

“ We are fortunate in having a chief executive who has a voracious and insatiable appetite for information and knowledge and that has helped us limit our universe of unknown unknowns. ”

Of NZX boss Mark Weldon by NZX chairman Andrew Harnos.



Alchemy alert: Liberty Financial



Rob Stock
Money Editor

FINANCIAL ALCHEMY is the process of turning deadweight assets into solid gold through the application of an intercompany guarantee, an insurance policy, or some other bit of wizardry.

However, too often it results in producing nothing more than fool's gold.

In New Zealand we have had plenty of great examples of financial alchemy, including:

- ▶ Blue Chip investors mortgage payments were guaranteed to be met if anything went wrong. It did. They weren't.

- ▶ Investors in New Zealand finance company OPI Pacific were comforted by the guarantee provided by its Australian parent to pay for the shortfall in any loans transferred to the Kiwi company. The loans were of awful quality and the parent collapsed owing far more than it could pay.

▶ Bridgecorp, Compass and Capital + Merchant all “insured” loans they made on property developments with Lloyds of London. This was a major selling point to investors. But now that insurance may never be collected.

A conservative estimate of the costs in the above cases would put losses to Kiwi investors at around a billion dollars.

Why am I writing this now? Because without fanfare a new finance company has been set up and it is living proof that financial alchemy is alive and well.

The finance company is called Liberty Financial and is the result of the partial purchase of a company once called Business Finance by Australian Liberty Financial Pty (until late last year called Liberty Financial), a company boasting a couple of billions worth of loans in Australian dollars.

The purchase was made by injecting \$22.1m face value of junk bonds owned by another Liberty business called Secure Funding into Business Finance.

These “mortgage-backed notes”, potential debenture investors in Liberty Finance are told, will provide a capital base and income stream for the company as a foundation for growth.

However, what these bonds are is the “equity” slice of a collateralised debt obligation (CDO). Credit-rated bonds secured against loans in a bond warehouse have been sold to institutions but the unrated bonds injected into Business Finance take the first loss on any of the loans in the trust.

Buying a finance company using illiquid assets that are hanging around on another balance sheet is a business masterstroke. The financial alchemy comes in by Liberty in Australia guaranteeing to make any interest and capital payments to secured depositors, if the Kiwi finance company cannot.

Even so, the guarantee earned Liberty Financial only a lowly BB credit rating, putting it firmly into the area of “junk” bonds which are suitable for only a small portion of an investor's portfolio, and a higher-risk investment.

Liberty in Australia is a privately owned company and its full financial reports are not publicly available. A press release in April claimed it had equity of \$A232m and assets of some \$A2.3 billion. I've no reason to doubt that, or that although Liberty Financial is small, the guarantee is manageable. But the credit ratings agency Standard & Poor's have

not been unremittingly positive about the strength of the guarantee, giving Liberty Financial a BB credit rating.

The history of guarantees past dictates caution and provides investors with this wisdom: invest in a finance company based on the quality of its assets, not immaterial promises.

They also need to get paid adequately for their risk.

Actually, there's a form of madness going on in the BB section of the deposit-taking market (see below), where deposits at “junk” rated finance institutions are paying rates of between 4% and 8.5%.

Liberty Financial does not appear to score too badly on that front.

DOUBLE JEOPARDY

Institution	Rate for two-year 12-month deposit
Avanti Finance	8.5%
Liberty Financial	7.7%
Fisher & Paykel Finance existing investors	7.5%
Fisher & Paykel Finance	7%
PGG Wrightson	6.95%
First CU	5%
CU Baywide	5%
Police CU	4.8%
CU North	4.7%
CU South	4%

Irish matchmaker avoids currency exchange fees

By **ROB STOCK**

CUTTING THE cost of international money transfers involves cutting the banks out altogether, says a Dublin-based company aiming at winning customers in New Zealand.

CurrencyFair has put up a flag here in the hope of building customers for its “internet-mediated peer-to-peer” currency exchange.

For those wanting an English translation of that mouthful of jargon, CurrencyFair runs a

Trade Me-like market bringing people together to exchange currencies.

Although that may sound like a forum for currency speculation, it is not, says Sean Barrett from CurrencyFair, which is setting up an Australian office next week.

Participants are real people, who have sums of cash they want to get from one bank account, say in Australia, to another in a different country.

They deposit the money they want transferred in a CurrencyFair trust account in whichever country

they want to send the money from, and through the market seek an exchange with someone in the destination country.

The beauty of the system is there are no bank commissions to pay, and as no money has to be sent from one country to another, there are no transfer fees.

People may not be able to exchange all their money in one go, said Barrett, but CurrencyFair acts as a marketmaker if there aren't enough people using the market at any point in time.

There are around 5000 active

users worldwide, a tiny portion of the cross-border transfer market, but Barrett is convinced the savings will see that rise rapidly.

Generally, Barrett said, using a bank to transfer money involves paying a transfer fee of somewhere in the region of \$45, and a 3% margin on top of the interbank exchange rate.

Deals at CurrencyFair have been taking place at below the interbank rate, Barrett said. CurrencyFair's charges are \$5 per “transfer” and 0.3 to 0.55% of the amount exchanged.

FINANCIAL PRODUCT

Product: The Peace of Mind Plan
Offerer: Auckland City Brokers, among others

Offer dates: Available now
How it works: People's estate plans are too often a total shambles. Badly drawn and interlinking, wills and trusts can result in estate assets going to people the deceased didn't nominate. A handful of advisers, such as Auckland City Brokers (ACB), have now entered this area using a system run out of Australia called the Peace of Mind Plan. The idea of the plan – which is executed by lawyers not the adviser – is to create what ACB's Richard Hurley calls an “efficient” legacy. Australian research shows that around 95% of estates do not achieve exactly what the deceased intended. The Peace of Mind Plan is a structured process which a person goes through to identify assets, liabilities, family circumstances and aims. Once a plan is in place, and has been vetted in Australia, local lawyers provide the legal documents.

What we like: Revisiting estate-planning does need to happen frequently. There is no reason financial planners cannot help. Some of the reasons people's estates meet only some of their objectives are summed up by the Peace of Mind Plan, such as “the Anna Nicole syndrome” (new younger spouse gets the money meant for the kids), “Step sibling seepage” (stepchildren end up with too much of the money), and “delinquent documents” (out-of-date or lost documents end up undermining intentions). All of these are, perhaps pointlessly, trademarked phrases, and each encapsulates a nugget of wisdom.

What we don't like: The attraction of a new business stream for advisers at a time when investment income is down is obvious. That's fine so long as there is a need and the system is sold responsibly. Hurley says ACB aims at top-end clients with income of \$500,000 or more, or investment wealth of \$750,000. For many people a simple will may be sufficient. Could cost between \$3000 and \$8000.

Conclusion: The decision to use it or not and the value it offers, must be judged on a case by case basis.

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