

Roger Montgomery examines the new meaning of 'blue chip stocks' in **WEALTH** on **SATURDAY**

Know the rules on funds and estates

MONICA RULE



I am often asked: "What happens with a self-managed superannuation fund when a member dies?" It's an important question and in common with many matters related to estate planning the answer will depend on how diligent the fund had been in making future plans. Here are the key questions.

Was the deceased member in receipt of a pension? If the deceased was in receipt of a reversionary pension before their death, then the pension will continue to be paid to the nominated reversionary pensioner. If the deceased was in receipt of a non-reversionary pension or was not in receipt of any pension, then a lump-sum death benefit has to be paid out as soon as practicable or a new pension commenced.

Did the deceased have a binding death benefit nomination? If they did, the nomination should have been put in place as per the requirements of their SMSF's trust deed. There have been many disputes played out in the courts that highlight the errors made by SMSF trustees in the payment of death benefits. The precedent cases have shown the importance of:

- Ensuring a trustworthy person is chosen to act as the co-trustee
- Having a binding nomination instead of a non-binding nomination
- Ensuring the nomination has not lapsed
- Using the correct language when nominating someone to act as the legal personal representative.

Ensuring the person nominated for a death benefit is not a different person nominated for the reversionary pension is also something that has caused problems for beneficiaries.

If the deceased member does not have a BDBN, then the remaining trustee has the discretion of determining how the deceased's superannuation will be paid out. If the deceased member wanted their superannuation to be distributed in accordance with their legal will, then they would have had to put in place a BDBN in favour of their legal personal representative who is their executor or administrator of their estate to receive the death benefit. The death benefit would then form part of the deceased's estate and would be distributed in accordance with their will.

Is a tax exemption applicable? If the deceased member was in receipt of a pension, the tax exemption available on investment income from assets that were supporting the pension will continue to be exempt, until the death benefit is paid out of the SMSF. Any capital gains derived from the sale of pension assets would also retain their tax exempt status. However, the tax exemption would not apply to any amounts allocated to the pension account after the member's death, such as an anti-detriment payment or a life insurance proceeds.

Is a minimum pension payment required? On the death of a pensioner there is no requirement to pay the minimum amount of the pension if the pension is a non-reversionary pension and is commuted in the year of death and is paid out as a lump-sum death benefit or a new pension commences. On the other hand, if the pension reverts to another member then a minimum pension payment is required.

Does the SMSF need to be wound up? If the fund is a single-member SMSF and is no longer required to operate, then it needs to be wound up by paying out the death benefit, paying all expenses and tax liabilities, lodging the final income tax return, notifying the ATO of the wind-up date, and closing the SMSF's bank account.

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Sun may be setting on SMSF residential property loans

Tighter lending curbs are eating away at access to credit

MIRANDA MAXWELL



Australian property investors have become complacent about access to home loans, but a tightening of lending practices has been eating away at available credit.

To the glee of DIY super fund holders, the government rather shockingly ignored advice from David Murray and the Financial Services Inquiry to drop lending for residential property to self-managed super funds. It was the only proposal of 44 not to be adopted. Celebrations by would-be SMSF home-borrowers may prove premature though. In a twist, lenders themselves are voluntarily reining in the practice.

This means self-managed retirees wanting to join the chorus of fellow DIY super fund holders rapidly leveraging their retirement funds to property best get a wriggle on. You probably missed it, but in the days before Christmas AMP Bank voluntarily introduced big curbs on lending to SMSFs for property.

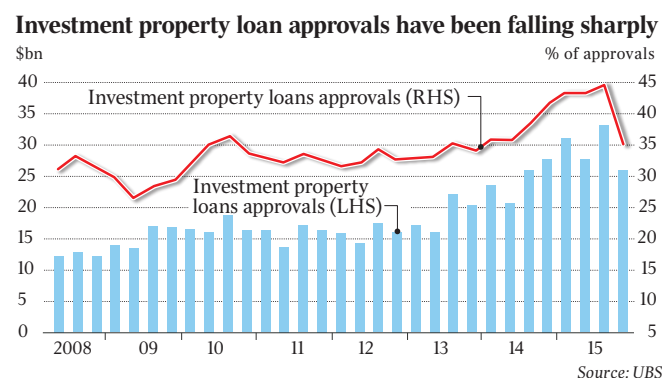
AMP had already suspended loans to new deals for several months as its lending to property investors had reached such strong levels it was threatening to breach new lending criteria from APRA (the regulator has restricted banks to a 10 per cent a year increase in property investor lending).

AMP Bank advised mortgage brokers it would no longer lend for properties less than six months old, including off-the-



MARK STEWART

New property developments will be hit first by the changed rules



plan developments. It also lowered its maximum loan-to-valuation ratio from 80 to 70 per cent, and stipulated a minimum SMSF fund size of \$200,000 for DIY superannuation borrowers.

These stricter loan conditions come after NAB quietly suspended loans on residential property to SMSFs last year (it still lends on commercial property to SMSFs), saying merely it was a neat solution to reduce growth in property loans to investors, and thereby appease the regulatory crackdown on property loans to that particular group.

Borrowing to buy property with your retirement funds presents a particular set of issues:

- The main area of concern is that the retiree is too exposed to a single asset category. For someone without a large amount in their super, being geared up with a large loan against property may not be a prudent spread of risk.
- The other issue is that the borrower may not be able to pay back the loan within the SMSF structure if they are close to retirement and losing their salary, seeing their income stream and super contributions dry up.

port from UBS shows investment property approvals falling sharply in the three months to September 30 last year (see graph).

Regulator ASIC has been cracking down on property spruikers who encourage the unwary to take on an SMSF and ramp up leverage to housing.

Property group Park Trent, in Hurstville, in Sydney's south, was recently found to be unlawfully "persuading relatively unsophisticated investors of the virtues of using their superannuation accounts to purchase investment properties and to establish SMSFs". Some of these 860 investors suffered financial losses as a consequence, ASIC said.

Limited recourse borrowing (LRBA) is the most common structure for investors using SMSFs to finance property: the tax office estimates outstanding LRBAs at September 2015 of \$18 billion, or 3.1 per cent of SMSF total assets. SMSF property holdings were worth \$94.7bn, up from \$82.7bn in September 2014.

Figures for DIY activity also show that SMSF property holdings is one of the few areas of growth against the backdrop of sliding share market valuations and low cash rates. But if you intend to join the ranks of SMSFs leveraged to residential property, be prepared to stump up a deposit in the order of 30 to 40 per cent and to buy an existing property to satisfy new and more stringent lender criteria.

Would-be borrowers must also be aware that with the government set to review its decision to allow the practice in three years, and the lenders themselves increasingly choosing not to issue this type of loan, the days of SMSF residential property loans may well be numbered.

Heavyweight offers well-packaged income

DIVIDEND DETECTIVE

ASX CODE: PGH
SECURITY PRICE: \$4.99
INDUSTRY: Packaging
FORECAST DISTRIBUTION: 21.5c per share

DAMEN KLOECKNER

Pact Group is Australia's leading manufacturer of rigid plastic packaging, operating out of 70 sites throughout Australia, New Zealand and Asia.

The majority (70 per cent) of Pact's revenues are derived from packaging for fast-moving consumer goods such as chilled food, dairy and beverages and other household consumables.

The remaining 30 per cent of revenues are derived from industrial packaging and materials handling, which includes waste handling, construction and commercial printing. The above product categories typically display low, non-cyclical demand and grow in line with economic themes such as population growth, GDP growth and inflation.

In Pact's case, other key drivers of profitability include ANZ dairy production volumes, and plastic resin prices. As signalled in August, weakness in the NZ dairy market will likely translate to weaker NZ dairy packaging demand. Pact's diverse product and customer mix will soften the impact of weaker dairy demand, particularly with a hot summer contributing to stronger consumption of chilled foods and dairy in the first half of FY16.

However, Pact's key driver is its ability to execute on its consolidation strategy. Given the low-growth, defensive sector it operates in — Pact was originally

part of the Pratt group — organic growth is slow and constrained.

One of the primary reasons for listing Pact was to pay down debt and free up the balance sheet for future acquisitions. Pact had clearly shown an ability to make synergistic, earnings-accretive acquisitions by buying smaller, lower-margin packaging companies, and stripping out costs to realise efficiency gains.

Through consolidation, Pact has already gained a superior scale position in ANZ, which it has leveraged to achieve higher margins relative to its peers.

Moreover, Pact's higher profitability is sustainable, assuming it continues to focus on making smart acquisitions and improving efficiency. With an estimated \$200 million balance sheet, Pact is likely to make further acquisitions in FY16.

Pact's superior profitability translates well into strong cash flows which, means higher dividends. Pact's forecast dividend yield of around 4.7 per cent compares well to domestic peers, particularly as it offers higher franking (65 per cent) than many of its peers. We view fair value for PGH as \$4.72 in FY16 (against a current stock price of about \$4.99) with value growing at 9-10 per cent per annum over the medium term.

Though Pact faces some short-term headwinds to production volumes due to a weaker NZ dairy market, it remains a well-run, highly cash generative and high-yielding company, with defensive and well diversified revenues.

Assuming it continues its consolidation strategy in a disciplined and opportunistic manner, Pact's emergence as one of Asia Pacific's leading packaging companies should continue unabated.

Damen Kloeckner is an associate analyst at Clime Investment Management

Global sharemarket slump an overreaction to China slowdown

DON STAMMER



In January, sharemarkets were volatile and mostly gloomy. Expectations of a hard landing for the Chinese economy were a major concern.

Commodity prices, led by the price of oil, collapsed. What's more, worries developed that the US cash rate could be raised too quickly in 2016 — hurting equity valuations and causing the US dollar to move uncomfortably higher.

The dangers of disinflation, and even deflation, rattled many investors, even though global monetary policy remained highly accommodative.

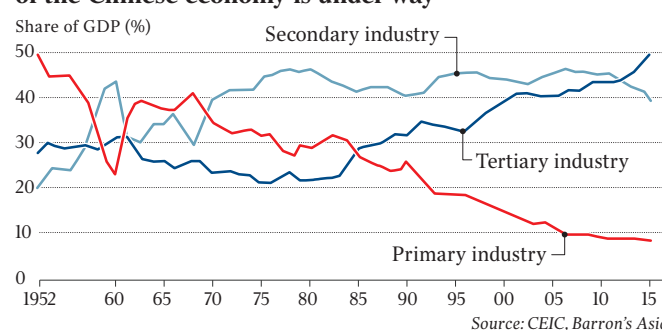
Today's column looks at two aspects of recent sharemarket stresses that are particularly important for Australian investors — the heightened volatility in average share prices and the intensely negative perceptions of the Chinese economy. The high level of sharemarket volatility experienced recently reflects these diverse global influences:

- The huge purchases of bonds by the US Fed under its "quantitative easing" program had helped to repress volatility in investment markets in the US and around the world. US quantitative easing ended in late 2014; its stabilising effects are wearing off.
- In December, the US Fed took its first move in normalising its cash rate, which had been set at close to zero for seven years. Senior Federal Reserve officials have indicated they expect four further increases in the US cash rate during 2016 — a projection which many equity investors find disturbing.

Late last year sharemarket valuations were somewhat stretched — at a time when global growth seemed to be losing momentum and concerns of a hard landing in China intensified.

- The scope for banks and brokers to stabilise panicking markets is now more limited. As

Despite challenges, the rebalancing of the Chinese economy is under way



Mohamed El-Erian, the former Pimco executive now with the Allianz group, puts it: "Facing tighter regulation and sharply reduced market appetite for short-term earnings deviations, broker-dealers are a lot less willing to take on inventory when the market overshoots."

"The good news is that such dynamics ultimately exhaust themselves ... but a much better resolution would be if improving fundamentals could support and validate financial asset prices ..."

Recurring bouts of volatility seem likely to be a feature of investment markets in 2016 — and seem on course to affect bonds as well as shares.

Investors need an investment strategy that recognises their individual tolerance of risk — and to stick with their considered investment strategy when markets turn skittish or exuberant.

As gloom descended in January, many investors feared the world economy would tip over into recession.

Mark Tinker, a fund manager with Axa, summarised the prevailing sentiment: "Market corrections are more common than recessions. The effects of the last big correction spilled over into the real economy so markets are automatically assuming this one will as well."

Tinker's view, which I share, is that investors' interpretation of Chinese economic data has become somewhat too negative; the impact of China's slowing economy on bulk commodity prices is being overdone; and the impact of the global oversupply of oil, gas, iron ore and coal has been underplayed.

Investors need to allow for the shades of grey in China's econ-

omic performance and prospects. The year 2016 is unlikely to be a repeat of 2008 but it may have similarities to 1998 and 2011.

Investors need to allow that trend growth in China is slowing as that country's GDP "base" expands and as productivity growth becomes harder to achieve.

The restructuring of the Chinese economy towards consumer spending and services and away from manufacturing and lumpy capital spending is delivering some gains, as the chart shows, but faces a lot of resistance.

But none of these complexities were given recognition by investment markets or by most commentators when China's GDP statistics were released in mid-January, showing growth rates of 6.9 per cent in 2015 and 6.8 per cent (annualised) for the December quarter.

Surprisingly, most reactions and reports seemed to accept the official figures for China's economic growth.

Instead, their focus was on growth "slumping to its worst level in 25 years" or, as one commentator put it, the "world's second biggest economy" was having "its worst quarterly performance in a century".

Given the shrill reactions to the Chinese data, it's no surprise that few investors bought shares when prices weakened in January's gloom.

Don Stammer chairs QV Equities, is a director of IPE and an adviser to the Third Link Growth Fund and Altius Asset Management. The views expressed are his alone.

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Developed by Millionaire FX Trader Greg Secker

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Thursday 4th February at 12am & 6pm

Mawson Lakes

Mawsons Lakes Hotel & Function Centre

Sunday 7th February at 10.30am & 2.30pm

Adelaide

Hilton

Monday 8th February at 12pm & 6pm

Double Bay

Rose Bay Marina

Friday 19th February at 10am & 2pm

Wollongong

Novotel

Tuesday 23rd February at 12pm & 6.30pm