Cuffelinks
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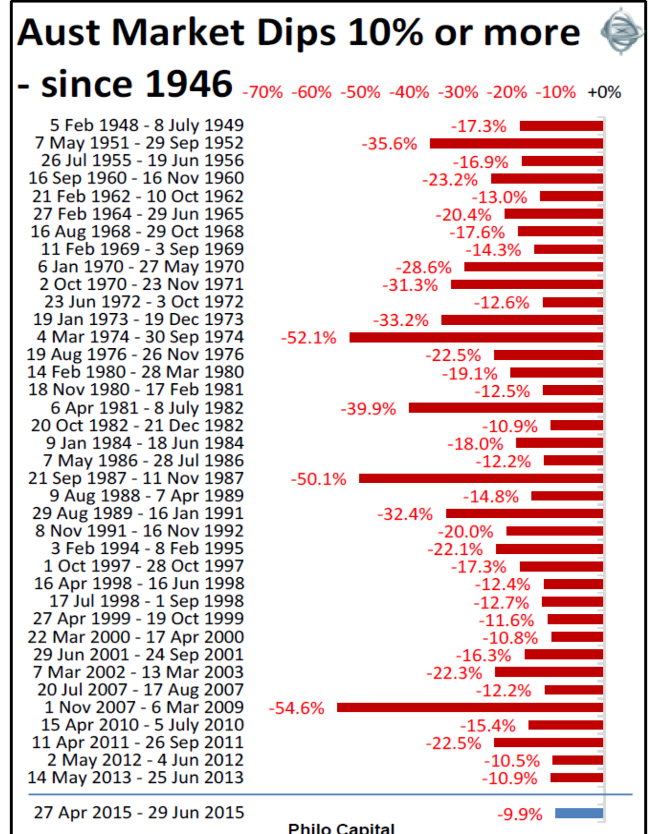
Anyone for a dip? Price falls a buying opportunity

Ashley Owen

Every day the prices of individual company shares rise and fall and so does the overall market index. Sometimes the broad market index falls because of a sell-off in a particularly large stock, as happened recently when Apple fell 4% on the 22 July 2015 after its profit report. As Apple is the largest listed stock in the world, the 4% Apple sell-off dragged down the market index due its large weighting in the index. But most market-wide sell-offs are caused by factors affecting general market confidence, like the Greek debt crises, which are unrelated to particular companies.

Long term investors look forward to market-wide falls because good companies are sold off along with the rest. It gives us a chance to buy into companies we have been wanting to buy but have been too expensive. Every market including Australia has a few fine companies but most of them are simply too expensive most of the time, so we need to wait until the share price drops in general sell-offs.

Fortunately for long term investors, sell-offs of 10% or more occur quite often, about once every couple of years. We have had 38 market dips of 10% or more in Australia in the past 70 years since shares came off war-time price controls at the end of 1946.



In recent years the overall market has fallen -55% in 2008-9 (sub-prime), then -22.5% in 2011 (Greece 1), -10.5% in 2012 (Greece 2), and then -10.9% in 2013 (US QE taper scare), but markets have been ultra-calm since then.

We had a nice 9% dip from 27 April to 29 June 2015 but it didn't quite hit -10% because the market rebounded. Investing requires patience and it seems we will have to wait a little longer for the next buying opportunity.

A brief look at the markets:

Australia

The local economy is still limping along as RBA governor Glenn Stevens warns the market to expect slower long term growth rates ahead. The corporate earnings season has kicked off and with some exceptions, the outlook is for very modest growth. The aggregate will be dragged down by mining company earnings which are expected to fall by around 20-30% due to the collapses in commodities prices and excess production. Iron ore prices fell heavily early in the month and ended down another 7% in July, down 23% year to date. Households and business were also warned of dramatic prices rises ahead for gas because cheap gas is being exported so foreigners reap the benefits of our LNG 'boom'. It is the opposite of the US, where government policy is for Americans to benefit from the energy revolution, and the debate is whether foreigners should be allowed to benefit at all.

Europe

July was a drama-filled month in the long-running Greek debt saga. As expected the government failed to repay the 'bundled' debts due at the end of June, then on 13 July the Greek government finally gave in and accepted an austerity and reform package to release another €86 billion in bailout funds. Even if tax rates are raised and pensions and other government spending items are cut, it is still unlikely that enough additional net revenue will be raised to repay the debt on schedule. The reason is that the austerity measures will most likely slow economic activity and tax revenues even further. As the debts pile up they are increasingly appearing impossible to repay, but Germany and the IMF look like resisting another bailout. Global stock markets fell in the lead-up to the Greek deal and rebounded strongly when the deal was done. The next critical milestone is 20 August, which is only a week away.

United States

The US economy is ticking along steadily, driven by relatively strong consumer spending and confidence, boosted in turn by falling fuel prices, rising house prices and share prices, and now rising wages. The Fed appears to be on track to start raising interest rates later this year but it is going out of its way to assure investors that the rises will be slow and well signalled to the market.

In the race for the Republican nomination for the presidential election next year, unlikely candidate Donald Trump had taken the lead. His strategy is simple but thus far effective – blaming Mexicans for just about everything wrong with America and the world. This is gaining traction particularly amongst working class whites. The African American share of the US population has remained relatively constant in recent decades at around 14% but the steadily rising Hispanic share will soon make whites 'a minority in their own country', and Trump's rhetoric is designed to tap into that base racial fear.

Asia

In China the main story continues to be the unwinding of the latest stock market bubble. Last year a range of government policy initiatives encouraged investors to switch to shares to give them something to gamble on while property prices were falling. As a result, share prices shot up astronomically and even the broad market indexes more than doubled in an almighty policy-induced, margin lending fuelled bubble. We wrote about this and its inevitable collapse in our April report this year. Speculators had little understanding of the companies whose shares they were buying. Miraculously the economic growth numbers for China came in at exactly 7%, spot on the government's stated goal, although few have any faith in the official government numbers.

Ashley Owen is Joint CEO of Philo Capital Advisers and a director and adviser to the Third Link Growth Fund. This article is educational only. It is not personal financial advice and does not consider the circumstances of any individual.

Learning when to buy and sell shares

Roger Montgomery

At a recent talk I gave at the Australian Investors Association's National Conference, I received one question more than any other: "Is it time to buy BHP?" Obstreperous commentators - paid by commissions on activity rather than returns – are incentivised to make headlines calling the bottom of the resource slump.

Price contains no information about value

Highly leveraged commodity producers with negative free cash flows, like America's largest coal producer Alpha Coal, have filed for Chapter 11 bankruptcy protection, amid a steel oversupply emanating from China, and slumping commodity prices. This is the shot-across-the-bow for Vale and Fortescue, and places a darkening cloud above the prospects and future returns for BHP and Rio because highly leveraged producers must produce even more of the commodity amid declining prices to meet their interest expenses.

But these arguments are in fact superficial. At the core of the question is a lack of understanding of the difference between price and intrinsic value. Value is not presented simply because a share price has fallen. Price information is free and the reason it is free is because it contains no information about value.

Predicting share prices, which is in essence what the resource commentators are trying to do, is impossible to do consistently well, at least in the short-term.

Intrinsic value is the vessel that helps navigate the sometimes tempestuous changes in share prices. If you have formed your view on the intrinsic value of a company, you can navigate clearly through the thunder and high seas, the gloom and the hype.

Your share portfolio may still be buffeted around by the twin tides of fashion and sentiment, but with each rise and fall you are able to strengthen it, buying more below intrinsic value and perhaps selling when share prices are well above.

Suppose you have your eye on a company and its shares fall from $15 to $12. Should you buy now? What if you buy at $12 and the shares fall to $10? Suppose you decide to buy more. What if they then decline even further to $8 or even $6? When exactly do you buy?

Only if you are confident that the business is actually worth $15 per share are you able to see a fall in the share price – from $12 to $6, for example – for what it is: a terrific opportunity. The right response is to buy more. If you're like me and you like chocolate, then surely it is rational to order more when your favourite block is on 'special' at the supermarket? It's the same with shares.

Shares are like groceries

Treat buying shares the same way you buy groceries. You actually want the share price to go down so that you can buy more. Share price declines, particularly those that are produced when everyone around you sees only doom and gloom ahead, are precisely what you want.

But how do you know the shares are cheap? Without the beacon of intrinsic value, how do you know whether to buy more or to panic? Many investors don't know the value of their shares. They frequently panic when shares fall, and also suffer from the consequences of paying too much.

I have often asked an audience of investors the following question, 'If the shares of (insert your favourite company) were trading at half price today, would you buy them?' The response is both rapid and enthusiastic, 'Yes!' And yet, sometime later, when the share price does indeed fall 50%, only a small handful of the original group ever buy the shares. Why is that? It is because share prices only fall 50% when there is bad news, either about the company being considered or about the economy or market more generally. And unfortunately, such news often perverts good ideas to bad ones. What was seen initially as a brilliant opportunity becomes a high risk 'play' that should be avoided until there is more certainty (and a higher price of course).

Your mother probably told you that first impressions are usually correct. She may not have been talking about shares on sale, but she was right again. What is good advice for choosing friends is also good for selecting shares.

The challenge is knowing when to buy

The easier part of investing is knowing what to buy. For example, is it really so difficult to see that CSL is a better business than Slater & Gordon? Is it that challenging to see that an investor should favour the fund manager Platinum Asset Management over Qantas?

The challenging part of investing isn't identifying good businesses that you would like to own. The challenging part is knowing when to buy, while the prices of all these companies are gyrating amid noise and influences that may or may not ever impact their businesses.

Nobody should miss out on buying shares in great businesses because of the fear that the shares will go down even more. And there is no need to panic and sell at depressed prices either. But such rational behaviour requires you to have something other than the price to look at. You need to know the value of the business and its shares.

Of course in order to value a company's shares, one needs to be aware of and have appraised the prospects for the business and its products or services. When the price of iron ore was $140 per tonne, we challenged the notion that the long run average would bear any resemblance to the then recent prices. Indeed at $140, we thought $40 per tonne was more likely to eventuate. We now believe the prospects for Australia and the resource sector are likely to worsen and so we arrive at valuations for resource companies that are much lower than current prices.

Roger Montgomery is the Founder and Chief Investment Officer at The Montgomery Fund, and author of the bestseller 'Value.able'. This article is for general educational purposes and does not consider the specific needs of any investor.

Companies crying wolf

Marcus Burns

"Greed, for lack of a better word is good. Greed is right, Greed works. Greed clarifies, cuts through and captures the essence of evolutionary spirit."

Gordon Gecko in Wall Street

These inimitable words from Gordon Gecko, portrayed adroitly by Michael Douglas in Wall Street, captures the process of creative destruction of the market perfectly. The market will reward companies it thinks will allocate capital well and similarly punishes those who don't. It tries to anticipate the future and thus the changes in future returns on capital before they happen.

Can managers think counter-cyclically?

Good news travels fast and bad news travels slowly. So too is the case with management teams who get good news from the troops quickly and bad news slowly. If all we did was listen to management's current views on their businesses we would miss changes to future returns. If you had listened to the mining CEOs two years ago, things could not have been better, they were racing to expand capacity, Chinese demand for everything was insatiable and the backlog for capital equipment orders was at record highs. Just as the last capacity addition was being announced, prices for most commodities started to fall and have continued to slide since.

Whilst demand is not in the hands of commodity producers, supply certainly is and disciplined managers would start to think about reducing capacity to restore over supplied markets back to a balance rather than simply focussing on their own marginal costs – which continually signals for them to produce more. Their future is collectively in their hands but so long as they continue to act as if they have no impact on market prices it won't be. The same dynamics play out in all commodity style businesses and it is without doubt the managers who can think counter-cyclically will make more money for their investors than those that run with the pack. Sure running with the pack is fun, it's contagious, why heck you might even let off a wolf cry or two but why don't MBA courses have titles like "How to operate against the cycle (and ignore the Board's imperative)" or "How to buy your competitors when they are on their knees due to overzealous expansion?".

Excess executive compensation

Allied to this issue are current practices in executive compensation. On this front we have been vocal recently in voting down packages for management teams where we feel our investors' interests haven't been properly represented. Managers have several things under their control including operational

excellence and capital allocation. Those two drivers, above all, will help to determine how their businesses and ultimately how their share price will perform. Often however, an executive team will inherit an overly optimistic share price through no fault of their own and in spite of producing decent operational performance and the prudent use of capital their shares will still decline or underperform peers. The converse is also true. Thus it seems to us utterly silly to include TSR (total shareholder return) as a key metric for executive performance measurement. Most senior executives have a relatively short tenure at the top (3-5 years seems to see most CEO's out) and it would be close to a fluke if the beginning of their tenure were to coincide with a perfectly valued share price. Installing KPIs which reflect how operations should best be run into performance packages as well as return on capital improvements seem a far better way to us to align shareholders' interests with the things management can actually control. Knowing you will be judged on the capital you deploy, might slow down or even encourage management teams to think against the grain and thus better position their companies to profit from the cycle rather than be purged by it. More of a lone wolf howl than a wolf pack yap!

No free cash flow in many resource companies

Two of the critical issues we focus on in small cap investing are return on capital and cashflow generation. To use a crude medical analogy, cashflow is the lifeblood of a business and return on capital is the skeletal muscle. It is the interaction of these two primal financial forces that is the key to generating shareholder wealth. Layer over that capital allocation (which we have spoken of many times before as one of, if not, THE key skill required by senior executives) and valuation and you have the lingua franca of a good investment process. Applying this to smaller companies means that we end up very underweight some sectors.

We often get asked what we think of gold companies for instance. This was a sector that not long ago comprised almost 10% of the Small Ordinaries Index. Whilst we struggle to have much of a sensible view on gold per se, we do have a strong view on the underlying business economics. Unlike most commodities which are in some sense used or at least hard to recycle, gold is stored or worn or sometimes used in high end electronics which require a strong resistance to corrosion. The high value of gold ensures that a large proportion of the 'used' gold makes its way back into the system via recycling. The production of gold however is a virtually futile exercise from an investor's point of view. The average mine in Australia is currently mining grades at around 1gram per tonne of ore. Most mines, in addition, require the removal of several tonnes of overburden to get to the one tonne of ore in which the 1 gram of gold is contained. That's a lot of dirt moving merely to get to the tonne of ore which you then have to grind, float and process in order to extract the tiny fleck of a valuable substance known as gold. To make matters worse, of the twelve gold companies listed in the Small Ordinaries Index very few have produced free cashflow (the lifeblood remember) in any of the last five years. Only one has produced free cashflow in aggregate over five years – that honour goes to Alacer Gold. Alacer however is busy stashing cash for, you guessed it, a new US$600 million plant to enable them to process more complex ore!

Small gold companies are not alone. A quick glance down the 11 small oil companies in the Small Ordinaries Index produces an even more exceptional result. Once again there have been individual years when a few have produced free cashflow in individual years but none have produced free cashflow in aggregate over the past five years. Those years haven't seen bad oil prices either so it will be interesting to see how many shareholders will be keen to continue to give these companies money with the prevailing oil prices. Whilst it goes against the grain a little to highlight these two sectors when commodity prices and their share prices are down, the economics and capital allocation decisions within the sector leave a lot to be desired.

Outlook

As we head into the results season we would expect there to be a higher than usual degree of volatility within the small companies universe. A combination of what we feel is a fairly broad-based move to trend and momentum investing has pushed a number of stocks away from levels we would see as fair value in both directions. We witnessed some examples of 'snap backs' over July 2015 with holdings in Webjet, Pacific Brands and Sedgman all jumping between 16% and 45% within a few days of positive trading updates. On the other side of the

coin, several of the mainstream media names declined aggressively on reasonably modest earnings downgrades. We think our universe will remain a stock pickers market where adherence to the disciplines of cashflow and capital allocation will ultimately out as winning attributes.

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What does the current yield curve tell us?

Aaron Minney

Introduction

In May this year, the Reserve Bank of Australia (RBA) lowered the official cash rate to 2%. This move ushered in the lowest interest rate environment since 1959 when the money market was established in Australia. People often ask if it is worth investing in fixed income assets with a long horizon, such as annuities and long bond investments. There is a sense that 'rates will have to rise' and so people assume that it makes sense to wait.

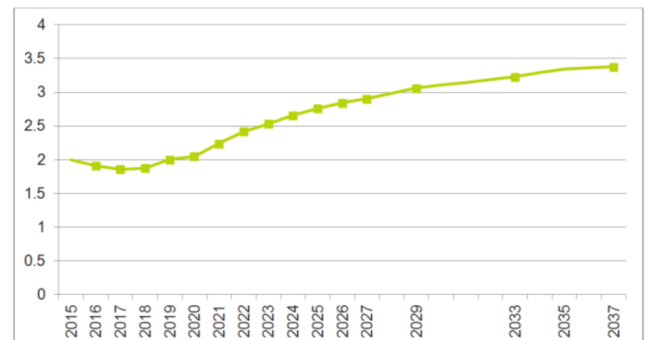
To range of factors determine interest rates, and the yield curve already reflects expectations of the future. In many cases, even if the rate looks low, not waiting will be the best strategy.

The yield curve

The yield curve is a series of market prices for interest rate-linked securities that have been plotted to create a smooth curve. The securities on the curve range from short-dated deposits to longer maturity bonds. Typically, the curve slopes upwards: it rises, with the longer maturities reflecting the 'term premium' that a lender or investor demands for having money tied up for longer.

The yield curve is the market's best view of expected changes to future interest rates. All around the world, highly motivated traders, analysts and investors are making decisions about the likely movements of interest rates for up to 30 years into the future. If those market participants think, for example, that interest rates are going up in 2017, you would already be able to see higher yields in the prices at the relevant part of the yield curve. Let's have a look at what the current yield curve is saying.

The chart below shows the market forecast for interest rates based on Australian government bonds with maturities out to 2037. The curve initially descends, then is flat for a while, but eventually slopes upwards. What the curve shows is that the market is saying: "We don't think interest rates are going up before 2017 and they are likely to remain below 4%."



Source: RBA

The role of long dated assets in times of low interest rates

In the accumulation stage, fixed interest assets are used primarily to minimise losses when markets fall. Low returns don't change the need to manage risk and long-dated assets provide that benefit. Investors in a low rate environment might need to take on more risk, elsewhere in the portfolio, to reach their targets, but the risk-reducing role of bonds remains. Also, low rates will not affect the yield to maturity of a fixed income asset held to term, regardless of what the 'mark-to-market' might look like.

In retirement, long dated bonds and annuities are used to generate secure income, not just reduce risk, so the return should matter. Putting aside the option to take more risk, the question is can a

retiree generate more secure income by avoiding long dated fixed interest assets?

Is it better to wait?

One of the problems with low rates is that people remember when rates were much higher. What they forget is that interest rates don't operate in a vacuum. High rates are generally accompanied by other negative factors and externalities, often a breakout of inflation. It would be like remembering that great hot summer from your childhood spent almost entirely at the beach, while forgetting that it was actually a really severe drought. There are great stories about 'someone's uncle' who bought an annuity in the early 1990s when rates were high. In hindsight, that was a great time to buy any long term interest rate-sensitive asset, but many other aspects of the economy at that time were potentially harmful to investors. Government bonds were over 13% and the Reserve Bank was yet to adopt an inflation target of 2-3%. Rates are unlikely to get back to those levels (without an explosion in inflation), but it is tempting to think that waiting until they get to 6% might be a good bet.

The problem with this way of thinking is that you might be waiting a very long time. Japan's history, for instance, shows us that rate movements are never a one-way bet. Yields continued to fall after the 1989 Nikkei collapse and cash rates have been 1% or lower in Japan for 20 years. The key drivers for low rates have been continuing low inflation (and deflation) and the demographics of an ageing population. The rest of the developed world is facing these conditions now.

Anyone waiting for higher rates can expect higher income down the track. This is exactly what the yield curve tells us. Instead of the 2% rate now, interest rates are expected to go above 4% in the future. But, waiting for interest rates to rise often means you lose out overall; you spend too long holding lower yielding short-term assets like cash and you are trying to 'time the market'. When rates increase in line with the expectations in the yield curve, the total income payments received are often less than a single longer term investment.

A role for low-yielding assets

The low rate environment is likely to be here for a while. Retirees still need a secure income stream, even if rates are low. Without simply rolling the dice and taking on more risk through investing in more volatile investments, retirees can benefit from buying low-yielding, long-dated assets now, rather than waiting and hoping that rates rise more than the market currently expects.

Aaron Minney is Head of Retirement Income Research at Challenger Limited. This article is for general educational purposes and does not consider the specific needs of any investor.

Calculation and use of BBSW and BBSY

Elizabeth Moran

The Bank Bill Swap Rate (BBSW) is an important metric in many markets including the ASX listed (such as hybrids) and over-the-counter bond markets. It's used as the floating rate note (FRN) benchmark, as a foundation to determine periodic (most commonly quarterly) interest re-sets on these FRNs. It also shows the market's expectation of future interest rates.

The Australian Financial Markets Association (AFMA) provides independently determined rates, including BBSW that can be used for the revaluation of investments by governments and financial institutions. These rates are collected and published (intra-day, end-of-day, end-of-week and/or end-of-month) for the following wholesale over-the-counter products:

- Bank Bill Swap Rates (BBSW)
- Bank Accepted Bills/Negotiable Certificates of Deposit (BAB/NCD)
- Live Cash and Repurchase Agreements
- Swaps
- Environmental Products Prices

BBSW

The AFMA BBSW benchmark rates represent the midpoint of the nationally observed live and executable best bid and best offer (NBBO) for AFMA Prime Bank Eligible Securities. The NBBO calculation is the average of all good samples of the best bid and best offer, such samples sourced from authorised trading venues and taken at three randomised intervals at and around 10:00am.

- The average of all good NBBO midpoint samples, rounded to four decimal places, is published at approximately 10:15am as the BBSW benchmark rate, for each tenor.
- BBSW mid rates are published on the AFMA website on the following Business Day, thus making them available to the general public.
- Financial news media outlets regularly report on BBSW rates.

BBSY

- 'Bid' and 'Ask' values for each tenor are published at approximately 10:15am using a set difference respectively of five basis points above and below the BBSW rate.
- The Bid and Ask values of BBSW are used, amongst other things, by market participants to price floating rate loans. Being directly derived from BBSW and where the only difference is the predetermined and non-variable bid/ask spread to BBSW, rates published on BBSY are a familial derivative of BBSW and not a separate benchmark.
- The 10 basis point spread between the Bid and Ask values may not be changed without the express consent of both the AFMA Benchmarks Committee and the AFMA Market Governance Committee, and consideration of any change to this spread must be subject to prior consultation with market participants.

For more information, see AFMA BBSW, A Guide to the Bank Bill Swap (BBSW) Benchmark Rate. To view BBSW on a 24 hour delayed basis, click here.

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Going global good for yourself and charities

Graham Hand

Successful fund-raising is primarily about good timing and execution, and occasionally, a transaction appears that achieves its aims with considerable style. Cuffelinks does not normally write about particular funds, but the Future Generation Global Investment Company (to list on the ASX under code FGG) offers an appealing structure and delivers great benefits to needy charities.

Much has already been written about this new Listed Investment Company (LIC), and details can be found in the offer documents, linked here. In brief, many of Australia's most prominent global fund managers have agreed to provide their services at no cost, and the 1% management fee charged by the LIC will be donated to charities committed to young Australians with mental illness problems. A worthy cause in need of much funding. This type of charitable structure was pioneered in Australia by Chris Cuffe when he launched the Third Link Growth Fund in 2008, but FGG is the first time it has been applied to global equities.

Rather than repeat what other articles have written (and not understating the charitable merits), I met with the Joint Chief Executive Officer of FGG, Chris Donohoe, to delve a little deeper into the investment side. Chris handled the IPOs of the two global offerings of PM Capital, and under the guidance of Geoff Wilson, he has been brought in to manage the fund-raising. The FGG team has been criss-crossing the country talking to brokers and investors, and is confident of going close to raising its very ambitious $550 million potential. This is a spectacular result for a LIC, and would have been unthinkable even a year or two ago.

Allocation to managers

On manager allocations, Donohoe says, "FGG has been very careful to pick managers who do things differently. It's not about index replication." The prospectus lists 17 managers who have committed initial capacity of $790 million to FGG. This is not a trivial issue: nine of these managers are closed to retail investors, and consciously limit the amount they manage to focus on generating superior results. For example, VGI Partners has allocated $30 million from its small $1 billion capacity.

Such managers usually make up for the limited capacity by charging clients higher fees, and Donohoe estimates the range of base fees for the individual funds of these managers would be up to 2.475% with performance fees up to 27.5% above some agreed index. This makes the donation amount of 1% of average monthly NTA a highly

competitive offer. In addition, with the majority of participants in the ongoing business of the LIC providing their services for free (including accounting, secretarial, tax advice, investment committee members and annual listing fees), the additional costs extracted from investor returns may be as low as two basis points a year.

Manager allocations will be determined by the investment committee in consultation with expert advice, but it is likely to be about 55% to the long-only managers, about 30% to the absolute return and 15% to the more quant-style. Maximum allocation at cost to any one manager is 10%. Some rebalancing over time is possible if, for example, a manager produces excellent results and goes well over the 10% level. Donohoe expects allocations will be "… done as if the initial allocations are retained for a long time". Of course, changes may be warranted due to personnel changes or a shift in manager style.

Likely performance

The prospectus cannot say much about how the fund is likely to perform, but Donohoe says, "We have checked the numbers on how this portfolio would have performed in the past, and the gross outperformance is too big to state." This is a strong result given many of the managers have an absolute return focus. It is fair to expect such a fund to underperform an index like the S&P500 when it runs strongly, since some managers rightly have a low beta emphasis and focus on capital protection. This is one of the strong features of the fund, as it should outperform in a falling market. Downside protection always has appeal if it comes without sacrificing returns.

The absence of performance fees should also not be underestimated. A manager which outperforms its index by 10% based on a 25% performance fee earns a healthy 2.5%, perhaps on top of the base 2%. In FGG, this manager would forgo the 4.5% and only 1% would be 'charged' to the investor for the charitable donation.

Another clever point is the initial price of $1.10. Geoff Wilson is probably Australia's foremost LIC expert, and he believes that some LICs with an initial price of $1 but a NAV of say 97 cents (with an attached options worth say 5 cents making up the value shortfall) struggle to breach the psychological $1 barrier. Starting at $1.10 and based on a subscription of $550 million and known expenses, the NAV of the fund is estimated at $1.089, and it should trade initially around that level. Better than starting trading at 98 or 99 cents.

So what are the costs?

This transaction is as close to a win (for investors) and a win (for charities) and a win (for doing-good service providers) as any in financial markets. At the risk of being churlish, a balanced review should ask who is making money from such benevolence. On page 51 of the prospectus is part of the answer. At the maximum of $550 million, total estimated expenses are $8.6 million. With most participants acting pro bono, the cost comes down to two main items: broker stamping fees of $7.7 million, and ASX listing fees of $537,000.

Stamping fees are paid on valid applications bearing an AFSL holder's stamp, excluding any money lodged in priority offers to either Wilson's clients or those who hold shares in the domestic equivalent of FGG, the Australian equity fund listed as FGX. Stamping fees are a healthy 2% (actually, 1.81% plus GST). If anything, this is higher than normal. So the obvious question is, why should fund managers and other service providers commit to an indefinite provision of services pro bono while brokers are paid a healthy fee?

Donohoe is open in his response. "We asked ourselves how we could do the most good with this offer, and the answer is by bringing in the most money. We are leaving it to the brokers to decide what to do." Some have committed to donate their fees to charities, while others will split in some proportion. Donohoe is confident a lot of the money will be donated back. He also expects the large take up of priority offers and general applications without stamping will keep the cost down.

And half a million dollars paid to the ASX? They have waived ongoing costs, keeping the fees for running the business highly attractive. Donohoe says there's even a wealthy individual meeting whatever audit costs they have.

What else to consider before investing?

Most retail investors are underweight global equities, where 98% of companies are listed and most of the big global opportunities, often in sectors not available in Australia. SMSFs, for example, have only an estimated 10-15% of their assets offshore (see this article for more details). Large super funds

normally have around 20-25%, and many retail investors should consider higher offshore allocations.

Investing in a minimum of 17 managers prevents the investor having a material exposure to any one name, and while this may be good, if an investor really likes a global manager, then it may be better to go directly to that manager's fund. It's also not practical to form a view on 17 or more managers in the way an investor can with only one or two, but this is true of any multi manager fund.

LICs offered with options have the complication of the potential dilution from exercised options affecting future returns. In FGG's case, the options expire on 15 September 2017, over two years from now. This issue is discussed here.

And the Australian dollar is now at a six-year low against the US dollar, and while many expect even lower levels, ideal timing would have given the currency upside more potential.

But the bottom line is at $550 million (or $1.1 billion if all options are exercised), this LIC will generate $5.5 million (or $11 million) a year for mental health, which Geoff Wilson says will make it the largest funder of such services in Australia other than governments. It's worthy of consideration for most diversified portfolio.

FGG is expected to close on 28 August 2015 with listing on the ASX on 10 September 2015. The details are provided here.

Graham Hand is Editor of Cuffelinks and has no connection with the Future Generation Global Investment Company. This article is general background and any individual considering an investment should seek professional advice for their own circumstances.

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