

This Week's Top Articles

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How to sound smart watching the World Cup

Graham Hand

Russia 2018 is the first FIFA World Cup I have not attended since 2002. The treks around the world following the Aussies are now wonderful memories, with amazing games and sad exits from Germany 2006, South Africa 2010 and Brazil 2014.

My first game remains the highlight, after 32 years away from the World Cup for Australia. That extraordinary day in Kaiserslautern has entered our football folklore. Tens of thousands of Australians covered the town and stadium in a sea of green and gold, the music of Men at Work and The Angels blared through the streets, and we beat Japan in breathless style. Anton Tagliaferro sat behind me and I learned a few new swear words that day. In 2006, the glorious German summer sun shone over fan zones by the Rhine, the steins of beer flowed, and sausages never tasted so good. I was hooked, although arduous criss-crossing of South Africa and Brazil to far-flung stadiums in deserts and jungles were more exhausting experiences.

In 2018, I'm watching the games from Russia in a lounge room in Sydney, with friends who see round ball football every four years. Oh dear, it shows. Explaining the offside rule is quite a distraction in the middle of the game.

The 2018 FIFA World Cup qualifying started in Dili, Timor Leste on 12 March 2015, and 210 countries competed for final places, including Bhutan, South Sudan, Kosovo and Gibraltar making their debuts. Imagine that, a World Cup qualifying game on a rock in the Mediterranean. It's the sort of global coverage other football codes only dream of, with a larger audience than the Olympics. The World Cup brings nations across the globe to a standstill and unites their people. More Australian children play this type of football than any other, but they call it soccer.

It's a time when followers of other codes make mistakes which confirm their ephemeral expertise. They jump on the global bandwagon, suddenly familiar with an eccentric Brazilian forward who a month earlier sounded like a brand of coffee.

For those people who steal the word football for sports that are predominantly played with the hands, here is an attempt to minimise the inevitable embarrassments.

Don't make these common mistakes

Criticism of a shortage of goals reveals a deep lack of understanding. The goal rarity is one of the strengths of the game. Any collector of stamps or coins knows that value comes from scarcity. A goal is a truly wonderful thing, a joy enhanced by its relative infrequency. The knowledge that there may be no other goal in the game heightens the thrill, while familiarity breeds contempt. Many 1-0 games are exciting to watch, nerves jangling at the closeness. Just one goal in open play from Australia against Denmark would have changed the way the nation thinks about this team and its performances at the World Cup.

No informed cricket follower believes a maiden over in a test match is boring because there are no runs. Contrast it with basketball. There is so much scoring, each basket is of little consequence. They even need loud music and a commentator at the stadium to build the excitement. No football fan can warm to basketball for this reason.

The inexperienced do not know how to talk about the game properly. Footballers do not 'kick' goals, they 'score' them. It is only a penalty inside the defending penalty area, otherwise, it is a free kick. Anyone who refers to a direct penalty has misunderstood. Never mention a 'Manchester' player, as the distinction between United and City is vital. There are no umpires, but it is fine to refer to linesmen, as hardened followers have no time for the politically correct 'assistant referees'. All measurements are in yards, not metres, because the English invented the game, not the French.

The rules are intuitive. It is a sport that follows natural instincts rather than creating silly devices like scrums, lineouts and mauls. Handling the ball is only an offence if it is deliberate. A player is not necessarily offside simply because he is in an offside position. A goalkeeper cannot pick up a back pass that has been kicked by his or her own player. That's it. The rest is obvious.

Hints that give a chance to impress

A neat comment may impress. Observe that English players perform better for their clubs than their country, and any speculation on the reason why is acceptable. Express amazement that Italy, The Netherlands and the US did not qualify. Defend the referee's decisions. It is so instinctive to criticise referees that doing otherwise unsettles everybody and offers the beginner a chance.

Contrast the way players in other forms of football use their heads. That's the part of the body that contains the brain. Rugby players are taught to stick it between other men's legs, turning ears to cauliflowers and noses to mash. Proper football players use it to rise high above others and score goals.

The sacred nature of football is confirmed by the official rule that prohibits advertising on the hallowed turf. What a scourge on other football codes that they allow sponsors to plaster their names directly on the pitch. Is it something to read during the game?

Team formations

Nothing baffles the novice more than the way teams are set up to play. When I was a boy, a hundred years ago, there was little variation from two fullbacks, three in the middle and five (yes, five!) forwards. This would be called 2:3:5 now (not counting the goalkeeper), although it is no longer used. Position descriptions such as centre-forward, inside-right and winger are left over from these days.

Then most teams switched to 4:4:2, with only two forwards and four in defense including two centre backs. These became known as a 'stopper', playing just in front of the other three defenders, and 'sweeper', cleaning up at the rear. A more attacking formation might be 4:3:3 pushing a midfielder forward, sometimes called 'playing in the hole'. Recently, three at the back has become more common (England is using this system in the World Cup), but it requires two 'wing-backs' to both attack and defend in a highly-demanding role. In this World Cup, some lower-ranked teams are using 5:4:1 in attempt to stifle strong opponents.

Watch the formation used by four midfielders. Sydney FC has been successful with a midfield diamond structure with one back, one forward and one wide on each side. A joy of attending live football is watching these formations take shape and vary.

What did Australia do under Bert van Marwijk before its group stage exit? It was 4:2:3:1. Four at the back, Sainsbury and Milligan in the middle and the two fullbacks, Risdon and Behich, defending but encouraged to go forward. Two midfielders, usually Jedinak and Mooy, protect the defense. Two wide men, Leckie and Kruse, are

mainly attackers with Rogic behind the lone forward, Nabbout or Juric, hassling the opposing defenders in a thankless slog.

Talking about formations and how they change during the game will move anyone beyond the novice.

The World Cup glorifies the only global team sport

Remember what Sydney was like during the 2000 Olympics? It's like that in an entire country during the World Cup. When the lowest-ranked team in the competition, Russia, won its second game, the nation went into a frenzied celebration. When Mexico beat Germany, seismic disturbance was (apocryphally) detected in Mexico City. Argentina observed a one-minute silence following their 3-0 loss to Croatia. Every team is competitive, whereas the two rugby world cups are dominated by one-sided games.

Football is the only global team sport. We can cheer the Wallabies and the Kangaroos and the Baggy Greens and the Bombers all we like, but the rest of the planet is watching something else. Once every four years, Australians join them. We will rejoice in a glorious month of football, embracing the spectacle of the world playing its favourite sport. Only one of Messi, Ronaldo, Neymar, Ramos, Hazard, Pogba, Muller or Kane can win, and become a national hero forever.

Graham Hand is Managing Editor of Cuffelinks and is not getting much sleep at the moment.

A different version of this article first appeared in the Crikey Magazine on 26 May 2002, under the title, 'Everything you need to know about real football'. Crikey's introduction said: "Graham Hand is better known to Crikey readers for his fabulous bank bashing book "Naked Among Cannibals" but he's also an expat Pom who has filed this entertaining preview to the biggest sporting event on earth."

Opportunities across the capital structure

Christopher Joye

We highlighted in [April 2018 in Cuffelinks](#) how cheap the hybrids market looked, and the sector has since bounced back. Over the first 21 days of June, the Solactive ASX Hybrids Index, which is a market capitalisation-weighted benchmark of all listed subordinated bonds and hybrids, has risen 1.01% (or 101 basis points) compared to the RBA cash rate increase of 8 basis points.

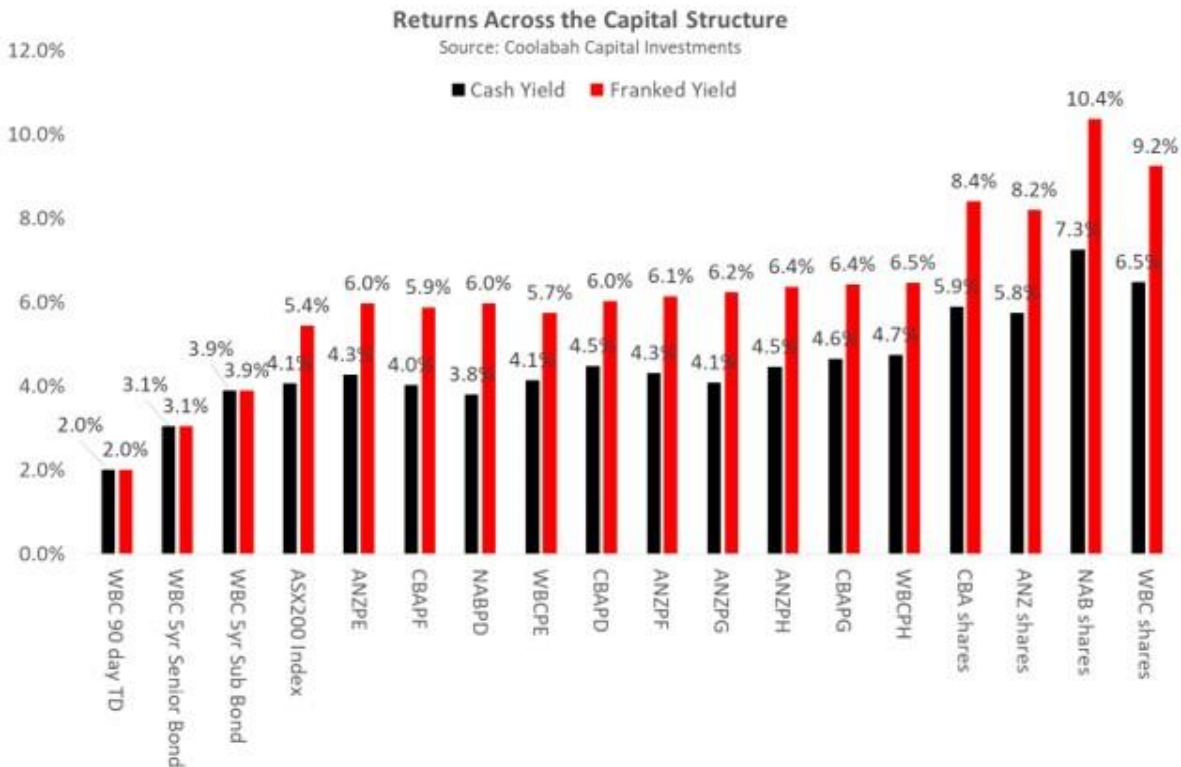
Effects of new supply

A tsunami of \$3.1 billion in new hybrid supply over February and March 2018, courtesy the Westpac and CBA issues (WBCPH and CBAPG), combined with Bill Shorten's threats to remove cash rebates from franking credits, hammered the listed hybrid market down 1.49% over those months.

The market then bounced up 0.69% in April only to endure headwinds again in May after Macquarie launched an unexpectedly large \$1 billion hybrid issue, which resulted in the sector suffering a 0.17% total return loss in that month.

By the end of May, major bank hybrids with five years left until final maturity (or call date) were paying franked spreads above the quarterly bank bill swap rate (BBSW) of 4.06%. This meant that total franked yields were as high as 6.6%, which compares favourably to the franked dividend yield on the ASX200 Index, which at the time was 5.44%. On an unfranked or cash basis, total yields at that time were a similarly chunky 4.9% on hybrids like CBAPD, which was above the 4.07% cash yield on the ASX200 Index despite the fact that hybrids have historically displayed one-quarter to one-third the volatility and downside risk of shares.

After the 1.01% total return over the first 21 days of June, where do valuations stand? The chart below shows the cash yields and franked yields on key ASX hybrids compared to the comparable yields on the ASX 200 index, and the major banks' term deposits, senior bonds, subordinated bonds, and ordinary equities. This gives a sense of the returns available right across the capital structure with each sector obviously having different levels of risk.



Transfer of wealth from equity to bonds and hybrids

Since 2013, I've argued that the major banks needed to significantly deleverage their balance sheets, which they have done, reducing leverage from over 25 times six years ago to around 19 times today. This reduces their returns on equity, which have fallen from 17% to about 13% today. As the return on equity falls closer to their circa 11% cost of equity, the majors also have to trade much closer to book value, which is what has happened. Price to book value ratios have slumped from 3.0 times to around 1.5 times, in what should have been a direct transfer of wealth from the major banks' equity holders to their bond and hybrid holders.

However, the surprising thing is, the much lower risks that the major banks carry today (as reflected by, amongst other things, vastly improved equity capital and liquidity coverage ratios), reinforced by the sale of risky non-core businesses, has yet to manifest in the form of tighter credit spreads, or a lower cost of debt capital.

At the end of 2006, CBA issued a 4-year senior bond at a 0.1% spread above BBSW that today would require spreads that are about eight times wider. In May 2007, CBA priced a lower-ranking subordinated bond with a 5-year call at just 0.24% above BBSW: similar bonds today trade six times wider.

CBA issued its PERLS IV hybrid in 2007 on a spread of 1.05% above BBSW, which is one-quarter of the spread CBA hybrids pay on the ASX today.

The investment thesis

In a world in which most assets, like equities and housing, remain very expensive by historical benchmarks (price/earnings multiples are above 2007 levels), these are pockets of opportunity.

Since the GFC was a financial credit crisis, the best value investments tend to be assets that were most adversely affected by this shock, such as the bonds and hybrids issued by banks and insurers, which are trading well wide of their 2007 levels in credit spread terms.

Christopher Joye is a Portfolio Manager with [Coolabah Capital Investments](#), which invests in fixed income securities including those discussed by this article. This article does not address the individual circumstances of any investor.

Talk to your family about ageing and your will

Don Ezra

Parents are often uncomfortable talking to their adult children about personal matters, but there are many benefits in having such a conversation. It should include our investments and more generally, our goals and plans.

My wife and I first did this some years ago, when I decided to graduate from full-time work. Most retirees find, after time passes, that it's useful to repeat the exercise, as circumstances change and nothing ever works out quite how you projected. It then could become the year's most important focal point.

I realise that some families, particularly in generations past, have found it difficult to discuss personal details at this phase of life with their adult children. Neither my wife nor I ever had such a conversation with our parents.

Our first talk

Our first effort with our own children has gone down in family history as 'Dad's Decumulation Talk'. Yes, as you might guess, I did most of the talking. Just before we started, my wife placed a cartoon in front of me. In it, there's a family sitting around a kitchen table. The youngest one's head barely comes above the table. And Dad is saying: "Before we begin this family meeting, how about we go around and say our names and a little something about ourselves."

I got the message: "Remember you're their father, not a businessman." I'm told I conducted myself appropriately. It became a bonding experience in the family, and we've been able to discuss financial matters with our children, our matters and theirs, ever since.

At the time I gave them a document entitled "Goals and Plans," which we prepared to give them enough background that, if and when the need arose, they could be confident about making decisions for us.

I'm including an outline of what our document contained as an [appendix](#), as some people asked for it when I mentioned it in a talk.

The following is not meant to be a comprehensive list or a substitute for talking to your legal and financial advisers. When I refer to your adult children or other close family members, that's a generic way of saying 'whoever it is that you'd like to have take charge of your affairs, during or after your lifetime'. That might be a professional or a financial institution.

I've found it helpful to think of three dimensions regarding the information to be shared.

1. Where the important documents are

The first is a list of important documents and where they are to be found, preferably in one place, known to your children. This includes government-issued documents relating to your identity (birth, marriage, citizenship etc.) Include in this information regarding assets and liabilities, such as home ownership, cars, bank accounts, savings bonds, credit cards, life insurance, savings plans related to work or retirement, other invested assets, and other miscellaneous things you own.

There are also important legal documents under this heading, such as your will, powers of attorney, and advance directives, like a living will, medical power of attorney, end-of-life instructions, and so on. And contact details of important people, not just professionals like your doctor, your lawyer, your financial professional, but also close friends and relatives.

It's often said that many people die without a will. My father-in-law, who was in the insurance business, told me that everybody already has a will. A will is a document that says what will happen to your estate after you're gone. The law says what will happen, if you haven't written your own document. So think of the law as your will. You do have a will, no matter what you think – it just may be that somebody else wrote it for you. Better to override it with your own wishes!

2. Sharing goals and plans

The second dimension relates to levels of involvement. (I found this at Anderson Elder Law, in an article in their Resources section dated 24 March 2015.)

The least involved level is where your children know where to find the information mentioned above. Next, you may want to share some of the actual information with them, such as your finances and your will. Once you start doing this, you will probably want to repeat the exercise periodically, as we now plan to do. At this stage you're still in full control. It may later become necessary for them to assist you, or to share responsibility for your affairs, or to take over that responsibility completely.

A friend who is going through her own parents' late phase of life reminds me that, in that phase, the relationship between parents and children can change completely. The parents need the children, rather than the other way around. The parents can become fragile and susceptible, and easy to be taken advantage of. The children worry about the parents and have to soothe them. My friend adds, feelingly: "I don't know what I'd do if I couldn't trust someone to take care of me ..."

No doubt, therefore, you will have consulted your children before making the required arrangements and got their agreement to whatever goes into the relevant documents. And you'll have given them a list of the medications you take and ensured that your professionals know they should consult your children and where to find them. It can provide great peace of mind to know that all of this has been discussed before the need for the arrangements to be carried out ever arises, even if one day you may not remember ever having done this.

It's peace of mind not only for you but also for your children, who may be worried about whether they'll have to support you financially at the end. For your children's sake, don't leave this conversation so late that your mental capacity is declining.

3. The 'estate event' (otherwise known as death)

The third dimension involves saving trouble for your executor after your estate event. (I was amused to discover that American insurance agents don't like talking about death. Instead, they refer euphemistically to your 'estate event'.)

Some wills are hotly contested by family members who can't stand one another. You may not be able to solve this conflict while you're alive. The angst that it may be possible for you to spare your executor arises from dividing up your personal possessions or leaving clear instructions about how to divide. Paul Sullivan (in his Wealth Matters column in The New York Times on 15 April 2016) wrote:

"... just think for a second what it would be like on Christmas morning if your children ran downstairs and there were all of these presents, bright and shining, big and small, but with no name tags on them. Can you imagine the free-for-all that would ensue?"

Don Ezra has an extensive background in investing and consulting and is also a widely-published author. His blog posts at www.donezra.com focus on helping people prepare for a happy, financially secure life after they finish full-time work.

**APPENDIX:
OUTLINE OF THE FIRST EZRA "GOALS AND PLANS" DOCUMENT**

1. Introduction: Purpose, summary, appreciation of good fortune, request for intervention if and when required
2. Goals
 - For ourselves: continuation of lifestyle
 - For our beneficiaries: during our lives, and after our second estate event
3. Background
 - What we've done, financially, over the years, and why
4. Our assets and liabilities, their current values and details of where they are located
5. Our lifestyle and other outflows
 - The normal budget for our spending and saving
 - Exceptional planned expenditures
 - Life insurance, long term care, other partial hedges against the vicissitudes of life
6. Lifestyle versus assets
 - Latest "personal funded ratio" calculations (I'll post information about how to calculate these in 2018)
 - Dials to be turned, if things go wrong: why, and how much
 - Caution: transition means this isn't carved in stone
 - Contact details for our financial professional
7. Current and future plans: what, when and how long
 - Work
 - Lifestyle
 - Real estate: downsize, move, perhaps rent, perhaps one day a reverse mortgage
 - Reassess every year, with a big review every 5 years starting at my age 70
 - When to start taking Social Security (that is, the Pillar 1 pension), and why
 - Rearrange the assets at age 70: laddered bonds, equities, deferred annuity; why
 - Where there are still elements of flexibility
 - Reminder of the life abundance portfolio as a framework: family and friends, work and play, mental and physical health, finances

ASIC is not soft: who's next in line for scrutiny?

Claire Wivell Plater

Although recent ASIC enforcement action and the Royal Commission have predominantly focused on the financial advice and lending practices of AMP and the major banks, emerging patterns teach us that non-bank lenders and financial advice firms are the next targets.

How do we know this?

ASIC's approach

ASIC's modus operandi is to first investigate potential regulatory issues within big targets, where misconduct is widespread and evidence is easy to find. This serves as a learning exercise, helping ASIC to ascertain the nature and scale of misconduct, and what to look for.

Investigation complete, ASIC generally releases a report on its findings and concerns. You'd expect that diligent compliance teams would read those reports, look within for similar problems, notify ASIC of any breaches and start a clean-up.

That's what ASIC hopes for too. But, if no one falls on their sword – and the past few years have demonstrated how reluctant financial advice licensees are to do so – ASIC brings out the big guns of enforcement.

Naturally, they'll start with the banks and big targets, who've proven easy to make examples of. But here's the rub. By the time that work is nearing completion, ASIC has a template for investigating smaller players. They know what to look for, where to find it, what questions to ask, with a standard methodology.

ASIC's methodology

It goes like this:

- Require from financial advisers a list of clients and information about the advice (s912C notice) and from credit providers, a list of borrowers and information about the loans from the lender (s266 notice).
- At the same time, require production of policies and procedures dealing with the area of concern (s33/s267 notice for AFSs/credit providers) and production of policies and procedures dealing with the area of concern of past files or loans.
- If their concerns are borne out, some recent files may be requisitioned to see if any improvements have occurred, hoping that by now the firm's compliance team will have acted on the report (s33/267 notice).
- An optional next step is for ASIC to bring the CEO or other senior managers in for questioning (s19/253 examination).
- If ASIC finds breaches which have not been voluntarily reported, enforcement action will follow.

So reading the tea leaves to be found in ASIC's [Corporate Plan for 2017/18 to 2020/21](#), its [Enforcement Outcomes report for July-December 2017](#) and the carnage emerging from the Royal Commission, here's a snapshot of what advisers and non-bank lenders should be looking for in their businesses. If they don't, ASIC will!

Concerns with non-bank advisers

1. Charging fees for no advice – Over 27,000 customers have received a refund of fees charged for ongoing services that weren't provided. ASIC estimates at least 150,000 more refunds will be required, and the problem is not limited to the banks. Selling grandfathered investment trail commission books must be in jeopardy, even if the government doesn't legislate to end grandfathering.
2. Life insurance churning and inappropriately recommending super money be used to pay for life premiums – ASIC now receives regular exception reports on high lapse rates from insurers, from which they've become highly adept at detecting bad practices.
3. Failing to consider whether clients' existing products will meet their objectives before recommending replacement – The minimum standard requires financial modelling of both options and a clear case for change, all of which is clearly explained in the Statement of Advice.
4. Inappropriately recommending SMSFs – It's not just low balances that ASIC is concerned about, as client financial literacy and willingness to manage the responsibilities inherent in an SMSF are just as important.
5. Recommending services that clients don't need or don't value – These could include platforms or simply high ongoing service levels.
6. Recommending in-house financial products to generate extra revenue when there's no additional benefit for the client – Vertical integration is not limited to banks. Advisers who operate Managed Discretionary Accounts (MDAs) or Separately Managed Accounts (SMAs) run the same risks.

Concerns with non-bank lenders

1. ASIC wants to make sure consumers have not been put into loans they can't afford, don't understand, or don't meet their needs. As part of its focus on credit, ASIC will be looking at brokers who do not arrange loans responsibly and lenders who do not lend responsibly.
2. Brokers are expected to assist consumers to decide whether they can afford a loan, and if they can't, help them to find a realistic method of achieving their goals. And lenders must not lend to customers if they cannot afford to repay. It's not sufficient to use the Household Expenditure Measure as a proxy for actual expenditure. Verified evidence of actual revenue and expenses must be analysed.
3. Interest only, vehicle finance, and high-risk products are a priority. Although home loans and personal loans are not immune, ASIC is especially concerned about interest-only home loans, car finance, and high-risk lending products such as payday loans and consumer leases.

4. Brokers and lenders must ensure that reverse mortgage borrowers – who are typically older people at or near retirement – understand the costs and implications of taking out these products. The minimum requirement is for these borrowers to be given a [Reverse Mortgage Information Statement](#), and taken through the [Reverse Mortgage Calculator](#) in person.
5. ASIC is preparing to get tough on lenders and lease providers using unfair contracts. It has recently warned lenders to 'fix up' unfair contracts immediately or face legal action. Some lenders have already paid heavy fines, refunded repayments, written off debts, or contributed to community programs. Others have lost their credit licence.
6. Lenders are now expected to have systems in place to identify and reduce the risk of loan fraud. This follows some egregious fraud cases where brokers either ignored forged or false documentation, or worse, falsified information for clients to increase the likelihood of their application being accepted.
7. The jury is out on mortgage broker remuneration. Commissions and other financially-based incentive schemes have a propensity to incentivise brokers to recommend loans.
8. Frustrated with its lack of progress in encouraging responsible lending practices through enforcement action, ASIC has taken the radical step of recommending that the industry move away from incentives that create conflicts of interest. This will be echoed by the Royal Commission.
9. Credit repair, where ASIC will take action against companies that charge consumers exorbitant fees to clean up their credit history or who put them into insolvency rather than negotiate hardship arrangements.

ASIC's track record is impressive

The criticism that ASIC is receiving in the Royal Commission and the media for being a soft cop on the beat isn't borne out when you look at the statistics. In the [second half of 2017](#) alone, ASIC's enforcement actions banned 54 people and companies from providing financial services or credit and instituted 232 summary prosecutions for liability offences and a further 17 sets of criminal proceedings. It raised \$21.7 million in civil penalties and \$94.4 million in compensation and remediation for investors and consumers.

If you're not sure whether your business is at risk, or if you receive an ASIC notice, it's best to get on the front foot.

Claire Wivell Plater of [The Fold Legal](#) is a leading financial services and credit lawyer. She actively advises both digital and 'analogue' businesses on commercial and regulatory issues and is a member of the Federal Treasurer's Digital Advisory Group. This article is general information and does not consider any entity's circumstances.

'Rorts and rip-offs' prevention in super legislation

Vinay Kolhatkar

The '[Treasury Laws Amendment \(Protecting Your Superannuation Savings Package\) Bill 2018](#)' was tabled in Parliament on 21 June 2018, with superannuation measures foreshadowed in the last Federal Budget.

Key provisions of the Bill

1. A cap on fees and no exit fees

The Bill prevents superannuation funds from charging administration and investment fees exceeding 3% per annum on balances of accounts below \$6,000. It also prevents exit fees when members close or rollover their superannuation accounts, no matter their balance. This will remove a disincentive to superannuation fund members consolidating and closing unwanted accounts.

2. Life insurance within super only if chosen

Fund trustees can provide life insurance and charge premiums only on an opt-in basis, and only to new members aged under 25 years, members with account balances below \$6,000, and members with inactive

accounts, unless a member has directed otherwise. Fund members can choose lesser cover or seek other providers, saving their nest egg from unintended diminution.

3. Consolidation

Accounts below \$6,000 will be transferred to the Commissioner of Taxation if they have been inactive for a continuous period of 13 months. The Commissioner will be empowered to then proactively pay these amounts, plus those lost accounts already held by the ATO, into the rightful owner's active superannuation account. In conjunction with the ban on exit fees, this will assist consolidation.

A political stab at Labor

The first paragraph of Federal Minister Kelly O'Dwyer's media release on the new Bill said it was:

"... action to protect the hard-earned superannuation savings of millions of Australians from rorts and rip-offs ... These measures address significant issues associated with the current default insurance arrangements in superannuation, which were also put in place in 2013 by then Minister for Superannuation, Bill Shorten."

This is a justifiable shot across the political bow, given that [Superannuation Legislation Amendment \(Choice of fund\) Bill](#) 2016 acknowledged that, due to enterprise bargaining agreements:

"Some employees cannot choose the superannuation fund into which their compulsory employer superannuation is paid. This prevents them making key decisions around their retirement savings, can result in the payment of unnecessary fees and insurance premiums, and can reduce competition between superannuation funds."

In May this year, O'Dwyer opined that "about one-third of accounts were unintended multiple accounts because employers have forced them into a particular fund of their choice or unions have through enterprise agreements".

Industry reactions

Industry reactions to the legislation is expected to be largely positive, although the loss of accounts will adversely impact some superannuation administrators and life companies.

Reaction to the consolidation measures included Julie Dolan, a principal of SMSF Consulting, who told SMSFAdviser:

"The ATO has already been tightening up on the efficiency of its current process of dealing with inactive accounts in order to transfer them into active accounts more quickly. The ATO are spending quite a lot of money on their data matching process and this latest measure is expected to push an extra \$6 billion into super across 3 million active superannuation accounts. So that's a good thing."

Treasury officials have estimated that there are roughly six million inactive super accounts in Australia belonging to four million members.

On the opt-out measure, AustralianSuper, Australia's largest super fund, has already stopped signing up new members under 25 into life insurance automatically. According to a Rice Warner, an actuarial consultancy firm:

"At the highest premiums, a blue-collar worker could be up to 34% worse off upon retirement age, or around \$600,000 short compared to a blue collar worker without insurance in their super."

Canstar, a financial comparison website, also reported that:

"There's been an average premium rise of 215% for death and TPD cover and 82% for income protection over the last four years means the impact of insurance on a super balance is greater than ever."

A person below 25 with no dependents and a low salary may not benefit from such a high dilution, or at least would benefit from greater tailoring of their life insurance needs. However, the industry should ensure the changes do not lead to under-insurance for people who need it.

Vinay Kolhatkar is an Assistant Editor of Cuffelinks.

2018: an SAA odyssey

James Bloom

Definition of Strategic Asset Allocation (SAA): A portfolio strategy that involves setting target allocations for various asset classes and rebalancing periodically to the original allocations when they deviate significantly from the initial settings due to differing returns from the various assets. From [Investopedia](#)

April 1968. Fifty years ago. It was perhaps the first mainstream introduction to fictional Artificial Intelligence (AI) when we met 'HAL 9000', the supercomputer controlling the spacecraft Discovery in Arthur C Clarke and Stanley Kubrick's confounding sci-fi epic *2001: A Space Odyssey*. HAL was an early exercise in AI over EI (emotional intelligence) and the omnipresent conflict between man and machine, pitting his hard-coded mission priorities over expendable human life, against his onboard human nemesis, scientist Dr. David Bowman.

In their battle, Bowman ultimately prevails by first deactivating HAL's advanced capabilities, regressing the supercomputer to a juvenile state. Then he permanently shut down his circuitry in emotionally-charged scenes of pathos rarely associated with the deactivation of a machine (a theme revisited again in Spielberg's *A.I.*). An eerie future glimpse perhaps, into the evermore humanlike connection we make today with assistants Alexa, Echo, or Siri...?

The risky odyssey continues after the GFC

We have been on something of our own uncharted odyssey in the years since the GFC. Central bank policies have kept bond yields low, allowing all financial assets to perform well against a low volatility backdrop. As a result, many superannuation funds have continued with a pronounced skew towards risk assets, retaining high equity allocations versus fixed income. And it's worked out very well. Risk asset prices rose and have kept on rising. Generally, the more risk while these interventionist 'training wheels' were in place, the more return you made. Not too many spills, given dampened volatility. Very nice.

But will this strategy continue to work in the future? Markets received their first real warning in March 2018, when volatility returned amidst a perception easy money would end sooner than expected. We knew the US Federal Reserve (the Fed) would continue hiking rates – they've telegraphed their message well over the past five years – but the combination of rising rates, tapering and budget and current account deficits eventually meant an inevitable resurfacing of volatility. With US Treasuries remaining the global benchmark by which other markets are judged, rising rates will remain a global phenomenon, despite low growth and inflation.

US Fed journey is a balancing act

There has been much conjecture over recent months on the near-term path for US 10-year Treasury yields. Currently hovering around the 3% mark (the highest in eight years) a new consensus suggests a continued climb onwards toward (and perhaps beyond) 3.5%, at which point more widespread rotation from equities to bonds would be likely. Inflation and continued growth are key, but so is new Treasury supply.

It's a balancing act. If Treasury yields continue to rise, it may choke future growth prospects, particularly with growth and inflation prospects remaining relatively benign. But solid employment gains, albeit with little wage pressure so far, combined with strong economic data point toward further post-GFC recovery. This provides the ammunition the Fed needs to return to a more normal short-term rate. But as we have seen over the past few months, the Fed is not immune from ever-present geopolitical rumbles. Tenuous, to say the least.

The Fed will normalise short-term rates over time, eventually reaching 2.5% or 3.0% over the next two plus years. A tougher question is what becomes of 10-year yields. Should the Fed hike too quickly, we could continue to see the flattening of the yield curve. However, US\$1trillion+ budget deficits combined with the Fed's tapering programme mean unprecedented supply in the coming years. Who will buy these bonds at current levels?

Watch sensitivity to rising rates, higher spreads and volatility

In a similar vein, the resurgence of volatility also left its mark in credit spreads, which remain wider than at the start of the year. However we view wider spreads as temporary in nature, due to short-term increases in corporate supply, rather than any deterioration in credit fundamentals or increase in default risks. Nonetheless, investors need to remain more cautious as market volatility increases, and not forget that we remain in a rising interest rate environment. Leaving your bond allocations sensitive to a change in rates and spreads is riskier today than in the past.

Fortunately, there exist a good number of strategies where that sensitivity can be neutralised. Any allocation to fixed income should exist as yin to the (equity) yang within portfolios, i.e. that it is uncorrelated (or negatively correlated). Investors should ensure it is proven so. Higher risk fixed income sectors can be closely correlated to equities when investors most want them not to be, notably during extreme risk off periods. The GFC is a fine case in point where certain high yield securities fell just as sharply as equities.

There is also no doubt that we still face a complicated set of extraneous geopolitical factors; the precarious relationship between 'frenemies' Trump and Kim, China's opaque economics, tit-for-tat trade warring, and the volatile US/Iran/Israel dialogue to cite some of the current clouds. Their negative impact on equity markets could be severe, though any one has sufficient energy to disrupt the status quo in fixed income markets too. It pays to find fixed income manager delegates that possess inherent and proven dynamic tools to make material defensive adjustments when storm clouds gather, and equally to take risk when opportunities present.

Time for a new course on the odyssey

At least technically, a reasonably compelling argument has emerged for a rebalancing back towards closer equilibrium between equity and bond allocations. Not in a rush, but tailwinds are building, and layering in at increasingly attractive forward yields is starting to appear sensible.

Equally, initial audience reactions suggested *2001* took time to prove itself, though it's come to be regarded as one of the greatest and most influential movies, dealing with complex themes of evolution, technology and AI. While the then fiction of human space travel has yet to materially progress from the moon landings of the late-sixties and early-seventies – notwithstanding ongoing efforts by the likes of Branson and Musk – *2001* gizmos such as flat screens, tablets, and smartphones abound.

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Five simple checks when investing long term

Michael Blake

The investment vehicles you choose can make a huge difference to returns, especially for long-term investments. Retirement is perhaps the most common long-term financial goal, but it is far from the only one. Investing to pay for a child or grandchild's education, to buy a house, or fund some other dream are expensive goals that need to be planned for. The best way to do so is with a long-term investment plan, started as early as possible and contributed to regularly.

For most of us, superannuation is the best long-term investment plan. It is only taxed at 15% in accumulation phase, and because contributing is mandatory, there is no need for discipline in terms of regular contributions. The problem with super is that you can't access it until you reach retirement age (i.e. between 55 and 67, depending on your age now), so it usually is not a suitable vehicle for any goal other than retirement.

Recent legislative changes have also capped the amounts that you can contribute to super on a pre-tax basis to just \$25,000 per annum. There is also now a cap of \$1.6 million on how much you can have in an allocated pension for retirement. Another factor seldom discussed is that, in the event of death resulting in the passing of superannuation or pension funds to a non-dependant, there are significant tax penalties incurred by the beneficiaries. This is a form of inheritance tax that many retirees are unaware of until it is too late.

Managed funds, on the other hand, are a good way to invest for the long term. The challenge is that you need to include any returns in your annual tax return, which means that all distributions or dividends you receive are taxed at your personal rate, which can be up to 45%.

Choosing how to invest long term

There are five features that should be considered when choosing new investments:

1. Risk profile

Risk is a fundamental consideration in investing. Identifying, quantifying and assessing your risk appetite against the risk category of the investment options should be the first step in any investment process. It will influence your investment decisions and impact the time required for you to meet your objectives.

2. Investment timeframe

Generally, the longer the investment timeframe, the higher the level of risk you can typically take. Conversely, if you have a short investment timeframe and may need to access your money, then investing in riskier or growth assets like equities may not be the best option.

3. Returns required to achieve goal

Once you have decided on your financial goal, the next step is a realistic assessment of how much it is going to cost, how much you need to invest, and the return you will require to get there. This will help you determine which investment assets or the mix of assets to suit you.

4. Tax effectiveness of the vehicle

The amount of tax you pay makes a big difference to the money you end up with in your pocket, particularly if you are on a high personal tax rate. When and how you pay the tax can also be important.

For example, investment bonds can be tax-effective because tax on returns from the underlying portfolio is paid from within the bond at the company tax rate of 30%. The effective tax rate can be even less if the underlying investment portfolio generates franking credits.

Returns from the bond are not distributed but are re-invested into the bond. This means that the investment bond or any returns from the bond do not need to be included in your tax return.

Another advantage of investment bonds is the lack of capital gains tax liability. Because earnings are automatically reinvested in the bond, there is no capital gain tax liability and reinvestment dates do not need to be tracked for capital gains tax purposes. Investment bonds are tax-effective on an ongoing basis, but the biggest advantage they have over other investment structures comes if they are held for 10 years, in which case, all the proceeds, principal and investment returns are distributed to the investor entirely tax free.

5. Flexibility of the investment structure

Despite your best-laid plans, you may need to withdraw funds from a long-term investment or switch investments due to changed requirements. It is important to compare the flexibility of the various investment options you may be considering.

It is possible to withdraw funds from an investment bond at any time within its 10-year tax-free period for example, although you may lose some or all of the tax benefits if funds are withdrawn early. It is also possible to switch between investment options without triggering personal capital gains tax.

What is an investment bond and how does it work?

An investment bond is like a tax-paid managed fund: investors choose from an underlying portfolio of assets that differ in terms of their risk profile and likely investment returns, and can include different asset classes – including equities, fixed interest, real estate or a mixture.

Investment bonds are simple to set up and can be started with as little as \$500 or as much as you like, and additional contributions can be made up to 125% of the previous year's contribution.

Due to their unique structure, investment bonds can make powerful estate planning tools. You can nominate a beneficiary, and if you die, this beneficiary will receive the proceeds of the bond tax-free, regardless of when this occurs. An insurance bond does not form part of your estate for the purposes of your will, so cannot be challenged.

Conclusion

The sooner we all begin contributing to our financial future, or to any long-term financial goal, the more likely we are to achieve it. The superannuation system is predicated on exactly this fact and super remains the most tax-effective investment strategy available when it comes to planning for retirement.

If, on the other hand, you are working towards a different, and not quite so long-term financial goal, like paying for tertiary education for your children or retiring early, then super may not be the best choice, because you won't be able to access it when you need it. Investment bonds may have a role to play to meet this type of investment goal.

Michael Blake is Head of [Centuria Life](#), a provider of investment bonds. This article is general sponsored information and does not consider the circumstances of any investor.

Podcast: What did you do during the GFC? Warning signs and lessons for investors

Gemma Dale And Graham Hand

The collapse of Lehman Brothers in 2008 is often seen as the catalyst for the Global Financial Crisis, which wiped trillions of dollars from global markets and shook confidence in financial systems across the world. The GFC actually started a year earlier in the global credit markets, but the equity markets ignored the warning signs. With hindsight, everyone had the chance to exit shares at elevated prices with plenty of notice, as the credit markets were screaming for all to see, in every part of the world.

As Graham Hand tells Gemma Dale of nabtrade, panic hit the multi-billion dollar borrowing programme he was managing a full 13 months before the Lehman crisis. In this fascinating and timely podcast, Graham discusses:

- How global funding markets effectively closed overnight
- The warning signs as a subprime debt crisis swept across the Atlantic
- How equity markets ignored the signals for over 12 months before collapsing, and
- What he learned, including steps he takes to protect his investments from similar risks in the future.



S&P/ASX200 January 2007 to October 2013, including GFC.

The equity market reached new highs after the August 2007 close of credit markets, and even kicked up again towards 2008 mid-year.

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