Cuffelinks
Connecting investors with ideas

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## This Week's Top Articles



## Interview with David Bell, CIO, AUSCOAL Super

### Graham Hand

*David Bell recently became Chief Investment Officer at the $8.5 billion AUSCOAL Super (AUSCOAL) fund. Previously, he ran his own consulting business and spent 12 years at Colonial First State.*

GH. Investing is an art as much as a science, how do you come into a business and bring your subjective opinions into an existing investment process?

DB. My first step is to make use of the asset management tools we have, and to realise the strengths and weaknesses of the science. Then you introduce the art. You have subjective overlays as you become more experienced. In a super fund, you are working with an investment committee and a trustee board to come to final decisions. An important skill is to explain the strategy clearly to both the investment committee and trustees so they are comfortable with your level of subjectivity. Some traditional trustees may not know the investment science, but they all have the subjective piece. AUSCOAL wants a CIO who can bring the thoughts together and lead the conversation.

GH. Is there anything in the portfolio that surprises you or you feel strongly against?

DB. It's a good portfolio in good shape. AUSCOAL was one of the first super funds to have a default fund which ran a lifecycle strategy and allocated to private assets. After the introduction of MySuper, about 20% of the industry is now running a lifecycle default strategy, dominated by the retail players who put mostly liquid assets into their lifecycle funds. I think there's a lot to be said to have a wider universe of investments, in terms of return and diversification opportunities. As long as you're confident you're being rewarded for it. So it's good that we're already investors in private assets.

GH. How much will you bring market timing into your investments and how will that vary from the past?

DB. In its recent history, AUSCOAL has not been an aggressive market timer. They make small tactical tilts in consultation with the asset consultant, Mercer, and the Investment Committee. It looks like some super funds last year made quite large tactical tilts, and some better performing funds probably did one or more of the following tactical trades: go overweight growth assets, go overweight global equities (even better if the currency exposure was unhedged) versus Australian equities. I'm not going to come here and say market timing is what differentiates AUSCOAL in the market.

GH. People will be encouraged by recent successes to do more market timing, so will you be managing that expectation?

DB. History and academia shows market timing is hard to do consistently. It is also one of those areas where it becomes clear in hindsight. We are probably more focussed on tactical asset allocation for risk reduction, and we will use our tactical budget when we see risks emerging. Even playing defensively you need to be careful. If you get out too early, you can have two or three poor years before you're proven correct. Across the industry there is the risk that a trustee says they can't take the heat. The investment committee and trustee has to come on the journey, buying into the process with you.

GH. How much pressure do you feel to match your competitors, putting emphasis on the peer risk?

DB. Since I've been here, there is more focus on member outcomes and our PDS defines our objective as CPI-plus. But the peer group element is still there. APRA has added to a peer group focus through initiatives such as the product dashboard. Nobody really knows what everyone else is doing, so it is difficult to manage for peer group risk on a forward-looking basis. You cannot be too worried about it and it's not what members want anyway. If we're telling members we intend to outperform a peer group, and in the GFC the median fund was down 20% and we were down 18%, the outcome is not properly aligned. In focusing on outcomes we create some risk that we might underperform peers in a good environment. To manage for this we need to educate – externally to explain to our members how we are contributing to their retirement outcome, and internally across all our staff, senior management and our trustee.

GH. Do you have a feeling this is not a great time to become a CIO with rates so low, US equity markets at all-time high, government debt out of control?

DB. You are challenged to find attractive value at present. But I would reverse the question and say, "Do you want to captain a ship in smooth waters or rough seas, where you can add the most value?" When values are stretched, that's when you want to be there, when members will benefit the most.

GH. Can we drill deeper, with your defensive allocation, where do you put your money?

DB. Fixed income has become challenging, and defensive options are trying to earn real returns but the real returns on cash are currently negative. It's a flat yield curve so taking term risk is not rewarded unless you think inflation will fall. Then you go out on credit spreads but both investment grade and high yield grade spreads are tight. So we start to see it's a tough sector. Predating me, we moved away from managers who have benchmarked portfolios to those who are more flexible, with a total return focus. You might allocate to a manager who has a CPI-plus mandate or a cash-plus mandate. There is so much complexity in fixed income that there is value to be added in this sector by skilled managers. We pay a little more for these mangers but we feel they are a better fit with our objectives. There are some good opportunities in mortgage-backed securities in the US, so we give money to a manager in that space.

GH. Do you always gain exposure to an asset class through managers rather than going directly?

DB. Nearly everything we do is through managers. Generally, the industry funds who are managing money themselves have $20 billion plus and at that level they have a constant debate about efficient implementation. So for example Unisuper with $40 billion manages 50% internally. Some smaller groups such as Equipsuper manage Aussie equities internally.

GH. Do you give global managers currency hedging instructions?

DB. Generally, with global fixed income we fully hedge our currency exposure. Fixed income is low volatility and currency volatility would swamp it, defeating its role in your portfolio. We have a strategic target for global equities. We use a currency overlay manager to make and implement tactical calls around this strategic target.

GH. Are there any asset classes that you feel active asset management is not worth paying for, that you should save your 'fee budget'.

DB. I'm a bit of a contrarian to the marketplace. I'm quite happy to pay higher fees than most for fixed income as I feel there are a lot of opportunities for value to be added. In equities, our managers have done well over time, but the question for me has been how much of that was due to the ability of the manager versus a simple style-based rule. That's something we're working more on. This brings it back to the point about 'science'. Can we use some of these simple style-based rules ourselves?

I think there's more potential for active managers to outperform in Aussie equities than there is in the global space. Much of the academic literature paints a poor picture of outperformance in global equities, where you pay fees without much reward, and our experience has been that active performance in global equities has not been as compelling. So what's the best way to achieve global equity exposure? In recent years, the emergence of smart beta (style-based) strategies increases our ability to assess their true value-add, and also broadens our range of implementation options.

GH. Is it worth paying active fees for other assets such as property and alternatives?

DB. Yes, we have allocations there. But the more you move into non-traditional asset classes, the harder it is to benchmark your managers. For example we have found it difficult to find a good property benchmark which reflects what we are trying to achieve. The benchmark we have is a little more aggressive than our property objectives so you have to be mature to accept that our portfolio will likely underperform in current buoyant market conditions. We have a lot of team experience investing in hedge funds but again you have to really understand what you are getting for that exposure. I see a triangle of risk, return and fees, and one of my roles is to decide the appropriate balance.

GH. Australian super funds have traditionally focussed on accumulation, but more recently on retirement incomes and outcomes. Why doesn't AUSCOAL make its best estimate of likely retirement balance and resulting income and give clients a number they can understand?

DB. There's a lot of responsibility in providing that number. We are pushing down the path to produce the information. But there is much greater opportunity than the addition of a single number to a statement. Imagine if you had a tool that could project outcomes with a range of possibilities, and members could interact with this tool. This may help direct them to a more appropriate portfolio mix. Then if they give us a bit more information, such as their personal balance sheet and savings characteristics, we can give them an interactive tool with a clearer picture. This same system could be used to tailor the design of our lifecycle default strategy, and could also be used by our financial planners. We are building these models at the moment, I'm very excited about it.

GH. Do you think longer term you'll be doing more in-house and having your own traders?

DB. I think there are a lot of good managers out there, and there's a lot to be said for transaction skills. You might lose a lot through execution without realising it. Slippage and market impact costs are not well understood. If we have a good idea, we might use an external party to execute it. I can't see us having ten traders inside the office. So even if we go down a core/satellite approach, we'd likely use a manager to implement the core for little cost rather than do it ourselves. We use mandates rather than unit trusts so we have all the tax efficiencies. I don't think people overcharge for execution, and the big players have purchasing power. There's a lot of operational risk doing it internally, one mistake and it's very expensive. An external manager will generally pay for any mistakes they make.

GH. So have you seen where many of your members work, down a mine?

DB. That part of my initiation is coming soon. There are 2,000 kilometres of tunnels around Lake Macquarie, some two kilometres deep. It's going to be quite an experience.

*In addition to being Chief Investment Officer at AUSCOAL Super, David is working towards a PhD at University of NSW and is a Principal at Cuffelinks.*

## Does your will treat your super fairly?

### Noel Whittaker

It is a common strategy to arrange your life insurance through your super fund. The fund can often buy insurance at wholesale rates, and by using salary sacrifice, you can effectively pay the premiums from pre-tax dollars.

But tax may be payable on the proceeds of the policy if it is left to a non-tax dependant. Often a young single person has, say, $300,000 of death cover through their work super fund. They are unlikely to have dependants for tax purposes, so if they were killed in a car accident the Tax Office would take around $100,000, leaving around $200,000 in their estate.

Where tax is payable by an estate, the tax becomes a general liability of the estate. As a result things can get much more complicated if the deceased is older and the estate does not have the money to pay the tax.

Think about a single father aged 50 with three adult children who all work, and one of them lives at home with him. His house was worth $380,000 in 2008 when his will was drafted. He has $300,000 in super Fund A, and just $15,000 in super Fund B. There is also a $300,000 insurance policy in Fund B – this fund is paying the premiums because it has the smallest balance.

He wanted his will to treat his children equally. Therefore, it was drafted to give the first child the proceeds of Fund A, the second child the proceeds of Fund B and the residue of his estate to child three who was living at home. The father figured that would be the house and the contents and each child would receive roughly the same amount.

Unfortunately, the will drafter did not understand the effect of the death tax on insurance policies held in superannuation.

When the father died suddenly, the children got a terrible shock when they discovered they were not going to be treated equally at all. Ordinarily it would be thought that the first child would receive around $255,000 as the proceeds from Fund A would be taxed at 15%, while the proceeds of the insurance policy held by Fund B would yield approximately $215,000 after the tax of approximately $100,000 was deducted. Life insurance proceeds held within superannuation suffer a much higher tax than ordinary superannuation benefits because they are treated as 'untaxed' and are subject to 30% tax (excluding Medicare levy) when paid to a non-dependant.

Problem 1: Super funds do not deduct the death tax and send the balance to the estate. Rather, they send the entire amount to the estate - it is the estate which has the obligation to send the death tax to the ATO.

Problem 2: Because the will specifically gave "the proceeds of Fund A" to the first child and "the proceeds of Fund B" to the second child, they would be entitled to the whole of $300,000 and $315,000 respectively. The tax still has to be paid, but it won't be coming out of the proceeds received from either of Fund A or Fund B. The executor of the estate has a responsibility of paying $145,000 to the Tax Office ($45,000 death tax on Fund A and $100,000 death tax on Fund B).

Because children one and two have received specific bequests, the tax can only be paid out of the residue of the estate. Using a concept known as 'marshalling', the executor will probably have to sell the home to pay the $145,000 tax bill leaving child three with net benefits of only $105,000. Not only has the third child borne the cost of the tax payable on both of the superannuation payouts, but the family home has been sold to pay the tax bill.

It is critical that anyone drafting a will understands that all assets are not treated equally for tax purposes. The difference between CGT-free assets like the family home, and investment properties that carry a CGT liability, are generally well known. But few understand the tax treatment of insurance policies held within superannuation, let alone the different tax treatment of the various components arising from contributions made to superannuation funds. As the above example shows, failure to take this tax into account can have disastrous and unforeseen consequences.

*Noel Whittaker is the author of Making Money Made Simple and numerous other books on personal finance. His advice is general in nature and readers should seek their own professional advice before making any financial decisions. His website is www.noelwhittaker.com.au.*

## All the world's a stage for peer-to-peer lending

## Steve Ward

No offense to Hamlet, but the question is not 'to be or not to be', but whether to go 'p-to-p'. And Polonius, who 'neither a borrower nor a lender' wanted to be, was equally mistaken.

Today, with the advent of big data, integrated web services and platform technologies in the cloud, a more relevant quote may be:

> *"neither a borrower nor a lender be, unless through a platform that provideth both parties with contractual certainty and a better deal than hadst they used an intermediary such as a bank"*.

Admittedly, back in Shakespeare's day, investors couldn't access a diverse pool of borrowers via the internet. They were pretty much stuck with the rabble at the playhouse. They also couldn't assess those borrowers based on multiple data sources in real time. They couldn't slice and dice the loans easily into small slithers, enabling lenders to diversify risk and apply the law of large numbers to build a portfolio made up of many small loans.

**Bank super-profit pools**

This capability is what allows investors to gain access to asset classes that have previously been the domain of the banks. In Australia in the 2013 financial year, the major banks collectively earned margins of about $2 billion from their Consumer Finance portfolios, which mainly consist of credit cards and unsecured personal loans. These returns have doubled since 2007/08, placing return on equity for the banks on par with retail mortgages. For a large bank like the Commonwealth, Consumer Finance in 2013 made up 20% of its retail bank Net Profit After Tax, despite being only 3% of its balance sheet.

The profitability of personal lending has been increasing due to improving Net Interest Margins (which are about 10x the level of home loans) and losses that are low and stable. According to JP Morgan Research (March 2014), income is approximately two thirds that of the banks' mortgage books.

Investors have only been able to access this asset class directly with the advent of peer-to-peer (P2P) lending platforms, also known as online consumer lending. In Australia, the only platform available today is SocietyOne, although it is expected others will follow.

**A growing phenomenon**

P2P platforms have been expanding rapidly around the world as first individual investors, and now venture capitalists and institutional investors, are pouring hundreds of millions of dollars into equity funding to the burgeoning industry. Over 200 companies worldwide are now building online marketplaces for consumer credit using different models and different methods, pushing into new markets and developing asset classes in exciting new directions from medical loans to solar energy.

The sector is now 'supercharged' with loan volumes to borrowers increasing at rapid rates. The US and the UK (and arguably China) are the world's largest P2P lending markets. Lending Club and Prosper, the two biggest P2P lenders in the US, are growing at close to 200% a year. The loan origination growth for Lending Club has been exponential and now exceeds $1 billion per quarter. It is estimated that P2P lenders will collectively originate US$6.25 billion in 2014, with Europe contributing another $4 billion. At this rate, the sector is predicted to become a US$1 trillion industry globally by 2025. Lending Club has filed its IPO in the US and will list with an expected market capitalisation of circa $5 billion. Early shareholders of the company include Google and Blackstone.

**Understanding the risks**

With a proven track record overseas, the P2P lending model for personal loans is poised for greater traction in Australia as well. In a low interest rate environment, investors continue their search for yield. While RBA cash rates have fallen over the last few years, personal loan rates have remained stubbornly high at circa 14-14.5% with defaults well contained at around 2-3%.

P2P lenders collect a platform fee in the same way as eBay and Uber, enabling investors and borrowers to share the margin that banks would otherwise keep as profit. The investor takes the credit risk and hence takes the majority of the margin.

But as with any investment, interested investors should first understand the risks involved in P2P lending. The key risk is the exposure to loan defaults that diminish the returns and potentially the capital if they are not well diversified. Typical gross returns on unsecured personal loans are 11-12% before defaults, with the overall default rates across the platforms typically 2-4%. It is important to diversify across as many loans as possible to approximate the platform default rate.

Although the investment takes on many characteristics of traditional fixed income products with consistent, predictable and regular cash flows (probably daily if there are hundreds of loans in a portfolio), investors are locked in for the term of each loan, which are generally 36 months. It took five years in the US for a secondary market in loans to emerge and one does not exist yet in Australia. Many investors treat P2P loans as an annuity-type product giving them similar regular cash flows.

When building a fixed income portfolio and selecting term deposits, bonds, bond funds and hybrids (if one considers hybrids fixed income), investors could potentially also consider P2P lending to gain further diversification in loans that are arguably less correlated to other common assets in an overall portfolio.

**New asset classes**

As P2P lending becomes more mainstream, investors will be able to access other asset classes. An example in the U.S. is small business loans, a new segment that Lending Club has recently entered. Other online fintech companies like Kabbage are also increasingly using big data to tie merchant finance to B2B commerce sites like eBay, PayPal and Amazon. This gives the platform real time access to sales, inventory and other data to assist the retailers with lines of credit. The continuing and evolving access to big data will enable more lending products on these platforms, sometimes in niche areas where returns are good and volumes are too small for banks.

A home-grown example of a niche loan product is SocietyOne's P2P Livestock Lending Program developed in partnership with Ray White Rural. The program was developed for the purpose of purchasing livestock with the loan secured by the cattle. An unintended consequence of mandated ID tags on cattle for biosecurity reasons is the fact that a lender can register an interest in the government tracking database and record these tags in the security register. SocietyOne provides a structured program with a robust settlement process giving investors access to an agricultural related investment with low correlation to equity or property markets.

In summary, P2P lending platforms give investors the opportunity to access asset classes that have previously not been widely available. Over time, the range of asset classes available will increase as innovation and competition reveal opportunities in other areas. As always, investors need to do their due diligence and understand the business model, the risks and the products being offered.

*Steve Ward is Head of Investor Services at SocietyOne. This article provides general information and does not constitute personal advice.*

## Company reporting and tired excuses

## Ben MacNevin

Two key themes emerged in the 2014 reporting season that many companies attributed to adverse performance: an unseasonably warm winter and weaker consumer confidence after the Federal Budget. Some even cited a combination of the two.

It was easy to relate to this commentary, as autumn and much of winter felt quite warm and there was plenty of negative media interest surrounding the tough budget. But as investors, it's important to understand if those companies were using temporary issues as an excuse for structural pressures. This concept may seem obvious, but how often is it applied in practice?

Every reporting season is defined by challenges, such as weather, tough budgets, poor consumer sentiment, the threat of higher interest rates, rising unemployment, lower commodity prices, a strong Australian dollar, increased regulation – the list goes on.

But if you held or bought shares in a company after considering that a challenging environment was temporary, did you follow up in subsequent periods to ensure that the company's operating performance returned to expectations? Or did the company point to another set of factors to explain itself, with no reference to previous commentary?

To illustrate, let's delve into the commentary of previous periods to understand what challenging (but temporary) conditions were cited for underperformance. The commentary surrounding these market conditions was just as prolific as the unseasonable weather and tough budgetary concerns in FY14.

In 2013 it was claimed that consumers were cautious during the national election. In 2012, some companies pointed to the minority government, a slowing Chinese economy and European instability to justify their disappointing performance. In 2011, weaker conditions were caused by the carbon tax debate, uncertainty in international financial markets and domestic natural disasters. In 2010, the challenges took the form of abnormal weather and interest rate increases by the RBA.

While many of these events may seem like distant memories, they may have influenced your investment decisions. When viewed with an historical perspective, it can become apparent that temporary events may not be the underlying cause of multiple periods of disappointing results.

When a company continually attributes operational performance to external factors, it is an admission that it does not have a sustainable competitive advantage. This is much like a boat on the ocean, whose movement is dependent on the coming and going of the tide.

Whenever you buy shares in a company, you should believe the company will sustainably outperform the wider market. But how can you generate excess returns in the long run if a company continually references difficult external conditions?

Top fund managers strive to invest in companies with sustainable competitive advantages that can provide meaningful returns during most stages of the market cycle. While these companies are not immune to challenging market conditions, management will typically reference internal forces, rather than external forces, to justify returns.

The unseasonable weather and budgetary concerns from FY2014 will soon fade from company commentary and the market's consciousness, and you can be sure that other challenging market conditions will present in the next reporting period for underperforming companies. We hope the moral of this article is more enduring.

*Ben MacNevin is an Analyst at The Montgomery Fund.*

# Infrastructure debt versus infrastructure equity

## Alexander Austin

This article follows on from Gerald Stack's excellent article for Cuffelinks comparing listed and unlisted infrastructure. Just as investors have a choice between investing in listed or unlisted infrastructure equity, there is also a choice between investing in the equity or debt part of the capital structure.

Investors in infrastructure are generally seeking:

- returns driven by the underlying long term cash flows (ie yield focussed rather than growth focused returns)
- capital stability, particularly compared to equities
- some degree of inflation protection or inflation linkage. Typically underlying revenues of infrastructure assets are linked to inflation and, hence, infrastructure assets offer the prospect of inflation protection.

By definition, equity and debt sum to the value of the asset (or equivalently, the value of equity is the value of the asset minus the value of debt). This means that the characteristics of underlying infrastructure businesses feed through to the characteristics of infrastructure debt and equity investments.

Infrastructure equity:

- receives a disproportionate share of the upside in performance of the underlying infrastructure business
- is more impacted by adverse developments through the impact of leverage.
- must consider the cost and availability of debt finance - during the GFC many of the sharp falls in infrastructure share prices were driven by this factor, rather than by declines in the operating cash flows of their underlying businesses
- benefits from control and directly/indirectly is responsible for the management of the asset.

Infrastructure debt:

- has lower returns (on average) and doesn't participate in the upside of underlying infrastructure asset
- is much less risky (see below)
- is a shorter term investment – with terms to maturity typically 3-7 years. In contrast, infrastructure equity is a very long term investment as assets are usually valued based on cash flow models that go for more than 30 years
- doesn't necessarily benefit from the same inflation protection as the underlying asset – particularly in the case of fixed rate bonds. However, many projects issue floating rate debt where interest payments move with bank bill rates (a rise in inflation would be expected to flow through to higher bank bill rates) or inflation linked bonds (where interest and principal payments are directly linked to CPI).

There are lots of different ways to think about risk. But one way of comparing the risk of infrastructure debt and equity is to look at the performance of listed infrastructure stocks that had floating rate bonds on issue through the GFC. While this is a small sample, only four assets, it does allow the comparison of risk outcomes between debt and equity in the same underlying asset.

| Entity | Equity Risk | Debt Risk | Debt Basket |
|---|---|---|---|
| Sydney Airport | 30.5% SD<br>-55.8% min 12m | 3.1% SD<br>-8.3% min 12m | Nov 2014 FRN<br>Nov 2015 FRN |
| DUET GROUP | 22.6% SD<br>-49.5% min 12m | 3.1% SD<br>-6.8% min 12m | Apr 2017 DBNGP FRN<br>Apr 2018 DBNGP FRN<br>Oct 2014 UE FRN |
| transurban | 20.2% SD<br>-45.4% min 12m | 4.7% SD<br>-6.5% min 12m | Nov 2015 FRN<br>Nov 2017 FRN |
| spark infrastructure | 25.1% SD<br>-42% min 12m | 2.4% SD<br>-3.6% min 12m | Feb 2013 Citi Pwr FRN<br>Jul 2015 ETSA FRB |

Source. Monthly returns July 2007 to August 2014. SD is annual standard deviation. Min 12m is the worst 12 month rolling return in the sample window.

Depending on whether you focus on standard deviation or worst 12 month return, this analysis argues that senior floating rate debt is 4-10 times less risky than equity in the same asset. Of course, this comes with a return trade off.

Just as infrastructure equity has listed and unlisted forms of investment, different types of infrastructure debt (loans versus publicly traded bonds) have differing levels of liquidity and, hence, illiquidity premia.

Which is the better investment? Ultimately that depends on relative pricing and risk adjusted returns, as well as the time horizon and risk appetite of investors. However, many investors tend to think purely of infrastructure equity when considering infrastructure investments and it may be worth thinking more broadly.

*Alexander Austin is Chief Executive Officer of Infradebt. Infradebt is a specialist infrastructure debt fund manager. This article provides general information and does not constitute personal advice.*

## Pension Loans Scheme should have much greater use

### Les Goldmann

Investment in Australian residential real estate ties up an estimated $5.2 trillion in capital and unlocking this capital may hold some of the solution to relieving the pressure on the government's budget. The expected future deficits are partly caused by the looming shortfall in retirement savings estimated at over $700 billion.

Various solutions to over-hauling the Australian retirement system have been suggested including making the superannuation tax concessions more equitable. If it ever passes the Senate, Joe Hockey's budget will enact measures that will reduce the level of the federal government's future aged pension payment commitments while also extending Australians' working lives.

But industry experts are increasingly looking at how equity tied up in residential real estate could become a potential fourth pillar of the retirement system.

Currently the most common method of unlocking equity in the family home is to take out a reverse mortgage. Reverse mortgages can be taken as a lump sum or as an income stream. With no repayments, the capitalising interest on the loan can become ruinously expensive in the long term. But as John Maynard Keynes once wryly observed, "In the long run we are all dead", which is precisely the point.

A less well-known alternative is the Pension Loans Scheme (PLS), administered by Centrelink, part of the Department of Human Services. The PLS allows asset rich (home owners) but cash poor retirees, who miss out on receiving maximum pension payments, to top up their pension income stream to the maximum amount allowable via a loan from the federal government.

Retirees may be eligible if they (or their partner) are of age pension age and have real estate to offer as security in Australia but only receive a part pension. The amount of the loan available may depend on the amount of collateral offered and the age of the retiree. The loan can be paid back anytime but must be repaid either when the house is sold or from the owner's estate when they die.

The pension loan has a 5.4% effective annual interest rate (charged at 5.25% fortnightly), which compares favourably with commercial reverse mortgages interest rate of around 7%. It is likely that the overall uptake of the PLS will increase as the number of Australians that only qualify for a part pension increases, if people know about the scheme.

Think tank, The Australia Institute, has recently floated the idea in their report '*Boosting retirement incomes the easy way*' that the PLS should be made available to all Australians of pension age, rather than just those too well off to receive a full age pension. "The expanded PLS would let pensioners boost their incomes using their own equity, without cost to the budget," says The Australia Institute report.

The report notes however that there may be opponents to an expansion of the PLS on ideological grounds. Economists generally agree that private sector financial intermediaries are the most appropriate distributors of credit across the economy. Maturity transformation is what private sector financial institutions do. The Australia Institute's proposal would involve a further opening up of the federal government's balance sheet to the residential housing sector.

However if the cuts made to the aged pension level in the recent budget begin to bite and the population demographic continues to age, a less traditional economic stance might find favour.

Private sector financial institutions are already stepping up with innovative new home equity release products. A recent Cuffelinks article by Christine Brownfield on home equity release noted some of the difficulties slowing the rate of product innovation, including the small size of the home equity release market currently; the public's emotional attachment to the family home; a lack of product providers, and the current absence of the government backing that may be required to build residential equity into a significant fourth retirement pillar.

In the meantime, the PLS offers a competitive interest rate on flexible terms, and may provide a valuable income top up for many people in retirement.

*Les Goldmann has over 20 years' experience as a Chartered Accountant, and his roles have included freelance journalism, shareholder advocacy for the Australian Shareholders Association and senior roles in the commercial and non-profit sectors. This article provides general information and does not constitute personal advice.*