How to navigate the aged care minefield

JAMES GERRARD

Speaking as a financial adviser, I can say the financial aspects involved in placing a loved one into aged care is mind-boggling and filled with twists and turns that's way beyond the understanding of the average Australian.

I'm not at all surprised to hear the whole sector will now be the subject of a royal commission into aged care announced this week.

What I have learnt to date is that anyone who must engage with the system needs a strategy.

Here's what I recommend: if you are an older person who requires care services, the first step is to contact the federal government department, aptly named My Aged Care, and they will assess your needs.

From there, if you require a lower level of assistance and wish to stay in the family home, you may be assigned a home-care package.

> Moving into an aged care home involves upfront fees and layers of ongoing fees

This covers services such as assisting with personal hygiene and care, dressing and undressing and food preparation.

You pay a daily fee depending on your income level. If you're a full pensioner, you'll pay $10 per day, whereas if you have other income and financial assets, you may pay up to $40 per day.

If you are assessed as requiring a higher level of care, you will be directed to move into an aged care home and this is where it starts to get tricky.

There can be both upfront and ongoing fees. The upfront fee, which is called a refundable accommodation deposit, is a lump sum that the aged care provider asks for upon admission.

Although it's an upfront fee, it can be negotiated as an ongoing payment or as a part lump sum and part ongoing payment.

For the upfront lump-sum option, the range of deposit expected varies from a few hundred thousand up to $1 million for the more exclusive aged care homes.

The main requirement is that the aged care provider cannot ask for a lump sum that leaves you with less than $45,500 in assets.

There can be negotiation on the deposit amount so it's not an equitable system. One person may be asked to pay a $1m deposit while another person $100,000 for the exact same place, with the differences occurring due to different level of assets and ability to negotiate a lower deposit.

The alternative to the lump sum deposit, is to pay a daily accommodation payment.

This fee is calculated by applying an interest rate on the lump sum that you should have paid that is set between 3.75 per cent and up to a maximum 5.96 per cent.

Number crunching then comes in to work out whether the family home can be kept, rented out and the daily accommodation payment paid from the rental income received.

However, given the interest rate on the unpaid lump sum can up to 5.96 per cent, the net rental yield on the family home will usually fall short of this and result in cash being depleted over time, at which point there is no choice other than to sell the family home and pay the proceeds to the aged care provider.

And just when you think you can relax having dealt with the upfront entry costs, you're hit with the realisation that there are ongoing costs, which can be significant.

To make it more complicated, there are several layers of ongoing fees to deal with.

If you wish to move out of the family home but don't require higher level aged care services provided at an aged care home, an alternative option is an over-55s retirement village.

Entry costs vary from a few hundred thousand to more than $1m depending on the location and property.

But as you can probably guess by now, it's another minefield of complexities.

This was drawn out in the ABC's *Four Corners* expose into Australia's largest listed retirement village group, Aveo, last year.

There are different forms of ownership such as leasehold estates, licences to occupy, company share arrangements and strata title ownership.

All of which has different legal rights and costs.

Add to that a sector that is infamous for complex contract and hidden costs and it's a recipe for disaster.

James Gerrard is the principal and director of Sydney financial planning firm www.financialadvisor.com

Aged care involves many difficult financial decisions

Dollars and sense of ethical investing

MY WAY
Former investment banker Mara Bun is a director of Australian Ethical Investments and promoter of the renewable power company Enova Community Energy

HOLLIE ADAMS

Former investment banker Mara Bun is focused on the rewards of ethical investment and renewable energy

Endless surveys show ethical investments outperform standard investments. Why?

Because corporations that replenish nature and contribute to sustainable development are less risky and perform better. Following this logic, ethical investment has quadrupled since 2014.

According to a Harvard Business School 2015 study, a dollar invested 20 years ago in a standard portfolio of listed companies would have grown to $14.16, but the same investment in a portfolio of companies growing their business with strong environmental and social focus would have grown to $28.36.

But can we rely on those returns forever — won't everyone tick the boxes soon?

Authentic ethical investing involves sustained, deep analysis and a constant evaluation of how ethical values and investment impacts are shifting in a changing world. There's plenty of growth left. That's the momentum I'm betting on.

You started your career in Silicon Valley investment banking ... are the tech stocks such as Google getting too big now?

Yes, at one time I was a senior financial analyst in the Morgan Stanley San Francisco Technology Group and later I led Macquarie Bank's internet equities research team in Sydney. But I will say I never dreamed that network effects and global trade would enable the lightning rise of FANGs (Facebook, Amazon, Netflix, Google).

The Internet of Things brings Google searches and Amazon shopping onto our kitchen benchtops. Sensors measure heat, air quality, water use and waste volumes. It's getting harder to hide impacts. These platforms' algorithms create echo chambers that literally block us from exposure to the real world in its full complexity. Soon the algorithms will be so complex that only machines will be able to evolve them.

> 'A dollar invested 20 years ago in a standard portfolio would have grown to $14.16, but $1 in firms with strong environmental and social focus would have grown to $28.36'
>
> MARA BUN
> AUSTRALIAN ETHICAL INVESTMENTS

As for the issue of size and scale, I am inspired by a new generation of anti-trust lawyers such as Lina Khan who recognise the risks of equating price with consumer welfare. Regulators took 41 years to bust Standard Oil in 1911. Surely the exponential growth of platform market power justifies a faster response today.

What are your interests now?

I'm a non-executive director of Australian Ethical Investments. These days I also consult to the Food Agility Co-operative Research Centre's agrifood digital transformation program and support Simba Global's digital and sustainability transformation.

You're also involved with the Enova alternative energy venture. What is that?

Enova Community Energy is a purpose economy start-up. It's got the same unholy alliance of farmers and greenies behind it who stopped coal seam gas at the NSW border and came together to build this community-owned energy retail company focused on a localised renewable energy transition.

You could say it is the retail part of the energy value chain that will make community-centred distributed energy possible in Australia. Enova is a start-up run by professionals leading a new energy model, accountable to a board that includes senior retired business executives.

How on earth did you get National Party and Labor officials to both back an alternative energy project?

Funnily enough, in the Northern Rivers region of NSW politicians of all persuasions recognise community values: people hate coal and love renewables, pure and simple.

You must take interest in the royal commission into banking. Will it lead to genuine change?

I enjoyed bashing banks while leading advocacy at CHOICE in the 1990s. They were exposed for fee gouging and misleading advertising. The inherent conflict between selling and managing wealth management products was apparent.

The royal commission now exposes what was anticipated then. But they have not yet pinned the tail on the political donkeys who crippled regulators along the way.

As recently appointed chair of the Australian Conservation Foundation, you must have been surprised at the $443m that John Schubert and his foundation received from the Turnbull regime. What do you think should be done with the money?

The decision to outsource reef research to a private foundation was made for political expedience: the government had to spend this huge amount in one hit in order to comply with World Heritage commitments. It's pretty clear that they are not equipped to cut the mustard, especially after the political fallout. Sadly — because the Great Barrier Reef Foundation has some great people and excellent research leaders — they made a shemozzle of it.

I think the funds should be invested through the collaboration model promoted by Innovation and Science Australia.

What are your own investments — can you tell us your portfolio approach?

I am a boring investor: all my superannuation is either with Australian Ethical Investments or the Commonwealth Superannuation Corporation. I lend money to social enterprises — it's a great pleasure to support their evolution. I own Australian Ethical and Enova shares and some technology managed funds in the US.

Oh yes, and I'm investing in a sustainable home on acreage in Tallebudgera Valley in the Gold Coast hinterland.

Buyer beware: high valuations based on unrealistic growth hopes

ROGER MONTGOMERY

There can be little doubt in any fund manager's mind that prices for many companies listed on exchanges around the world can only be justified by assuming rates of growth few companies have ever sustained.

In many cases the anchor of conventional metrics has been cast aside by unrealistic expectations associated with the almost cliched themes of an ageing population or a booming Chinese consumer, or the infinite margins associated with a globally scalable technology platform.

In every boom a dominant theme emerges that provides scope for valuations to disengage with reality. This current boom is no different.

Take a look at the market capitalisations of some of listed businesses whose share prices have rallied on the back of hopes of global domination: a2 Milk, Afterpay Touch, Xero, Wisetech Global, Altium and Appen have an aggregate market capitalisation of $29.5 billion, combined revenue of less than $2bn and combined net profits of just $245 million.

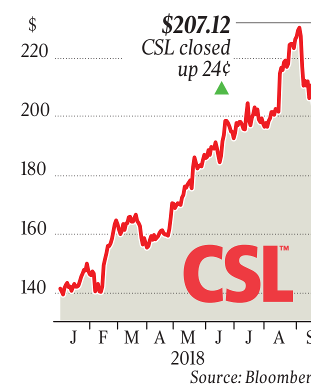
Of that profit a2 Milk is responsible for $131mn and Xero and Afterpay Touch are losing money. I should add that a quarter of consumer "factoring" Afterpay's revenues come from late fees which jumped over 364 per cent in 2018.

Even the large caps aren't immune to a bout of optimism. An analyst from British wealth manager Schroders recently revealed its consternation by breaking down the price of CSL. The blood products company is now one of the top 10 most commonly held stocks in Australia. It is also a company whose shares I sold a long time ago, after concluding it was overpriced (it has since almost doubled).

The analyst noted that if the assumptions are made that CSL's product portfolio is mature (of course it isn't), that product pricing is fair (it can probably rise), and that they'd be willing to accept an 8 per cent return and therefore pay 12.5 times for CSL's business, then they'd be prepared to pay $37.5bn for the company's $3bn of operating earnings.

The market obviously disagrees with that valuation because every other owner is willing to pay $107.5bn (even holding it at these prices, an owner is implying they're willing to buy it here).

In other words, the market is willing to pay $70bn above a conservative valuation for the next



phase of growth. And even though the company already dominates its markets — China is the next frontier — investors are willing effectively to pay, now, the price of two more CSLs to be created in the future.

Think about that because it really is the definition of hoping the company can grow into its price.

Investors should be cautious when such hope is built into prices because it is much harder for a company to execute on its business strategy, and it takes much longer to do so, than it is for hopes to be reflected in share prices.

If the Schroders analyst had applied the same metrics to miner Rio Tinto's operating profits — in other words the same 12.5 times multiple they applied to CSL (remembering there was an implied $70bn being paid for blue sky) — the Rio valuation could allow for operating profits to halve.

Alternatively, a margin of safety of about $100bn opens up between the current price and the valuation. But investors would have to get excited and treat Rio the way they are treating CSL for that margin of safety to close.

While you may not be compelled to buy Rio, the point I'm making is that you should be very cautious about buying CSL at these prices. And the same goes for Appen, Wisetech and friends.

You might remember I painted a pretty dim picture of the prospects for Kogan investors earlier this year. At the time the shares were trading above $9. Those same shares now trade at $5.87. While I do not believe Kogan is in the same universe as CSL, investors are justifying their investments on an equally irrational basis — paying a very high price for growth that is yet to materialise or a rate of growth that may be unprecedented.

While market highs continue to be broken and elevated valuations persist, I sound like the canary in the coal mine.

Popularity wins in the short run. But in the long run the market can't help but reflect the actual, rather than hoped-for, performance of the business.

Roger Montgomery is founder and chief investment officer of the Montgomery Fund.

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