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Weekly Review

WEALTH

– Issue – 20 Jan. 2017

It's time to do a review and rebalance your portfolio risk.

BY TONY KAYE • EUREKA REPORT • 18 JANUARY 2017

Why your portfolio review is probably overdue

New Year's resolutions are often made with the best intentions of following through, only to be forgotten within days or weeks.

Key Point

- ***While blue-chip stocks are regarded as stable investments, not all are a nd changing market conditions make some vulnerable. More self-managed investors are venturing out into stocks outside the top 100.***

If you made a resolution to review your investment portfolio, and to take steps to rebalance it in the new year, do yourself a favour and make sure you actually do that review – and sooner rather than later. If you didn't make that pledge, add it to your priority task list.

As I noted in my article ***Time to get into some super rebalancing*** (December 14), regular portfolio reviews are prudent to ensure your overall investment strategies remain focused and your asset allocations are well balanced. Investment portfolios, like cars, need to be checked and re-tuned on a regular basis. Parts need to be replaced from time to time, and staying on cruise control isn't an option.

Which is why investment research released this week by stockbroking firm CommSec is somewhat alarming, especially when it is overlaid with September quarter self-managed superannuation fund (SMSF) statistics published in December by the Australian Tax Office.

In a nutshell, CommSec's research shows SMSF trustees are fixated on Australia's top 20 largest stocks when it comes to the share market.

SMSFs were the largest net investors in the ASX Top 20 during 2016, with the four major banks making up more than 32 per cent of SMSF holdings. That's despite increasing concerns among analysts about the earnings sustainability of the big banks, with ratings agency Fitch also revising its outlook on the sector to 'negative' earlier this week.

According to CommSec, banks comprise nearly a quarter of all trades by value for SMSFs.

Our own analysts have Hold ratings on ANZ, Commonwealth Bank, NAB and Westpac, and every other company in the ASX Top 20 for that matter except for Brambles, which currently is being recommended as a Sell. (**Click here** to see our full list of stock recommendations.)

Now, that's not to say that investing in our biggest companies is a bad strategy. Far from it, and they should form part of every share portfolio and long-term investment strategy. But it's also important to diversify, across shares and other asset classes.

Separate SMSF investment data from the ATO shows that Australian shares were the biggest beneficiaries of investment funds in the September quarter, with the total value of self-

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DISCLAIMER This publication is general in nature and does not take your personal situation into consideration. You should seek financial advice specific to your situation before making any financial decision. Past performance is not a reliable indicator of future performance. We encourage you to think of investing as a long-term pursuit.

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directed super dollars invested in stocks rising by $8.8 billion in the three months to $192.4bn.

But that figure is almost matched by the huge amount of SMSF funds ($157.4bn) invested into cash – which is equal to about one-quarter of total SMSF investor assets – an alarming statistic in its own right given the dismal returns from bank accounts. (See our story last week, ***SMSFs in a high-risk cash gamble***).

Investors would be much better served, returns wise, by redirecting more of their cash into assets such as shares that generate higher growth and income.

That's where picking the stocks with the best prospects is crucial.

After the big banks, CommSec's research shows that SMSF trustees prize the big resources stocks BHP and Rio in their portfolios (11 per cent), with Materials and Energy accounting for nearly another quarter of trades by value for SMSFs. Other key holdings include telecommunications stocks, namely Telstra (7.8 per cent), diversified financials such as Macquarie and big insurers QBE (6.4 per cent) as well as Wesfarmers and Woolworths (6.0 per cent).

Yet pleasingly, the CommSec research shows SMSFs are also moving towards the mid to small cap market.

According to Marcus Evans, head of SMSF Customers for Commonwealth Bank, while SMSFs were net buyers of the banks and resource stocks over the past 12 months, CHESS holdings of stocks outside the ASX100 have grown by 3 per cent.

The use of exchange-traded products – such as exchange traded funds (ETFs), listed investment companies (LICs) and exchange-traded managed funds – to diversify into international equities has remained constant at around 2 per cent of total CHESS holdings. SMSFs make up about a quarter of all ETF trades, although ETF activity was down marginally on 2015.

According to Evans: "One pattern that is emerging is the move from ETFs to direct shares when the market spikes down and specific shares become attractive from a valuation perspective."

Current SMSF research by Super Concepts also indicates an increased allocation to hybrids by the funds under its administration. SMSFs make up 50 per cent of hybrid holdings in CommSec, and in total these have increased by 18 per cent in the period from August 2015.

Starting the review process

There's no time like the present to check your portfolio holdings and it's a relatively quick process. In fact, reviewing the health of your investment portfolio should be a regular habit.

Click to InvestSMART's free **portfolio manager tool** to enter your asset details and view your current asset allocation ratio, based on your specific investment goals.

For investors with a lower-than-recommended Allocation Exposure Score the most prudent course of action is to rebalance one's asset allocation to improve diversification, reduce risk and improve returns.

A good way of doing this is to simulate changes to your current investments and/or add new investments to see how they could affect your overall portfolio's diversification.

Before leaping into any investments, it's vital to undertake comprehensive research. This is an area where many investors fall short and they often either overpay or fail to take into account the underlying dynamics of either the broader market, a sector and – when buying shares – those factors impacting a specific company.

The key to successful portfolio management is having, and sticking to, defined investment objectives. Emotion should never come into play but when circumstances dictate active investors should be ready, and prepared, to respond.

It's all about being in control, using the vast array of information available to build and maintain a well-balanced portfolio of assets, and to maximise investment returns over the longer term.

This is an ideal opportunity to learn from our experts about some of the current investment trends and the range of managed investment products available.

BY MITCHELL SNEDDON • EUREKA REPORT • 18 JANUARY 2017

Join our new Smart Investor Sessions

At InvestSMART, our primary objective is help you to become a smarter investor.

So, starting as of next week, we will be launching our Smart Investor Sessions, a series of free face-to-face educational sessions run by our in-house financial experts.

They have been designed to help guide you with your overall investment decision-making processes and to learn more about your options in the confusing world of investing.

Learn more about managed investment products

The first round of sessions will focus on how to assess a managed investment product. For many self-directed investors the thought of using a fund manager, exchange-traded fund or a listed investment company has probably crossed their mind. But selecting the right manager can be as difficult as selecting an individual stock.

Each Smart Investor Session will focus on how to assess the people, the process and the product.

When it comes to looking behind the scenes at an investment team, we will look for experience, transparency and key man risk.

The process matters just as much as the people putting it into practice. What we are looking for here is a repeatable process. There is no use in getting a return one year or picking a good stock if you don't know how you did it. The process is also important because a robust process will allow a manager/funds management business to ride out the ebbs and flows of members of the investment team coming and going.

Finally, we look into the way the managed product is packaged and offered. Investors at different points of their journey will have different needs when it comes to flexibility.

We will break down the pros and cons of listed and unlisted investment options so you can narrow down your options.

Register today

Smart Investor Sessions will take place regularly in small groups in our Sydney and Melbourne offices.

For those not in Sydney or Melbourne, or who are unable to attend, we also will be holding a monthly live webcast as well.

To find out the times and dates, and to register, click here to view our new events page on InvestSMART at **www.investsmart.com.au/events**

Managed super funds enjoyed a strong finish to 2016 from Australian and global share markets.

BY TONY KAYE • EUREKA REPORT • 19 JANUARY 2017

Super returns enjoy a late surge

Australian managed super funds achieved a fifth consecutive positive annual return in 2016, thanks to a strong share market surge in December.

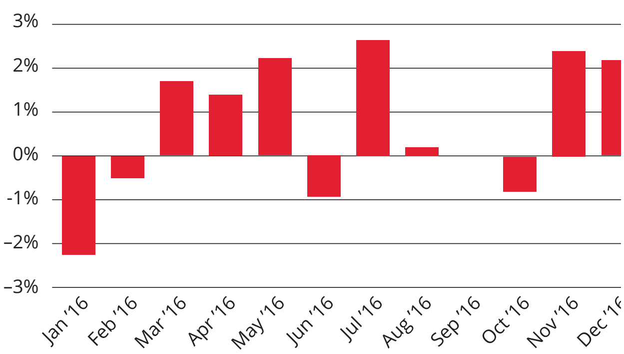
Key Point

- ***Super investors, including self-managed super funds trustees, should brace for more market volatility in 2017.***

Data released Thursday by superannuation research firms SuperRatings and Chant West shows the median return from managed super funds exceeded 7 per cent in the 12 months, despite negative returns in January, February, June and October.

SuperRatings said the median balanced return, based on an allocation of 60 to 76 per cent in growth assets, was 7.3 per cent over the year to December 31. Chant West said the median growth fund return, based on a similar asset allocation of 61 to 80 per cent in growth assets, was 7.7 per cent for the year.

Chart 1: Median balanced (60–76) option calendar year returns



Source: SuperRatings

Returns ranged between 4.2 per cent and 10.1 per cent, with both firms ranking the Catholic Super Balanced fund and the Hostplus Balanced funds in top place with annual returns of 10.1 per cent.

Next was the Cbus growth fund with 9.6 per cent, the CareSuper Balanced fund with 9.4 per cent, and the SunSuper Balanced fund with 8.9 per cent.

Longer-term returns for super continue to sit close to funds' inflation targets, with the seven-year return sitting at 7.6 per cent per annum. The 10-year return is sitting at 5.1 per cent per annum due to impact on returns of the Global Financial Crisis.

However, over longer periods, superannuation funds have generally delivered solid performance, and while 10-year returns are marginally below the common inflation plus 3.5 per cent target, medium-term returns continue to sit well above these levels.

Table 1: Top 10 Super Funds in 2016

RANK	FUND – BALANCED (60–76%) OPTION	2016 RETURN
1	Catholic Super – Balanced	10.1
2	HOSTPLUS – Balanced	10.1
3	Cbus – Growth (Cbus MySuper)	9.6
4	CareSuper – Balanced	9.4
5	Sunsuper for Life – Balanced	8.9
6	EISS Super – Diversified	8.8
7	Energy Super – Balanced Option	8.8
8	Media Super – Balanced	8.7
9	Equip MyFuture – Balanced Growth	8.6
10	HESTA – Core Pool	8.4
	Median return	7.3

"When you look at the long-term performance of super as a whole, it is clear that Australians have been well served by the system," according to SuperRatings chairman Jeff Bresnahan. "It is important to note that, since the GFC, there has been only one year of negative returns, and 2016 represents the fifth consecutive year of robust positive returns. While 2017 will certainly have its own challenges, we expect long-term performance to hold up."

> **Infrastructure performed particularly well, with unlisted infrastructure generating 17.3 per cent and global listed infrastructure 12.7 per cent.**

Australian listed and direct property were the top performing asset classes in 2016, but super funds were also bolstered by strong performance from local shares.

"Three of the key stories in 2016 were the shock 'Brexit' vote, the equally surprising Donald Trump election victory and the timing of the second US interest rate hike," said Chant West director Warren Chant.

"All of these created uncertainty, but share markets again proved how resilient they can be. Investors chose to focus on the gradual improvement in the US economy and what that might mean for global growth, and as a result international shares returned 8.9 per cent in hedged terms and 7.9 per cent unhedged. Australian shares did even better, returning a healthy 11.8 per cent."

Infrastructure performed particularly well, with unlisted infrastructure generating 17.3 per cent and global listed infrastructure 12.7 per cent. Private equity produced a more modest return of 7.8 per cent.

Defensive asset sectors yielded the lowest returns but were still in the black. Australian and international bonds gained 2.9 per cent and 5.2 per cent, respectively, while the return from cash was just 2.1 per cent.

Ongoing market nervousness around the aftermath of the election of Donald Trump and the impending UK Brexit is helping gold and our dollar.

BY ROBERT GOTTLIEBSEN • EUREKA REPORT • 18 JANUARY 2017

Negativity has some investment positives

Last night we saw a dramatic reaction to a combination of the exit speech by British PM Theresa May and Donald Trump's continuing threats of higher tariffs which China and Mexico respond with trade war threats.

Key Point

- ***Australia's big resources companies are hopeful that Trump's infrastructure plans will translate into higher commodity prices and exports, especially as uncertainty continues around Chinese demand. But China's moves in the banking sector could have implications for our property market.***

We saw gold jump, the US dollar fall and sterling rise, plus a big fall in the London share market and a lesser one on Wall Street. Trade war talk between the US and China usually hits our markets, so it was no surprise we opened lower this morning.

While markets are focusing on Brexit and the inauguration of President Trump, underneath the froth and bubble is the development of a series of fascinating trends as the global investment community positions itself for a period where the rules are going to change.

And for old timers like me, nothing cheers me better than to see that at a time of uncertainty and nervousness the gold price is doing what it always has done – rising. For generations, wherever there has been turmoil, gold has risen in price. People feel good about gold and, of course, that extends to shares in gold companies.

So it is no surprise that at this time we see gold rising. I must confess that apart from a sally into the silver market a few decades ago I have never felt it necessary to include gold as a cornerstone of my portfolio. I don't think I will change that stance, but I must say that the level of possible change in the global community on the election of President Trump is greater than I can ever recall as a result of one particular election result.

The long road ahead

As I described in my last email to you for 2016 (***Into 2017: Prepare for a volatile year***), I think that the domestic changes in the US will take longer to take place than the market expects. Erecting infrastructure is not a fast process, and it takes years to develop a project. Switching plants to the US and developing new US plants again will take longer. And if the US suddenly reduces taxes, as seems likely, I will be surprised if the money poured into the US overnight.

But these events look likely to happen and they are being superimposed on a completely new look at the United States foreign policy and defence strategies. Trump is being aggressive towards China and is questioning the funding of NATO, plus he is saying what we all know to be true – Europe is a mess and could well break up. Brexit and the clarity of British PM Theresa May's speech adds to that pressure.

Put all that together and you can see why gold has a greater attraction than we have seen for a long time. The gold buffs will lose if the level of change that Trump engineers is less traumatic than is currently being canvassed.

That nervousness about the extent and speed of change, plus the talk of trade wars, is being reflected in the weakness of the American dollar. We saw our currency fall sharply when Trump won the US election, but it has now strengthened to go beyond 75 US cents. So, in a strange way gold is being preferred over the American currency.

The inauguration address will either confirm that the whole process will take longer than initially thought or alternatively that the US is really going to move, and move fast. In that case we will see the US dollar start rising again.

Miners find new reasons for optimism

Meanwhile, in commodities like oil, iron ore and copper there is an increasing sense of optimism that Trump is going to engineer a much higher level of long-term demand. Conversely, coal is looking weaker. As you look around Asia

> **“Erecting infrastructure is not a fast process, and it takes years to develop a project. Switching plants to the US and developing new US plants again will take longer.**

the economies including China appear to be going pretty well with strong internal demand. Even if President Trump is able to attract more investment in US manufacturing, it will take a long time before it affects China. Of course, if events in Taiwan and the South China Sea turn nasty then Chinese exports to the US are likely to fall sharply and there is no doubt we will be affected, possibly severely.

Leaving that aside, we are about to enjoy a fantastic mining company earnings season. Miners like BHP and Rio Tinto have achieved good volumes for high prices for iron ore, oil, copper and other minerals. At the same time they have slashed their costs. If you are a shareholder in one of the large miners, get ready to enjoy yourself next month as the profits come through.

In the case of BHP, Donald Trump has met with chairman Jac Nasser and CEO Andrew Mackenzie. They will have warned him about their fears of aggressive action towards China, but Trump would have underlined to BHP that he will lower the US tax rate and has invited them to step up their investment in US oil, gas and copper. And my guess is that they will do exactly that, and that is where Australian iron ore cash will end up.

China and the Australian property market

Meanwhile China is greatly concerned about the state of its banks and does not want its domestic liquidity run down too far because that will require more government funds to be diverted towards keeping its dodgy banks alive. As a result, the Chinese Government is making it harder and harder for its citizens to invest in property in Australia, Canada and other parts of the world.

In Sydney the percentage of Chinese (including local Chinese) buying apartments has fallen from about 80 to 50 per cent of the market and continues to head south. Normally this would cause a fall in apartment prices, but increasingly Australians are getting sick of the our Government’s superannuation games and are deciding to go for bricks and mortar. The negative gearing buying of apartments in Sydney has jumped and absorbed the Chinese fall. Indeed, the price of apartments has risen slightly.

In Melbourne that is what has happened in the inner suburbs, but there is a glut of one bedroom apartments in the city where the Chinese are having great difficulty in settling contracts. That is confusing the market. But I am sure as we look around the nation we will be seeing a rise in negative gearing in residential property in many property markets. In time this will affect government revenues, but the Government only has itself to blame.

The rise in the US bond interest rates is pushing up the cost of Australian bank borrowings and the banks are trying to maintain their profitability by increasing rates to home owners and lowering term deposit rates. Normally such a rise in interest rates would dampen the property market, but those that negatively gear appear very confident.

Of course, if Bill Shorten wins the next election and stops negative gearing on existing properties then it will cause considerable damage to the residential market. If the current trend towards a higher rate of negatively geared property continues it will be very dangerous for any political party to reverse it.

Location, location applies to holiday houses as does consideration of their unique challenges.

BY NERIDA CONISBEE • EUREKA REPORT • 16 JANUARY 2017

Can holiday homes ever be a good investment?

Like many Australians, summer is the time of year I look forward to most, and my favourite place to be at this time of year is Byron Bay.

Key Point

- ***For capital growth, go for proximity to capital cities and strong regional economies. For rental yield, cheap locations can pay off.***

Whenever I get the opportunity to visit, I find myself daydreaming about one day owning a holiday house there, preferably near Clarkes Beach. Sadly, the daydream quickly dissipates when I look at the investment required to make my dream a reality.

Holiday homes traditionally have a reputation of being poor investments, driven by an emotional response to a relaxing holiday. But is it possible to make money from investing in a holiday house?

Which holiday destinations offer the best investment?

Putting aside the challenges, there are some good places to invest in a holiday house. These are some areas worth considering:

1. Within commuting distance of a capital city

The holiday destinations with the most capital growth are those located within commuting distance of a capital city. This is partly because they tend to be easier for people to access for a weekend away or short term stay. However, these areas are increasingly seeing good capital growth because our capital cities are becoming less affordable. As a result, many people are using the locations as permanent homes.

Look to Gold Coast/Sunshine Coast in Queensland, Central Coast/Bowral in NSW, Mornington Peninsula/Surf Coast in Victoria and Fleurieu Peninsula in South Australia as attractive options.

2. Cheap locations

If you have a small amount to invest, want to upgrade from camping, or are prepared to drive some distance from a capital city, then buying in very cheap locations can have merit. Given the low cost of housing, the rental yield that can be achieved can also be quite attractive. Remember, however, low-cost locations generally have far lower capital growth, and prices can even go backwards.

Most of the cheapest seaside destinations are located in South Australia and Victoria where you can still get a holiday home for less than $250,000. In Victoria, consider Loch Sport, Seaspray and Golden Beach in Central Gippsland. Cape Jervis on the Fleurieu Peninsula and Port Vincent and Wallaroo on the Yorke Peninsula in South Australia are also worth considering.

3. Areas with a strong economy

Regional areas with a strong economic base and forecast population growth can also be worth considering, even if they are located some distance from capital cities. Places like Byron Bay and Port Douglas are strong tourist destinations in their own right, attracting people from all over Australia and the world. Newcastle is currently experiencing strong economic growth, and holiday destinations in nearby towns could present opportunities. Likewise, the surf coast in Victoria, while arguably still within commuting distance of Melbourne, has a strong surf industry and the increasingly popular business hub of Geelong is just up the highway.

What are the challenges?

The idea of owning a holiday house is an attractive concept, so if you're in the market there are some things to consider before you dive in:

1. Beware of emotional buying

If you are buying th e property to use purely as a holiday house without any concern about capital growth or income return, then you can afford to be as emotional in your decision making as you like. However, in order to maximise income from the property, or to ensure capital growth, you need to be more hard-nosed. Consider removing yourself from the bidding or buying process and enlist an unemotional third party.

> **“ Buying in very cheap locations can have merit. Given the low cost of housing, the rental yield that can be achieved can also be quite attractive.**

2. Understand the tax rules

It is relatively clear that in Australia you can’t claim tax deductions if you do not lease the property, so understanding what can be claimed is important. Owning a holiday house can have some tax advantages. Negative gearing is the most obvious one, however it may also be possible to claim depreciation of furniture and white goods. The Australian Tax Office regularly cracks down on holiday house ownership, particularly with people who claim deductions with little effort to lease the property.

3. How frequently will you actually use it?

Having a holiday house can restrict you to holidaying in the same location every year. And if you are looking to generate income from the property, peak holiday periods – such as over New Year’s – can deliver two to three times as much money than at other times of the year. Unfortunately, peak season is also when you may most like to use the home. If you’re not sure you will use it regularly during off-peak times, then it can be far more cost effective to simply lease a property in your favourite location during the peak season instead.

4. Who’s managing the property?

Traditionally local agents manage many holiday lettings. However, services such as Airbnb have changed how people look for short-term holiday rentals. Using a service like Airbnb to let your property can save you money on management fees, but it will also mean that you need to work out how to manage and maintain the house. The instant online feedback from people using the house also means that problems need to be dealt with quickly to ensure a bad review doesn’t deter others from wanting to stay.

5. Maintenance

Maintaining a holiday house is much more management intensive than other forms of residential investment. A large number of different people leasing the property throughout the year means more cleaning and potentially more damage and wear and tear to the property. Although this can be covered in the cost of leasing the property, it is important to factor it into your calculations.

If you are looking to buy a holiday home primarily for your own use, then something in your favourite location which is relatively accessible is the best option.

However, if you are looking to make money, you need to look at it as any other type of investment, not just somewhere to holiday regularly. The main difference from a permanent occupancy investment is that leasing and maintaining the property can be much more expensive and time consuming.

Buying in cheap seaside locations can provide decent rental returns, however the level of capital growth is likely to be low. Alternatively, locations close to capital cities are now achieving decent capital growth, but offer lower rental returns.

For me, my daydream will remain just that. I will continue to lease a holiday home in Byron Bay whenever I can, and look elsewhere for unemotional investment opportunities.

Nerida Conisbee is chief economist at REA Group.

The rebound in investor activity in Sydney and Melbourne has come amid trends that suggest the housing market should be cooling.

BY CALLAM PICKERING • EUREKA REPORT • 18 JANUARY 2017

Doubling down: Investors reignite the housing market

Investors are jumping back into property, despite the major banks' hiking interest rates, as the Sydney and Melbourne property boom finds a second wind.

Key Point

- ***Dwelling prices in Sydney and Melbourne have increased by almost 10 per cent over the past 12 months.***

The Australian Bureau of Statistics (ABS) released new data on mortgage lending activity this week, providing evidence of renewed vigour among property investors, which could support dwelling price growth in the near term.

Historical trends suggest that the housing market should be cooling. The major banks' are lifting interest rates and, as it stands, real interest rates aren't even that low in the first place. Buying behaviour in Sydney and Melbourne has been frantic for several years now, which normally leads to a period of softer prices and lower transactions. Meanwhile, rental yields have dropped to their lowest level in recorded history, with rents falling across much of the country.

Each of these factors, by themselves, would be enough to warrant caution for property investors and owner-occupiers. Nevertheless, prices continue to rise and investors cannot get enough of residential property. Let's crunch the numbers.

Lending resurgence

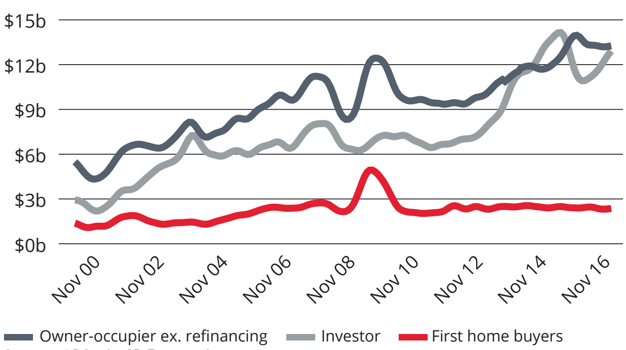
According to the ABS, new mortgage lending activity rose by 0.9 per cent in November on a trend basis, the ninth consecutive monthly rise, to be 5.1 per cent higher over the year. Lending activity has surged 7.4 per cent from its recent trough but remains 2.3 per cent below its peak in May 2015.

Much of that recent strength has been concentrated among property investors. New investor lending activity rose by 1.7 per cent in November on a trend basis, a touch weaker than recent months, to be 17.1 per cent higher over the year.

First-home buyer activity remains weak, reflecting high prices and a difficult savings environment.

Investor activity has already returned to a level that is likely to concern the Australian Prudential Regulation Authority (APRA). The first stage of the recent boom occurred in an environment in which mortgage rates were falling; by comparison, the rebound has occurred in an environment where banks are raising rates. There is arguably greater risk in the system now than there was when investor activity peaked in April 2015.

Chart 1: Australian housing loan approvals, value of monthly commitments; trends



Source: ABS; via CP Economics

Greater regulatory oversight and tighter lending standards is a clear risk for property investors over the next few years. It would be a surprise if we didn't see a response from APRA in the coming months.

Record prices

Dwelling prices continue to send mixed messages both with regards to different cities as well as different dwelling price measures.

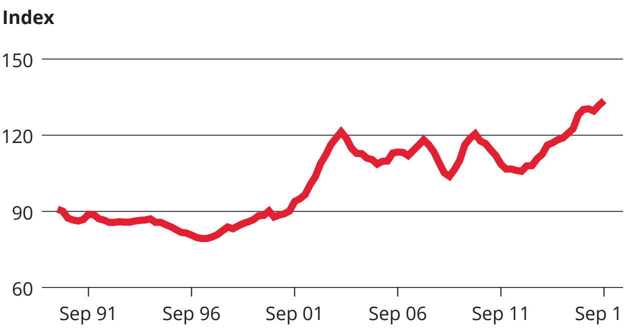
Nationwide housing valuations have never been higher. The house-price to income ratio is at its highest level in history and has increased by 26 per cent over the past four years. The house-price to rent ratio is also at its highest level in history.

Nevertheless, the national figures aren't all that useful since conditions differ significantly from city to city. According

> **New investor lending activity rose by 1.7 per cent in November on a trend basis, a touch weaker than recent months, to be 17.1 per cent higher over the year.**

to the ABS, dwelling prices in Sydney and Melbourne, for example, have increased by almost 10 per cent over the past 12 months. By comparison, prices in Perth have fallen by 4.5 per cent over the same period.

Chart 2: House price-to-income ratio (long run average = 100)



Source: ABS, via CP Economics

Other house price measures, such as from CoreLogic, suggest that prices in Sydney and Melbourne have increased at 15.5 and 13.7 per cent over the past year, respectively.

Despite different methodologies, the ABS and CoreLogic measures of dwelling prices have historically been quite similar. Recent changes to CoreLogic's methodology, however, has called into question their accuracy and the Reserve Bank of Australia has started to place greater emphasis on the ABS measure in its reports.

Remembering that mortgage lending activity remains below its peak, it is somewhat surprising that there hasn't been any genuine weakness in the Sydney or Melbourne markets. This might reflect the fact that around 30 per cent of housing transactions do not involve debt – creating a disconnect between lending activity and prices – though it is certainly beneficial for investors to utilise debt.

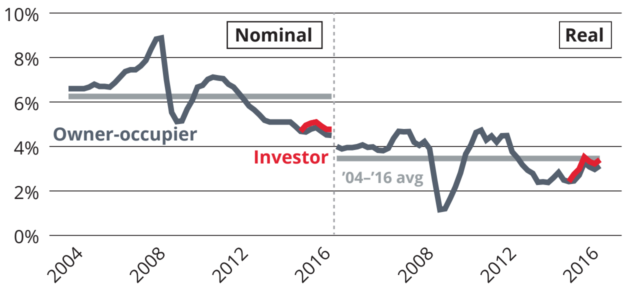
It's also worth noting that new construction, mainly funded from abroad, may be having a greater influence on prices than has been the case in the past. Capital inflows from abroad may have allowed the housing market to stay strong when lending activity moderated.

Rates brake

What is fascinating about the rebound in investor activity in Sydney and Melbourne is that it has occurred in an environment in which interest rates really aren't that low.

The graph below compares nominal and real mortgage rates against their long-term average (defined in this situation as between 2004 and 2016). After adjusting for inflation, mortgage rates for investors are just 6 basis points below their long-term average and have tightened by 100 basis points over the past 18 months.

Chart 3: Australian variable mortgage rates



Source: ABS, RBA, via CP Economics

Earlier this week NAB and ANZ announced they would increase their fixed mortgage rates. NAB will increase its two-year fixed rate by 23 basis points and its three-year rate by 20 basis points. ANZ will increase its two-year and three-year fixed rate by 23 basis points.

With higher funding costs – and a requirement to hold greater capital – it is likely that banks will widen the spread between mortgage rates and the cash rate in an attempt to maintain profitability and dividends.

As a result, the cash rate may be at its lowest level in history but lower inflation and rising spreads has led to tighter lending conditions. Property investors are stuck in an awkward position – if inflation returns to more normal levels then they have made a sound investment, but if low inflation is persistent then borrowing costs are much higher than they have anticipated.

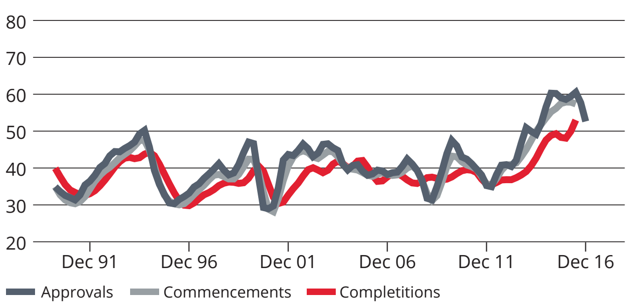
> “Nationwide housing valuations have never been higher. The house-price to income ratio is at its highest level in history and has increased by 26 per cent over the past four years.

It's a risky bet but one that, at least for now, thousands of investors are willing to make each month.

Building activity

I touched upon residential construction in last week's article (***Economic scorecard shows good results***, January 11) so I will only touch upon it briefly this week. Although building approvals have started to decline, building activity will remain at an elevated level throughout 2017 (even if construction activity falls a little from its current level).

Chart 4: Australian residential building activity (quarterly trend)



ABS, via CP Economics

This creates a range of opportunities for property investors, although the data suggests that these developments are typically funded by foreign investors. Domestic investors are more interested in purchasing established property.

Nevertheless, a large increase in the rental supply is likely to put downward pressure on domestic rents. Rents have always been a bit of an afterthought for domestic investors – the focus has always been on capital gains – but stagnant or even falling rents is hardly ideal for the savvy investor.

We are already beginning to see the effect of the boom on nationwide rents – with newly negotiated rents falling across most cities – and may continue over the next year or two. At the same time, net migration rates have declined to their lowest levels in 15 years, which may lead to lower-than-expected demand for new housing.

Investor activity may have rebounded in the property market but there are still a few headwinds that need to be navigated. Higher supply could weigh on prices and rents and low inflation – if persistent – will increase the debt burden on both existing and new investors.

Investors need to be aware of these factors when they consider their next purchase. They must also be aware that they are entering a market that has remained up a lot longer than most experts suggest. The opportunities for capital gains may not be over but are certainly not as widespread as they once were.

There are big differences between hybrid and bond issues. Two recent cases highlight that hybrid notes have few of the same characteristics.

BY PHILIP BAYLEY • EUREKA REPORT • 19 JANUARY 2017

Timely reminders that hybrid notes are not bonds

There were two events in the ASX-listed hybrid note market just before Christmas that provide a reminder that hybrid notes are not bonds. Hybrid notes have many of the characteristics of ordinary equity and few of those of bonds and, yet, are sold as being bond-like in terms of their income producing and capital preservation ability.

Key Point

- ***As a hybrid note holder you stand at the end of the queue for repayment when a company stumbles, just ahead of shareholders.***

The market value of a hybrid is likely to be more volatile than that of a bond, particularly where both pay floating-rate distributions or coupons. And the distributions paid on a hybrid may cease indefinitely and never be paid. This sounds much more like ordinary equity where the market value can move up and down and dividends may or may not be paid.

Insurance Australia Group (IAG) Capital Notes

On December 22, Insurance Australia Group announced the final size of its IAG Capital Notes issue (IAGPD), which would commence deferred settlement trading on the ASX the next day. The final size of the issue came in at $404 million, up from $350m after the bookbuild in late November, and up from $300m at launch in mid-November.

The notes will pay a distribution of 4.7 per cent over the 90-day bank bill rate, fully franked, and can be called in June 2023. Thus, the term to call is 6.5 years and the period to mandatory conversion is 8.5 years.

Demand for the notes in the secondary market was immediate and strong.

Despite a short trading session on December 23 and only two full trading sessions on the 27th and 28th, the price of the notes jumped to $103.80, from a face value of $100. This led stockbroker Morgans to downgrade its buy recommendation on the notes to hold, the day before trading on a normal settlement basis would begin.

Morgans had a fair value target of $101.53 on the notes and observed that the trading margin on the bonds had already fallen to 4.03 per cent, from 4.7 per cent at issue.

Curiously, IAG noted that rollovers from the $337m of IAGPC notes, due to be called in May this year, amounted to only $224m. The IAGPC notes pay a distribution of only 4 per cent over the 180-day bank bill rate.

It may well be that 34 per cent of IAGPC holders have an alternative use for their funds after May, and it is likely that some portion of these simply didn't receive notification of the opportunity to rollover, or failed to act for whatever reason. But as **previously noted**, ASX-listed debt security issuance could be sparse this year.

The total value of debt securities listed on the ASX is expected to fall as redemptions are likely to exceed new issues. In fact, redemptions in 2017 are expected to total $8.9 billion, but $5.4bn of these securities may not be replaced.

The potential lack of opportunities for debt security investment in 2017 is no doubt a factor driving up debt security prices at the present time. The price of the IAG Capital Notes has since moved past $105 but investors may well be underestimating the downside risks that can appear over time when pushing hybrid note prices so high and so quickly.

Paperlinx Step-up Preference Securities (SPS)

The Paperlinx SPS notes are an example of the very real equity-like risks that hybrid note holders are exposed to. It is a story that has been around since early 2007 and one that turned sour during the GFC.

The story will be familiar to many readers but perhaps less so to others.

Maybe it was deliberate, maybe it wasn't, but since outlining an offer to exchange Paperlinx SPS notes for Spicers' ordinary shares in mid-October, Spicers Limited (formerly Paperlinx) chose December 20 to advise the ASX that it had entered into a binding agreement with the Responsible Entity of the PaperlinX SPS Trust to implement the exchange.

> **“Investments can sour for bond holders, hybrid note holders and shareholders alike. But as a bond holder you stand close to the front of the queue for repayment when a company stumbles.**

As it is, the announcement doesn’t mean much.

The exchange proposal is fundamentally unchanged from that outlined in October in an announcement to the ASX, no extra spice has been added, and any exchange remains subject to the approval of both Spicers shareholders and holders of the SPS notes that are not already held by Spicers.

Due to reporting obligations and legal requirements, this vote will not take place until April 21 under the schedule put forward by the company.

But before going further into the details and implications of the exchange offer, why does Spicers want to do this?

When $285m of the SPS notes – with a face value of $100 each – were issued in February 2007, PaperlinX (as it was then known) had a market capitalisation of $1.7bn. But then along came the GFC.

No distribution payments have been made on the notes since the end of 2011, and the notes effectively became perpetual when the first date for redemption was missed at the end of June 2012.

The company went on to record losses every year and at the end of fiscal 2015 had negative shareholders’ funds of $126m. Last year, the company recorded a small profit of $5.3m.

The offer being put now to SPS note holders is an exchange of 545 Spicers’ ordinary shares for each SPS note held. This is expected to give note holders 68.3 per cent of the company, once the exchange is completed.

While this is a significant dilution of the position of existing shareholders, the value of the offer was put at just $14.72 per SPS by Morgans.

The offer is little better than the first offer made to note holders in October 2013. Then, Paperlinx offered a share exchange that valued the SPS notes at approximately $14 each but the shares were worth more and the exchange ratio was set at 250 ordinary shares to one SPS note.

SPS note holders were not thrilled with the offer and by the end of February 2014 Paperlinx closed the offer with acceptances from just 7.85 per cent of note holders.

In the meantime, a new note holder group emerged alleging that Paperlinx undertook share buybacks in 2013 and 2014 in breach of the terms and conditions of the notes. Such a breach would trigger an automatic conversion of the notes at full face value, into ordinary shares.

Conversion at this rate would give note holders around 94 per cent of the company, although this allegation appears to have been unfounded.

The latest offer is unpalatable for both shareholders and note holders but, as pointed out in Spicers’ latest announcement to the ASX, if the exchange is not approved by both then dividends and distributions will remain suspended for the foreseeable future, legal disputes with major SPS holders will likely continue and there will be no other feasible alternative for resolving the company’s complex capital structure.

Well, maybe the last point is open for further negotiation but this has been dragging on for years already.

Investments can sour for bond holders, hybrid note holders and shareholders alike. But as a bond holder you stand close to the front of the queue for repayment when a company stumbles; as a hybrid note holder you stand at the end of the queue, just ahead of the shareholders.

These outcomes could see the ASX-listed debt securities market shrink in size by as much as $7.5bn in 2017.

Philip Bayley is a former director of Standard & Poor’s and now works as an independent consultant to debt capital market participants. He is associated with Australia Ratings.

Uranium, not usually a commodity to interest most investors, is a case study for what's happening more broadly across the small to mid-tier resource market.

BY TIM TREADGOLD • EUREKA REPORT • 17 JANUARY 2017

Small miners reflect uranium's glow

Any doubts about whether seeds are being sown for a revival in the small to mid-tier section of the resources industry were dispelled last week when there was a minor boom in the most downtrodden group of mining stocks, those exposed to uranium.

Key Point

- ***While conditions are far more subdued than the boom years, there is evidence of a sustainable recovery in the resources sector.***

Largely forgotten, and still very high risk, the uranium revival saw the biggest local producer, Energy Resources of Australia, rise by 33 per cent (16.5c) over five trading days thanks to an unexpected increase in the price of the nuclear fuel.

ERA, which is an arm of the diversified mining giant Rio Tinto, was last in the news 18 months ago when it stopped mining at its Ranger project in the Northern Territory and switched to processing stockpiles, which it can do until 2020 without producing any fresh ore.

Back in mid-2015 ERA saw its share price devastated by the end-of-mining decision with the price plunging 75 per cent – from $1.34 to 33c – in a matter of days. Current trades at around 70c mean the stock is halfway back to its pre-crash level.

Other uranium-exposed stocks have done almost as well. Bannerman, which is exploring in Africa, rose by 31 per cent last week. Deep Yellow, another African explorer, gained 16 per cent, while Toro, a local uranium hopeful, was up 12 per cent in the week (to 6.2c – a price which means it is close to doubling since hitting a 10-year low of 3.5c last month).

What's driving uranium is the same force which is at work in zinc, oil and other commodities, and that's production limitation events – such as mine closures – designed to remove price-damaging surpluses from the market and, hopefully, spark a long-term price recovery.

Glencore, one of the world's biggest miners, has been largely responsible for the zinc price almost doubling from US65c to $US1.25 since this time last year, closing some of its mines in the hope of encouraging a metal-price recovery. In addition, Kazatomprom, the uranium business of the Kazakhstan Government, has help lift the uranium price from $US18 a pound to $US24 by announcing a 10 per cent production cut which will trim global uranium supply by 3 per cent a year.

The supply limitation strategy is working in zinc and uranium, and might also work in oil because cutting supply (even for six to 12 months) acts as a circuit-breaker that should see surplus material absorbed. This would permit a return to a conventional commodity cycle which could restart in time for what is expected to be a period of stronger global growth – barring a trade war between China and the US.

Uranium, which is definitely not a commodity to interest most investors, is a case study for what's happening more broadly across the small to mid-tier resource market, which is following the lead set by the top-end revival that has lifted the bigger producers (***Can mining repeat its resplendent 2016?*** January 12).

Across the resources sector there are green shoots to be seen, and while conditions are far more subdued than the boom years there is evidence of a sustainable recovery aided as much by higher commodity prices as sharply lower construction and operating costs.

New projects are not in the mega category of the boom, but there is a surprisingly long list of resource projects under construction or soon to start, including:

- **Gold Road** and its $500 million Gruyere gold mine in Western Australia being developed in partnership with South African mining giant, Gold Fields.
- **Albemarle** of the US and China's Tianqi and their $US300m expansion of the Greenbushes lithium project in WA.
- Locally-listed **Syrah Resources** making brisk progress on its $US185m Balama graphite mine in Mozambique.
- **Heron Resources** redeveloping the Woodlawn zinc and copper mine in NSW at a cost of $144m.
- Locally-listed **Paringa Resources** developing the $US40m Buck Creek coal mine in the US.

“For investors the latest events in the resources sector are pointers to 2017 being a continuation of the recovery which started at this time last year.

- **Pilbara Minerals** heading towards a mid-year start-up of its $214m Pilgangoora lithium mine in WA.
- **OZ Minerals** starting construction on its $975m Carrapateena copper mine in South Australia.
- **Mount Gibson Iron** developing its small but life-extending Iron Hill iron ore mine in WA at a capital cost of up to $3m.
- **Rio Tinto** developing the $US1 billion Silvergrass iron ore mine in WA to maintain overall production at current levels.
- **Dacian Gold** starting work on its $220m Mount Morgan goldmine in WA.

Those 10 examples are not the full list of projects under construction or about to start, but their value lies in demonstrating that the resources sector, after five difficult years, is regaining its strength.

Other signs of the resources recovery can be seen in measures such as a 2 per cent rise in Perth residential property prices in December; a small increase but one which could be signaling the end of the dramatic collapse in the one-time boom town.

Rising job advertisements for mining professional is another indication of the change in market conditions, with the best example being a search by Australia’s richest person, Gina Rinehart, for 500 additional workers for her part-owned Roy Hill iron ore mine in WA.

Other clues pointing to a sea-change in resources include:

- Deal flow with **EMR Capital**, a fund led by long-term mining executive, Owen Hegarty, paying $US210m for the historic Golden Grove copper and zinc mine in WA.
- **Birimian**, a low-key ASX-listed explorer, announcing that it has signed a deal to sell its Bougouni lithium project in Africa to a Chinese company for $107.5m in cash – an interesting price, as Birimian is currently valued on the market at $62.5m.
- Takeover interest with higher commodity prices generating an urge to merge, with the latest being a proposed $US5bn deal between London-listed goldminer **Acacia Mining** and Canada’s **Endeavour Mining**.
- Indications of an increase in initial public offerings (new floats) by small mining companies, with 13 resource-linked stocks listed by the ASX trying to raise capital (though most of those – nine – appear to be struggling, with listing dates postponed).
- Strong cash flows from higher prices and lower costs enabling small (and large) miners to retire heavy debt loads taken aboard during the lean years.

That final point is best demonstrated by the upgraded credit rating awarded last week by S&P Global Ratings to Atlas Iron, an iron ore miner once struggling to survive a deadly mix of high debt levels and a low iron ore price.

With iron ore at $US80 a tonne, Atlas is making solid profits and retiring debt (including a $54m payback last week), which has been good enough for S&P to upgrade it from its low CCC rating to B-minus (still considered by ratings agencies to be below investment grade status).

For investors the latest events in the resources sector are pointers to 2017 being a continuation of the recovery which started at this time last year.

The next clues to whether the revival can continue will come from the commodity markets, especially China’s appetite for resources, and from the political climate which is becoming more interesting as Donald Trump moves closer to starting his four-year term as US president.

St Barbara is blazing a golden trail – with other miners following – as rising cash flows and falling debt put expansion and dividends back on the agenda.

BY TIM TREADGOLD • EUREKA REPORT • 19 JANUARY 2017

How will miners splash their cash?

St Barbara, the goldminer named after the patron saint of miners, performed what some investors might regard as a miracle by achieving debt-free status in the December quarter and moving towards an expansionary phase – and possible payment of dividends.

Key Point

- ***The change in resource-sector finances has set the scene for a classic re-run of the owner-versus-management tussle.***

Good news as that is for shareholders, who have already enjoyed a 75 per cent rise in the value of their investment over the past 12-months – and a spectacular 1100 per cent rise over the past two years – St Barbara is not alone among gold miners, or the wider resources sector.

Sharply lower operating costs forced on the industry by the collapse in commodity prices during 2014 and 2015 are being supercharged by an unexpected recovery in metal (and oil) prices, delivering rivers of cash that are dramatically altering the outlook for the sector.

Repaying debt is the current focus of the miners enjoying the cash splash, but that trend could change over the course of 2017 if profits remain high and the urge to do something with the cash becomes irresistible.

Fortescue Metals, once regarded as having a debt servicing problem, has seen its share price rise by 300 per cent over the past 12 months, thanks, in part, to retiring more than $4 billion in debt as well as earning a credit-rating upgrade (as it moves towards a net-debt free position by next year, if the iron ore price stays high).

Atlas Iron has survived a near-death experience and retired a large proportion of its debt and has also earned a ratings upgrade. Whitehaven Coal has paid back $1b of its debts over the past 18 months, and South 32 has been free of net debt since the middle of last year and is now accumulating cash.

The change in resource-sector finances has set the scene for a classic re-run of the owner-versus-management tussle.

Shareholders, after a few lean years, will be demanding higher dividends. Management, with an eye on the depleting nature of all mines, will be looking to add assets by developing or expanding mines, or by mergers and acquisitions (M&A).

Both sides will be praying that history is not repeated and mistakes of past 'good times', such as Rio Tinto's ill-timed $US40bn acquisition of Alcan or BHP Billiton's equally ill-timed $US20 billion plunge into US shale oil.

It is those glaring, and relatively recent, management errors which mean the cash flowing into resource company accounts today is more likely to find its way to shareholders than to project expansion or M&A.

In other words, mining companies are moving towards 'cash cow' class, which will add to their investment appeal so long as the good times last – which leads to an obvious question: will they?

As always, when it comes to mining and oil, that's a question to keep investors on their toes because the world will be a different place from Friday (Saturday morning our time) when the new US president, Donald Trump, is sworn in and a damaging trade war with China gets a little closer.

Gold, if Trump delivers on his protectionist threats, could emerge as one of the winners from a trade war and its currency-value implications; that's why the price of the metal has added $US80 an ounce over the past month to $US1204 and the Australia gold price has moved back above $1600.

St Barbara was able to ride the gold price and achieve sharply lower costs in the December quarter when it lifted gold output to 98,982oz (up from 92,546oz in the September quarter) at a cost of $A876/oz versus $A935 in the September quarter.

That strong result enabled St Barbara to repay another $US20 million in debt, leaving a residual $US20m which will be repaid in the next two months. Set against the remaining debt is a cash balance of $A31m and another $A23m in gold.

The Gwalia mine in WA is the major contributor to St Barbara's good fortune today, but it is also a reason for the company to be looking for other opportunities because it is old and very deep (more than a kilometre) and a natural end to mining looms because depth in mining equals cost (with the saving grace for Gwalia being its rich ore).

> **BHP’s debt-to-equity ratio, according to Deutsche Bank, was 43 per cent in 2016 and is expected to fall to 25 per cent this year.**

Other recent examples of the cash flood being enjoyed by miners include Evolution Mining, which is expected to report increased gold production at a lower cost next week, and Wesfarmers, which has enjoyed a windfall of up to $140m from its coal operations.

Whitehaven, the biggest of the pure-play coal producers on the Australian stock market, is expected to be debt free by the middle of the year according to Morgan Stanley, an investment bank.

“We expect Whitehaven to be net cash by around the end of the 2017 financial year, a stark contrast to this time last year when a common debate was whether it would repay $A1bn in debt by 2019,” Morgan Stanley said in a note to clients on Tuesday.

Deutsche Bank, in a review last week of the mining sector, generated estimates which highlight the shifting financial tide caused by the inflow of cash with two sector leaders, BHP and Rio, expected to see a sharply improved debt-to-equity ratio this year and next.

BHP’s debt-to-equity ratio, according to Deutsche Bank, was 43 per cent in 2016 and is expected to fall to 25 per cent this year and then down to 21 per cent in 2018. Rio’s ratio last year was estimated to be 20 per cent, falling this year to 15 per cent and then down to 11 per cent in 2018.

The trend of increasing cash, falling debt ratios and more miners achieving net-debt free status promises to be the scene-setter for the resource sector this year if prices stay high, costs stay low and Trump doesn’t ignite a trade war with China

Questions and answers on the treatment of defined benefit pension schemes, non-concessional contributions and transition to retirement strategies.

BY BRUCE BRAMMALL • EUREKA REPORT • 17 JANUARY 2017

Advisor Q&A: The hottest super topics

Defined benefit pensions, recontributions and TTR strategies seem to be the issues causing the most angst for Eureka Report's self-managed super fund army right now.

Key Point

- ***Couples' strategies will be one of the most crucial elements of all super strategies in years to come.***

I've received many questions around the topics raised in my columns on how DB funds will be treated regarding the upcoming changes (see ***The new rules for defined benefit schemes***, November 2016) and also regarding the removal of segregation (***In defence of SMSF borrowing restrictions***, December 2016) for pension funds in SMSFs.

So today I'm going to try to answer some of those. Where questions overlapped on similar topics, I've generally used the one that allowed me to cover off on the topic best, or most succinctly.

Q: *At what point in time will the boffins value the DB? At the time the pension is commenced or using some method at June 30? The reason I ask is that I will commence my DB pension in February 2018 and also have an SMSF. There is no way of predicting the final pension I will receive in February 2018 as there may be pending pay rises, etc, which will affect the final pension payment amount. How can I calculate my total super balance at June 30, 2017 if I do not have a value for the DB at this date?*

A: An interesting one that Aaron Dunn from The SMSF Academy helped me with.

You will be able to continue to run your SMSF pension as normal, until such time as you start to take the defined benefit pension. At the time the DB pension starts to be paid, you will then have to switch back part of your SMSF pension to accumulation.

For example, say you have the full $1.6 million in pension mode in your SMSF. In February 2018, you start to receive your DB pension of $50,000. The value of a DB pension (for the purposes of the $1.6m limit) is to multiply the pension amount by 16. So a $50,000 pension is worth $800,000. That would mean that you would have to turn back $800,000 (or in this case, half) of your $1.6m SMSF pension.

Further, if you were to start your pension with $1.6m on July 1, 2017 and it was valued at $1.7m by the time the DB was turned on, you would only have to switch back $800,000 of the SMSF pension to accumulation, leaving $900,000 in the pension.

This goes back to the fact that DB funds are valued at the top of the chain, because they can't be commuted, said Dunn.

Q: *I am 71 and have an SMSF. I'm still working part-time with a taxable income of $80,000, while my wife is 68, retired, with no taxable earnings. I also receive a defined benefit tax-free pension of $100,000. Upon my death, my wife will receive that death benefit pension. In our SMSF, we are both in pension mode. My wife's current balance in SMSF is $850,000. I will have to cease my SMSF pension and transfer to accumulation mode by July 1, 2017. How much can I transfer to my wife's SMSF as a non-concessional contribution?*

A: Sadly none, as your situation stands. In the horse trading that went on for the Government to get its legislation through, the plan to raise the age limits for contributions to 75 got dropped.

Yes, you'll have to turn your SMSF pension back to accumulation, because your $100,000 DB pension will be valued at $1.6m.

Unfortunately, the only way you will be able to get money into your wife's superannuation account would be to qualify for contributions under the work test rules. That is, she would need to work 40 hours in a 30-day period.

If she were able to do this in the current financial year, then she would qualify to be able to put in up to $180,000 as a non-concessional contribution to super. If she then also qualified in the FY18 year, she would be able to contribute another $100,000.

Those 65 and older aren't able to use the pull-forward provisions.

> **“Transition to retirement strategies were once so wonderful. But since their introduction, governments have whittled away at their effectiveness.**

Next: Two questions about couples' super strategies, covering off on recontribution and super splitting.

Q: *I have seen no discussion about the possible use of a recontribution strategy for pension accounts that exceed the $1.6m pension cap coming into effect in July 2017. A member whose pension balance exceeds $1.6m could make lump sum withdrawals and recontribute these funds to a member with less than $1.6m, providing they don't exceed the non-concessional contribution cap.*

Q: *I understand the benefit of super splitting with your spouse if one balance is over $1.6m. However, is there any advantage (or possible future advantage, given potential changes of government) for a retiree with a balance a little under this figure to transfer some super to their spouse with a much smaller super balance?*

A: I have touched on the sorts of strategies required to help even-up super funds between couples several times. This will be one of the most crucial elements of all super strategies in years to come. And many should have already started, including by potentially using recontribution strategies.

For more information, please see columns from me **here** and briefly **here**. The first one will contain the Government's plans from the May Budget, many of which were changed, but the rough detail is still appropriate.

Specifically with regards to recontribution strategies, yes, this will make some sense, though you need to be careful around being able to get the money back into super.

Where one member with a large balance who is over 65 is coupled up with a younger member with a small balance who is under 65, this could work well. As they have hit 65, they can withdraw from their super and, assuming they can get it into the younger member's account, they will be able to put in up to $540,000 this financial year, or $300,000 in FY18 (using three-year pull forward at the new rate of $100,000 a year).

But more importantly, couples must start to even-up super balances from a younger age. This could mean using the 'spouse super splitting' strategies of moving concessional contributions from one partner to the other.

Q: I am 62 and have a transition-to-retirement (TTR) pension with super balance above the $1.6m limit. To convert the TTR to an account-based pension (ABP), you state one has to change jobs. Are you able to elaborate?

A: TTRs were once so wonderful. But since their introduction, governments have whittled away at their effectiveness. It's our fault. We saw them not for what they were meant to be (a way of gently easing out of the workforce), but for what they could be (a great way to save tax in your final years in the workforce).

The pension funds backing TTRs will be taxed from July 1 as if they were in accumulation phase. So if you wish to stop that occurring, you should take advantage of an opportunity to switch your fund from a TTR to an ABP, should you qualify.

It's less about changing jobs and more about 'ceasing an employment arrangement' after turning 60 that will allow you to end the TTR pension. One way of ceasing an employment arrangement is to change jobs. Another is to retire after hitting 60.

You might have a number of roles that you work in. You only need to cease one of those employment arrangements after hitting 60 to qualify. But make sure you get some advice from a financial advisor or accountant in this area before going ahead.

Bruce Brammall is a licensed financial advisor, a mortgage broker and an expert on self-managed super funds. He is a regular contributor to Eureka Report. To contact Bruce, please ***click here****.*

The information contained in this column should be treated as general advice only. It has not taken anyone's specific circumstances into account. If you are considering a strategy such as those mentioned here, you are strongly advised to consult your advisor/s, as some of the strategies used in these columns are extremely complex and require high-level technical compliance.