Bramwell Brown Ltd

Investment Advisers – Brokers

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Bramwell Brown Limited – Newsletter – June 2011

Regulation

I'm pleased to finally be able to report my financial adviser authorisation has been approved by the Financial Markets Authority. It has been a long and expensive exercise (time and money), however I think the new legislation will ultimately be of benefit to the public. My financial services provider number is FSP28047, and you can view details of my authorisation status on the Companies Office website (http://www.business.govt.nz/fsp/). A register of all Authorised Financial Advisers is available on the Financial Markets Authority website (http://www.fma.govt.nz/).

Fees

Thanks to those of you who have responded positively to last month's item about fees. I've had a good uptake from clients wanting to take advantage of the offer of ongoing personalised advice. If you haven't been contacted yet, don't worry – I am yet to make a start on getting in touch with individual clients to see which type of service they require. I forgot to mention in last month's newsletter that the fee for ongoing personalised advice is tax deductible, so before it has even started it has gone from good value to exceptionally good value!

Fixed Interest

I've lost count of the number of clients who have recently been looking for good fixed interest opportunities. New issues are few and far between, and the secondary market is struggling to offer anything that would tempt money out of the trading banks. Bank term deposit rates are sitting between 4.50% and 6.00%, and there are very few good quality bonds offering yields over 6.00%. In the past we would look to the likes of Contact Energy, Vector, Fonterra, Genesis Energy and Auckland Airport to source better-than-bank interest rates. Currently all these companies have bonds yielding no more than 5.50%. Part of the reason banks are more competitive than in the past is because of the Reserve Bank's new Core Funding Ratio. The new rules set out that banks must secure 65% of their funding from retail deposits and wholesale sources such as bonds with maturities of more than one year. These rules are designed to reduce New Zealand banks reliance on short-term offshore wholesale funding. There are, however, still opportunities in the fixed interest market. Some of the perpetual securities could be good buying, provided you understand their rate-set characteristics, and depending on your

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view of future interest rates. Some of the capital notes, the likes of Fletcher Building Finance, GPG Finance, and Infratil are trading at yields in excess of 7.00%, however, again it is essential you understand their characteristics before considering making an investment.

Shares

The very low yields in the fixed interest market are one of the factors driving our share market at present. Those seeking higher yields are turning to shares that pay good dividends and offer the possibility of future growth. Here are the current yields of some of the more popular shares.

Company	Share Price	Gross Yield
Auckland International Airport	2.30	5.25%
Cavalier Carpets	3.95	6.51%
Contact Energy	6.00	5.86%
Fisher & Paykel Healthcare	2.88	6.15%
Fletcher Building	8.93	3.83%
Freightways	3.30	6.17%
Goodman Property Trust	0.95	8.35%
Hallenstein Glasson	3.93	11.27%
Kiwi Income Property Trust	1.04	7.58%
Port of Tauranga	8.80	4.87%
Property for Industry	1.19	7.01%
Sky City Entertainment	3.67	6.71%
Steel & Tube	2.65	5.93%
Telecom	2.42	8.68%
Trustpower	7.40	6.86%
Vector	2.53	8.05%
Vital Healthcare Properties Trust	1.17	7.31%

Don’t forget the yields are based on today’s share price, and the dividend paid in the previous twelve months. Both could change at any time. Also remember share ownership generally carries more risk than fixed interest.

Budget

Most of this year’s budget cuts were publicised well in advance, and would have come as no surprise to many. It was always a budget that was going to cause pain to some; however at the risk of politicising this newsletter, I think it was reasonable. As I’ve said in the past a country isn’t necessarily all that different from a household. We borrow, we work, we earn, we invest, and we spend. The combination of those activities determines how well we do, and can be measured both financially and socially. Many households in the last few years (and some governments) have realised that spending more than they earn is unsustainable, and have put measures in place to turn their finances around. Our Government is no different – faced with huge deficits and equally large borrowings they have taken fairly drastic action to get the books back in the black. Amongst all the politically charged commentary I couldn't help but agree with what Owen Glenn had to say.

On New Zealand in general. "I believe we have become a country that expects too much to be provided by the Government. As a country we need to grow up and take responsibility for our lives and the standard of living we want in retirement."

On Working for Families. "Having children isn't a right, it's a privilege – love is vital, but it doesn't pay the bills and neither should the Government be expected to."

On student loans. "It disgusts me to think New Zealanders can become skilled in a particular area with the assistance of an interest-free Government loan, and then disappear overseas to earn significantly more as a result of their qualification, while shirking their repayment obligation." Apparently 43% of all student loans will be written off this year.

So what was in the budget for investors? The main areas that investors should be interested in is KiwiSaver, the partial sale of state assets, the Earthquake Kiwi Bond, and possibly the $1 billion cut to the public service.

KiwiSaver

Possible changes to the KiwiSaver scheme were well documented before the budget and are:

1. A reduction in the Government matching tax credit to fifty cents in the dollar. In the past the Government has matched members' contributions dollar for dollar up to a maximum of $1,043 per annum, or $20 per week. For the year ending June 30th 2012 the Government will only offer a fifty percent subsidy up to a maximum of $521. The $1,000 kick-start subsidy paid by the Government when you join KiwiSaver will remain.

2. The Government will now tax the contributions made by employers to members' KiwiSaver accounts. In the past only employer contributions over 2% of a member's pay were taxed. From April 1st 2012 all employer contributions will be taxed.

3. Employees and employers will have their minimum contributions lifted from 2% of their gross pay to 3%. These changes come into effect on April 1st 2013.

Most of our KiwiSaver clients are retired or self-employed, and the only change to affect them will be the reduction in the Government's matching contribution. Although it's been cut in half, a $521 annual subsidy is still worth having. Eventually this subsidy will be scrapped altogether so I believe investors should make the most of it while it is still available. For KiwiSaver members who have been in the scheme prior to July 1st 2010, make sure you have contributed $1,043 to your account before the end of this month. If you have done this the Government will match that contribution for you. For those who joined the scheme after July 1st 2010, the Government will match your contributions up to $20 per week from the date you joined.

Sale of State Assets

This has been widely publicised previously, however National is now making the partial sale of state assets an election issue. Meridian, Genesis, Solid Energy, Mighty River Power and Air New Zealand have all been earmarked for partial sale. As much as I would like to see the addition of such companies to our stock market I fail to see how selling such assets to pay down debt is good for our country. Surely these companies are generating a return well in excess of the Government's cost of borrowing. If so, I don't see the point in selling them. If not, how do they expect to market them as a good investment to consumers?

Earthquake Kiwi Bond

Many investors have called on the Government to issue a bond to help finance the Christchurch rebuild. I was always sceptical of the idea due to the Government's ability to borrow money at very low rates. They have recently issued a four-year Earthquake Kiwi Bond, offering a return of 4.00%. Kiwi Bonds are similar to a bank term deposit in that they don't trade on the secondary market – you must hold them until maturity. The rate is low; however Government bonds are considered our only truly risk-free investment. The bond may appeal to those investors with an affinity to Christchurch, or those who simply like to feel they are doing their part to help. We have investment statements available at our office.

Public Service

The Government has also asked state service bosses to find a way to save $1 billion over three years. The effect of this is bound to be seen in staff cuts and rationalisation of services and departments. Wellington will be most affected, and my concern from an investor's point of view would be for a company like AMP Office Trust. Much of their Wellington office space is leased to Government departments.

Z Energy

Greenstone Energy, a company formed by Infratil and the New Zealand Superannuation Fund, last year bought the assets of Shell New Zealand. The company has recently rebranded to Z Energy, and has indicated it may issue a retail bond shortly. Any issue would likely be on similar terms to the issue of secured bonds undertaken in 2010, with bondholders sharing the same security as Z's banks on an equal ranking basis. Further details will be in next month's newsletter.