



Margin lending

Margin lending is the use of borrowed money to increase the amount you can invest in shares and managed funds. The shares or managed funds are held as security for your margin lending facility.

How does it work?

Investors start with their own money and take out a margin lending facility to increase the amount of funds they are investing in shares and managed funds. This means the investor can now effectively multiply their opportunities for wealth creation.

It allows the investor to strengthen their personal capital base, boost their share portfolio and actively invest in a wider range of opportunities.

Margin lending is best suited to those who:

- Are comfortable with a higher level of risk
- Have a high level of disposable income and consistent sustainable cash flow; and
- Have a long-term investment time frame.

What are the advantages of margin lending?

Flexibility

Margin lending provides you with the flexibility to adapt to the changes in the investment environment or your personal circumstances. This includes:

- The ability to decide on the level of gearing you are comfortable with, provided it is within your limits, and

- The option to sell a portion of the portfolio at any time, provided you maintain adequate security to cover the amount owing under the portfolio.

Diversification

Margin lending provides you with more funds to invest across a wider range of securities. This means you can invest in a wider range of asset classes including international assets and managed funds (subject to your risk profile). This provides greater diversification of assets and greater control of how your investment risk is spread.

Liquidity

Gearing simply means borrowing money to invest. Gearing into shares and managed funds generally does not involve the longer-term commitment you make when investing in property. The inherent liquidity of the investments enables the investor to move in and out of the market depending on the economic environment or their personal circumstances.

Faster wealth accumulation

With more money working for you, there is the potential to build wealth faster and to take advantage of opportunities as they arise. Margin lending also allows you to make regular contributions to build up your investment.

Taxation advantages

Using a margin lending facility to gear your investments may generally have the following tax consequences:

- The interest component you pay to service the lending and related borrowing costs in any year may be tax deductible.
- If you claim the interest expense as a tax deduction, the deduction may be applied against assessable income earned throughout the year.
- As an individual investor, you should only be liable for Capital Gains Tax on half the realised nominal gain arising upon disposal of any part of your share or managed fund portfolio where they have been owned for 12 months or more.



- Dividends paid on Australian shares in your investment portfolio may yield imputation credits. Any dividends you receive may already have had an amount of tax paid (fully or partly franked), which may in certain circumstances allow you to further reduce your tax liability.

Your tax position will depend on your personal circumstances and we recommend you get advice from a taxation specialist.

What are the risks of using margin lending?

As with any investment, margin lending involves some degree of risk. Some of these risks are:

- If the market declines, so will the value of your portfolio. If this happens, you will need to ensure the amount owing does not exceed the security value of your portfolio. If the Loan to Valuation Ratio (LVR) on your loan exceeds that permitted by the lender, a margin call will occur.
- If you need to sell shares or managed funds to bring LVR back into order, this may result in significant losses as you may be selling investments at a lower value.
- While gearing can increase your opportunity for gains in a rising market, it will always magnify your losses when it declines.
- Interest costs on the funds you borrow can exceed the gains you receive from your investment. Therefore, you cannot rely solely on dividends or distributions to fund your interest costs.

Be aware of your risk profile and the type of investor you are, and understand your financial strengths and weaknesses. It will enable you to more appropriately weather the market fluctuations and reduce the risk of a margin call.

What do I do when a margin call occurs?

A margin call can occur when the LVR exceeds the maximum limit set by the lender. When this occurs, steps must be taken to bring the loan into order (i.e. to restore the account so it is no worse than the agreed LVR). These steps include:

- Lodging additional approved shares or managed funds into your portfolio;

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- Reducing your outstanding liability by either paying down your variable rate loan or having adequate cash reserves at call to offset the balance of your loan; or

Selling some of your shares or managed funds so that the proceeds can be used to reduce the balance of your loan.

You should also have a strategy to restore the security value of your portfolio.

This may consist of one or a combination of the following:

- Having access to extra funds.
- Having access to extra shares, managed funds or approved securities.
- Creating a priority list of the part/s of your portfolio you are willing to sell.

Are there ways to reduce the risk of a margin call?

Yes, there are ways you are able to reduce the risk of a margin call occurring. These include:

- Not borrowing to the full extent allowed for any approved investment that you have in your portfolio. By reducing your gearing by as little as 10% you can add protective measures to your portfolio.
- Diversifying your portfolio across a number of industry sectors and shares. With more to invest, you can achieve a wider spread of investments, which may also result in higher returns in the long term.
- Making regular interest payments to help keep your portfolio and gearing level in balance.
- Monitoring your portfolio on a regular basis.
- If possible, deposit/transfer dividends and distributions to your portfolio.

Need further information?

If you have any queries regarding the material covered in this fact sheet, or require further information or the address of your local branch, please contact FuturePlus on 1300 883 788 between 9am and 5pm on any business day.