

# MARGIN LENDING STAR RATINGS

## IN THIS REPORT:

- We look at proposed changes to margin lending Regulations to further protect investors.
- What happens when you get a margin call and who is responsible for acting on a that call.
- The decline of margin calls in line with a strengthening market.
- We track interest rates over the past year and compare three key rate indicators.
- We look at 11 margin lenders to find those offering outstanding value.

## UNDERSTANDING THE MARGIN JARGON

The high profile Storm Financial case has highlighted the need for the pending regulatory changes to margin lending. In a scenario not unlike the workplace where failures are only discovered when key staff go on holidays, the global financial crisis shone the spotlight directly on to gaping holes in the Storm Financial *modus operandi*. Unfortunately, as a result, many investors found themselves facing the stark reality of losing homes and life savings.

It seems from the various reports and articles written about Storm Financial that a proportion of investors were unaware of how a margin loan operates, how geared their assets were, appropriateness of the advice received and exactly what would occur should markets go south.

Prior to the collapse of Storm Financial, the Australian Government had started to seek and draft reforms of the Consumer Credit Code in order to further protect investors. Up until this point margin loans had not been directly regulated and weren't subject to state-based consumer credit laws.

The regulatory changes proposed will assist in ensuring borrowers are adequately assessed and advised prior to proceeding with a margin loan.

### Some of the proposed regulatory changes include:

1. Persons providing financial services or products (i.e. lenders or financial advisers) are required to hold an Australian Financial Services Licence



2. Lenders are required to ensure that the prospective margin loan holder has sufficient means to satisfy their ongoing financial obligations to the margin loan as well as their ability to meet a 'margin call' without causing financial hardship
3. The use of 'double gearing' (using for instance residential property to obtain the equity to contribute to the margin loan), will be incorporated into the assessment to decide whether the customer is unsuitable to obtain a margin loan
4. Clearly define the manner in which margin calls will be handled.

Although the regulatory changes will go far in potentially reducing the amount of defaults, borrowers will still need to take an active role in managing their margin loan. This applies from the application stage through to the day-to-day management.

The new national Consumer Credit Code will commence on 1 July 2010.

## WHAT HAPPENS WHEN YOU GET THAT CALL?

**M**argin calls are those dreaded calls letting you know that your portfolio has gone over the acceptable limit and you have (in most cases), 24 hours to get it back below the limit.

For most borrowers, the 24 hours after the call can be very stressful, as they have a number of issues to deal with straight away. Do they have sufficient savings? Do they have access to more shares? Are they able to sell down their portfolio in time to meet the call?

It is at this point the ultimate question is asked, why didn't my lender alert me to the high level of gearing before it resulted in a margin call?

Isn't it their responsibility? The short answer is no. The borrower is required to take ownership of the portfolio and manage the day-to-day monitoring of their debt levels. Should their portfolio start to head towards a high level of gearing above what is deemed acceptable, appropriate action is needed to bring it back down to a "safe" level.

Most institutions apply a 5% buffer which triggers before a margin is hit. Most borrowers will be alerted when they reach the "buffer zone". It is at this point, if you haven't already started, you need to make provisions to reduce the level and get it out of the 'danger zone'. Waiting on the hope that the stock or fund will rebound, although optimistic, will potentially put you on track for a margin call. Instead of taking advantage of the extra time provided by the lender you would now only have 24 hours to meet your obligations.

Should you not adhere to the margin call, you do run the risk of the lender either selling a portion or the whole of your portfolio. That is why it is important to move swiftly when you either see your debt level increasing or a margin call is received.

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**Waiting on the hope that the stock or fund will rebound, although optimistic, will potentially put you on track for a margin call.**

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## CALL MY FINANCIAL ADVISOR FIRST

**U**tilising a financial adviser can help in the day-to-day managing of your portfolio. Even though, as previously said, it is legally the borrower's responsibility to manage their portfolio, a financial advisor can be nominated to receive all alerts from your margin loan lender and have access to reporting on your portfolio.



However, this is where margin loan customers can be caught out if lenders alert the adviser to the margin call situation but the call is not passed on to the customer. This results in the customer not satisfying the margin call requirements.

If you do decide to nominate your adviser to receive margin calls, ensure you take a strong interest in the management of the portfolio. After all, it is your money you should

be worrying about, not your advisor's ego.

## KEEPING CALLS IN CHECK

**T**here are numerous ways in which you can reduce the chances of receiving a margin call:

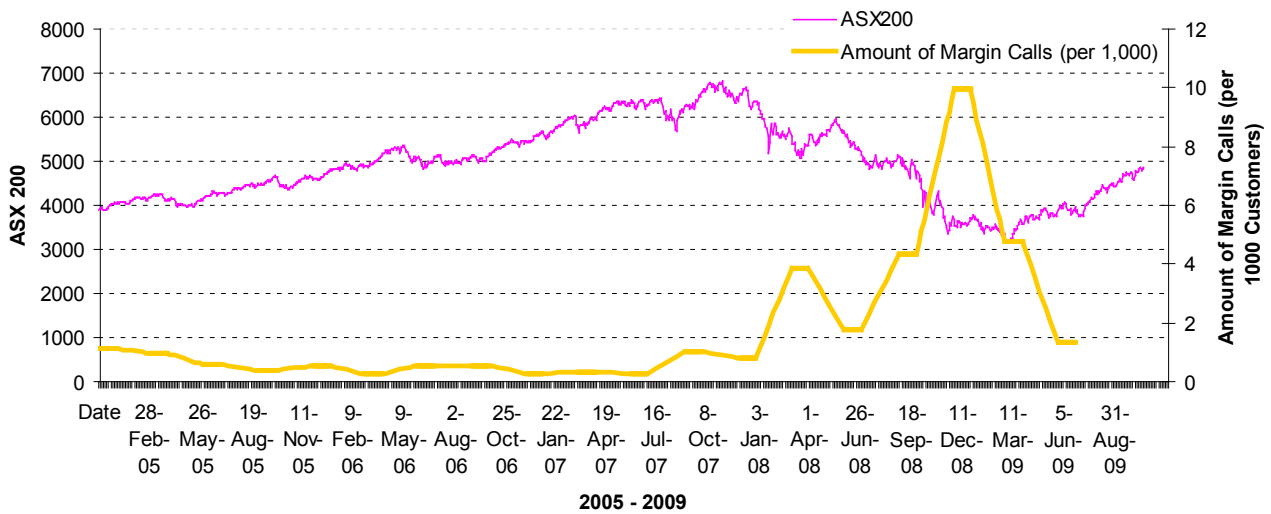
1. **Diversify your portfolio** – spread your investments across several stocks/funds. That way should one investment go down, the other investments may have sufficient equity to stave off a margin call.
2. **Keep track of your portfolio** – check your balances regularly and if you notice a reduction in your balance, explore avenues to reduce your level of gearing i.e. selling down, investing further capital etc.
3. **Obtain Advice** – Financial Advisors can provide a wealth of knowledge and assist in tailoring an investment strategy to your financial goals and openness to risk.

## MARGIN CALLS WIND BACK

Win September last year, margin calls reached their highest level since reporting started in 2000 by the Reserve Bank.

It can be said that not many people saw the magnitude of the plummet in share prices coming and were blinded by the effect the drop in share price had on their gearing levels.

## Margin Calls



Source: RBA & CANSTAR CANNEX October 2009

The average gearing level at June 2008 was 38% but by December the average gearing level had increased by 12% to just over 50%. Through this period we also saw the ASX200 share price drop 35%, which would have been a factor in the average gearing level rising.

It is at this point we saw nearly 1 in 100 margin lending customers (December 2008) receive a margin call. As at June 2009, gearing levels have returned to just under 40%. This can be attributed to investors being more risk adverse in light of the current climate and also the resurgence of the share market.

The more benign market and maybe a reduction in the appetite for risk have also resulted in margin calls decreasing.

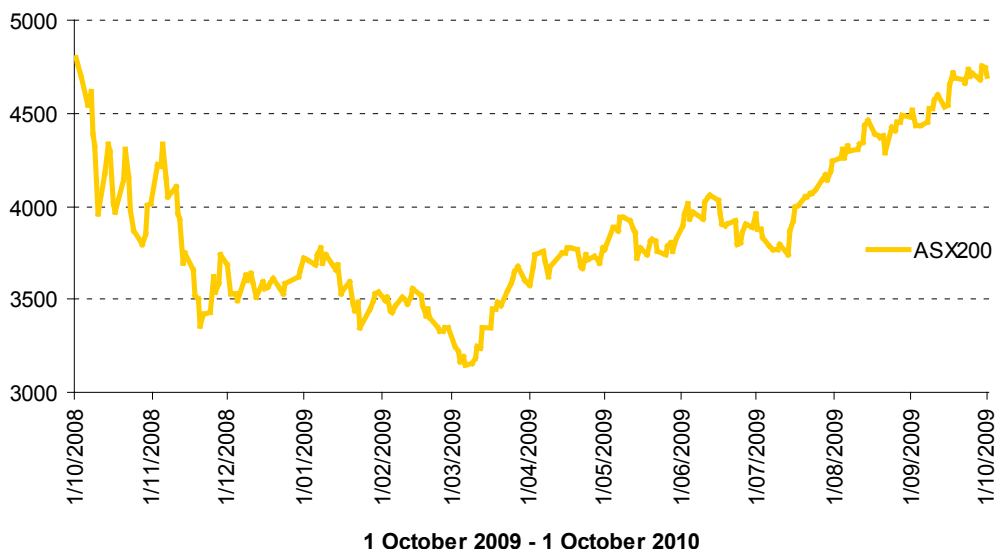
## THE GLOOM LIFTS

The past twelve months has been tumultuous for investing in the share market, to say the least.

The ASX200 had its lowest closing share price on 6<sup>th</sup> March 2009 at 3145.50, but since then, although fluctuating, the ASX200 has been on the rebound.



## ASX200



If we were to look at 1 October 2008 on 1 October 2009

in the graph above, the ASX200 has only dropped by



1.95%. Considering what has occurred both domestically and internationally over the past twelve months, this is good news for investors, especially for long term investors and for almost all Australians who have their retirement funds sitting in a super fund.

There is still a considerable way to go until we see the heights of November 2007 where we saw ASX200 hit 6828.7, but the current upward trend does reflect the rise in consumer sentiment.

## REFLECTING ON RATES

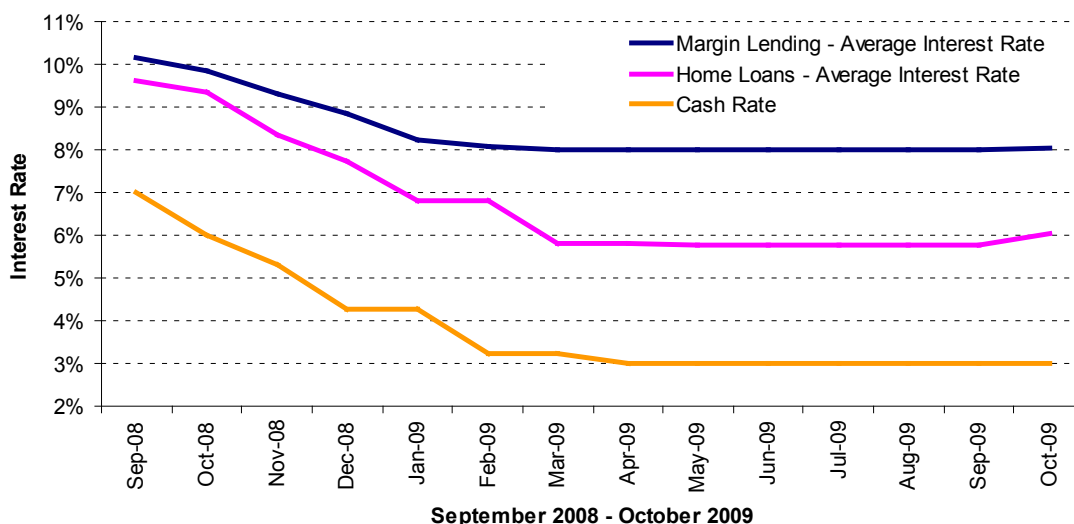
The main focus of interest rates over the past 12 months has been on the home loan variable rate, which is understandable but what effect did the

spiraling cash rate have on margin loans? Over the past twelve months we have seen interest rates on margin loans reduce by an average of 2.14%.

The reduction wasn't as large as those seen in home loan interest rates which recorded an average drop of 3.85%. This is likely due to the significant element of risk associated with margin loans in comparison to home loans where property is used as security.

The stock market which always has an element of volatility will naturally be seen as a higher risk component by lenders who will price interest rates accordingly. This is very similar to business loans, credit cards and personal loans.

Interest Rate Movements



Source: CANSTAR CANNEX October 2009

## YOUR GUIDE TO 5-STAR PRODUCTS

When researching and rating margin loan providers CANSTAR CANNEX focuses on what matters most to investors by assessing products according to two profiles – Share Investor and Managed Fund Investor.

Each of these profiles considers certain features to be more important than others. For example, we have assigned a heavier weighting to advisor services and instalment gearing facilities for the Managed Fund Investor compared with the Share Investor. For the Share Investor profile, direct trading services assume greater importance.

This time around, out of 11 lenders Colonial and Commonwealth Securities proved once again that their products offer outstanding value across both star ratings profiles. St George Margin Lending maintained their five-star rating for the Share Investor Profile, while ANZ's Margin Loan Accounts was promoted to five-star status in the same profile, thanks largely to a competitive re-pricing of this product.

The results of our comparative research give you a clearer view of products that may suit your purpose, whether you are a Share Investor or a Managed Fund Investor.

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# Margin Lending Star Ratings: Share Investor Profile

## October 2009 Summary Report

Company	Interest Rate \$50k (%)		Info Line	Website
	Variable	1-Year Fixed interest prepaid		
<b>★★★★★ "Outstanding Value"</b>				
ANZ	8.24	7.74	1800 639 330	<a href="http://www.anz.com.au">www.anz.com.au</a>
Colonial Margin lending	7.99	8.25	1800 252 351	<a href="http://www.colonialgearedinvestments.com.au">www.colonialgearedinvestments.com.au</a>
Commonwealth Securities	8.1	8.25	13 17 09	<a href="http://www.commsec.com.au">www.commsec.com.au</a>
St George Margin Lending	7.8	7.7	1300-304-065	<a href="http://www.stgeorge.com.au">www.stgeorge.com.au</a>
<b>★★★★</b>				
Goldman Sachs JB Were ML	8.1	8.15	1800-780-809	<a href="http://www.jbwere.com.au">www.jbwere.com.au</a>
Leveraged Equities	8.1	8.1	1300-307-807	<a href="http://www.leveraged.com.au">www.leveraged.com.au</a>
Suncorp	7.99	7.05	1800115211	<a href="http://www.suncorpmetway.com.au">www.suncorpmetway.com.au</a>
<b>★★★</b>				
Bank of Queensland	8.1	N/A	1300 78 37 09	<a href="http://www.boq.com.au">www.boq.com.au</a>
BT Margin Lending	7.79	8.25	1800 816 222	<a href="http://www.btfunds.com.au">www.btfunds.com.au</a>
Citigroup Margin Lending	7.65	7.65	1800 062 794	<a href="http://www.ssmb.com.au">www.ssmb.com.au</a>
nab	7.55	7.6	1300-135-145	<a href="http://www.national.com.au">www.national.com.au</a>



# Margin Lending Star Ratings: Managed Fund Investor Profile

## October 2009 Summary Report

Company	Interest Rate \$50k (%)		Info Line	Website
	Variable	1-Year Fixed interest prepaid		
<b>★★★★★ "Outstanding Value"</b>				
Colonial Margin lending	7.99	8.25	1800 252 351	<a href="http://www.colonialgearedinvestments.com.au">www.colonialgearedinvestments.com.au</a>
Commonwealth Securities	8.1	8.25	13 17 09	<a href="http://www.commsec.com.au">www.commsec.com.au</a>
<b>★★★★★</b>				
Leveraged Equities	8.1	8.1	1300-307-807	<a href="http://www.leveraged.com.au">www.leveraged.com.au</a>
St George Margin Lending	7.8	7.7	1300-304-065	<a href="http://www.stgeorge.com.au">www.stgeorge.com.au</a>
Suncorp	7.99	7.05	1800115211	<a href="http://www.suncorpmetway.com.au">www.suncorpmetway.com.au</a>
<b>★★★</b>				
ANZ	8.24	7.74	1800 639 330	<a href="http://www.anz.com.au">www.anz.com.au</a>
Bank of Queensland	8.1	N/A	1300 78 37 09	<a href="http://www.boq.com.au">www.boq.com.au</a>
BT Margin Lending	7.79	8.25	1800 816 222	<a href="http://www.btfunds.com.au">www.btfunds.com.au</a>
Citigroup Margin Lending	7.65	7.65	1800 062 794	<a href="http://www.ssmb.com.au">www.ssmb.com.au</a>
Goldman Sachs JB Were ML	8.1	8.15	1800-780-809	<a href="http://www.jbwere.com.au">www.jbwere.com.au</a>
nab	7.55	7.6	1300-135-145	<a href="http://www.national.com.au">www.national.com.au</a>



## Margin Lending Star Ratings: Product Features

### October 2009 Summary Report

Company	Min Loan Amount	No of AU Shares/Managed Funds		Buffer Shares/Managed Funds		International Shares	Property Security	Instalment Gearing	Protected Loan	Option Trading Available			
										Long Call	Short Call	Long Put	Short Put
<b>ANZ</b>	20000.00	988	642	5%	5%	X	X	✓	✓	X	✓	✓	X
<b>Bank of Queensland</b>	No min	437	1361	5%	10%	X	X	✓	✓	X	X	X	X
<b>BT Margin Lending</b>	2500.00	370	2288	10%	10%	X	X	✓	✓	X	✓	X	X
<b>Colonial Margin lending</b>	No min	466	2347	10%	10%	✓	✓	✓	✓	✓	✓	✓	✓
<b>CommSec</b>	No min	466	2347	5%	5%	✓	✓	✓	✓	✓	✓	✓	✓
<b>Goldman Sachs JB Were ML</b>	50000.00	2000	1800	7.50%	7.50%	✓	X	✓	✓	✓	✓	✓	X
<b>Leveraged Equities</b>	20000.00	447	2320	10%	10%	X	✓	✓	✓	✓	✓	✓	✓
<b>Morgan Stanley Sm Barney</b>	No min	389	900	5%	10%	X	X	✓	✓	✓	✓	✓	X
<b>nab</b>	No min	381	1057	5%	10%	X	X	✓	✓	✓	✓	X	X
<b>St George Margin Lending</b>	No min	574	1311	10%	10%	X	✓	✓	✓	X	✓	X	X
<b>Suncorp Bank</b>	20000.00	522	1225	5%	10%	X	X	✓	✓	X	X	X	X

# MARGIN LENDING STAR RATINGS

## WHAT IS THE CANSTAR CANNEX *margin lending star ratings*?

CANSTAR CANNEX *margin lending star ratings* is a consumer-friendly benchmark or value index, unique to CANSTAR CANNEX that compares both the Cost and Features across margin lenders. CANSTAR CANNEX star rated lenders represent a short list of quality institutions. This short list narrows the search for consumers to lenders that have been independently assessed and ranked. Five-star lenders are considered to offer outstanding value for money.

CANSTAR CANNEX's rating methodology is transparent and extensive. The methodology compares all types of margin lending products for an array of characteristics such as:

- Interest Rates
- Fees and charges
- Loan to Value Ratio (LVR)
- Features
- No. of shares/funds available

The results are reflected in a consumer-friendly *5-star* concept, with a 5-star product denoting one that offers outstanding value.

## HOW ARE THE 'STARS' CALCULATED?

CANSTAR CANNEX ranks margin lenders based on value-for-money measures and then awards a star rating according to rank. Typically the top 3 lenders will be awarded a 5 star (or outstanding) rating. The number of lenders awarded each of the 3 to 5 star ratings will ultimately depend of the dispersion of final scores.

Scores are awarded to each lender on the basis of rates, fees, services and list of approved securities. The methodology is revised and parameters are updated on a regular basis to make sure that the products are analysed using the most up-to-date information capturing all industry developments. A detailed methodology is provided below.

CANSTAR CANNEX assesses margin lenders from the perspective of two different consumer profiles: the Share Investor, and the Managed Fund Investor. Each profile assumes that the consumer will have a preference over one of these forms of security against the other, but will also seek some content from their secondary security type.

To arrive at the total score CANSTAR CANNEX applies a weight against the Pricing score, Features score and Acceptable Securities List score. This method can be summarised as:

$$\text{TOTAL SCORE} = w_1\text{PRICING} + w_2\text{FEATURES SCORE} + w_3\text{ASL SCORE}$$

## PRICING

CANSTAR CANNEX accounts for both current and historical interest rates in the calculation of the PRICING component of each product's overall score, which comprises of:

1. **Standard 1 Year Fixed Rate in Advance** – rates at June 2008 for \$50,000, \$250,000 and \$500,000 loan amounts;
2. **Historical Performance of Standard Variable Interest Rates** – average of rates over the past 12 months for \$50,000, \$250,000 and \$500,000 loan amounts.

Those products with the lowest cost receive the highest score in the scenario analysis.

## FEATURES

CANSTAR CANNEX allocates points for over 250 Features of a margin lending product. These include flexibility, operating terms and conditions, investor tools and imposed product parameters. The points are totalled for each product and then indexed to determine the product's Feature ranking.

Features have been assessed separately for the two investor profiles (Share Investor and Managed Fund Investor), to take into account the fact that each of these two main categories of investor will have differing priorities when choosing their margin lender.

## ACCEPTABLE SECURITIES LIST

CANSTAR CANNEX currently reviews the Acceptable Securities List (ASL) for only those securities that have either an APIR (Managed Funds) or ASX (Australian shares) code. International shares are not included in the calculation of the ASL score.

The score for ASL is comprised of:

- The number of Listed Shares and Managed Funds available against which to borrow funds
- A product's average LVR for Listed Shares and Managed Funds
- Diversified and undiversified portfolio offerings

Each of the above components are calculated at six points during the six months preceding the star ratings calculations. This provides an ASL score on historical performance and benefits the institutions with a consistent high offering on both the number of stocks/managed funds and the LVR.

A higher number of funds and shares on a menu, along with a high average LVR, will result in a high relative score. Contribution of shares and managed funds to overall ASL scores will be reviewed in relation to their market size for each star rating.

As with Features, the ASL score is assessed differently for the two investor profiles, with scoring weighted towards the more relevant of the two main security types in accordance with the profile.

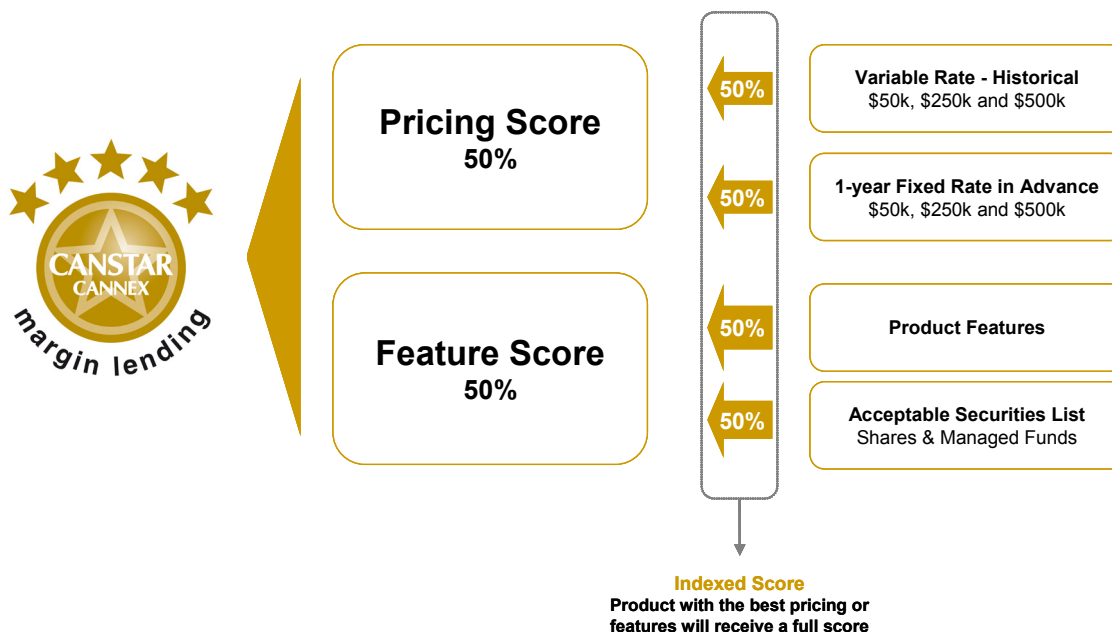
## WEIGHTINGS

The Pricing, Features and Acceptable Securities List scores are weighted for each product to reflect the relative importance of each component in the determination of value for money. Current weights are:

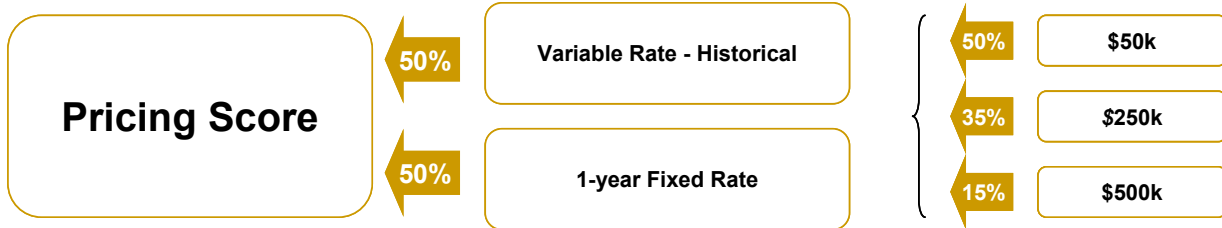
<b>Pricing</b>	<b>50%</b>
<b>Features</b>	<b>25%</b>
<b>Acceptable Securities List</b>	<b>25%</b>

## TOTAL SCORE

The Pricing plus Features plus ASL point scores are indexed and then totalled to provide the Total Index Points. Stars are awarded according to the Total Index Points.



### Pricing Score:

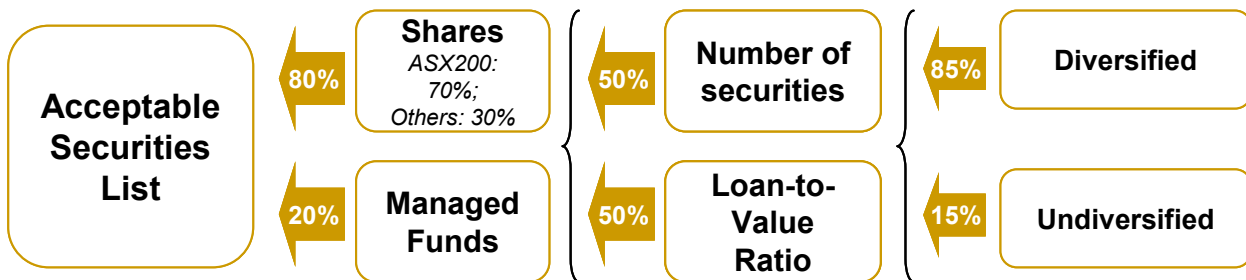


### Feature Score:

This score differs according to which investor profile is being assessed. The methodology is the same for both profiles, the weightings within each methodology differ, as indicated below:



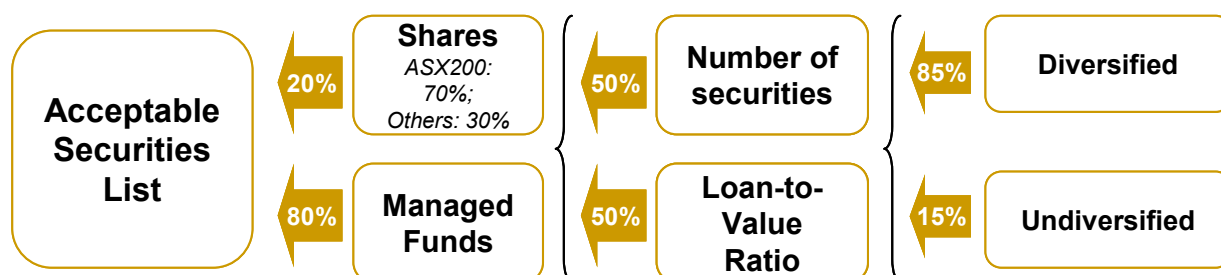
### Share Investor Profile:



- **80% weighting assigned to shares portion of ASL**
- **Focus on features such as Direct client services, Margin loan trading, and Transaction costs**

Product Features	
Categories	Weights
Direct client services	11%
Settlement Acct & Risk Mgmt	10%
Lending terms	9%
Margin loan trading	9%
Margin information	7%
Repayments	6%
Transaction costs	6%
Fees and charges	6%
Options trading	6%
Security	6%
Advisor services	5%
Protected equity facility	5%
International shares	4%
Portfolio platforms	3%
3rd party trades	1%
Cash advance	1%
Discount broker partnerships	1%
Dividend distribution	1%
Progressive drawdowns	1%
Split/Combination features	1%
Switching	1%

## Managed Fund Investor Profile:



- **80% weighting assigned to managed funds portion of ASL**
- **Focus on features such as Advisor services and Instalment gearing**

### Product Features

Categories	Weights
Advisor services	11%
Instalment gearing	10%
Settlement Acct & Risk Mgmt	10%
Lending terms	9%
Repayments	6%
Direct client services	6%
Portfolio platforms	6%
Fees and charges	5%
Margin information	5%
Margin loan trading	5%
Protected equity facility	5%
Transaction costs	5%
Options trading	4%
Security	4%
International shares	3%
Cash advance	1%
Discount broker partnerships	1%
Dividend distribution	1%
Progressive drawdowns	1%
Split/Combination features	1%
Switching	1%

## HOW OFTEN ARE ALL PRODUCTS REVIEWED FOR RATING PURPOSES?

All ratings are fully recalculated every six months based on the latest features offered by each provider. CANSTAR CANNEX also monitors changes on an ongoing basis. The results are published in a variety of mediums (newspapers, magazines, television, websites etc)

## DOES CANSTAR CANNEX RATE OTHER PRODUCT AREAS?

CANSTAR CANNEX researches, compares and rates the suite of banking and insurance products listed below. These star ratings use similar methodologies to guarantee quality, consistency and transparency. Results are freely available to consumers who use the star ratings as a guide to product excellence. The use of similar star ratings logos also builds consumer recognition of quality products across all categories. Please access the CANSTAR CANNEX website at [www.canstarcannex.com.au](http://www.canstarcannex.com.au) if you would like to view the latest star ratings reports of interest.

Agribusiness  
Business banking  
Car insurance  
CFD trading  
Credit cards  
Deposit accounts  
Direct Life Insurance  
Health insurance  
Home & Contents  
Life Insurance  
Low-doc home loans  
Margin lending  
Mortgages  
Online broking  
Package banking  
Personal loans  
Reward programs  
Travel Insurance



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