Code: ILU) was trading at \$5.00. Some analysts valued the stock at \$4.00 yet over the following months it rose to \$18.00 almost without pause. The reason why the Iluka stock price rose is not important and clearly analysts had no idea that changed investor sentiment was brewing. If you had listened to the analysts you may have overlooked buying Iluka whereas momentum investors would have bought, enjoyed the ride to \$18 and hopped off when the stock price turned down and hit their trailing stop.

## Adding a Good Defence

Every great sporting team has two core strategies to compete and secure victory; a great offense and a solid defence. Without one, the chances of success are limited. The same factors are required for successful stock market investing.

Consider, though, the average fund manager lost between 40% - 50% during 2008. A 50% decline in capital requires a 100% gain just to recover. Over the (very) long term the stock market has an annual price rise of about 8.5% which means it will take 3100 days, or over 8-years, to get back to where you started, assuming an average rate of return. This is a long time in anyone's investing life, but it also presents a lot of angst and pressure for those nearing retirement.

This shows is that many fund managers lack a good defence. But here's the rub; we as individuals are actually in a much better position to outperform those fund managers.

Many investors are unaware that a fund manager's mandate is to invest in stocks at all times rather than just during the good times. When a downturn occurs their strategy is to switch to defensive stocks or those that go up a little in good times yet don't decline so much in bad times. Common defensive stocks might include Woolworths, Coca-Cola Amatil and CSL Limited. However, when we get a significant price shock event, such as the GFC, there is really nowhere to hide in the market, even if invested in defensive stocks.

The safest place in a downturn is in cash. But, as we already know, fund managers do not have a mandate to invest in cash. However as a retail investor, you can invest in cash during uncertain times. You can play a good defence. How? By recognizing and riding trends and using a trailing stop to get you out when the trend turns down.

Nick Radge is Head of Trading & Research at [www.thechartist.com.au](http://www.thechartist.com.au). He has been in the industry for 26 years. His latest book, *Unholy Grails – A New Road to Wealth*, is receiving excellent reviews. Nick will be presenting 2 fully disclosed momentum strategies at the AIA Annual Conference.



# Is Retirement DEAD?

Rosemary O'Connor

Advances in medical sciences and improving healthcare are driving longer life expectancies.

By 2030, the average Australian life expectancy is anticipated to be 84.5 for men and 87.8 for women respectively. While the over 65 age group represented 14% of the population in 2011, the Australian Bureau of Statistics estimates this figure will be around 24% in 2056. One important implication of this trend is the retirement savings gap, where there is a shortfall in sufficient savings to enable a comfortable retirement.

Not only are we living longer, generally, we are also living healthier for longer. In addition to the retirement savings gap, there is a growing 'retirement time gap' where people can expect to enjoy relatively good health for an extended period beyond age 65.

Many of the leading edge Baby Boomer generation - those now aged 60 or more - reject the traditional notion of retirement. They want to continue to be engaged with the world, to use their hard won skills and experience in productive ways, and to have the option to earn extra income.

Increasingly for these people, traditional retirement - the gold watch at 65, playing golf and tending the garden is seen as akin to a living death. As Phil Ruthven, founder of IBISWorld has said, "Who would want to be retired for 30 years?"

It is noteworthy that growing numbers of older workers say they will never retire. The most recent Australian Bureau of Statistics (ABS) Survey of Retirement and Retirement Intentions shows that 13.3% of people aged 45 and over say they intend never to retire.

## The 'Encore Career'

Regus, the international provider of flexible and virtual work locations and services, refers to "third place" locations as a significant avenue for growth. While the office and the home are seen as first and second places respectively, Regus defines the third place as being anywhere else, for example, a café, a park or a railway station. New technologies, having revolutionised communications, facilitate this trend. Businesses and individuals are delivering services and interacting via the virtual world. Fast broadband and devices such as smart phones and tablets, are increasing access to information and enabling greater work flexibility. Teleworking is growing. We are now less constrained by time and place. Flexibility is the great enabler. We only have to look around us to see examples of this trend. Hotel lobbies, cafes and other public spaces are frequently used

for business meetings, to check emails and access news services and other information.

Longer life expectancy, greater health in later life, and technology advances are creating a broader range of options than ever before. Work locations can be anywhere we like. The internet, ready access to information and the dramatic growth of online businesses are changing our lives. Meanwhile, starting a business, and reaching potential clients has never been easier.

Those leading edge Baby Boomers who reject the traditional retirement models are taking advantage of these factors to create encore careers.

## What is an Encore Career?

Marc Freeman, CEO and founder of Encore.org is credited with coining the term "Encore Career" in the USA. The New York Times has described him as "the voice of aging baby boomers who are eschewing retirement for ... meaningful and sustaining work later in life." The Encore.org website states that encore careers combine personal fulfillment, social impact and continued income, enabling people to put their passion to work for the greater good.

Encore.org cites a recent study that indicates that up to 9 million people aged 44 to 70 in the USA have already chosen encore careers, with many more millions planning to do so in coming years.

While in the USA there has been a greater focus on the social good, and leaving the world a better place, a broader concept of encore careers is gaining popularity in Australia. This encompasses a flexible approach where paid employment or self employment, whether part or full time, is a significant part of the equation. ABS and other research show that there are quite different motivators expressed by high income and low income Baby Boomers concerning their later year careers or retirement plans.

High income Boomers are more likely to embrace a change of career, or career reinvention, which may include paid work, income from private business activities, pro bono work and mentoring of younger people. Low income Boomers are more likely to perceive they will have to continue to work beyond retirement age purely for financial reasons. Their choices are much more constrained by necessity.

While the term encore career is not yet in common use in Australia, many older people are now engaged in one, whether they know it or not. From my own experience and observation, often those individuals, who have a choice, continue some involvement in their former field of work on a part time basis. Along with this, they spend more time on developing their knowledge and skills to better manage their finances (for example, they frequently have self-managed super funds), and doing voluntary work in areas they wish to support including the arts, charitable organisations and local community groups.

How do people make this transition to an encore career? As the great racehorse trainer, Colin Hayes was fond of saying; "The future belongs to those who plan for it."

There is no roadmap or well worn path to planning later careers, and it tends to be a very individual process. While some make a seamless transition, others struggle, especially in the early years. A small number of people get professional advice to help clarify their goals and to map out a plan.

## Some Conclusions

While traditional retirement is far from dead, there is a clear trend towards older people delaying retirement and working for longer. Whether this is from financial necessity or choice, there are significant implications, not only for these individuals themselves, but for policy makers, service providers and businesses. The leading edge Baby Boomers are a large group and the numbers following them are even greater. Those organizations that recognize the changing landscape and develop quality targeted services will benefit. Providers of financial services should take note!

Rosemary O'Connor ~ Member AIA

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**Advances in medical sciences and improving healthcare are driving longer life expectancies.**

# Demystifying aged care

Louise Biti

Increasing life expectancies and improvements in medical technology mean we can expect to have longer and more productive retirements. There is however, still a high chance that help will be needed with daily living activities and/or medical care, especially at older ages.

For some people this may mean accessing aged care services at home. For others it may require a move to a residential care facility.

Careful planning of your finances will provide you with more choices and greater control over where and how you live and receive care. It may also create opportunities to decrease the fees and/or increase your government benefits.

How likely is it that you will need care?

Approximately \$1million retirees in Australia access aged care services. Of these people, around 215,000 live in residential aged care with 70% classified as high-level care.

## Did you know?

At age 65, the chance of needing aged care during your remaining lifetime is:

- 68% for a woman
- 48% for a male

Women have longer life expectancies and on average live longer than their husbands - this increases a woman's chance of needing care.

*Source: Australian Government Productivity Commission Inquiry Report: Caring for Older Australians, 28 June 2011.*

With these sorts of odds, it is never too early to start thinking about your options and putting plans in place, either for yourself or for a family member.

Can you afford aged care?

The cost to care for someone in a residential facility can be as high as \$225.75 per day (\$82,399 per year) but luckily these costs are heavily subsidised by the government. The Federal Government currently spends over \$12 billion a year on aged care. This is in addition to costs incurred by care providers for building and maintaining the facilities. With the percentage of Australia's population over age 85 set to triple over the next thirty years the pressure on finances is increasing and changes to the fee structures have been proposed by Government.

If passed into legislation, the new rules will apply to people entering aged care from 1 July 2014. The current rules will continue to apply to those receiving care before that date.

What is the value of financial advice?

Not all investments have the same impact on the fees you pay or the age pension you receive. Understanding the implications of selling or keeping the home and how to invest any surplus cash can therefore alter how much disposable income you can create and how much you have left in your estate.

Take for example Agnes who has \$100,000 in the bank and a home worth \$780,000. If she decides to sell her home when she moves into care to pay a \$350,000 accommodation bond and puts the rest of the money into the bank she will lose around \$319 per fortnight in age pension and pay daily care fees of \$758 per fortnight.

However, with some good financial planning advice, Agnes could decide to invest in an annuity that is specifically designed for people moving into aged care. Compared to the bank account option, this reduces her fees by \$129 per fortnight and she gains a small age pension increase of \$22 per fortnight.

All this, without reducing how much is still available in her estate to help her children after she passes away.

It is important to work with a financial planner who has expertise in aged care because the interactions between Centrelink (or Veterans' Affairs), taxation, aged care fees and estate planning can be complex.

Good advice may also help to remove much of the stress faced by families when looking at aged care and can help you to make a smoother transition.

How should your family be involved?

Working out which care option is most appropriate and how to structure your finances is often best solved as a family. You should decide in advance to have a family meeting and talk to your children, their partners and other close family members.



Having open discussions with your family can help your children to know what you want and help to minimise disputes among your family members.

The list below might get you started with things you should talk about as a family:

- What is important to you when making a decision where to live?
- Who should be responsible for making decisions - about your finances and/or medical / lifestyle requirements?
- How your estate will be distributed?
- Where you keep copies of all your important paperwork - including your will, bank account details and copies of insurance policies?
- What should happen with your home if you can no longer live there?

Remember that by the time you need to move into aged care, it is probably your children who will need to make the arrangements and the decisions.

What can you learn at the conference?

Aged Care Steps is the leading provider of aged care support to financial planners, accountants and lawyers. Attend the AIA conference session on Demystifying Aged Care Strategies to help you understand what is involved in gaining access to aged care, the steps you need to take and the financial opportunities available, including how that annuity works.

This knowledge can get you started if you need to help a family member with a move to care or outline the practical steps you need to take to plan ahead and be prepared for the future.

Financial aspects are only one consideration when preparing for your care years. It is also important to consider your family needs and estate planning considerations as well as access to other government benefits and concessions. These are all decisions best made early and not just when the move to care is needed.



# Calendar of Events

Date	Event	Time	Venue	Topic
<b>JUNE</b>				
01-Jun-13 - 02-Jun-13	Trading and Investing Expo	10.00 - 5.00pm	Brisbane Exhibition Centre, Cnr Merival & Glenelg Streets, South Bank	Members can download free tickets via the website
04-Jun-13	Adelaide Information Meeting	7.00 - 9.00pm	German Club, 223 Flinders St, Adelaide (Wolf Blass Weinkeller Room)	Non Residential Property Investment
04-Jun-13	Perth Information Meeting	7.30 - 9.30pm	Wembley Downs Tennis Club, Cnr Morden & Ednah St, Wembley Downs	John Abernethy from Clime
05-Jun-13	Brisbane Information Meeting	1.30 - 3.45pm	Broncos Leagues Club, Fulcher Rd, Red Hill	Colin Nicholson: How to find and assess good prospective investments in the stock market.
11-Jun-13	Melbourne Information Meeting	1.00 - 3.30pm	Telstra Conference Centre, R1, L1, 242 Exhibition St, Melbourne	TBA
12-Jun-13	North Shore Information Meeting	7.00 - 9.30pm	The Chatswood Club, 11 Help St, Chatswood	Colin Nicholson: How to find and assess good prospective investments in the stock market.
12-Jun-13	Gold Coast Information Meeting	9.30 - 11.30am	Robina Community Centre, Robina Town Centre Drive, Robina	Stephen Jennings
14-Jun-13	Sydney One Day Seminar	9.00 - 4.30pm	SMC Conference & Function Centre, 66 Goulbourn St, Sydney	Estate Planning, Protect your wealth
15-Jun-13	Brisbane One Day Seminar	9.00 - 4.30pm	Broncos Leagues Club, Fulcher Rd, Red Hill	Improve your investing skills
<b>JULY</b>				
02-Jul-13	Adelaide Information Meeting	7.00 - 9.00pm	German Club, 223 Flinders St, Adelaide (Wolf Blass Weinkeller Room)	Chris Hall
02-Jul-13	Perth Information Meeting	7.30 - 9.00pm	Wembley Downs Tennis Club, Cnr Morden & Ednah St, Wembley Downs	TBA
03-Jul-13	Brisbane Information Meeting	6.30 - 8.45pm	Perpetual Private Wealth, Level 15, Central Plaza 1, 345 Queen St, Brisbane	Perpetual Private Wealth
10-Jul-13	North Shore Information Meeting	7.00 - 9.30pm	The Chatswood Club, 11 Help St, Chatswood	Stock valuation workshop - Clime Analysts
28-Jul-13	Gold Coast Seminar	1.00 - 4.30pm	Surfers Paradise Marriott Resort & Spa, 158 Ferny Ave, Surfers Paradise	Building Blocks of Financial Security, Hints, tips and Strategies to begin to fast track your financial freedom.
28-Jul-13 - 31-Jul-13	<b>AIA NATIONAL CONFERENCE</b>	Opens: 5.00pm Sun 28-Jul-13 Closes: 4.30pm Wed 31-Jul-13	Surfers Paradise Mattiott Resort & Spa 158 Ferny Avenue, Surfers Paradise QLD	Where To From Here?
<b>AUGUST</b>				
06-Aug-13	Adelaide Information Meeting	7.00 - 9.00pm	German Club, 223 Flinders St, Adelaide (Wolf Blass Weinkeller Room)	David Middleton
06-Aug-13	Perth Information Meeting	7.30 - 9.00pm	Wembley Downs Tennis Club, Cnr Morden & Ednah St, Wembley Downs	Mike Young will cover the broad investor concepts
07-Aug-13	Brisbane Information Meeting	1.30 - 3.45pm	Broncos Leagues Club, Fulcher Rd, Red Hill	TBA
13-Aug-13	Melbourne Information Meeting	1.00 - 3.00pm	Telstra Conference Centre, R1, L1, 242 Exhibition St, Melbourne	TBA
14-Aug-13	North Shore Information Meeting	7.00 - 9.30pm	The Chatswood Club, 11 Help St, Chatswood	Regina Meani - Using technical analysis to your advantage in the market
21-Aug-13	Gold Coast Information Meeting	9.30 - 11.30am	Robina Community Centre, Robina Town Centre Drive, Robina	Simon Bylsma - Smart Strategies for SMSF Investors
03-Sep-13	Adelaide Information Meeting	7.00 - 9.00pm	German Club, 223 Flinders St, Adelaide (Wolf Blass Weinkeller Room)	TBA
03-Sep-13	Perth Information Meeting	7.30 - 9.00pm	Wembley Downs Tennis Club, Cnr Morden & Ednah St, Wembley Downs	David Chia
04-Sep-13	Brisbane Information Meeting	1.30 - 3.45pm	Broncos Leagues Club, Fulcher Rd, Red Hill	TBA
11-Sep-13	North Shore Information Meeting	7.00 - 9.30pm	The Chatswood Club, 11 Help St, Chatswood	Rudi Filapek-Vandyck The big confusion that is the Share Market

As AIA events are confirmed, details are posted to the AIA website [www.investors.asn.au](http://www.investors.asn.au). Please note topic is subject to change.



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