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Chris Andrews
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La Trobe Financial Pooled Mortgages Option

Australian investors don't like volatility. They don't like uncertain returns but they do like investments that generate income and preserve capital using asset classes and processes they understand, writes Alex Dunnin.

In a time of heightened uncertainty when investors are being jostled and battered by world equity markets and concerns of deflation, an investment able to deliver reliable income and preserve capital is likely to tick many of the boxes required by retirees or those thinking ahead for their retirement.

If such an investment is easy to understand as well, it is likely to gain a lot more traction.

And if all this can be delivered by investing into an asset class that delivers income immune from the vagaries of destabilised world credit markets because it is underpinned by something Australian investors know and understand, such as property, and especially residential property, then even better.

Such an investment is the La Trobe Financial Pooled Mortgages Option (PMO).

"Investors are after an investment that is free of intra-day capital market revaluations and free from market volatility," said Chris Andrews⁰¹, head of funds management at La Trobe Financial.

The PMO achieves this because it is designed to take advantage of the outstanding risk and return characteristics of the Australian property debt market, and particularly residential property.

"It also offers an investment that pays monthly income at a premium to cash or term deposits," said Andrews.

Philosophy

La Trobe Financial has been investing into property debt since 1952 when the company's founder, Ray O'Neill, a returned serviceman, realised that investments didn't need to be complicated to be reliable and successful.

His belief in the reliability of property debt and conviction that it could be used as the basis of a long term investment was the hallmark around which the company has operated ever since.

Andrews said this is core to the company's philosophy: that investing should always be simple and transparent.

In 2002 the company started the PMO to give retail investors access to the asset class. After six decades of combined experience in mortgage origination and credit assessment, they have an edge in selecting mortgages.

It also gave La Trobe Financial the ability to better screen which borrowers should be included in the portfolio.

"Mortgages put into the fund are only of the highest quality," he said.

These selection procedures include full independent valuations of each security property and limiting maximum loan-to-valuation (LVR) ratios to 75% for residential properties, 70% for commercial properties and as low as 55% for rural properties.

Exposures to the security types are also tightly controlled. Construction and development loans, for example, account for just 5% of the capital pool – a striking contrast to many competitor funds in the sector.

This approach results in the average LVR of the PMO portfolio being only 60%. And the tilt towards quality property debt helps explain why the PMO has not delivered a negative return since inception.

Its loss history over the past seven years is an incredibly low 0.16% of the fund's capital base, all of which have been comfortably covered by the PMO's Interest Income Reserve. "No investor in the PMO has ever experienced a cent of capital loss," explained Andrews.

Reliable performance

Andrews said La Trobe Financial focuses on residential mortgages because, in good times and bad, they pay income to investors, even in times of economic stress.

While the PMO focuses on residential mortgages, it also invests in other sectors such as commercial, light industrial and rural. But residential comprises almost 60% of the portfolio, with the weightings to each sector monitored and regularly reviewed.

Put another way, the PMO is highly diversified as a conservatively structured fund because the residential weighting is complemented by a diverse spread of exposures to other property sectors.

In today's investment environment, this design has given the PMO a performance reliability that is attracting investors' attention, said Andrews.

"Many investors are coming to us now because they can't get appropriate returns from cash or term deposits," he said.

This appeal explains why the fund has doubled in size in the past three years, a growth path assisted by positive ratings from Lonsec and Zenith that rate it 'recommended'. S&P and SQM Research both rate it four stars.

A question of balance

The reliable and robust structure of the PMO portfolio makes it especially suitable for retirees or people about to retire, said Andrews.



The quote

La Trobe Financial has been investing into property debt since 1952 when the company's founder, Ray O'Neill, a returned serviceman, realised that investments didn't need to be complicated to be reliable and successful.

"But every investor has part of their portfolio that should be devoted to capital stable income producing assets," he said.

Australian investors are heavily exposed to risk assets such as Australian equities and the PMO allows them to balance against this, added Andrews.

This enables the PMO to efficiently complement other aspects of a retiree's portfolio because it is designed to meet their investment appetite for income and capital preservation, while providing critical asset class diversification.

Crucially, this is achieved without adding extra volatility. The PMO has a low correlation to other asset classes so it acts as a portfolio stabiliser.

Track record

The product design is underpinned by debt against quality properties, which helped deliver the fund's consistent and high performance.

"Over 1, 3, 5 and 7 years, the PMO has achieved average monthly income returns of 7.5% to 7.8% per annum, which can be re-invested," said Andrews.

In addition to these returns, the fund is responsive to inflation, which is valuable for investors when addressing global inflationary pressures in the medium term.

Ultimately, Andrews said diversification is a major reason why the PMO has achieved stable returns. "It's the most diversified fund in the sector and has outperformed all the major asset classes."

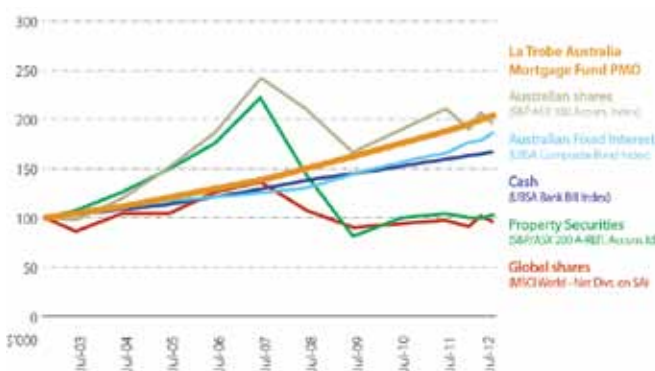
Headquartered in Melbourne, La Trobe Financial manages \$1.2 billion in assets, of which more than \$460 million is invested in this fund. **FS**

Figure 1. PMO performance vs other asset classes



Source: La Trobe Financial

Figure 2. PMO accumulation comparison since inception



Source: La Trobe Financial