DIVIDEND DETECTIVE

Value to be had in service stations

Viva Energy REIT
ASX CODE: VVR
SHARE PRICE: $2.33
INDUSTRY: Real estate
FORECAST 12-MONTH DISTRIBUTION: 13.9c

GARETH ABERNETHY

Viva Energy REIT is an ASX-listed real estate investment trust that gives investors exposure to 425 high-quality metropolitan and regional service station assets across Australia. Viva only recently joined the ASX, listing in August at $2.20 a security.

The REIT was conceived when Viva, the country's largest private fuel company, spun off its property assets from its balance sheet. As a result, Viva is the sole tenant of the REIT's properties, which subleases the stations to Coles Express. All the sites operate under an alliance agreement between the two, where Coles Express runs the retail operations and Viva supplies the oil products. The stations are run under the Shell brand, maintained through a long-term licensing agreement.

Viva's service station portfolio was recently valued at $2.1 billion, netting an NTA of $2.07 a security. The lion's share of the REIT's portfolio is weighted towards the Eastern seaboard, with 80 per cent of the portfolio's rental income attributed to NSW, Victoria and Queensland.

The split of the portfolio between metropolitan and regional stations is roughly 75 per cent and 25 per cent respectively.

Viva has a number of lucrative investment attributes, including a triple lease structure, considerably reducing its capex obligations and indemnity protection from Viva in the event of potential environmental damage. It has a long-dated WALE (weighted average lease expiry) just shy of 15 years with 100 per cent occupancy, combined with contracted rental increases of 3 per cent. Viva has maintained a 40 per cent holding in the REIT after the spin-off.

The trust is undertaking the acquisition of a further four service stations in NSW, Queensland and the Northern Territory for $26.2m. These were earmarked in the prospectus and will likely push gearing to the middle of management's range of between 35 per cent and 45 per cent. After settlement of the transaction, Viva will still have scope for further acquisitions.

The REIT offers exposure to a long WALE portfolio of assets with high certainty of revenue, contracted rental increases now well above inflation and an attractive yield, combined with the potential for further growth through acquisitions.

At current prices, Viva offers a 12-month forward yield of almost 6 per cent — good value to an income-focused investor.

Gareth Abernethy is an analyst for Clime Asset Management.

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Posing a supermarket scare: It's not Amazon ... it's Aldi!

The online giant hogs headlines, the German chain draws customers

GUY CARSON

Retail investors are focusing hard on the future of Coles versus Woolworths.

The main loser to date from Aldi's rise has been Woolworths as Coles is more or less maintaining its market share after gaining ground between 2009 and 2015.

The reason for Coles's success during this period is twofold.

First, under new ownership, the company spent a lot of money on store revamps to make its offerings more appealing.

In recent years it has spent a significant amount of growth capex to catch Woolworths. The chart below compares their capex spend to their depreciation charge (a proxy for sustaining capex) to show how aggressive the spend has been.

With more appealing stores, Coles closed the quality gap between itself and Woolworths.

The second aspect of its success was undercutting Woolworths on price.

Coles typically ran earnings before interest and tax margins of less than 5 per cent versus Woolworths' 6 per cent-plus. Consumers started to migrate to the cheaper option.

Woolworths' margins (which were the highest of any supermarket in the world) were simply unsustainable. The company has now realised this and has started to compete with Coles on price, as can be seen by the fall in margins below.

The problem for Woolworths and Coles is that they are probably fighting for a smaller pool. The rise of Aldi is unlikely to slow any time soon because of its aggressive rollout plan.

Aldi continues to have significantly lower margins with lower grocery prices and smaller store areas (meaning lower overhead costs such as rent).

EBIT margins for Aldi in Australia were 4 per cent last year, according to the Australian Taxation Office.

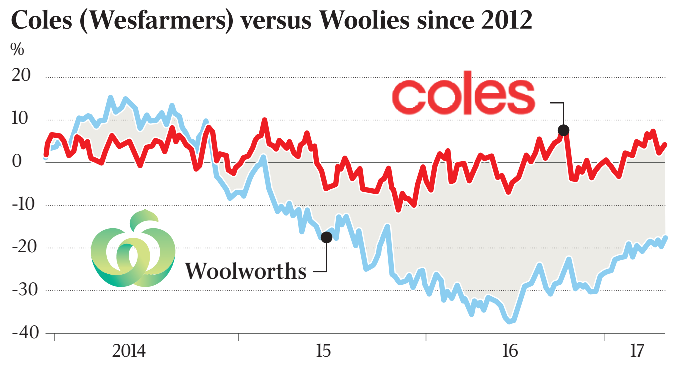
Another competitor set to gain market share is Costco, whose unique business sees it run EBIT margins of less than 3 per cent.

Costco makes over three quarters of its profit from membership fees (now $55 a year in Australia) so can sell goods to consumers near cost, hence the name.

The rise of Aldi is unlikely to slow any time soon because of its aggressive rollout plan

AFP

Coles (Wesfarmers) versus Woolies since 2012



Source: ASX

The Amazon decoy

Then there is the imminent arrival of Amazon in Australia.

This is less of a worry than the above threats. Amazon has struggled to make meaningful headway in the US as consumers still prefer physical stores for groceries. Its market share stands at about 1 per cent in the US and, in an attempt to grow, the company is experimenting with bricks-and-mortar outlets in Seattle.

While Amazon is grabbing headlines, the biggest threat for the major supermarkets remains Aldi. The constant of an aggressive low-cost competitor means life will remain difficult.

Despite that, we have seen a solid rally in Woolies' share price since June. The rerating has been driven by two consecutive quarters of solid sales growth and a rerating in the price to earnings ratio from about 16x to 23x.

Meanwhile, Wesfarmers, the parent company of Coles, has gone the other way and seen its P/E ratio fall from more than 20x to 16x (driven by a flat share price and rising earnings from its coal division).

The rerating of Woolworths' price-to-book valuation multiple has been on a similar scale, going from about 3x to 4.1x — a level similar to what the company traded on between 2009 and 2014.

This is despite return on equity (which is the return on the book value that should justify the above multiple) having fallen significantly in recent years.

From the above valuation metrics, it appears the popular trade is to bet on a Woolworths turnaround. But if we were running an index aware strategy, we would much prefer to take the 16x on Wesfarmers rather than pay 23x for Woolworths.

In addition to a cheaper valuation, Wesfarmers has the added advantage of owning Bunnings, a high-quality business that represents 34 per cent of Wesfarmers' EBIT. It is now growing at a double-digit rate and has a return on capital employed of more than 35 per cent.

While we would be more likely to invest in Wesfarmers than Woolworths at present, we don't because of concerns that the market is underestimating the continuing growth of Aldi on both businesses.

It's an odd thing, but if you were to travel back in time five or 10 years and asked Australian fund managers to name some of the highest quality companies listed on the ASX, there would be a very good chance that several of them would name Woolworths.

For a long time the company was so consistent with its store rollout, earnings growth and returns on capital that it was hard to go wrong buying its shares. Unfortunately that has changed.

Guy Carson is head of Australian value strategies at TAMIM Asset Management.

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Effective philanthropy and how to achieve it

GRANT HOOPER

It makes sense to give to charities — it's a tax-effective way to support the community and direct help to where it's needed the most. But when and how we choose to give — often spontaneously towards the end of the financial year — doesn't make as much sense.

As June 30 approaches, we place far greater value on tax deductions, although those benefits can be locked in at any time.

Ad-hoc giving also raises other issues.

Most people who contribute to charities do so in response to being asked, whether by a charming collector on the street, a compelling letter received in the mail, or by a persuasive phone caller — even though they strongly dislike it — according to a recent Giving Australia survey.

Opportunistic giving comprises the bulk of the $2.62 billion individuals donated to charities in 2013-14. Almost two-thirds of those who gave to charities did so impulsively, according to Giving Australia, but almost one in five said they would also consider becoming a regular donor.

Regular donations make a significant difference to charities by enabling them to increase their focus on core activities rather than fundraising and administration, which are common supporter concerns.

A regular direct debit is a good starting point but can risk becoming a set-and-forget exercise. A formalised structure such as a perpetual charitable fund, set up under an existing Public Ancillary Fund (PuAF), can offer the best of both worlds for many people.

These structured vehicles, which require an initial minimum of $20,000, are one of the best ways to turbocharge effective philanthropy. Contributions to a PuAF account are tax deductible and can be spread over five years.

This makes it a highly effective giving structure for the 45,000-plus individuals who contributed at least $5001 to charities, based on ATO data for 2013-14.

PuAFs, which must distribute 4 per cent of the fund's value to charities each year, tend to grow over time because both earnings and capital gains are tax free.

The initial investment can effectively keep generating money for charities over many years. Many people name their PuAF accounts in memory of someone special or after their family to encourage greater interest in philanthropy among the next generation.

A number of employers are now also setting up their own PuAF accounts as a way to encourage a greater sense of workplace community.

Employee donations are taken directly from pre-tax salary, allowing them to enjoy an upfront tax deduction.

Private ancillary funds (PAFs) are another similar structure aimed at high-net worth individuals and families with at least $500,000 in investible assets to donate. PAFs offer the same tax advantages as PuAFs but are required to distribute 5 per cent of their market value each year.

Structured giving

While Australians are generous supporters of charities, many still hold concerns about administrative costs and whether their money will reach those in need.

Those who engage in structured giving have a different view. They contribute six times more dollars than those who donate spontaneously (including those who make ad-hoc donations several times a year).

This suggests those who give with a structured approach are more confident their donations will be effective and feel a greater involvement in the charities they support.

A PuAF account set up within an overarching umbrella fund encapsulates both these elements.

It can take advantage of economies of scale such as lower fees and efficient administrative processes, as well as provide help finding charitable organisations that match donor interests.

There are now more than 1550 PuAFs holding $1.73bn in assets, generating more than $300 million in charitable distributions every year, according to the ATO. Similarly, PAFs generated more than $300m in charitable distributions.

The end of the financial year is traditionally a time when we make last-minute tax-deductible donations.

But this could be the year you make an impact that lasts a lifetime by setting up a charitable foundation that empowers change across society while lowering your tax bill.

Grant Hooper is senior grants manager at Equity Trustees.

Why it pays to stay under the cap with your non-concessional super contributions

MONICA RULE

With so many superannuation changes happening from July 1, you could be forgiven for not understanding all aspects of the new laws.

One new law that affects the amount that you can contribute into your superannuation fund is the very important cap on non-concessional (post-tax) super contributions, which will be set at $100,000 per annum.

The cap does not restrict you from putting more money into super if you want to. It just limits the amount that will be exempt from tax. Anything in excess of the limit will attract tax.

If it was just the limit on the cap that changed, it would be easy to understand.

However, the federal government changed the law, so there are other criteria that need to be satisfied before you can make contributions into your superannuation fund.

It also put an eligibility threshold on how much you can contribute. So from July 1, you have to check two things. Can you make non-concessional contributions into your super fund and how much can you contribute?

You need to make sure your total superannuation balance is below $1.6 million to be able to make non-concessional contributions into your fund. Then the amount that you can contribute is based on the following thresholds:

- If your super balance is less than $1.4m, you can contribute up to $300,000 in non-concessional contributions.
- If your super balance is $1.4m and below $1.5m, then you can contribute up to $200,000 in non-concessional contributions.

> The cap does not restrict you from putting more money into super if you want to

- If your super balance is $1.5m and below $1.6m, you can contribute up to $100,000 in non-concessional contributions.
- If your super balance is $1.6m or more, then you cannot make any non-concessional contributions.

You will only be eligible to make more than the $100,000 non-concessional contributions if you are under 65 at any time in the year of the contributions and you have not fully used your bring-forward cap in the past two financial years.

If you are already 65 or over on July 1, you are limited to making just the $100,000 annual limit, provided your super balance is less than $1.6m.

What many superannuation members may not realise is that if your super balance is $1,599,999 it does not mean you can only contribute $1. You can actually contribute up to $100,000, because you are still considered to be below the threshold.

The $1.6m total super balance is tested each financial year. This means, even if you qualify for the two-year bring-forward limit, it does not guarantee that you will be able to contribute up to $300,000 over three consecutive years.

For example, let's assume at June 30 your super balance is $1,399,999. Then in the 2017-2018 financial year you contributed $150,000 in non-concessional contributions and triggered the two-year bring-forward cap of $300,000.

Then at June 30, 2018, due to good investment performance, your super balance increased to $1.6m. Although you have only used half of your $300,000 bring-forward cap, you will not be able to make any further non--concessional contributions in the 2018-2019 financial year.

If your good investment performance continues, and your super balance stays above $1.6m in the following year, it means you will lose the balance of your unused bring-forward cap.

Separately, in last week's federal budget, the government allowed a small variation to these forthcoming rules on non-concessional superannuation contributions for those who sell their home when downsizing ... but we will leave that issue to another time.

Monica Rule is an SMSF specialist and author of The Self Managed Super Handbook.

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