

FINANCIAL STANDARD GUIDE TO MARGIN LENDING



GUIDE SERIES **2**

PROUDLY SUPPORTED BY



PUBLISHED BY

Financial Standard
a Rainmaker Information company

Catch
bigger
returns.



Margin Lending

Good with people. Good with money.

St. George Margin Lending offers you a host of ways to maximise your clients' investment power. Our flexible lines of credit can be secured against cash, property or existing investments in shares, managed funds or master trusts. It's the perfect way to diversify your clients' portfolios in a tax-effective way and help them invest more. To find the best way to maximise your clients' wealth and grow their investments, call **1300 304 065** today or visit stgeorgemarginlending.com.au



This information has been prepared without taking account of anyone's objectives, financial situation or needs. Because of this, before acting on this information, individuals should consider its appropriateness, having regard to their objectives, financial situation and needs. St. George Bank Limited ABN 92 055 513 070 AFS Licence No. 240997.

CONTENTS

INDUSTRY SNAPSHOT 3

WHAT IS A MARGIN LOAN? 5

UNDERSTANDING HOW MARGIN LOANS WORK 6

DEALING WITH MARGIN CALLS 9

CHOOSING THE RIGHT MARGIN LOAN 11

FEES 13

CASE STUDIES 15

THE MYTHS OF MARGIN LENDING 20

UNDER THE BONNET 27

EASY GUIDE 30

GLOSSARY 32

Editor

Michelle Baltazar
michelle.baltazar@financialstandard.com.au

Writer

John Kavanagh
john@thesheet.com

Research

Andrew Keevers
andrew.keevers@rainmaker.com.au

Publisher

Christopher Page
christopher.page@rainmaker.com.au

Production Manager & Designer

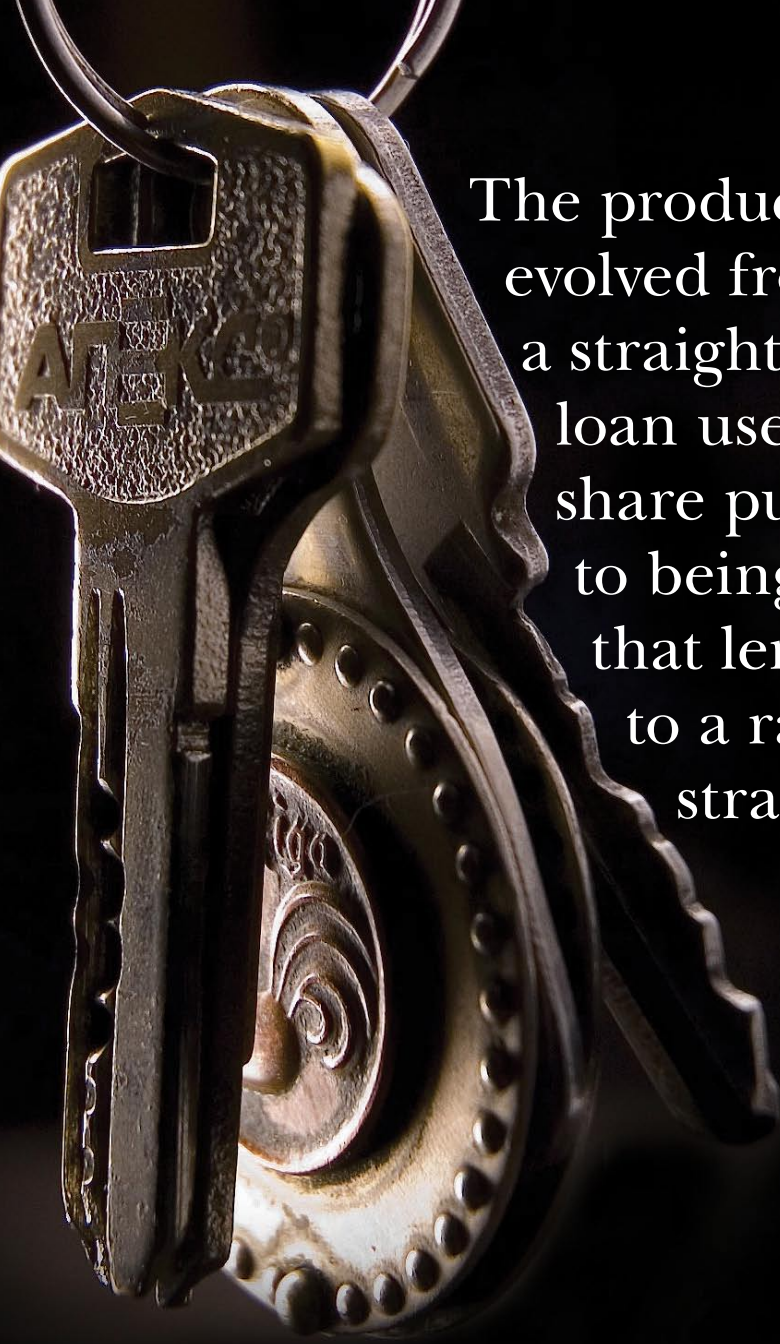
Kym-Maree Apps
kym-maree.apps@financialstandard.com.au

Level 2, 151 Clarence Street, Sydney NSW 2000
Phone: 02 8234 7500 Fax: 02 8234 7599

www.financialstandard.com.au
www.rainmaker.com.au

Financial Standard is an industry publication owned and published by Rainmaker Group, a publishing and research data group that was founded in 1992 and has established a reputation as a leading financial services information company in Australia providing database services, consulting services, publishing and conferences.

The Rainmaker Group is comprised of Rainmaker Information, Rainmaker iTV, Rainmaker Select Series and Financial Standard.



The product has evolved from being a straightforward loan used to fund share purchases to being one that lends itself to a range of strategies.

INDUSTRY SNAPSHOT

MARGIN LENDING HAS MOVED from the fringes of the retail investment market into the mainstream over the past decade. The number of investors using the product to introduce leverage into their investment strategies has more than doubled over that period. There are more lenders and there is a greater diversity of product.

Originally a product that stockbrokers offered their clients, margin loans are now in the toolkit of many financial planners. As margin lending has entered the financial planning market, the product has evolved from being a straightforward loan used to fund share purchases to being one that lends itself to a range of strategies.

However, there is a large number of planners who do not recommend margin loans to their clients.


Figures from the Reserve Bank of Australia show that at the end of 2007 more than 200,000 investors had a total of \$37.7 billion of margin loans outstanding. When the RBA started collecting data on margin lending in 1999 it reported that margin loan outstandings were a modest \$4.7 billion. The market has had an eight-fold increase.

The RBA's data shows that the great majority of investors use their margin loans prudently. The aggregate credit limit is \$76 billion. This means that outstandings are just under half the amount of credit advanced by lenders. The value of underlying securities in margin loan accounts is \$92.8 billion, which means that the average gearing level is a modest 42 per cent.

Back in 2000, when margin loan outstandings were \$6.7 billion, the value of underlying securities was \$13.4 billion – exactly double. Today the value of underlying security is 2.5 times. It would be simplistic to suggest that all of that increase in underlying security is due to investment returns but the figures do indicate a positive long-term trend for investors.

The range of products includes instalment loans, that allow investors to make geared monthly contributions into managed funds, protected loans, that include capital protection in the loan structure and loans that allow investment in offshore securities.

Leaders in the margin lending industry include Commonwealth Bank, St. George Bank, Leveraged Equities, Macquarie Bank and BT Financial Group.



A trend in recent years has been towards wider approved lists – not only more stocks and funds but also equity derivative products such as options.

WHAT IS A MARGIN LOAN?

A MARGIN LOAN is nothing more complicated than borrowing to invest in shares or managed funds using cash, existing shares or funds as security. It provides leverage, which means that it increases the total amount invested and in that way increases potential returns

The loan is structured as a line of credit with a great deal of flexibility around interest rate options, repayment schedules and tax outcomes.

Its principal purpose is to provide greater access to markets with the aim of achieving financial goals more quickly, but there are a number of additional benefits. It can unlock equity in existing investments for use as loan security. It can be used to raise cash for other investments without having to sell assets. It can help diversify a portfolio.

There are several enhancements to a standard margin loan that suit particular needs:

- **Protected loans** allow risk-averse investors to use gearing without the risk of losing capital.
- **Instalment loans** allow investors without existing savings or investment to establish a savings plan with an accompanying margin loan facility.
- **Asset access loans** allow investors to use equity in their homes as security for a margin loan.

All equity investments, whether through direct shares or managed funds, are subject to rises and falls. Margin loans provide greater access to markets and so the greater the investment the greater the impact of market movements on the portfolio. A margin loan will magnify gains just as it will magnify losses.

All lenders have a list of approved securities, stocks and funds, against which they will lend. A trend in recent years has been towards wider approved lists – not only more stocks and funds but also equity derivative products such as options.

Cost incurred in producing assessable income are tax deductible and the interest paid on a margin loan comes under that heading. Tax breaks are a secondary but important part of geared investing.

UNDERSTANDING HOW MARGIN LOANS WORK

LIKE ANY INVESTMENT PRODUCT, a margin loan comes with a range of interest rate and repayment structures, tax outcomes and strategic possibilities. It is a product that can be tailored to a variety of purposes.

Interest

All margin loans are interest-only loans and lenders will allow borrowers to capitalise interest up to the gearing limit. Borrowers can use this to manage their cashflow. An investor who borrows at a loan to valuation ratio of 50 per cent on a portfolio with a maximum LVR of 70 per cent can forgo interest payments until the loan amount reaches that maximum LVR level.

Some investors capitalise interest for six months at a time and then use dividends or fund distributions to pay interest. In this way the gearing becomes partially or fully self-funding, depending on the flow of income from the portfolio. Other investors will capitalise over a longer period – up to a couple of years – and then take profits from their holdings to repay the loan.

Prepaying interest is a popular way of bringing forward tax deductions. Most margin lenders will allow borrowers to pay 12 months' interest in advance. Borrowers can make an interest payment in June for the financial year ahead, then claim a deduction for the whole amount against taxable income in the current financial year.

Security

Investors have several options when it comes to securing their margin loan. The most common approach is to use existing cash combined with the loan to invest in shares or funds. Another common approach is to use an existing portfolio as security to borrow money to buy additional shares or funds.

A strategy that is less common is to use third party security. Investors can take out a loan secured against another person's assets. Spouses could use this approach with the result that the partner in a high tax bracket takes out the loan against a portfolio held by the low income earning partner. The high income earner gets the full value of the deduction on the interest payments, while the low income earner gets the benefit of a lower capital gains tax rate.

Tax management

Interest paid on a margin loan is generally tax deductible. Investors using a margin loan are eligible for franking credits distributed with company dividends.

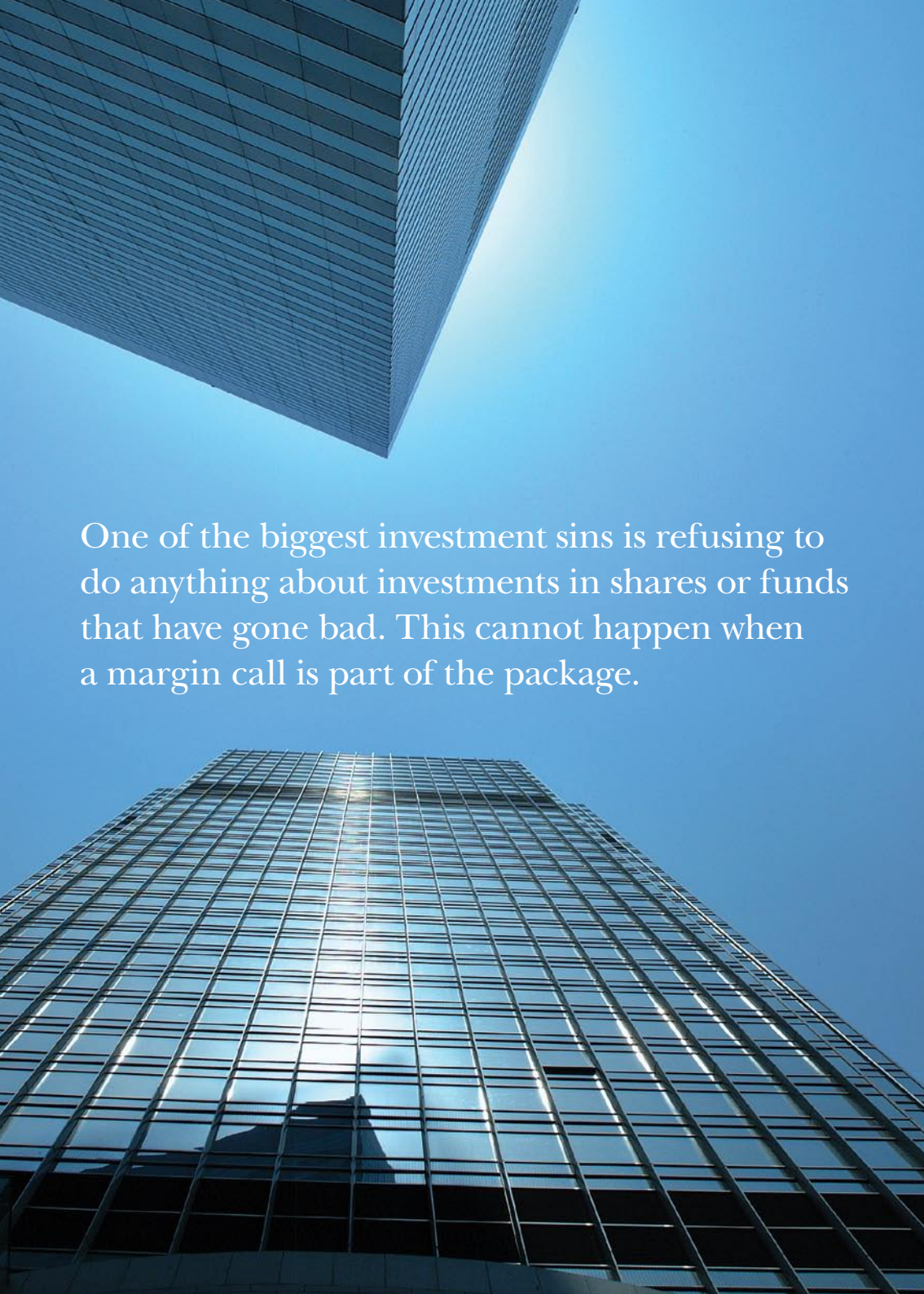
A big issue for investors is how to free up cash from their investment portfolios without triggering a capital tax liability. One way of getting around the problem is to use the increased value of the equity in the portfolio to increase the line of credit. The new borrowing releases cash that can be reinvested. Beneficial ownership of the portfolio is not affected and there is no tax consequence.

Where more than one investor is involved in creating an investment portfolio, both spouses for example, questions of ownership may have a bearing on tax management. If the plan is to negative gear the investment, so that interest cost exceeds income from dividends and fund distributions, then it makes sense to put the assets in the name of the high income earner to maximise tax deductions. If the plan is to positive gear, so that dividends and distributions exceed interest cost, then the assets should be in the name of the low income earner to minimise the income tax charge.

Convenience

These days margin lenders are very much part of the online world. Lenders provide internet access so that investors and their advisers can have 24 hour access to their accounts.

In many cases margin loan accounts are linked to online broker accounts. In such systems, the investor or adviser can place an order for stock and the broker system will automatically check the margin loan account for available funds. The time needed to complete a transaction is reduced and the investor or adviser can go online to check the gearing position and portfolio balance at the same time. Wealth management companies have undertaken similar integration programs with their retail investment platforms.



One of the biggest investment sins is refusing to do anything about investments in shares or funds that have gone bad. This cannot happen when a margin call is part of the package.

DEALING WITH MARGIN CALLS

ANY DISCUSSION of the pros and cons of margin loans has to begin with the margin call – the event that geared investors dread. But this is where things get interesting. Is a margin call a con, as most investors would assume at first sight, or a pro?

A borrower receives a margin call when their loan exceeds the maximum loan to valuation ratio. Lenders provide what they call a buffer – if the value of the security falls and the loan value exceeds the limit by only a few percentage points, the account is “in the buffer” and no action is required.

Most lenders have a buffer of 5 per cent, some 10 per cent. When the loan balance exceeds the limit by more than the buffer, it is time for action.

In such a situation the borrower must do one of three things: provide additional security, repay part of the loan or sell securities. Lenders say that in most cases borrowers are able to settle margin calls by putting in extra cash.

Nightmare scenario? Quite the contrary, many lenders argue. They promote margin calls as a safety net, where the lender uses the mechanism as a way of making sure that borrowers address their situation while they still have plenty of equity left in their securities.

The borrower and their planner are required to review the situation and make a considered decision about whether the securities are worth holding onto. This is a very different situation from an investor who sits on a loss-making investment in the forlorn hope that it will come good. One of the biggest investment sins is refusing to do anything about investments in shares or funds that have gone bad. This cannot happen when a margin call is part of the package.

One way to manage the risk of a margin call is to keep the gearing level below the limit allowed by the lenders. Lenders allow a maximum loan to valuation ratio of 70 per cent to 80 per cent on many stocks and funds. Some financial planning groups limit their clients to 60 per cent. Securities would have to fall a long way to trigger a margin call in such circumstances.

Leverage increases access to markets and offers the prospect of higher returns. The benefits of leverage can only come with a commensurate increase in downside risk. That risk can be managed by setting a gearing level appropriate to the investor’s risk tolerance. There are a number of other risk management issues that need to be attended to.

Investing in a diversified portfolio reduces the risk that a big loss on any one security will do serious damage. Managed funds offer a wide variety of different stocks. Investors should have cash reserves or other securities that can be tipped into the margin loan account if required.

Finally, having some insurance cover, such as income protection, life cover, total and permanent disability cover or critical illness, will cover a range of contingencies and allow investors to meet margin calls or restructure their holdings without being forced to sell securities.

The risk of a margin call

Maximum gearing %	Actual gearing %			
	70	60	50	40
	Fall in the value of securities before a margin call			
70	13	25	38	50
60		14	28	42
50			16	33
40				20

Source: St. George Bank

CHOOSING THE RIGHT MARGIN LOAN

THE GREAT MAJORITY of investors who decide to gear their investments use a standard margin loan. They, or their advisers, are often unaware that there are several different types of margin loans designed to suit different investment strategies, risk tolerances and established asset structures.

Protected loans

An investor can use a protected loan to borrow for a term of between one and five years with a guarantee that at the end of the term 100 per cent of their capital will be returned.

If the shares or funds have lost value by the end of the loan term, the borrower has the right to give the shares or units in the fund to the lender and extinguish the debt. Borrowers never receive a margin call. Protected loans are suited to uncertain times and to investors who have very low risk tolerance.

Protection comes at a cost. Repayments are made up of interest plus a protection component, which pays for a derivative contract such as a put option over the portfolio. With the cost of protection added into the repayments the cost of a protected loan will usually be four or five percentage points higher than a standard margin loan. Think of the extra payment as an insurance premium.

Because the structure of protected loans is a little more complex than standard margin loans there are some tax consequences. The Australian Taxation Office does not allow a full deduction for interest payments. It apportions some of the interest payment as a non-deductible cost of protection. Because of this it is advisable to stick to protected loans that have ATO product rulings.

The range of securities against which a protected loan can be raised is limited in comparison to a conventional margin loan. This is because of the need for the lender to be able to structure the protection mechanism.

An investor using a protected loan has the same right to dividends, franking credit and capital gains that an investor using a standard margin loan would have.

An important feature of a protected loan is that securities are protected separately. If the investor makes gains on one security they will not be cancelled out by losses on another holding.

At the end of the loan period the investor can, in the event of a fall in asset values, require the lender to purchase the securities. If the securities have increased in value the investor can extend the protected loan for a new term, convert the loan to a standard margin loan, sell the shares to repay the loan or keep the shares and repay the loan with cash.

Instalment loans

A common investment strategy for young people starting their wealth accumulation plans and people with high incomes but no savings is to make regular contributions to a fund or group of funds. Most fund managers have regular contribution plans. An instalment loan, sometimes called a savings gearing loan, is one that can be linked to such a savings plan.

The investor makes an initial investment of their own money along with some borrowed funds. The initial amount varies according to the minimum initial investment required by the fund manager. The fund manager may have a minimum ongoing monthly contribution amount, as do some lenders. The strategy does not work for direct shares.

Asset access loans

A more recent development in the margin loan market is the introduction of loans that allow people with equity in their homes to use that equity to borrow for investment. Investors can nominate a portion of the credit limit in their home loan (the available equity) as security for a margin loan.

Usually the home loan and the margin loan must be with the same lender. There is no extra interest on the home loan; the borrower pays interest on the margin loan as the funds are drawn.

The maintenance of separate home loan and margin loan accounts helps keep the borrower's tax position simple. Interest payments on the margin loan are deductible, while interest payments on the home loan are not.

A borrower with \$45,000 available in a home loan would be able to borrow up to \$180,000 to purchase shares or funds. This would result in a margin loan gearing ratio of 80 per cent.

FEES

MARGIN LOANS do not carry a heavy burden of fees and charges. In most cases individual borrowers do not pay application fees and only a couple of lenders charge transaction fees.

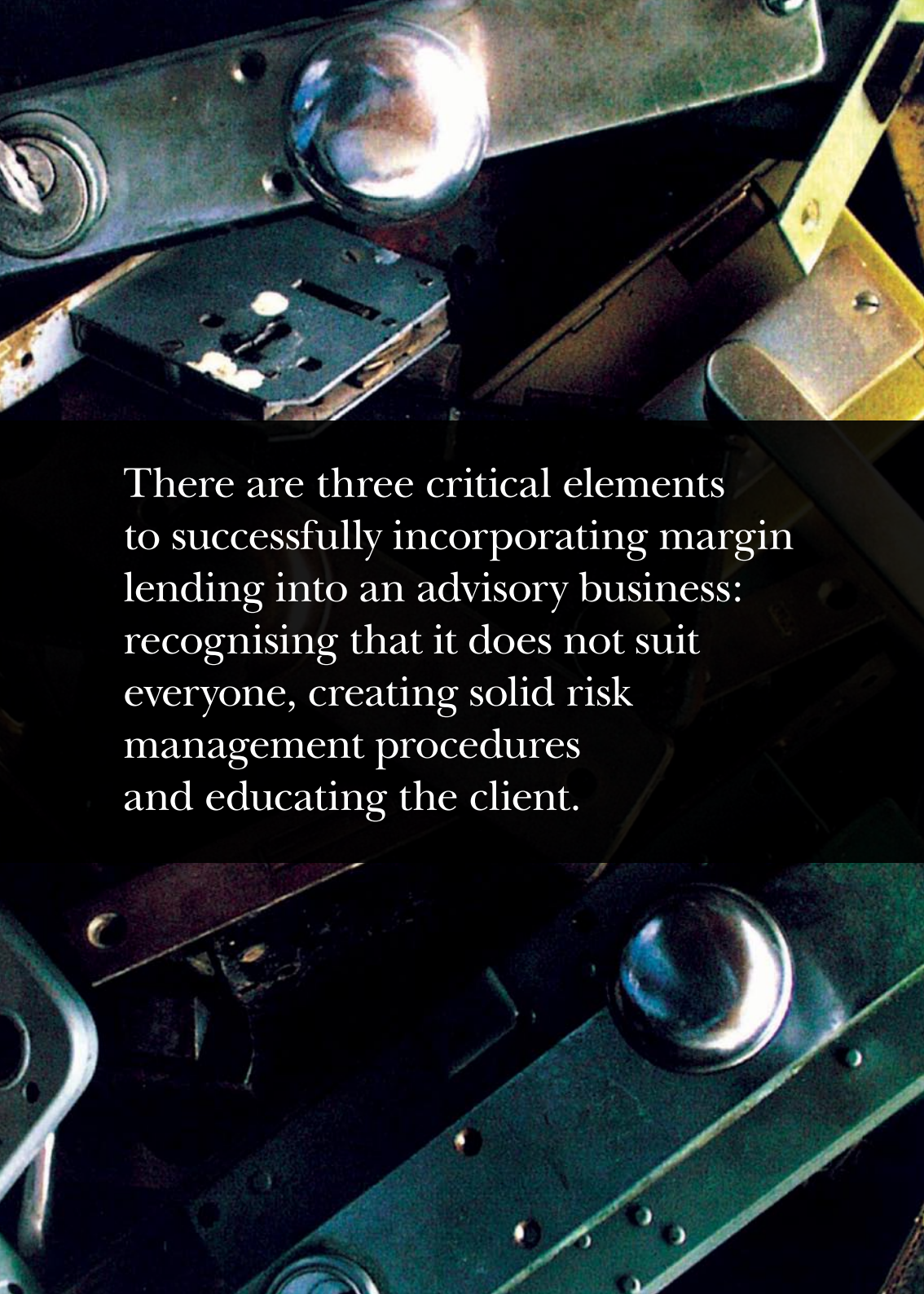
Application fees do apply to companies and trusts. According to the banking industry research group Infochoice, the standard application fee for companies is around \$150, with the range between \$130 and \$200. Application fees for trusts are a little higher, ranging between \$150 and \$250.

In most cases there are no early repayment fees. A few lenders charge fees if repayments are made within the first few months. Repayment fees range between \$200 and \$500.

The majority of lenders allow unlimited transactions free of charge. One lender allows borrowers 10 free transactions and then charges \$10 per share settlement. Another charges \$5 per transaction if the loan balance is below \$20,000.

The majority of lenders
allow unlimited transactions
free of charge.



A close-up, high-angle photograph of a microscope's objective lens and stage. The lens is prominent in the upper left, reflecting light. Below it, the stage is visible with a specimen slide. The background is dark, emphasizing the metallic and glass components of the instrument.

There are three critical elements to successfully incorporating margin lending into an advisory business: recognising that it does not suit everyone, creating solid risk management procedures and educating the client.

CASE STUDIES

Case study 1

Mark Lockhart, financial planner

Financial planner Mark Lockhart believes there are three critical elements to successfully incorporating margin lending into an advisory business: recognising that it does not suit everyone, creating solid risk management procedures and educating the client.

Lockhart has been a planner since 1993. He is an authorised representative of Aon Wealth Management and works at Moneywise Wealth Management in Wollongong, New South Wales.

Moneywise has been using gearing as part of its clients' wealth accumulation strategies for a long time and Lockhart says the planners at the firm are able to draw on this experience to develop a strong sense of when it is appropriate for a client.

He says, "It works well for certain groups. The first is people who have an investment timeframe that allows them to establish a long term strategy and who understand that gearing will expose them to market volatility from time to time. I have to feel confident that they will stick to their strategy.

"It is a tool for wealth accumulators. I would not recommend it to anyone looking to generate income from their portfolio. It is particularly useful for young people who have good jobs that pay well but have no capital to invest.

"For those people, an instalment gearing strategy will improve their access to the investment market. If those clients are on high incomes there may be some tax benefits as well.

"It is an obvious choice for the more aggressive wealth accumulators. We talk to people in their 40s and 50s who have sold a property or received an inheritance and who want to use leverage to build on that capital.

"From time to time we recommend margin lending to clients who have ignored financial planning until quite late in their working lives. They are playing catch-up with their retirement planning. Margin lending can be very useful for these people."

For any of these investors Lockhart insists that an investment strategy incorporating margin lending must be for a minimum of five to seven years.

"It is important to spend time educating clients, explaining the risks and rewards of leverage and demonstrating the impact of volatility. We talk about how it creates risk and opportunities.

“In our second interview with a client, before we issue the statement of advice, we spend time going through this. You need to prepare people because when they do experience volatile markets it is going to be quite a shock for them.

“You have to make sure they are not going to make any panic moves. When markets are falling we get calls every day from clients who want to be reassured.”

Apart from educating clients to anticipate the ups and downs of investment cycles, Lockhart says it is important to put some risk management measures in place.

The first is conservative gearing. His firm’s policy is not to gear above 60 per cent. That leaves plenty of room for stocks or funds to fall before the client has to face a margin call.

The second thing is to make sure the client has cash reserves that can be used to meet contingencies, such as topping up security in the margin loan account. Lockhart recommends a minimum of \$5,000 to \$10,000.

Third is a well-diversified portfolio. Moneywise uses wholesale managed funds and will take existing shares as security. If the client wants to gear a concentrated equity portfolio Lockhart will recommend a lower gearing level.

RISK MANAGEMENT

Financial planners should consider a four-point risk management plan when putting together an investment strategy for clients that involves margin lending:

- **Conservative gearing**

Do not gear up to the maximum allowed by the lender.

- **Cash reserves**

A minimum of \$5,000 to \$10,000 will meet contingencies.

- **Diversification**

Managed funds offer a bigger spread of stock. If the client insists on gearing a concentrated equity portfolio then reduce the gearing.

- **Life insurance**

A client should have enough cover to generate an amount of cash that will give the planner room to restructure the portfolio.

Finally, he says insurance is vital. Lockhart does not cover the amount of the loan fully; instead, he gets his clients to take out enough income protection or trauma insurance to provide a cash injection and give the planner room to restructure the portfolio.

“We make the recommendation and the client makes the decision. We have always believed in life insurance.”

Lockhart says none of his clients had margin calls during January 2008, when the Australian sharemarket fell more than 20 per cent from five-year highs reached the previous November.

A client of one of the other principals of the firm had margin loans where the loan-to-valuation ratio increased to 78.6 per cent. The client had some extra shares that could be added to the margin loan account to bring the LVR back into line.

Lockhart says that over the past five years gearing has helped produce return of 40 per cent and 50 per cent a year on invested capital for his clients.

“We have to remind clients that these returns are unusual. What we aim for over the long term is a return using gearing that is 50 per cent higher than what they would make on the underlying capital if it was ungeared.”

Lockhart says none of his clients had margin calls during January 2008, when the Australian sharemarket fell more than 20 per cent from five-year highs reached the previous November.



Case Study 2

Jennifer Hunt, client

JENNIFER HUNT concedes that she presents an interesting problem for a financial planner. She came late to investing but is keen to retire early – by age 50 or even 45 if she can afford it.

What saved her planner from going prematurely grey was that Hunt had plenty of disposable income. She has a good job with an IT company in Melbourne and no family commitments.

Her planner suggested she start investing in funds and shares. The purchase of units in the funds was done through regular monthly contributions supplemented with an instalment gearing loan.

Instalment gearing is a margin loan linked to a regular savings plan. The investor makes an initial investment of their own money along with some borrowed funds to buy units in a fund or funds, and then monthly contributions that are also a combination of the investor's own money plus loan funds.

Hunt uses savings to buy shares on an irregular basis, after discussing the markets with her planner and looking at her savings balance. She uses a margin loan in conjunction with these investments as well.

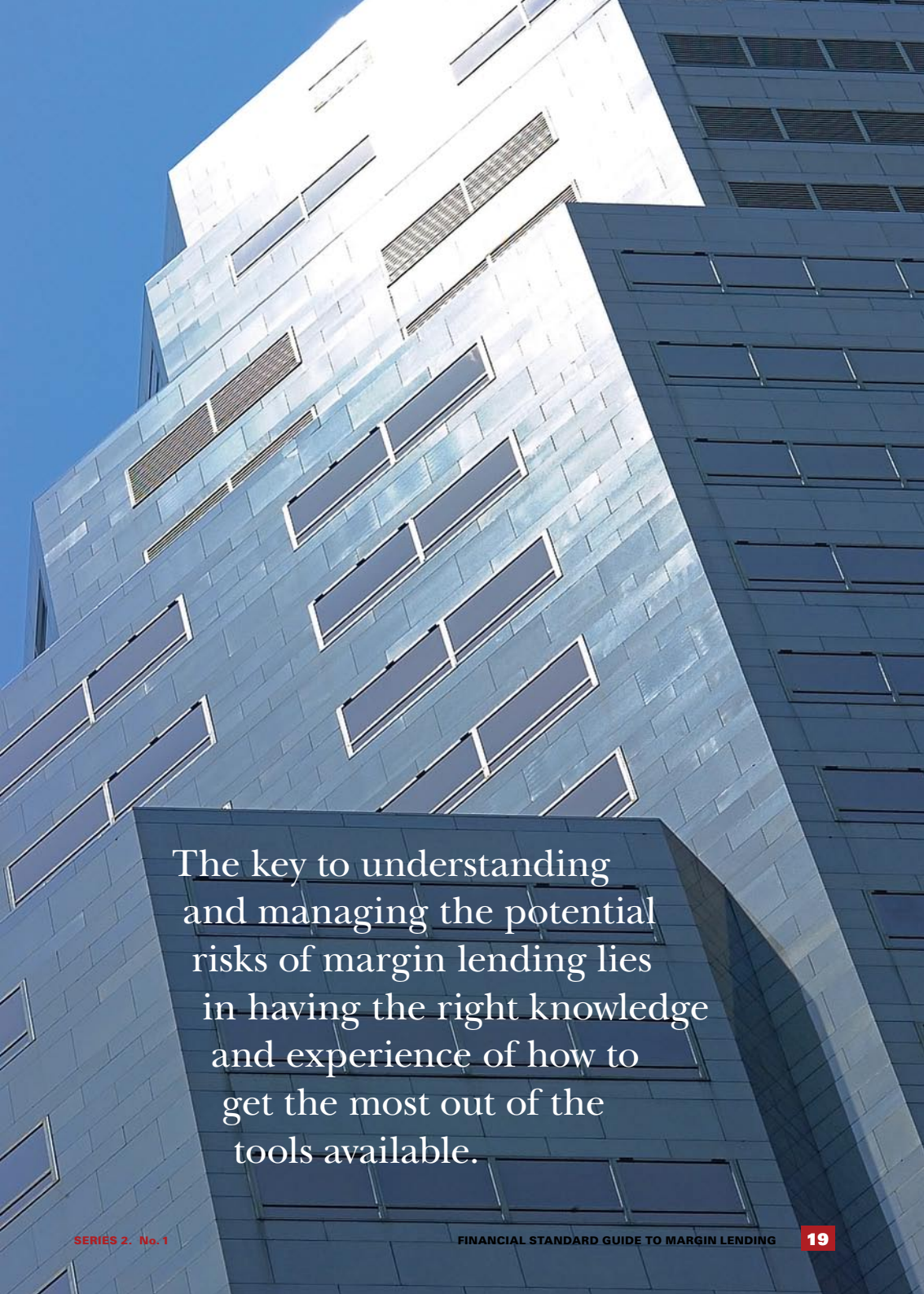
She has been using the strategy for the past six years and is very happy with the outcome. Her returns have increased each year ahead of what she would have earned investing only her own capital. She got through the big sharemarket correction in January 2008 without having to deal with a margin call.

She says she talks to her planner on a regular basis and has been buying selected stocks during the market correction.

When Hunt talks about retiring young she does not necessarily mean giving up work altogether. She wants the financial freedom to be able to do what she likes and that may include continuing to work – but on her terms.

She is confident that she is on her way to her goal. The margin loan has played its role, not only by giving her greater access to market but also by providing some tax benefits.

She recognises that she is taking on more risk using margin lending but says what gives her comfort is her relationship with her planner. She has regular contact and feels that, even though she is no financial expert, she is well briefed on what is happening to her portfolio.



The key to understanding and managing the potential risks of margin lending lies in having the right knowledge and experience of how to get the most out of the tools available.

THE MYTHS OF MARGIN LENDING

Sponsored statement

Paul Lewis, National Sales Manager, St.George Margin Lending

MARGIN LENDING, also known as gearing or borrowing to invest, is a popular wealth creation strategy that has been embraced by many investors. There still remains doubt among some who consider “gearing” too risky or confusing. In reality, gearing is a common strategy suitable for different investors with varying knowledge and financial goals. As their trusted adviser, you can help dispel some of the myths of margin lending that might be limiting your clients from realising their true wealth potential.



Paul Lewis
St.George Margin Lending

MYTH 1

Margin lending is too complex

Margin lending is a simple and tax effective way to build your clients' wealth. It is perhaps best explained by comparing it to another well-known basic form of gearing – property investing. Just like investing in property, where the loan is secured against the property, a margin loan is secured against shares and managed fund investments, or against your client's surplus cash.

With the growing popularity of margin lending, margin lenders continue to provide a range of tools and educational resources to both clients and advisers to help remove this perceived complexity. This includes:

- Information seminars to educate clients on the benefits of wealth accumulation strategies.
- Regular monthly statements to keep clients informed of their loan balances and portfolios.
- Online simulators to enable investors to simulate scenarios to understand the impact on their gearing ratio.
- Internet account access to regularly monitor their portfolios and gearing ratio.

- Flexible and convenient repayment options including prepay, in arrears and capitalised interest.
- A range of products to suit all types of investors including instalment gearing via savings gearing, protected loans and asset access.

St.George Margin Lending understands the importance of education and encourages all advisers to visit our Planner Assist website, which has been designed to improve their understanding of margin lending. The Planner Assist website offers you a simple, practical and easy to use set of tools and guides to help you keep up-to-date with gearing issues, so you can assist your clients in leveraging the power of margin lending and close your sales with confidence.

Today, over 1000 advisers have referred to The Gearing College (in conjunction with Gryphon Learning) as a useful source of gearing education including the ability to earn CPD points.

To learn more visit www.plannerassist.com.au or call St.George Margin Lending on 1300 304 065.

MYTH 2

Margin lending is too risky

Any investment strategy involves some form of risk. The key to understanding and managing the potential risks of margin lending lies in having the right knowledge and experience of how to get the most out of the tools available.

Quite often, the perceived risk of margin lending is a result of advisers and clients not properly educating themselves on how to manage the inherit risk involved with gearing. Without taking the time to properly educate themselves and their clients, it comes as no surprise that some advisers continue to perceive margin lending as too risky.

However, there are simple risk management strategies to highlight to your clients:

- **Diversification** – Holding a diversified portfolio across a broad range of sectors and asset classes will help to minimise the impact of a market fall on their portfolio.
- **Reinvest their income** – To help increase your client’s security value, reinvesting any share dividends or managed fund distributions back into the loan can give your clients further reassurance that you’re managing their loan effectively.

- **Long-term outlook** – Your clients should maintain a long-term outlook, particularly when borrowing to invest. Quite often, clients can be distracted particularly by short-term market volatility.
- **Borrow less** – By borrowing less than the amount your clients are entitled to borrow will help absorb market movements without triggering a margin call.
- **Maintain a cash reserve** – If your clients are particularly worried about receiving a margin call, the best practice is to keep some surplus cash so they can comfortably restore their gearing ratio if called upon.

MYTH 3

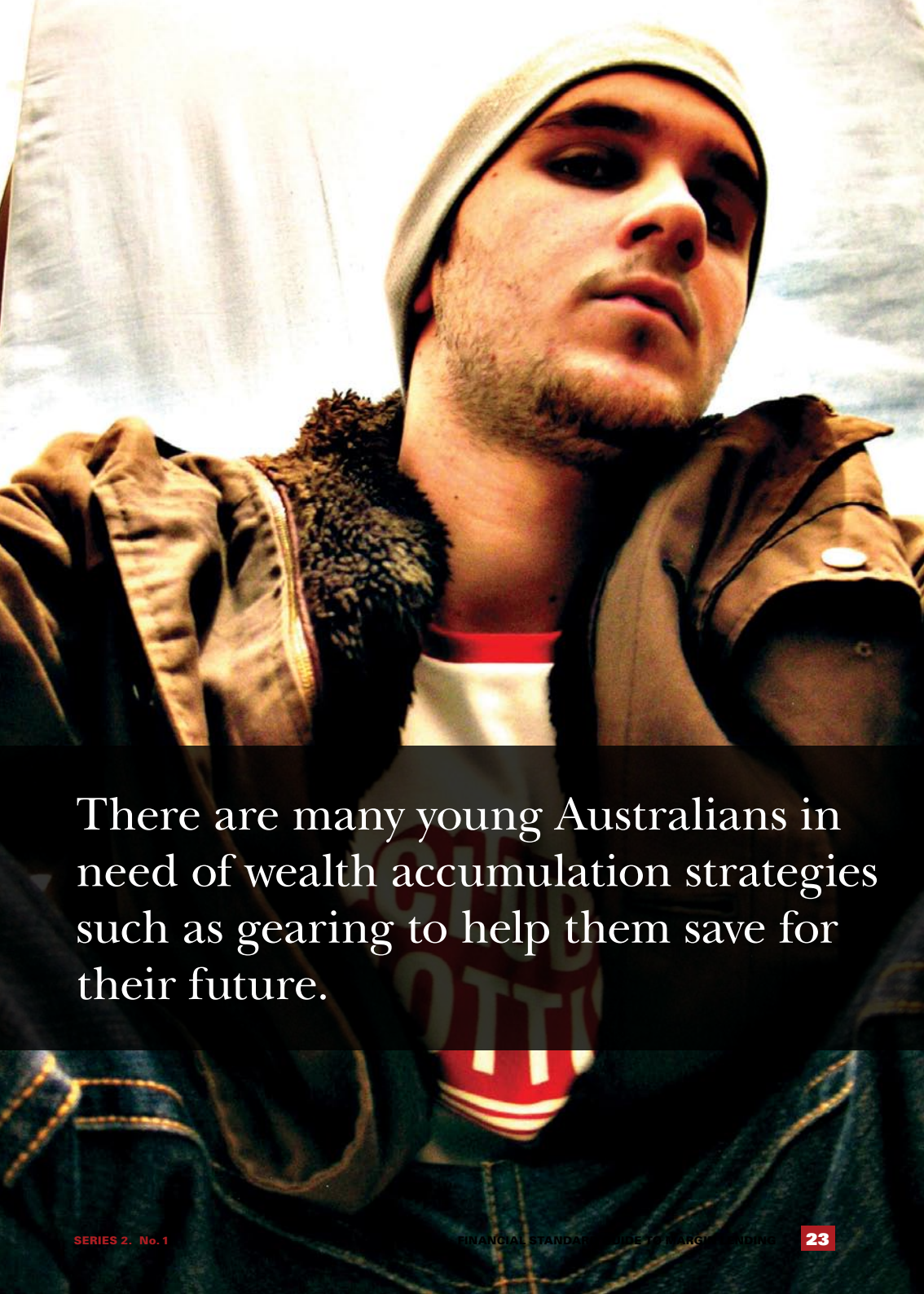
Margin lending is not suitable for my type of clients

Given the benefits margin lending can provide to all types of investors, it comes as a surprise when advisers claim that margin lending is not suitable for their clients. This may be more a case that they have not diversified their client base enough and may be depending too much on the baby boomers who are coming into retirement (aged 55–75).

With the growing needs of the wealth accumulator segment – “Generation X” (aged 32–47), there are many opportunities available for advisers to further build their business. There are many young Australians in need of wealth accumulation strategies such as gearing to help them save for their future.

Whether it is saving for a deposit for their first home, managing capital gains tax or perhaps developing a savings plan to fund their children’s education, many prospective clients could benefit from a long term investment strategy using margin lending.

A St.George Margin Lending Business Manager would be happy to help you review your client base to identify potential client opportunities.



There are many young Australians in need of wealth accumulation strategies such as gearing to help them save for their future.

MYTH 4

Home equity loans are better than margin loans

Home equity loans are structured to allow clients to draw down against the equity in their home. Your clients may have considered using this equity to invest in the share market via a home equity loan.

In some cases, this may be perceived as the easiest and fastest option of “borrowing to invest”. In other cases, it may be that your clients are simply comparing the interest rate of their home equity loan to the interest rate of a margin loan.

However, it is important to educate clients on the specific features and related benefits of a margin loan facility. Remember, margin loans were specifically designed to fund and monitor share market investments. Therefore, they have been purpose built to help advisers and clients effectively manage their risk exposure when they have leveraged their portfolio.

Also remember that come tax time, having a margin loan with separate monthly statements and tax reporting, can make calculating any tax deductible interest payments far simpler than trying to separate the deductible and non-deductible debt from a home equity loan.

MYTH 5

Margin calls scare my clients

Despite what your clients may have read in the newspapers or heard through friends, your clients should not fear margin calls. In fact, margin calls are a useful risk management tool, acting as an early warning to reassess their portfolios.

Without margin calls, the fact is many clients would be worse off in the event of a falling market. A margin call can be a timely reminder to reduce their exposure and reassess their portfolio position. Quite often, the reason margin calls scare investors is because of a lack of knowledge and proper education. That's where you as their trusted adviser can play a key role in explaining how they work and how to minimise the chance of a margin call.

Remember, as outlined in Myth 2, there is a range of risk minimisation strategies if your clients are still concerned about margin calls.

MYTH 6

Fixed rates are only for June

Whether to fix your loan or not is a question often addressed leading up to June, but the decision to fix and the benefits of doing so are relevant all year round. Fixing not only protects your clients from potential interest rate rises, it also allows them to pre-plan and pre-pay their loan interest in advance. Furthermore, fixed rates can be lower than variable interest rates. So it's important to highlight the tax deductibility of interest paid does not depend on the time of year the loan is fixed.

MYTH 7

Interest rates are too high

When interest rates start to climb, clients are naturally cautious about taking on new debt, particularly if they are already suffering rate rises on their home loans. It's important to differentiate between tax-deductible debt used for investment purposes such as a margin loan and non-deductible debt like their home loan.

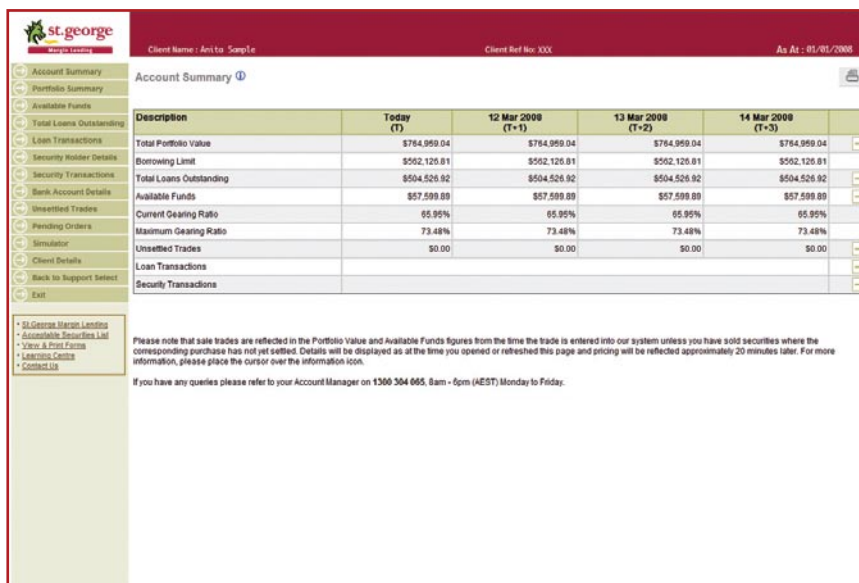
By choosing to invest in quality stocks that pay reliable dividends, your clients can use this income to reduce their loan amount, in turn reducing the interest they pay. It's also important to remember that margin lending should form part of a long-term investment strategy. With the right education and financial advice, your clients should see returns that should offset the impact of interest costs over the long term.

UNDER THE BONNET

THROUGH THE INTERNET, financial planners and their clients can access margin loan accounts 24 hours a day, seven days a week. While different margin lenders have different online services, the main screens are broadly similar. Here are some basic screenshots to illustrate.

ACCOUNT SUMMARY

A snapshot of your clients' account helps you keep track of the margin lending facility.



Description	Today (T)	12 Mar 2008 (T+1)	13 Mar 2008 (T+2)	14 Mar 2008 (T+3)
Total Portfolio Value	\$764,959.04	\$764,959.04	\$764,959.04	\$764,959.04
Borrowing Limit	\$502,126.81	\$502,126.81	\$502,126.81	\$502,126.81
Total Loans Outstanding	\$504,526.92	\$504,526.92	\$504,526.92	\$504,526.92
Available Funds	\$57,599.89	\$57,599.89	\$57,599.89	\$57,599.89
Current Gearing Ratio	65.95%	65.95%	65.95%	65.95%
Maximum Gearing Ratio	73.48%	73.48%	73.48%	73.48%
Unsettled Trades	\$0.00	\$0.00	\$0.00	\$0.00


Please note that sale trades are reflected in the Portfolio Value and Available Funds figures from the time the trade is entered into our system unless you have sold securities where the corresponding purchase has not yet settled. Details will be displayed as at the time you opened or refreshed this page and pricing will be reflected approximately 20 minutes later. For more information, please place the cursor over the information icon.

If you have any queries please refer to your Account Manager on 1300 304 065, 8am - 6pm (AEST) Monday to Friday.

The screens are provided courtesy of St. George Margin Lending. Copyright belongs to St. George Bank Ltd.

PORTFOLIO SUMMARY

Allows you to view a summary of your clients' portfolio, including the names and codes of securities, the market price, units held, market value, gearing ratios and borrowing limits.


Client Name : Anita Sample
Client Ref No: XXX
As At : 01/01/2008

- Account Summary
- Portfolio Summary
- Available Funds
- Total Loans Outstanding
- Loan Transactions
- Security Holder Details
- Security Transactions
- Bank Account Details
- Unsettled Trades
- Pending Orders
- Simulator
- Client Details
- Back to Support Select
- Exit

Portfolio Summary Print

Security Code	Security Name	Market Price \$	Units Held	Market Value \$	Gearing Ratio %	Borrowing Limit \$
AHH	Arana Therapeutics Limited	0.0000	1,000.0000	900.00	60.00	540.00 →
AGK	AGL Energy Limited	10.4300	1,342.0000	13,907.06	75.00	10,497.80 →
AHP	AHP Limited	6.8400	4,000.0000	27,360.00	75.00	20,520.00 →
AIN	Ansell Limited	12.2900	800.0000	9,832.00	70.00	6,882.40 →
APA	APA Group	2.7300	8,588.0000	23,445.24	65.00	15,239.41 →
BHP	BHP Billiton Limited	36.2300	1,000.0000	36,230.00	75.00	27,172.50 →
BHP	BHP Billiton Limited	36.2300	3,000.0000	108,690.00	75.00	81,517.50 →
CBA	Commonwealth Bank of Australia	36.2700	420.0000	16,073.40	75.00	12,055.05 →
CEY	Centennial Coal Company Limited	4.0000	2,025.0000	8,100.00	65.00	5,265.00 →
CMU	Consolidated Media Holdings Limited	3.7500	579.0000	2,171.25	60.00	1,302.75 →
CPJ	Computershare Limited	8.0800	2,000.0000	16,160.00	70.00	11,312.00 →
CWN	Crown Limited	10.3100	579.0000	5,989.49	75.00	4,477.12 →
FXJ	Fairfax Media Limited	3.7700	4,895.0000	18,114.85	75.00	13,586.14 →
JST	Just Group Limited	3.6400	2,000.0000	7,280.00	60.00	4,368.00 →
NAB	National Australia Bank Limited	26.2100	3,000.0000	78,630.00	75.00	58,972.50 →
ORG	Origin Energy Limited	9.2500	1,950.0000	18,037.50	75.00	13,528.13 →
PPT	Perpetual Trustees Australia Limited	48.9000	1,000.0000	48,900.00	70.00	34,230.00 →
RHC	Ramsay Health Care Limited	10.4500	1,015.0000	10,606.75	70.00	7,424.73 →
RIO	Rio Tinto Limited	121.4500	1,000.0000	121,450.00	75.00	91,087.50 →
RMD	Resmed Inc	4.2900	1,000.0000	4,290.00	75.00	3,217.50 →

Print Next

Unsettled equity purchases are not reflected. However, unsettled equity sales and managed fund redemptions are reflected.

The abbreviation 'BR' which appears next to the Security Code stands for 'Broker Receivable' and represents the sale proceeds from an unsettled sale trade. It is already included in your available funds and is the amount you will receive when the trade settles.

TOTAL LOANS OUTSTANDING

Allows you to keep track of what your clients owe and how much interest they are paying.

st. george
Margin Lending

Client Name / Aristo Sample Client Ref No: XXX As At: 01/01/2008

Total Loans Outstanding ⓘ

Variable Loan Balance \$	Interest Rate % p.a.	Interest Accrued \$	
0.00	9.40	0.00	→

Fixed Loan Balance \$	Interest Rate % p.a.	Start Date	Maturity Date	Interest Amount \$
504,526.92	7.95	29/06/2007	27/06/2008	40,000.00

Total: \$504,526.92

- Account Summary
- Portfolio Summary
- Available Funds
- Total Loans Outstanding
- Loan Transactions
- Security Holder Details
- Security Transactions
- Bank Account Details
- Unsettled Trades
- Pending Orders
- Simulator
- Client Details
- Back to Support Select
- Exit

- St George Margin Lending
- Associate Securities List
- View & Print Forms
- Language Centre
- Contact Us

SIMULATOR

An online simulator is an easy way to see how trading may potentially impact your clients' margin lending facility before making an actual trade. Just enter the stock/s and click the simulate button to see the possible outcome.

Client Name : Anita SompLe Client Ref No: XXX As At : 01/01/2008

Simulator

Security Code	No. of Units	Price	Gearing Ratio	Brokerage	Trade Type	Total	Delete
BOB	1,000	21.97000	75.00	0.00	Buy	21,970.00	X
					Buy		X
					Buy		X
					Buy		X
					Buy		X

	Estimated Position Before Simulation	Estimated Position After Simulation
Total Portfolio Value	\$704,959.04	\$786,929.04
Borrowing Limit	\$562,126.81	\$578,804.31
Variable Loan Balance	\$0.00	\$21,970.00
Fixed Loan Balance	\$504,526.92	\$504,526.92
Total Loans Outstanding	\$504,526.92	\$526,496.92
Available Funds	\$67,589.89	\$62,107.39
Current Gearing Ratio	65.95%	65.91%
Maximum Gearing Ratio	73.48%	73.63%

Please note that this simulator should be used as a guide only to show how trades may impact your account and will not execute any transactions on your account.

The "Estimated Position Before Simulation" is based on the information in our systems at the time you last opened or refreshed the page. The figures include any pending buy orders in our systems.

If you have any queries, please contact your Account Manager on 1300 304 065, 8am - 6pm (AEST) Monday to Friday.

EASY GUIDE

An easy guide to margin lending products.

COMPANY	EARLY REPAY FEE	TRANSACTION FEE	OTHER BROKER	OTHER FEES
St.George Bank	\$500 (within 2 mths)	X	Broker of choice	X
BT Financial Group	X	X	—	X
BT Financial Group (online)	X	Up to \$5 ¹	—	X
Colonial Margin Lending	May apply	X	Broker of choice	X
Goldman Sachs JB Were	On fixed rate loans	X	\$20 fee	X
Leveraged Equities	\$200 (within 4 mths)	X	—	X
Macquarie Bank	X	Details on request	Broker of choice	Bank fees
Smith Barney Citigroup	\$500 (within 4 mths)	X	—	X

Source: Infochoice

Note

1 \$5 if loan balance below \$20,000; five free per month for loan balances between \$20,000 and \$250,000; free above \$250,000.

ONLINE BROKER	INSTALMENT GEARING	OPTIONS TRADING	INTEREST ON CREDIT FUNDS	PORTFOLIO ONLINE
directshares.com.au	✓	✓	✓	✓
Westpac Broking & E*Trade	✓	✓	✓	✓
Westpac Broking & E*Trade	✓	✓	✓	✓
www.commsec.com.au	✓	✓	✓	✓
All brokers	✗	✓	✓	✓
✗	✓	✓	✓	✓
DirecTrade	✓	✓	✓	✓
Any online broker	✓	✓	✓	✓

GLOSSARY

Approved securities	All margin lenders publish a list of shares and funds against which they are prepared to lend. A maximum loan to valuation ratio (LVR) is assigned to each security, based on its level of volatility. In recent years equity derivatives, such as options, have been included on approved lists.
Buffer	To accommodate small fluctuations in share and unit prices margin lenders will allow the loan to valuation ratio to exceed the limit by a certain amount before making a margin call. This is called the buffer and is five or 10 per cent above the maximum LVR, depending on individual lenders.
Equity access loan	A loan that allows people with equity in their homes to use that equity to borrow for investment. Investors can nominate a portion of the credit limit in their home loan (the available equity) as security for a margin loan. The maintenance of separate home loan and margin loan accounts helps keep the borrower's tax position simple.
Franked dividends	Australia's dividend imputation system allows companies to attach franking credits to dividends in proportion to the amount of company tax already paid on the earnings. A fully franked dividend means that the dividend is paid out of earnings on which the full 30 per cent company tax rate has been paid. Investors can claim a credit for the company tax paid before paying income tax on the dividend income.
Instalment gearing	A loan that can be drawn down in regular instalments, usually monthly, and used to accompany a savings plan.
Loan to valuation ratio (LVR)	Also called 'loan to value ratio'. This is the amount you can borrow as a percentage of the value of the security. For example, a loan of \$50,000 secured by a portfolio valued at \$50,000 would be 50 per cent LVR.
Margin call	A margin call occurs when the loan to valuation ratio exceeds the borrowing limit and the buffer. When markets fall and asset values go down the LVR will go up. Once a margin call is made the investor must take action to restore the account to its appropriate LVR.
Negative gearing	The income produced by the investment is less than the interest on the borrowing used to purchase the investment. The claim for a tax deduction on the interest cost results in a net tax benefit.
Pre-payment	Lenders allow investors to pay their interest a year in advance. This can be useful for tax management because the tax rules allow an interest payment made in June for the coming financial year to be claimed as a deduction against current financial year income.
Protected loan	Lenders guarantee 100 per cent protection of the secured assets. There is an interest rate premium for this security.
Security	The value of the cash or investments the borrower provides the lender as security for the loan.



Big on
service.



st.george

Margin Lending

Good with people. Good with money.



At St.George Margin Lending we pride ourselves on our high levels of service and expertise. They've helped us become one of Australia's leading margin lending providers. For the service you and your clients deserve, call **1300 304 065** or visit stgeorgemarginlending.com.au



Financial Standard

a Rainmaker Information company



Margin Lending

Good with people. Good with money.