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HD **SMSFs aren't going mad about residential property**

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It's a different story with Chinese investors

IT'S a myth that Australian self-managed super fund trustees are going mad on residential property, Credit Suisse analyst Hasan Tevfik says.

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While they put just over $1.4 billion into that asset class in 2012-13, their rate of investment is slowing sharply and they will only invest about $700 million, or half that amount, in housing in 2013-14, he says.

``While SMSFs are increasingly allocating to equities, they're now buying residential real estate in Australia at a slower rate,'' he says.

This means their investments are dwarfed by some foreign players such as those from China.

Tevfik estimates that Chinese investors are pouring $5.4bn a year into Australian residential housing, equivalent to 12 per cent of new supply.

Non-resident investors are not allowed to buy established houses but may buy off the plan.

He is not passing judgment on the level of Chinese buying, which has been widely reported, so much as emphasising that buying residential real estate is not where he believes SMSFs are, or should be, investing.

``The benefits of owning a residential property in your SMSF have always been marginal,'' he says in a report titled A Nation of Selfies.

``Banks will lend to SMSFs to buy property, but the rates are higher than normal,'' he says.

The tight rules on borrowing to invest in property in SMSFs require a separate bare trustee structure to be set up, specifically so that loans are ``limited recourse''. That's to protect the super fund if the loan goes bad, but not surprisingly the banks charge higher rates on the loans. The only way round that problem, and there is always a way round a financial problem, is for the bank to demand a personal guarantee on the loan. That way the SMSF trustees' personal assets, rather than their super fund, are at risk.

Tevfik says tax benefits from negative gearing are less significant and that, most important, ``the yield on Australian residential property is low when compared to property trusts or stocks''.

He sees the hunt for dividends as being self-fulfilling to a degree. ``It is clear companies know that SMSFs are powerful and they try to keep their precious investors happy,'' he says.

``By being income-focused, SMSFs could be distorting the capital allocation decision. In an attempt to grow dividends and keep SMSFs happy, companies may have to revert to more cost cuts, less capital expenditure and scrip dividend payments.''

He says his colleague Richard Hitchens, a quantitative analyst, has noted that the hunt for dividends has caused a distortion in corporate behaviour.

Hitchens says it is unusual ``to have dividends continuing to perform as a factor this far into a market recovery''.

The most negative element in Tevfik's report, at least as regards the mania for dividends, is that the distortions may well have negative consequences for our economy. ``SMSF trustees should understand that higher dividends could come at the expense of their children getting jobs.

``After all, the Telstra call centre has now moved to lower-cost Manila.

``With a low cost of debt, low cost of equity and plenty of cashflow, companies should be investing, creating more jobs and, hopefully, helping the economy to rebalance away from mining investment.''

So what is he recommending?

He says that after screening for companies with reasonable dividend yields and a solid dividend growth rate, the list of recommendations includes Fortescue, Macquarie **Group** and Sonic Healthcare.

On the negative side, ``companies where the dividend outlook is poor and which have elicited cashflow cover include Qantas, Crown and Metcash''.

``We add Sonic to our strategy long portfolio and Metcash to our strategy short portfolio,'' he says, meaning that for investors well enough organised to short-sell stocks, Metcash has just achieved the dubious privilege of being a better share to sell than to **buy**.

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