HORIZON
INVESTMENT SOLUTIONS

September 2018 — Over the Horizon Market Commentary by David Offer

September was a marginally negative month for the Australian share market, with the All Ordinaries index down 102 points (1.6%) to close at 6,325 points. For the first quarter of the 2019 financial year, our share market has managed to return just 0.57%, though this has increased to 1.86% with the inclusion of dividends.

October has started on a weak note, down 2.68% at the time of writing. We view three core reasons for this weakness. Firstly, following on from the theme of last month's letter, there has been some unwinding in the excessive valuations of growth shares, especially in the health (CSL and COH in particular) and technology sectors.

Secondly, the trade war retoric between the US and China is continuing to escalate, as evidenced by a detailed speech delivered by US Vic President Michael Spence last Thursday. This summary by Alan Kohler was provided in The Australian. I personally find many aspects the path China is travelling down concerning, particularly with respect to the Country's effort of implementating a 'Social Credit Score'. I would urge you to watch ABC's Foreign Correspondent story via this link - Leave No Dark Corner. If successfully implemented (and it appears likely that it will), the Chinese government will be able to exert a level of control and supervision never seen before by a government over its population.

Thirdly, ANZ has been the next of the banks to announce a post end-of-year write down. ANZ's not insignificant $800 million write down was on the back of costs associated with customer compensation stemming from the Royal Commission (RC) and along with IT write downs. Thus far, ANZ, Westpac, AMP and CBA have incurred costs exceeding $2.1 billion largely stemming from trying to make good on past sins highlighted by the RC, which thus far amount to around 8% of 2017 18 profits. More costs are expected from these banks with NAB is still to report.

In other company news, post writing about MYOB last month, the Company has since received an indicative cash offer for its shares at $3.70 by private equity firm KKK. While the offer is conditional, the fact that KKK has already acquired a 19.9% stake suggests that KKK is committed to some form of deal. We would expect KKK to have a good understanding of the business, having tried to acquire the business back in 2011. We would be reluctant sellers at $3.70 but would be more willing with an offer closer to $4.00. We will continue to monitor the situation. MYOB shares are currently trading at $3.60.

Last Friday, Wesfarmers provided the details to its planned demerger for Coles. Wesfarmers shareholders will receive one new Coles share for every Wesfarmers share hold. Westfarmers will continue to retain a 15% interest in the newly listed Coles and a 50% interest in the Coles Flybuys program. A shareholder vote is scheduled for 15th November and assuming shareholders vote in favour of the proposed demerger, Coles will commence trading on Wednedsay 21st November.

Finally, a common discussion point in recent months has been Labor's proposed policy to stop refunding of surplus franking credits for those not receiving the Age Pension. This stands to be a significant imposition on SMSF members, who generate a significant portion of their income from franking credit refunds.

Should Labor's policy come to fruition as planned from the 2019/20 financial year onwards, the enclosed article by Max Newhen published in the Professional Planner offers a more practical solution of addressing the policy by incorporating children into SMSFs.

In summary, the concessional contributions tax incurred by children contributing money into superannuation can be met by franking credits received on investments held by the parent's member account. For example, a husband and wife with a SMSF balance of $1 million which includes a share portfolio of $600,000 yielding 5% fully franked would receive $12,857 in franking credits. These would now be lost under Labor's proposed policy. However, if the husband and wife had two children contributing $25,000 each to super, this would result in combined contributions tax of $7,500. This would be met by franking credits and hence result in a franking credit refund of 7,500 for the husband and wife. Not ideal, but better than nothing.

For some parents, they may infact choose to start making an annual contribution to superannuation for their children to give them the benefit of the tax deduction contributing to superannuation provides; as well as not waste all the franking credits received within their superannuation fund.

The Liberal Government is presently proposing that the number of members allowed in a SMSF be increased from 4 to 6 members which, if passed into Law, for many families will further increase their options for incorporating children.

With a proposed start date for Labor's franking credit policy of 1 July 2019, it is appropriate to start thinking of these sorts of considerations now. This is certainly a topic we will raise as we meet in the year ahead.

If you would like to discuss any of the above or any other aspect of your investment portfolio, please do not hesitate to contact our office.

David Offer
Investment & Financial Advisor
phone: 08 9791 9188
fax: 08 9791 9187
email: david.offer@horizonis.com.au
website: www.horizoninvestmentsolutions.com.au

HORIZON INVESTMENT SOLUTIONS
UNIT 4, 2-4 JETTY ROAD,
BUNBURY WA 6230