Weekly Review

RESEARCH

– Issue – 17 Mar. 2017

Origin is selling its production business to reduce debt, but will it make much difference to the investment case?

BY GAURAV SODHI • INTELLIGENT INVESTOR • 14 MARCH 2017

Origin readies for split

For the first time since listing, Origin released its recent interim results without Grant King in sight. Frank Calabria, who formally ran the domestic retail business, is the new boss and things are already changing.

Key Points

- ***Spilt of production assets confirmed***
- ***Will improve cash flow***
- ***Debt still too high***

ORIGIN ENERGY (ORG) / HOLD

Price at review	Max. portfolio wght.	Business risk	Share price risk
$6.54	4%	Med–High	Med–High

BUY Below $4.50 | HOLD | SELL Above $12.00

$6.54

We rated King highly, even after the losses from LNG. Before anyone else, it was Grant King who saw the benefits of vertical integration and understood how renewables and gas would alter the energy market. His replacement appears keen to make his mark, making changes in swift time.

With the APLNG project now completed and contributing cash flow, the focus has shifted to lowering Origin's enormous $9bn debt pile.

Production split

To that end, Origin will split its oil and gas production business from the rest of the company via either a trade sale or an IPO.

The new company will include fields in the Cooper Basin, the Otway Basin, the BassGas project, fields offshore New Zealand and, perhaps the best asset of the bunch, the newly discovered Waitsia onshore gas field in WA.

The sale will raise $1bn–2bn and help lower debt.

Lowering debt is certainly a good thing but, by losing its production business, Origin will lose a vital advantage: operating energy assets gave it a natural hedge against price changes at its energy retail business. Without the production business, Origin will be more exposed to price swings.

Different split

The sale will, however, lower capital intensity and reduce cash outflows. The production business routinely sucked in capital and spat out little cash. Expelling production assets will help to conserve cash.

We have long imagined a split, but we didn't think it would look like this. Instead of spinning off APLNG, Origin has elected to keep it. We might yet see a sell down or exit from the LNG business if oil prices get higher but, for now, Origin will remain a dual-natured beast.

Continued on page 2 ...

CONTENTS

IMPORTANT INFO

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Continued from page 1 …

The core energy markets business remains the top earner. Its $12bn of assets should comfortably generate at least $1bn in operating profit annually and spit out healthy free cash flow.

Table 1: Origin valuation

	US$50 OIL		US$90 OIL	
	EARNINGS	VALUATION	EARNINGS	VALUATION
RETAIL ($M)	800	10,000	1,100	13,750
PRODUCTION ($M)	100	2,000	400	4,500
APLNG ($M)	400	4,000	1,000	10,000
DEBT ($M)		(8,500)		(8,500)
CORP COST ($M)		(800)		(800)
TOTAL ($M)		6,700		18,950
SHARES (M)		1,750		1,750
$/SHARE		3.83		10.83

The LNG business is trickier. Over $20bn has been spent by Origin and its partners building APLNG. Origin's 37.5% stake has a notional cost of about $10bn but it is earning a pittance while oil prices remain low. Hedging will limit losses and write-offs will lower depreciation charges. As debt falls, so will interest costs and a decent flow of cash could ultimately come from the project.

At US$90 a barrel, APLNG was supposed to generate generous free cash flows of about $1bn a year. It might not get that high but it may not be too far off. All up, Origin's stake in APLNG could be worth $4bn–10bn, depending on oil prices.

Fairly priced

Adding the two pieces together (see Table 1) Origin itself is probably worth between $4 and $11 a share. The wide valuation reflects the huge variability imposed by oil prices, leveraged with debt.

Origin may now look a little different, but not much has changed about the investment case. Current prices are probably marginally cheap but not enough to elicit any action.

Origin still carries too much debt but the strong retail business offers armour its peers lack (we're looking at you, Santos). The LNG business also carries extensive hedging to limit downside if oil prices should crash again. We will update the situation following the asset sale but, for now, **HOLD**.

Note: The Intelligent Investor Growth Portfolio *owns shares in Origin. You can find out about investing directly in Intelligent Investor and InvestSMART portfolios by* clicking here.

Staff members may own securities mentioned in this article.

Shareholders will receive shares in a new company to be floated on the London Stock Exchange.

BY JON MILLS • INTELLIGENT INVESTOR • 17 MARCH 2017

Reckon to spin off Document Management

When we **upgraded Reckon** to Speculative Buy last August, we felt the sum of its three businesses was greater than the whole. It seems management agrees with us, and today it has announced plans to spin off its Document Management division to existing shareholders. As 85% of the division's revenue comes from overseas, primarily the United Kingdom and United States, the new company (Newco) will be listed on the AIM market of the London Stock Exchange rather than the ASX.

Key Points

- ***Document Management business to be spun off***
- ***Shareholders will also be able to invest further in Newco***
- ***Boosts earnings and cash flow of remaining businesses***

RECKON (RKN) / SPECULATIVE BUY

Price at review	Max. portfolio wght.	Business risk	Share price risk
$1.71	3%	High	Med–High

BUY Below $1.70 — HOLD — SELL Above $2.70

$1.71

As we explained in ***Reckon: Result 2016***, the company's Document Management business is its fastest-growing division. However, due to the expenditure required to market and integrate its SmartVault and Virtual Cabinet products – and develop a cloud-based version of these products – the division currently produces little free cash.

So while Reckon will lose its fastest-growing business, spinning off the Document Management division will increase the earnings and cash flow of Reckon's remaining Practice Management and Business divisions – at least in the near term – and the company will able to direct the cash flows from these businesses to other uses, such as further developing existing products, making acquisitions, reducing debt or returning it to shareholders.

For its part, Newco will be able to access the additional capital it needs via the public markets. To help it along, Reckon shareholders will also have the opportunity to invest further in Newco as part of the restructure.

Freed from its association with Reckon's slower-growing businesses, we wouldn't be surprised to see NewCo valued at high multiples of revenues given it's a fast-growing, subscription-based business with a large addressable market. This is another reason why it is being listed on AIM rather than the ASX.

More attractive to suitors

With its underlying earnings and cash flow now more apparent, investors may also focus more on the strength of Reckon's Practice Management division and the still-decent cash flows from its Business division.

During its strategic review 18 months ago, the company received a number of offers but management felt they undervalued the company. No doubt prospective purchasers considered the large development expenditure requirements of the various divisions in making their offers, so a reduction in this expenditure may make the remaining Reckon business more attractive to suitors.

In that vein, Reckon's Business division – which recorded $17m in underlying earnings before interest and tax in 2016 – could be attractive to a competitor. A purchaser would not only gain its existing 39,000 online customers but potentially the 100,000 to 150,000 customers that are estimated to still use its desktop products. These customers could be transferred to any purchaser's products at a lower cost than having to acquire them individually. Any deal would also remove the low-cost competitor in the small business accounting space, thereby potentially improving the profitability of remaining competitors.

While planning is still in its early stages, the potential spin-off suggests our investment case is on track. It also perhaps illustrates one benefit of investing alongside owner-managers.

The company will release more detailed information towards the middle of the 2017 calendar year and we'll provide a further update then.

The stock is hovering just above our $1.70 Speculative Buy price but, for now, it remains a **SPECULATIVE BUY**.

Disclosure: The author owns shares in Reckon.

High returns are being made today by this classifieds search business but we are unsure whether it will last.

BY ALEX HUGHES • INTELLIGENT INVESTOR • 13 MARCH 2017

Can Mitula keep making moolah?

On my first trip to Indonesia I rode to a remote beach on a rented scooter. As I approached, I was confronted by a drop-down boom gate blocking my way.

Key Points

- ***This vertical search operator looks cheap***
- ***But its value-add is questionable***
- ***Wait for lower prices***

MUTULA GROUP (MUA) / NO VIEW

Price at review	Max. portfolio wght.	Business risk	Share price risk
$0.89	N/A	High	High

The gate operator didn't own the beach, nor the road, or even the surrounding property. He simply owned the gate. This entitled him, at least in his mind, to charge fees to whoever passed. Despite offering no value, he had a thriving business thanks to a consistent stream of bewildered tourists, myself included.

Online businesses have emerged that resemble this Indonesian entrepreneur's. Lots of online traffic is very valuable when monetised with advertising. Just ask Google. But like the Indonesian entrepreneur, if the websites don't add value it's hard to imagine them staying in business for long.

Which brings us to Mitula, a search engine for classified websites, with 88 sites in 51 countries.

Its headline numbers caught our eye, **trading on less than 10 times enterprise value to earnings before interest, tax, depreciation and amortisation** (EBITDA). But we have concerns about the value it provides to its customers. It's making good money today, but we have no idea what it will be earning in five years, and that is keeping us away.

So, if you don't have any interest in learning about Mitula's business, we suggest you stop reading here. The rest is for the curious few.

Business model

Mitula's sites focus on real estate, cars and jobs. Instead of displaying original content, Mitula aggregates content from other online classifieds. The value that it adds is convenience. Instead of having to visit numerous sites, Mitula is a one-stop shop. It gets paid for referring visitors to the original classifieds. This contributes 66% of total revenue. The rest comes from display advertising.

Mitula's strategy can be depicted as a kind of leaky funnel. Step one is to pour as many site visitors as possible in at the top. Step two is to maximise the number that 'click through', and flow through at the bottom.

Along with a cash generative business, as table 1 shows, Mitula has some bright cookies holding the reigns. Its Chairman is Simon Baker, the ex chief executive of **REA Group**. Management also owns a lot of stock, so they certainly believe in the business.

Questions about consolidation

With aggregators, convenience is maximised when many classifieds compete. In markets like Brazil or the Philippines, where five or more classifieds go head to head in a single category, aggregation is a useful service.

Table 1: MUA financials

YEAR TO DEC ($M)	2012	2013	2014	2015	2016
REVENUE	8.1	10.6	10.7	20.6	28.0
EBIT	0.9	2.5	5.2	6.4	9.9
NPAT	0.6	1.8	3.8	2.6	8.2
OPERATING CASH FLOW	NA	NA	4.5	4.9	8.9

But what happens if these markets consolidate to the point where one or two classifieds dominate? REA Group and Domain cover Australia's property market, with significant overlap in terms of the underlying properties. Here, going direct to one classified gets the job done, so Mitula's proposition seems questionable.

It comes as a surprise then to see half of total revenue come from the UK, Australia, Denmark and France – markets where a smaller number of classifieds compete and we'd expect the aggregator model to be weaker. Profit from these markets isn't disclosed, however, so we are unable to see if the revenue generated in developed markets is profitable.

> "This just doesn't strike us as a very robust business, so we'd want to see a greater margin of safety before recommending it.

This risk we have outlined is based on the assumption that developing markets will eventually consolidate. It may be that the presence of aggregators like Mitula slows, or even prevents, industry consolidation.

Where's the value?

'Cost per click' models are reasonably common these days, but Mitula is much more peculiar. It competes with original classifieds for traffic, and then seeks to profit by directing the same traffic back to the same classifieds. It doesn't seem like a strong value proposition on the surface. Just imagine, if Mitula was wiped off the face of the earth, all of the original classifieds would still exist. It would simply take a few extra minutes to browse multiple classifieds.

Perhaps Mitula's real value is its screening, where it weeds out the tyre kickers and delivers higher value visitors to the classifieds. If that is the case, Mitula could then justify charging a higher 'per visitor' price compared to paid search. Operating profits in the core 'click out' business may reflect this. It is the difference between the revenue from referring visitors and the cost of attracting them after all. But operating profit by business activity is not disclosed, so we turn to a back of the envelope calculation to find the answer.

Display advertising generates 34% of total revenue. Mitula uses GoogleAdSense for this so there is almost no associated cost. After coding a portion of its webpages to AdSense, Google does the rest. So operating margins should be very close to 100% in the display advertising division. As group operating margins also approximate 34%, it seems that display advertising is the real profit centre for Mitula. Take away Adsense and you are left with a marginally profitable Mitula.

This may mean that our fears are unjustified. As long as Mitula can continue to generate a lot of traffic, even if its click out revenue only just covers the cost of generating traffic, it can maintain profitability from its Google AdSense business. This just doesn't strike us as a very robust business, so we'd want to see a greater margin of safety before recommending it.

With that said, Mitula is similar in some ways to **Webjet**, which has been confounding the sceptics (**ourselves included**) for years. Its fees can be avoided by transacting directly with the airline, but it has gone from strength to strength as consumers pay up for convenience. We might be making a similiar mistake with Mitula, but experience tells us that if we lack conviction, it makes sense to move on.

We'll keep an eye on the stock, but for the time being we won't be initiating coverage.

Staff members may own securities mentioned in this article.

The Australian cannabis industry is running on rocket fuel, but is it possible to pick winners?

BY GRAHAM WITCOMB • INTELLIGENT INVESTOR • 16 MARCH 2017

Medical marijuana and the one hit wonders

Behind the frosted windows of a generic-looking shopfront – just a few blocks away from my home in Vancouver – is an industry exploding. Later this year, Canada is set to be the first major developed nation to legalise recreational marijuana use, and there's no shortage of entrepreneurs wanting to make money from the move.

Key Points

- ***Demand will grow quickly as countries legalise use***
- ***Export market the big honeypot***
- ***No competitive advantages; first mover illusion***

Company info

COMPANY (ASX CODE)	CURRENT PRICE ($)
AUSCANN (AC8)	0.58
CRESO PHARMA (CPH)	0.68
MMJ PHYTOTECH (MMJ)	0.52
MGC PHARMACEUTICALS (MXC)	0.09
ZELDA THERAPEUTICS (ZLD)	0.08

I've never seen such feverish capitalism in action. It seems every second billboard has a cannabis-related message – where to find prescribing doctors, growers, business advisors, websites and retail outlets. In Vancouver, cannabis dispensaries now outnumber McDonald's restaurants. That the drug is still technically illegal seems a mere detail.

And this has all popped up in the last year or so, with companies trying to build their brands before the flood gates open. Recreational consumers may be known for their slow reaction times but the industry pros are in fifth gear.

Over the next few years, you're going to see a lot more hype around the business of marijuana. The drug was legalised for pain relief and medical use in Canada in 2001, so the industry there got a head start, but many countries are in the process of reducing restrictions, including Australia. Cannabis is already available in 28 US states, much of Europe and South America.

Path to legalisation

In February 2016, the Government legalised growing marijuana for scientific or medical purposes in Australia, too. Cannabis's medicinal consumption was legalised in Victoria and New South Wales late last year and it was legalised at the federal level in November.

By most hazy estimates, around one million Australians used marijuana in the past year, though – as you probably guessed – most people obtained the drug without using an 'authorised prescriber'.

The local cannabis industry has investors excited; several companies have listed on the ASX recently that focus on marijuana production, distribution or research. These include **AusCann**, **MMJ Phytotech**, **Creso Pharma**, **Zelda Therapeutics**, and **MGC Pharmaceuticals**.

The only hiccup was that – despite medical marijuana's legalisation – being able to actually supply the product to consumers in the short term was difficult due to a lack of cultivation permits. Providers need to import the medication from overseas, mainly from Canadian suppliers, on a case-by-case basis.

However, the industry got a further booster shot last week when the first licence to grow and harvest marijuana for medical purposes was granted to an Australian company, the soon-to-float Cann Group. As operations get up and running, local supply should increase to meet demand, and the Government has also introduced an interim scheme to make importing the drug easier for distributors. The share prices of most cannabis-related stocks have doubled since the beginning of the year.

So, is this an opportunity for investors? We know demand for purely medical purposes – and impurely medical purposes, if you prefer – is strong, so these companies aren't like other start-ups where eventual demand for their product is unknown. It also seems likely that legal barriers will be progressively lowered.

Export market

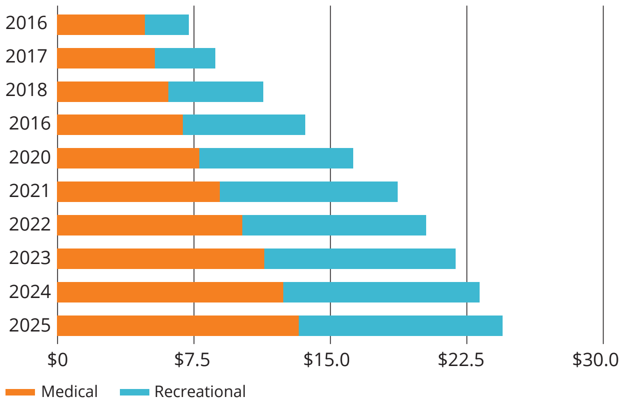
But, for the sake of argument, let's assume recreational legalisation in Australia never happens. What then? The licences to grow and research are still extremely valuable. Local demand can remain confined to the small medical community, but exports were almost certainly going to be the real honeypot anyway.

> **At this stage, we don't consider any cannabis companies to have a sustainable competitive advantage.**

Australia already has a reputation for the cultivation and export of pain-relieving drugs. Australian companies supply 50% of the world's raw legal narcotics, such as morphine, thanks to their large opium poppy plantations in Tasmania. That reputation for quality and safety standards won't go astray.

The cannabis export market could be huge. US cannabis sales are expected to triple over the next eight years to US$24bn (see Chart 1).

Chart 1: Projected US marijuana sales ($bn)



Source: New Frontier Data

When Canada legalises cannabis in a few months, 600,000kg will be needed to satisfy the recreational market each year. That exceeds the combined capacity of Canada's 36 licensed cultivators, according to a **recent report by Deloitte**. If expected yearly sales of C$5bn–9bn are in the right ballpark, then Canadians crave cannabis more than chocolate or wine.

So it's pretty clear there is room for an Australian export market and some companies have already established production facilities overseas as they wait for local licences.

MMJ Phytotech is better placed than most other ASX-listed cannabis producers on this front as it was recently granted an import permit by Health Canada and the Canadian Food Inspection Agency, making it one of the few companies able to import new cannabis varieties into the country.

MMJ's new British Columbia-based production facility will have the capacity to grow 7,500kg of cannabis by the end of this year, with plans to scale that up to 60,000kg over the next few years.

'This level of production will enable the company to establish a strong first mover advantage in the Canadian market, whilst also giving MMJ the flexibility to supply other regulated markets globally,' say management.

Not so fast

When considering up-and-coming industries, it's important to remember that there's a big difference between forecasting significant growth in demand and picking the individual companies that will benefit from it.

When the internet's popularity gained speed in the early 1990s, it was clear that it would soon be a huge money-spinner – but could anyone have predicted that Google, Facebook and Amazon would displace Yahoo, MySpace and Barnes & Noble? The first mover advantage is often an illusion.

At this stage, we don't consider any cannabis companies to have a sustainable competitive advantage. True, some have temporary moats in their cultivation licences or import permits, but there aren't explicit caps on issuing them, so it's only a matter of time before more competitors saturate the market and crush margins. Today's supply and demand imbalance is likely to be short-lived.

Like most agricultural products, cannabis production has significant **economies of scale**. Large farms supplying national and international markets would have lower average costs than the current small-scale warehouse business model. The largest Canadian grower, Canopy Growth, is six times larger than the biggest Australian-listed producer, AusCann. It has another thing going for it too – existing revenue.

The large agricultural conglomerates are also unlikely to let the opportunity go begging and, as cigarette sales become harder won, how long before big tobacco outfits like Altria and Reynolds American decide to take a slice of the pot pie (or should that be brownie?).

> **“Without any company possessing a moat and new competitors arriving every month, predicting long-term profitability for these stocks is next to impossible.**

Australian cannabis producers now work under a more favourable regulatory framework and that is undoubtedly a better place to be than where they were a few months ago. It's a reasonable bet that sales will grow at a record pace as capacity ramps up and more countries legalise consumption.

Nonetheless, without any company possessing a moat and new competitors arriving every month, predicting long-term profitability for these stocks is next to impossible. With no money coming in – and lots going out as they build their facilities – the companies have kept themselves afloat largely through capital raisings and taking on debt. Clean balance sheets are few and far between.

We claim no special insight into being able to pick the long-term winners in this new sector. Indeed, if anyone suggests to you that they can, we'd suggest you politely ask if they've been sampling the products.

Indeed it's quite possible that no-one will end up making outsized returns. We wish these companies the best, but until industry margins settle and we see consistent sales, we'll be searching for value elsewhere.

Staff members may own securities mentioned in this article.

CIMIC's bid for Macmahon has failed. What now?

BY GAURAV SODHI • INTELLIGENT INVESTOR • 14 MARCH 2017

CIMIC walks from Macmahon

CIMIC's bid for Macmahon has failed and ended with the suitor holding less than 24% of its target. The share price has risen and fallen with the changing prospects of the bid but now sits at 15c, 3% above our **previous sell price**.

MACMAHON HOLDINGS (MAH) / SELL

Price at review	Max. portfolio wght.	Business risk	Share price risk
$0.15	1%	High	High

CIMIC is, for now, out of the contest. We can't know whether they will make another bid for the business.

Macmahon itself has sought an alternative arrangement, announcing a deal with Indonesian miner AMNT to acquire mining equipment and a long-term contract in exchange for between 40–50% equity in the business.

If the deal goes ahead, Macmahon will issue fresh equity to AMNT at 20cps, a 33% premium to the current price but, given where the share price is, the market appears sceptical.

We concur. The potential new contract, worth $2.7bn in revenue over its life, is several times Macmahon's largest existing contact. It would be a large revenue earner for the business and allow it work on one of the biggest gold mines in the world. It would also introduce an unknown Indonesian business as a major shareholder and a new set of risks.

Indonesia is a graveyard for miners. The Grasberg mine on West Papua – the single largest gold deposit in the world – has been more a headache than a mint for its operator, Freeport. Several promising miners – **Intrepid Mines** and **Kingsrose** among them – have failed in Indonesia despite excellent geology. This is not an easy place to do business and we can't find many examples of partnerships working.

The timing of the AMNT deal is also noteworthy. In an industry swamped by overcapacity and competition, it's likely that this deal was put together with defence rather than profits in mind and we question how profitable it will ultimately be.

The Indonesian firm would hold enormous bargaining power and is incentivised to capture higher production margins rather than service margins. As Macmahon itself has learnt (as well as several peers in the sector) customer concentration is something to sweat not something to crow about.

CIMIC is out of the picture for now and we won't speculate on its next move. With billions of dollars' worth of new work, Macmahon could be cheap but that cheapness comes at considerable risk.

We've always viewed fair value at around the net tangible asset backing of 16–17c. Although we are slightly below that, there isn't enough upside to change our recommendation. **SELL**.

Staff members may own securities mentioned in this article.

It's often the nasty surprises – when the forecasting machine gets it wrong – that bring the best opportunities.

BY JOHN ADDIS • INTELLIGENT INVESTOR • 13 MARCH 2017

No easy pickings in a hard Brexit

Bad news often brings opportunity. Two weeks ago, for example, **iSentia** (ASX: ISD) joined our Buy List after it announced one of the worst results from the recently completed reporting season.

The result was so unexpectedly poor the share price was hammered, to a point where it offered great value. The market doesn't like surprises, making reactions to them punishingly extreme. It is the over-reaction that creates the opportunity.

So, will the triggering of Article 50 – the UK's official notification of its intention to withdraw from the European Union – which, according to Liam Fox, the UK's international trade secretary, could happen 'this week or next week or the week after' offer similar opportunities?

It's unlikely. The initial vote to leave Europe, like iSentia's recent result, was a surprise. The subsequent market adjustment offered us the opportunity to **upgrade a handful of stocks**. Article 50 isn't a shock; all we're waiting on is the timing.

Which is to say that share prices have already adjusted to the information, even though the event itself hasn't yet occurred. When you hear people say the market is a "forecasting machine" this is an example of what they mean. It is the gap between what the market expects and what actually happens that creates the opportunity.

Research director James Carlisle puts it like this: 'If an event with an 80% probability of happening actually occurs, the market might need to make a 20% adjustment. But if something is 100% certain to happen the adjustment occurs beforehand. In the case of Article 50, I reckon we'd be well into the nineties, so any share price reaction should be lost in the wash. Everything has adjusted already.'

The aftermath of the UK's departure from the EU, the so-called second order effects, might be different. There is far greater uncertainty about how the UK's departure will affect its economy.

No-one expects it to be easy. In 2014, the EU accounted for 45% of UK exports and 53% of UK imports. How Brexit eventually impacts those figures is anyone's guess, which is why it might deliver more opportunities than the official triggering of Article 50.

In investing, it's often the nasty surprises – when the forecasting machine gets it wrong – that bring the best opportunities. Unfortunately, Article 50 isn't going to be one of them.

But the parallel between the initial Brexit vote result and the fuss over Article 50 is instructive; if we want to buy cheap stocks then we all need to welcome uncertainty. You can't really expect one without the other.

The tax advantages of resetting shares to their market value

I don't understand the concept of selling shares to crystalise capital profits prior to the introduction of the $1.6 million cap. Why would this need to be done, as the shares are shown at their market value each year and as a result the gains have already been recognised?

16 Mar 2017 – **Tony Kaye**: Just because the shares held in an SMSF are shown at their market value each year does not result in the gain being recognised for tax purposes. The increase or decrease in the market value of shares results in an unrealised gain or loss that does not affect the tax paid by a super fund.

This means if the shares in your fund had a cost of $500,000, and over time have been revalued to a market value of $1m, your fund has unrealised capital gains of $500,000. The strategy to sell shares while still in pension phase, before assets are allocated to an accumulation account due to exceeding the $1.6m pension transfer cap, would result in a tax-free gain being made.

Thankfully, the legislators when drafting the legislation introducing the $1.6m pension transfer balance cap included capital gains tax concessions. The CGT concessions mean, where a member has to transfer assets back to accumulation to reduce their pension account balance to below $1.6m, the member can choose to have the value of the assets reset to their market value at that time.

This means the strategy of selling shares while still in pension phase is not necessary. As a result of the CGT concession, the shares in a fund transferred back to accumulation will have protected any unrealised capital gain that has built up over the time the shares were held.

What are the processes for preparing for the new pension cap?

I am not sure how an SMSF should process the Transfer Balance Cap and Transfer Balance Account? For the accumulation account receiving the excess over $1.6m, are we expected to have a different HIN and separate cash holding account? Given that segregation ends on June 30, I am presuming that the old system of having an accumulation sub-account under the main pension account is no longer acceptable.

16 Mar 2017 – **Tony Kaye**: There are no extra actions that trustees need to take when assets are transferred back to an accumulation account due to a member exceeding the $1.6m limit. Just because a fund has been in pension phase for many years there is nothing stopping the excess being commuted back to a new accumulation account set up to receive the excess.

There will not be a need to change share registrations such as a HIN, and also there will be no requirement to set up a new bank account that would be linked to the accumulation account. Super funds have always been able to have members in both accumulation and pension phase.

Because SMSFs with a member that has exceeded the $1.6m cannot use the segregation method, this requires them using the proportional method. Under the proportional method an actuary calculates what portion of the income each year relates to the pension accounts and what relates to accumulation accounts.

Impeaching The Donald

I'm very interested in what you think our stock market will do if Donald Trump is impeached over his alleged illicit dealings with Russia. Based on extensive research I have done, my view is that in on way or another it is very highly likely that Trump will exit his role - either impeachment or perhaps even resignation. Re timing, it's impossible to say, but I doubt he'll survive beyond 2017. If this is a correct assessment (and it may be incorrect of course) how do you think stock markets will react? My own guess is that they'll fall - say 10% or so due to crisis and uncertainty, but then probably recover under (I'm guessing) President Pence. I think this is a very important question to consider now if one believes (as I do) that Trump will not survive.

14 Mar 2017 – **Jon Mills**: We usually don't try to forecast macro or political events because, quite simply, they are very difficult to predict. Instead, we concentrate on analysing the fundamentals of the company in question and determining whether there is a margin of safety at current prices.

Should your predictions come true - and I note that impeachment just moves things to the US Senate, where a two-thirds majority is required to convict and remove the President - then hopefully investors overreact and there will be some bargains like with the Brexit panic. As such, **Brexit Buy list** gives an idea of how we'll address any stock market plunge as a result of a change in the leader of the United States.

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