

Issue 1 2014

Financial Directions

What is margin lending?

Although investor interest in margin lending dropped off in the wake of the financial crisis, many investors are now looking again at this type of leveraged investing, as a result of the improving stock market conditions and low interest rate environment.

Let's take a look at what margin lending is and how investors can balance the risks and rewards around it. Put simply, margin lending is a way of using your existing investments to increase your exposure to certain asset classes such as shares and managed funds.

The idea is that you use your existing investments, for example a basket of shares, to borrow money to increase the volume of your investment portfolio.

Margin lending often makes sense when interest rates are low (to keep the cost of borrowing down) and when an investor uses the loan to invest in stocks that pay high dividends. The idea is to use the dividends to pay down the interest associated with the loan.

It's also timely to consider margin lending at the end of the financial year when you can pre-pay the interest associated with the loan and claim this payment as a tax deduction in the current financial year.

Margin loans are, however, not without their risks. But there have been a number of innovations recently to help investors manage these risks.

For instance, some margin lenders, including CommSec, offer a feature so that investors are alerted if their account is close to receiving a margin call. A margin call happens when the value of the portfolio associated with the loan drops, resulting in the investor having to contribute additional money to the account, or sell assets.



Investors are also generally now borrowing less when they take out a margin loan, and making sure their investment portfolios are well diversified to reduce any risks associated with this strategy.

Some margin lenders will also allow borrowers to pay to protect the initial capital that is invested in a margin loan. Although this strategy is a good way of reducing the risk attached to this strategy, it will also dampen any returns from margin lending.

In the end, however, margin lending is one of the higher risk strategies in which investors can engage. While it can potentially increase returns, it can also magnify losses.

The idea is to ensure you understand your own appetite for risk, seek appropriate financial advice, and choose a strategy that's aligned with your investment goals and time horizon before you decide to take out a margin loan.

This article reproduced from an email newsletter issued by Third Party Banking, Commonwealth Bank of Australia ABN 48 123 123 124. Australian credit licence 234945.

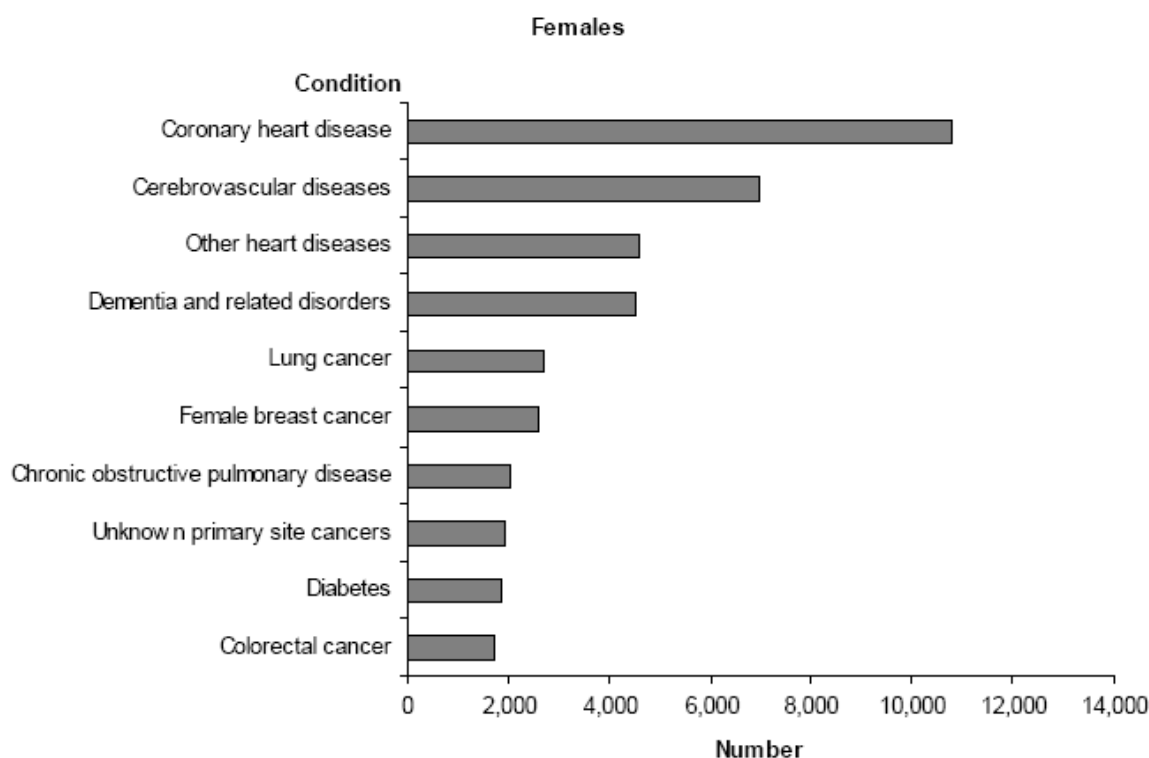
Women and Heart Disease- The Facts You Need To Know



Most Australians are well aware of the threat that major health concerns such as breast cancer, lung cancer and diabetes pose to their health. In the last Australian Institute of Health and Welfare survey (2006), breast cancer was responsible for the deaths of over 2,618 Australian women¹, diabetes caused 3,662 deaths² and lung cancer caused the death of 7,384 people.³

But did you know that in the same year over 23,000 Australians died of coronary heart disease? While this statistic may not be too surprising, it might shock you to learn that 11,000 of these fatalities were women⁴.

In fact about two million Australian women (one in five) have coronary heart disease, and it causes more deaths than any other disease group for them. Yet despite this, heart disease is still portrayed in the media predominantly as a male health concern, leaving many women in the dark when it comes to this most dire health risk.



Leading causes of Death (women of all ages) in 2006⁵

¹ <http://www.nbcc.org.au/breast-cancer/about-breast-cancer/breast-cancer-statistics>

² http://www.aihw.gov.au/cdarf/data_pages/mortality/index.cfm

³ http://www.aihw.gov.au/cdarf/data_pages/mortality/index.cfm

⁴ Australian Institute of Health and Welfare 2010. Women and heart disease: summary

⁵ Australian Institute of Health and Welfare 2010. Women and heart disease: summary. Cardiovascular disease series no. 34. Cat. no. CVD 50. Canberra: AIHW.

Did you know?

- One in three Australian women who died in 2006 did so as a result of a cardiovascular disease⁶.
- Approximately 2 million women are currently living with heart disease⁷
- Women who reach the age of 50 without heart disease still have, on average, a 39% risk of developing it in their life span.⁸
- 91% of women have one or more modifiable risk factors of heart disease⁹.
- Risk factors include: High blood pressure (27%), overweight/obesity (54%), insufficient physical activity (76%) and high cholesterol (48%)¹⁰
- Heart disease was listed as the most frequently associated cause in 21,848 deaths (gender neutral).¹¹

Not only do these statistics highlight the very real risk that heart disease poses to women, but it also raises the question of the associated financial risk if you are not insured. The costs involved in preventing, diagnosing and treating heart disease in women alone was the second highest for the Australian Health system in 2004-5 at \$2,682.8 million.¹² Yet even with the government spending this much each year there are still massive costs faced by the individual. These costs include; loss of income, ongoing treatments, patient carers, child minding and the costs involved in the death of a partner.

Given this it is alarming to note that women make up 45% of the total labour market, but only 15% of all insured incomes.¹³

However, it's positive to see that 23,400 women have AIA Australia's Priority Protection Crisis Recovery insurance. Having taken out this type of cover they can feel assured that if they were to develop heart disease and their claim is paid, AIA Australia may assist them to afford treatment costs and to continue to provide for themselves and their families.

The need for this cover was highlighted by an AIA Australia customer Jacky, who developed cancer and then suffered a stroke, but who fortunately had insurance. This is Jacky's story:

Even though Jacky found trauma and life insurance to be more expensive than she expected, having 2 young children aged 3 and 8, she felt that she could not do without it.

Three years after purchasing insurance Jacky developed cancer and had a stroke in the same week. She was 41. AIA Australia spent only one day assessing the case before agreeing to pay the claim and then continued her crisis plan payments for 6 months.

Unfortunately, due to the high cost of medical expenses the claim payment was used up quickly. To compound this Jacky's cancer had

returned and her partner informed AIA Australia that she only had days to live, but he did not want Jacky to find out (as it would only cause her worry in the last days of her life). AIA Australia contacted Jacky's doctor and requested him to fill out a claim form without Jacky's signature. AIA Australia then organised for a \$1,000,000 terminal illness benefit to be paid out.

A few days later Jacky slipped into a coma and passed away. A little while later her partner contacted AIA Australia to say that both he and Jacky were very appreciative of how AIA Australia had treated their claim, not only with dignity but with personal care.

There are things you can do to avoid Heart Disease such as not smoking, reducing your alcohol in-take, increasing your physical activity and seeing your GP for regular check-ups. But in many cases it can't be avoided, so by ensuring that you have current and appropriate life insurance you place yourself and your family in a much better position to cope.*

Article provided with compliments by AIA Australia

The above is general information only and was prepared without taking your personal needs, objectives or financial situations into consideration. Please read the relevant Product Disclosure Statement and consult your adviser before deciding whether you should acquire a financial product.

“Not only do these statistics highlight the very real risk that heart disease poses to women, but it also raises the question of the associated financial risk if you are not insured

”

For more information about AIA Australia's Priority Protection Crisis Recovery insurance, please contact your financial adviser or visit www.aia.com.au

⁶ Australian Institute of Health and Welfare 2010. Women and heart disease: summary. Cardiovascular disease series no. 34. Cat. no. CVD 50. Canberra: AIHW.

⁷ Australian Institute of Health and Welfare 2010. Women and heart disease: summary. Cardiovascular disease series no. 34. Cat. no. CVD 50. Canberra: AIHW.

⁸ Australian Institute of Health and Welfare 2010. Women and heart disease:: Cardiovascular profile of women in Australia

⁹ Australian Institute of Health and Welfare 2010. Women and heart disease: summary. Cardiovascular disease series no. 34. Cat. no. CVD 50. Canberra: AIHW.

¹⁰ <http://www.aihw.gov.au/publications/cvd/49/10748.pdf>

¹¹ http://www.aihw.gov.au/cdarf/data_pages/mortality/index.cfm

¹² Australian Institute of Health and Welfare 2010. Women and heart disease: summary.

¹³ <http://www.ratedetective.com.au/insurance/women-very-underinsured.htm>

* Payment of claim is at AIA Australia's discretion.

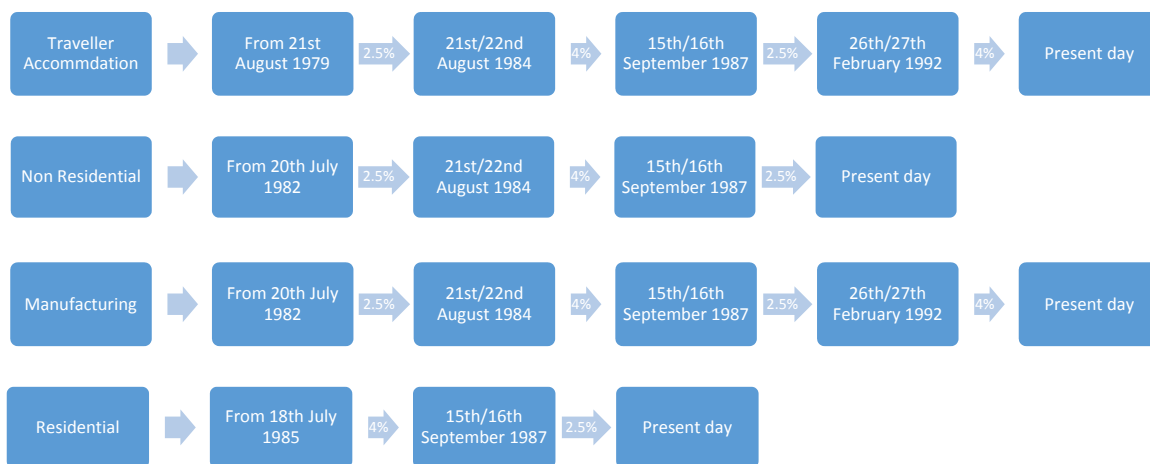
Depreciation schedules

When you own an investment property there are several items that are tax deductible. Interest cost, management cost and maintenance cost spring to mind but one that is sometimes overlooked is depreciation. Investors overlook depreciation as you do not need to spend extra money for it to be claimed.

Depending on the age of your building you may be able to depreciate either 2.5% or 4% of the building per annum. This is the actual bricks and mortar, the roof and all other structural elements of the building.

On top of that you can depreciate plant and equipment, which are the removable elements of a building, such as tap ware and carpets. Each item of plant and equipment may have a different lifespan.

The table below (from the Australian Taxation Office) shows the depreciation percentage you may be able to claim on your investment property's structural elements. There was no depreciation available before the commencement date shown on the table.



To get a depreciation schedule you contact a quantity building surveyor who will put it together for you. The depreciation schedule is valid for the life of the building or until you undertake renovations.

If you would like to build this investment option into your portfolio, please contact your Financial Advisor, they will arrange for a licensed Sentry property investment specialist to call you.



Why many Australians have poorly diversified portfolios

John Owen

Portfolio Specialist, MLC Investment Management

Australian shares have recently delivered robust returns: in the year to 31 December 2013, the S&P/ASX200 Accumulation Index returned 20.2%.

However, a closer look at where this performance came from gives cause for concern. Far from being a broadly-based market rally, this return outcome was actually very narrowly based.

A few stocks have done the heavy lifting

The performance of just five stocks (Commonwealth Bank, ANZ, National Australia Bank, Westpac, Telstra), which were the preferred investments of yield-seeking investors, together accounted for 54.9% of the Australian share market's return in 2013.

And this isn't a new phenomenon: in the decade to 2010, the banks and BHP Billiton accounted for 51% of the return of the S&P/ASX200 index.

“Creating a high level of Australian stock-specific risk in a supposedly diversified portfolio isn't hard to do.”

The concentration of the market's return among just a few stocks is one more sign that Australia's share market is too concentrated. Australian investors who choose a high exposure to Australian shares may find that over time, they become far too reliant on only a few companies for returns. While that may not be of concern if those companies are performing well in share price terms, there is always the risk they may not.

Creating a high level of Australian stock-specific risk in a supposedly diversified portfolio isn't hard to do. Together, the big four banks in the S&P/ASX200 index are now 29.5% of the index, up from just 16% at the beginning of 2001. The ten largest companies by market capitalisation now account for 55.3% of index value and the top 20 companies' share of index value is 66.5%.

A “diversified” portfolio can be surprisingly concentrated

Here's how an investor can build a “diversified” portfolio that results in significant and perhaps unintended Australian stock-specific risk. Let's say they have a portfolio of 40% in Australian shares, 25% global shares, 5% Australian REITs and 30% bonds. The client has opted to have their investments managed on an index basis. Below are the largest stock holdings that result from this asset allocation, based on the index weights of each company at 31 December 2013.

Commonwealth Bank: 3.8%

BHP Billiton: 3.6%

Westpac: 3.0%

ANZ Bank: 2.6%

NAB: 2.4%

Telstra: 2.0%

Apple: 0.3%

Exxon: 0.3%

By biasing the portfolio towards a concentrated share market like Australia's, this investor has created a portfolio that is poorly diversified, and has considerable stock-specific risk. Over 15% of the portfolio value is in five companies, four of them (banks) in the same industry. Exposure to each of the world's two largest companies, Apple and Exxon, is just 0.3%.

This portfolio is very vulnerable to unexpected events that may be adverse to the Australian economy, particular industry sectors and specific companies that dominate the stock market. If Australia's economy slowed, it could impact company earnings and possibly dividends. Developments overseas could also impact Australia, with a slowdown in China's economy the most obvious.

Restricted choice also limits diversification

The Australian share market's structure complicates the task of building a well-diversified portfolio. This is because there is limited investment choice in many industry sectors. For example, information technology is a growth sector globally, yet there are only five companies to choose from in the Australian Information Technology sector, which accounts for just 0.8% of our market's value. Compare this to a global shares index, like the MSCI All Countries World Index, in which the Information Technology sector accounts for 12.1% of the index and has over 220 companies.

Doubling up with direct shares

If the investments in the sample portfolio above are made through a managed fund, some investors could accentuate these stock-specific exposures by also owning Australian shares directly. This increases the stock-specific risk and dependence on them for returns.

Weighing up the reasons for investing in Australian shares

There are many valid reasons for having a meaningful exposure to Australian shares. Some Australian companies' dividends provide a useful source of income and tax franking credits, and the long-term returns of Australian shares have been competitive against other investments.

Some investors may tolerate the stock-specific risk that may exist in their portfolio. But for those who want more certainty about their long-term wealth creation outcome, there are many investment opportunities – such as global shares, alternatives, hedge funds, multi-asset class strategies and bonds – available through managed funds that can moderate these risks and provide additional sources of return.



Important information

This information has been provided by MLC Investments (ABN 30 002 641 661) and MLC Limited (ABN 90 000 000 402) members of the National Australia Bank group of companies, 105–153 Miller Street, North Sydney 2060.

Before making any decisions on the basis of this communication, you should consider the appropriateness of its content having regard to your particular investment objectives, financial situation or individual needs. You should obtain a Product Disclosure Statement or other disclosure document relating to any financial product issued by MLC Investments Limited (ABN 30 002 641 661) and MLC Nominees Pty Ltd (ABN 93 002 814 959) as trustee of The Universal Super Scheme (ABN 44 928 361 101), and consider it before making any decision about whether to acquire or continue to hold the product. A copy of the Product Disclosure Statement or other disclosure document is available upon request by phoning the MLC call centre on 132 652 or on our website at mlc.com.au.

Past performance is not indicative of future performance. The value of an investment may rise or fall with the changes in the market.

Financial Directions is a general advice communique issued by Sentry Group Pty Ltd ABN 40 125 343 384 on behalf of its related AFSL companies, Member Firms and Authorised Financial Advisers.

General Advice Warning: This editorial provides general information only.

Before making any financial or investment decisions we recommend you consult a Sentry Financial Adviser to take into account your particular investment objectives, financial situation and individual needs.

The following are jointly and severally referred to herein as “Sentry Group” or “Sentry”

Sentry Financial Planning Pty Ltd AFSL 247105
Sentry Financial Services Pty Ltd AFSL 286786
Sentry Wealth Management Pty Ltd AFSL 227748

Head Office: Level 1, 190 Stirling St Perth WA 6000

Tel 08 9267 3444 | Fax 08 9267 3499

www.sentrygroup.com.au