

# BRAMWELL BROWN LTD

## INVESTMENT ADVISERS – BROKERS

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### **Bramwell Brown Limited – Newsletter – March 2016**

#### **Interest Rates – how low can we go?**

Our Official Cash Rate (OCR) is now at its lowest ever level (2.50%), however looking at overseas markets it seems likely that we will go lower. The OCR has a significant effect on our economy and the returns on our investments. In a nutshell the OCR is a tool used by the Reserve Bank to manipulate the economy in order to keep inflation within a pre-determined range. That range is set in the Government's Policy Targets Agreement (PTA). The current PTA signed in 2012 seeks to keep inflation between 1 and 3 percent over the medium term, with a target for future average inflation around 2 percent. Manipulating interest rates is a relatively crude, yet effective, way of controlling inflation. If interest rates are reduced, economic activity will increase, which produces inflation. If you only had to pay 3% to borrow money you would be more inclined to do so to buy goods.

In January the Japanese Reserve Bank reduced its excess reserve rate (similar to our OCR) to negative 0.1%. So if the Japanese trading banks have surplus funds at the end of each day they must pay the Reserve Bank to park those funds. The intention is to get the banks lending money to businesses and individuals in an effort to stimulate economic activity. At present Japanese investors will receive only 0.01% to 0.10% on their bank term deposits. It makes our 4.00% rates look sensational. On the plus side they are able to borrow money for a house at 2.40%.

Other central banks already have negative interest rates, with Switzerland's central bank interest rate currently at negative 0.75%. Denmark, Sweden and the European Central Bank are also in negative territory. I wrote in the June 2015 newsletter about the many financial commentators predicting low interest rates for long periods – at present there doesn't seem to be a catalyst to change that viewpoint. The US talked briefly about raising interest rates; however a period of global volatility soon put that to bed. Our Reserve Bank is in a difficult position in that lowering interest rates is likely to pour more fuel on the Auckland housing market. Yet we have a dairy sector facing huge challenges, and a lower OCR should help them not only with lower interest rates, but with an accompanying lower exchange rate. I can only see the OCR decreasing through 2016.

The message for investors is that we all need to reassess our financial position, our goals and our tolerance for risk. We must have strategies to deal with long-term low interest rates.

## **Annuities**

Also in the June 2015 newsletter I mentioned the possibility of a return to annuities in New Zealand. The rise of KiwiSaver has seen everyday Kiwis amassing sizeable sums that will be available for their retirement. It is estimated that approximately 500,000 New Zealanders will reach 65 over the next fifteen years having squirreled away more than \$30 billion. Financial service providers will be looking to cash in on those savings by offering various retirement products. Annuities have been popular overseas for many years, yet have failed to gain traction in New Zealand. That may be about to change with The Lifetime Income Fund being developed by Ralph Stewart, the former chief executive of AXA. Lifetime Retirement Income has developed a variable annuity specifically designed to tap into investors' KiwiSaver balances.

How do annuities work? Historically an investor would hand over a lump sum to an insurance company, which then guarantees regular periodic payments until the investor dies. Regardless of the performance of the fund that the insurance company invests in, they guarantee to pay the investor until death. The insurance company takes the risk that the investor may live to 105, but benefits from those investors who may die early. You can think of an annuity as a life insurance policy in reverse. Instead of making periodic payments to the insurance company in return for a lump sum at death, you are making a lump sum payment in return for periodic payments until you die.

The Lifetime Income Fund offers an annuity, however you are able to withdraw the capital at any time, and any balance left at death is paid to your estate. Of course a guaranteed income for life doesn't come without cost – there are fees to pay. The guaranteed rate of return varies according to the age at which payments commence. The current minimum payment rates for each age group are:

➤ 65-69	5.00% per annum	70-74	5.50% per annum
➤ 75-79	6.00% per annum	80-85	6.50% per annum

This product may take some time to gain traction, however I'm sure there will be other providers looking to fill this space in the future. The biggest hurdle for investors is handing over a very large sum of money in the hope the provider will be able to pay as promised for the rest of your life.

## **KiwiSaver**

Before long many KiwiSaver investors will have amassed considerable sums in their accounts. Product providers including Lifetime Retirement Income will be looking to cash in on those sums of money. I would urge investors to thoroughly investigate any product offerings, and don't discount the idea of leaving your funds with your KiwiSaver provider. Setting up a regular withdrawal from your KiwiSaver account in retirement could be a very cost-effective option.

## **Fonterra**

Fonterra Co-operative Group is offering up to \$150 million of senior fixed rate bonds to institutional and retail New Zealand investors.

- Maturity date – March 7<sup>th</sup> 2023
- Interest rate – 4.42%
- Interest paid semi-annually in March and September
- Standard & Poor's credit rating – A-

Fonterra have distributed this bond using an institutional methodology, where no brokerage is paid to advisers. Investors seeking an allocation of these bonds will have to pay the usual 1% brokerage charged on secondary market fixed interest.

## **Meridian Energy**

Meridian Energy Limited is considering making an offer of up to \$100 million of unsecured, unsubordinated fixed rate bonds to institutional and New Zealand retail investors, with the ability to accept up to \$50 million of oversubscriptions at Meridian's discretion. It is expected that full details of the offer will be released in early March, when the offer is expected to open. No money is currently being sought and applications for the bonds cannot currently be made. It is likely the offer will be distributed in a similar manner to Fonterra, using an institutional methodology, with investors paying brokerage on any transaction.

### **CALL THE OFFICE IF THESE BOND OFFERS ARE OF INTEREST TO YOU**

## **Bank Rates**

Here is a summary of some of the bank rates on offer at present.

	<b>1 Year</b>	<b>2 Years</b>	<b>3 Years</b>	<b>4 Years</b>	<b>5 Years</b>
<b>ANZ</b>	3.65%	3.75%	3.80%	3.85%	3.90%
<b>ASB</b>	3.40%	3.60%	3.75%	3.85%	4.00%
<b>BNZ</b>	3.50%	3.60%	3.75%	3.85%	4.00%
<b>Heartland</b>	3.55%	3.60%	3.70%	3.75%	3.80%
<b>Kiwibank</b>	3.40%	3.45%	3.50%	3.50%	3.40%
<b>Rabobank</b>	3.69%	3.65%	3.80%	3.89%	3.99%
<b>UDC</b>	3.75%	3.50%	3.55%	3.65%	3.75%
<b>Westpac</b>	3.40%	3.45%	3.50%	3.55%	3.60%

## **NZX and ASX Settlements**

The NZX and ASX markets intend to reduce their current settlement period of trade date plus three business days (T+3) to a settlement period of trade date plus two business days (T+2) for trades on their markets.

### Why is the change being made?

Shortening of the settlement period on NZX and ASX markets will ensure NZX and ASX match international best practice in this area and align with each other.

### When is the change being made?

The new T+2 settlement period will apply to transactions entered into on or after Monday 7<sup>th</sup> March 2016.

### What does this mean for you?

If you buy securities (shares or bonds) on or after Monday 7<sup>th</sup> March 2016, payment must be made in cleared funds within two business days after the trade takes place.

If you sell securities on or after Monday 7<sup>th</sup> March 2016, payment will be made to you overnight on the second business day after the trade has taken place.

There is a strong push from the brokers we deal with to insist on electronic communication with our underlying clients. With such a short settlement period now it is unreasonable to rely on the post when settling a securities purchase. Our brokers cannot be expected to act as short-term financiers and will expect to be paid on time (they must settle the other side of the trade on time). Most investors are able to receive contract notes by email, and transfer funds electronically through their on-line banking programme. For those without electronic access (and instead pay by cheque) we will now insist on prior payment arrangements being made before an order to buy securities is placed.

Purchasing Australian securities through our Melbourne broker adds a further level of complexity in that we must pay in Australian dollars. Bramwell Brown has the ability to transact foreign exchange on your behalf, however we insist on cleared funds paid to our Trust Account before we will do so. Contact the office at any time to discuss how these changes may affect you.

## **Portfolio Administration**

Are you having trouble with the share registries sending your financial information via email rather than post? Are you spending hours searching for financial information for your accountant at the end of each financial year? If so Bramwell Brown can help. We offer a portfolio administration service where we handle all the mail associated with your portfolio and liaise with your accountant at the end of each year. Call the office if you would like to discuss this service.