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# theadvantage

Spring 2012

## Red Tape Really Needed

**The new Anti Money Laundering (and Countering the Financing of Terrorism) regime comes into force on June 30th next year.**

Called AML/CFT for short, the new regime will bring New Zealand into line with other countries with new protocols for dealing with money. The Financial Intelligence Unit (FIU) of the New Zealand Police along with Internal Affairs and the Financial Markets Authority have been involved in training businesses for the last two years. The FIU is one of about 120 members of an international group which first met in 1995 to fight financial crime. Our legislation, passed in 2009, is designed to improve systems and services, curtail criminal activity, protect legitimate business and protect New Zealand's international reputation.

It has been too easy for money to be laundered in New Zealand in the past. A minimal fee of $153.33 is involved in setting up a company on line in New Zealand and some of these shell companies have been involved in some serious scams.

In June of this year, it was alleged that US$150 million was used to pay kick-backs to Ukranian and Latvian officials through a New Zealand company called Falcona Systems Limited. The registered office in Albany was an empty town house. This case follows an earlier one involving Tormex Limited of Queen Street and US$680 million. Money passed from Tormex to a bank in Riga, the capital of Latvia, and no-one knew where it came from and where it went. Investigations have implicated the Russian mafia.

Before these last two incidents, another more sinister scam involving arms came to light. SP Trading Limited, a NZ-registered company, was involved in chartering a plane registered in Georgia to fly arms from North Korea to somewhere in the Middle East. The cache never reached its destination having been stopped in Bangkok.

We don't come across these sorts of things in our everyday lives as a rule but they are happening and New Zealand has to step up to the plate. The new rules will affect us, like it or not.

The regime adds another layer of compliance activity and cost to most businesses. We have been asked to attend training courses and are required to have systems in place soon to identify and deal with risks.

Of prime importance is the need to identify customers and the source of their funds. If we have insufficient information about an existing customer or there has been a change, we will begin new due diligence. We will verify names, dates of birth, addresses and the nature of the business.

A higher level of due diligence is required in the case of people with complex affairs, for private companies and trusts. Apparently, trusts are considered to be a source of high risk



*private wealth management solutions*

**Red Tape Really Needed** from front page

for money laundering activity in New Zealand. We'll need to identify people (settlors, trustees, beneficiaries, appointers, promoters, directors, etc) via prescribed documents that prove their home address details. If there are fewer than ten beneficiaries of a trust, we'll need to identify them individually.

Documents will have to be provided showing how funds were acquired and how they were disposed of. For example, if a farm or business was sold, we'll need to be satisfied that this was the source of the funds settled in a trust and the transactions were legitimate. We'll need to see that distributions from a trust are being paid out legitimately.

Whilst we have no concerns at present, if we are suspicious about a particular person or transaction, we have to report it within three working days. There's a "hot line" for urgent reporting. As a reporting entity, we will be audited every two years.

There's a certain sense of loss of innocence in all of this but we also need a healthy dose of reality. We'll willingly play our part in helping New Zealand to be a responsible international citizen and we hope you'll help us do that. No doubt, as June 30th 2013 gets closer, you'll be hearing a lot more about this.

# Renminbi

"Renminbi" is hard to say but a word we'll all need in our vocabularies soon. It's the name for China's currency, an emerging commodity in the global market place. The abbreviation is "RMB" just as we use "NZD". The denominations of RMB used in every-day life are
分 Fen (cent)
角 Jiao (dime )
圆 Yuan (dollar)

The rate of RMB to NZD is just over five at present. One New Zealand dollar buys a bit more than five yuan. In practical terms, an ice-cream would cost, say, three dollars here and 15 yuan in China. We talk about a rise/fall in the RMB or the NZD.

Only a very small part of the world's trade is currently transacted using RMB but that's changing. The relatively recent opening of trade between China and Taiwan in RMB has been a significant development. Taiwan is now the second off-shore RMB centre after Hong Kong. A RMB clearing and trading bank facility has opened. It allows for the repatriation of large surpluses that arise from China when these erstwhile protagonists trade. The bank has also started borrowing and lending with other domestic and overseas banks.

Companies are beginning to invoice and settle in RMB. Around 20% of businesses based in Germany, the Netherlands and the UK are invoicing in RMB and the others have plans to do so. The total amount of China's trade settled in RMB is not high (around 10% from 2% two years ago) but is rising. Companies using the Chinese currency report being able to get lower prices for goods they purchase and also being able to expand their network to suppliers who have less experience in handling foreign exchange issues. The speed for settlement has increased when RMB are used. Also assisting is a new system for international payments set up by the People's Bank of China.

The rise of the RMB as a trading currency is just the beginning, and the RMB is becoming an investible currency.

There are various bonds issued in RMB, the best known being the Dim Sum bonds that have been issued in Hong Kong for some time. The name relates to the Chinese cuisine that's a bit like a smorgasbord. Bonds are now being issued from within China. The China Development Bank has just placed 2.5 million RMB, some for a short term of 3 years at 2.9% and the rest in a very long 20 year bond at 4.3%. The offer was very popular, being oversubscribed more than three times. Incidentally, it was not rated but the issuer, China Development Bank, has a AA- rating from S&P. Buyers came from Europe, the Middle East, Africa and the Asia Pacific region. China's bond market is the youngest but largest bond fund market in Asia and is being increasingly supported by investors who have traditionally purchased bonds in developed markets but are now drawn by the region's growth potential.

There are some new RMB ETFs that have also just been launched. These allow foreign investors, for the first time, to access China's A Shares markets.

Investment using RMB is still developing and needs to acquire infrastructure around legal frameworks, dealing with default risk, ratings and so on but there is no doubt that it's off the starting blocks.

As a reserve currency, the RMB is unlikely to be held by governments and large institutions outside China for some time.

# When Big gets Bigger

Standard and Poors and Dow Jones merged in June this year to form the world's largest provider of index services. The joint venture firm is known as S&P Dow Jones. The name Dow Jones is familiar because it's the Dow Jones Industrial Average index that's mentioned on the television news every night. That particular index tracks the 30 largest industrial shares in the US and began in 1896.

S&P Dow Jones now provides information on 830,000 indices that capture movements in assets of US$1.5 trillion. The new business also owns the world's two leading commodity indices, the Dow Jones-UBS Commodity Index and the S&P GSCI (formerly Goldman Sachs Commodity Index). Also in their stable of indices is the VIX index, a measure of the implied volatility of the S&P 500 Index. The business is headquartered in New York and has major operational hubs in London, Hong Kong, Beijing and New Jersey (in the US).

The merger of S&P and Dow Jones follows a trend for investors to shift to passive investments. Markets have been difficult for some time and the cost of active management has added considerably to the burden of low returns. The use of Exchange Traded Funds (ETFs) has also risen markedly. ETFs allow an investor to purchase a whole market with one product. It's a quick, easy and cost-effective method of achieving wider diversification than picking stocks and it helps to reduce the risks that arise from holding too few securities or betting on certain sectors (or countries). The risk of a particular market is always there so it's also important to hold a variety of asset types like shares and bonds not just shares or bonds.

S&P Dow Jones will provide index information to 575 ETFs with US$387 billion in assets. In our part of the world, there are ETFs that allow investors to buy whole markets. That is, all the shares of the NZX (and segments of it), the ASX and other off-shore markets.

The level of an index is set by the prices of all the assets in it. For example, the share prices of the 50 largest listed companies in New Zealand in the case of the NZX50. There are various versions of most indices, some including dividends, others not. Indices can help to establish comparative returns where investors can compare their return with the index return to see if they did better or worse. There are many traps for the unwary and it's not as simple as it sounds so beware.

The Accordia Portfolios use ETFs for holding some assets and Accordia also uses index information when building and monitoring portfolios. We also publish index data in our regular Portfolio News updates and in client reviews.

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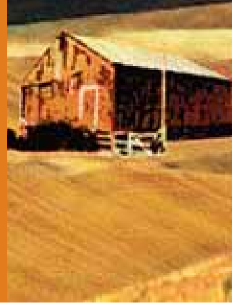

## Putting it Simply


### The "Carry Trade"

If there are differences in interest rates in different places, there may be an advantage in getting into the "carry trade". Money could be borrowed at a low rate to invest somewhere else at a higher rate. There are lots of issues to consider like the cost of borrowing, a change in the interest rate on the borrowing and also foreign exchange considerations on both sides of the deal. If the "planets were aligned" though, it may be a profitable, if risky, activity.

We've been talking about China a bit in this newsletter and most readers will be aware that our bonds are attractive to overseas investors like the Chinese and Japanese because our interest rates, particularly for the Japanese, are still pretty attractive – low as they are at present. When New Zealand's interest rates were much higher than now, there was a lot of carry trade activity here. Uridashi bonds (for Japanese retail investors) and Eurokiwi bonds have been popular and removed one of the elements of risk in the deal – one of the foreign exchange rate movements.

## Christmas Break

Our offices will close at midday on Friday December 21st and re-open at 9 am on Monday 14th January 2013. During the break, urgent messages can be left by phone on 0800 444 999 or by emailing service@accordia.co.nz

It seems much too early to be saying so, but we send our best wishes for Christmas and the New Year.

*The next edition of Accordia Advantage will be available in late January 2013. Back issues are available on the website www.accordia.co.nz.*


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|---|---|
| **Accordia Freephone** | **0800 444 999** |
| **Accordia Email** | service@accordia.co.nz |
| **Accordia Christchurch** | Unit 4B, 303 Blenheim Rd |
| **Accordia Auckland** | Plaza Level, 41 Shortland St |
| **Accordia Hamilton** | Suite 9, 9 Lynden Court |



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