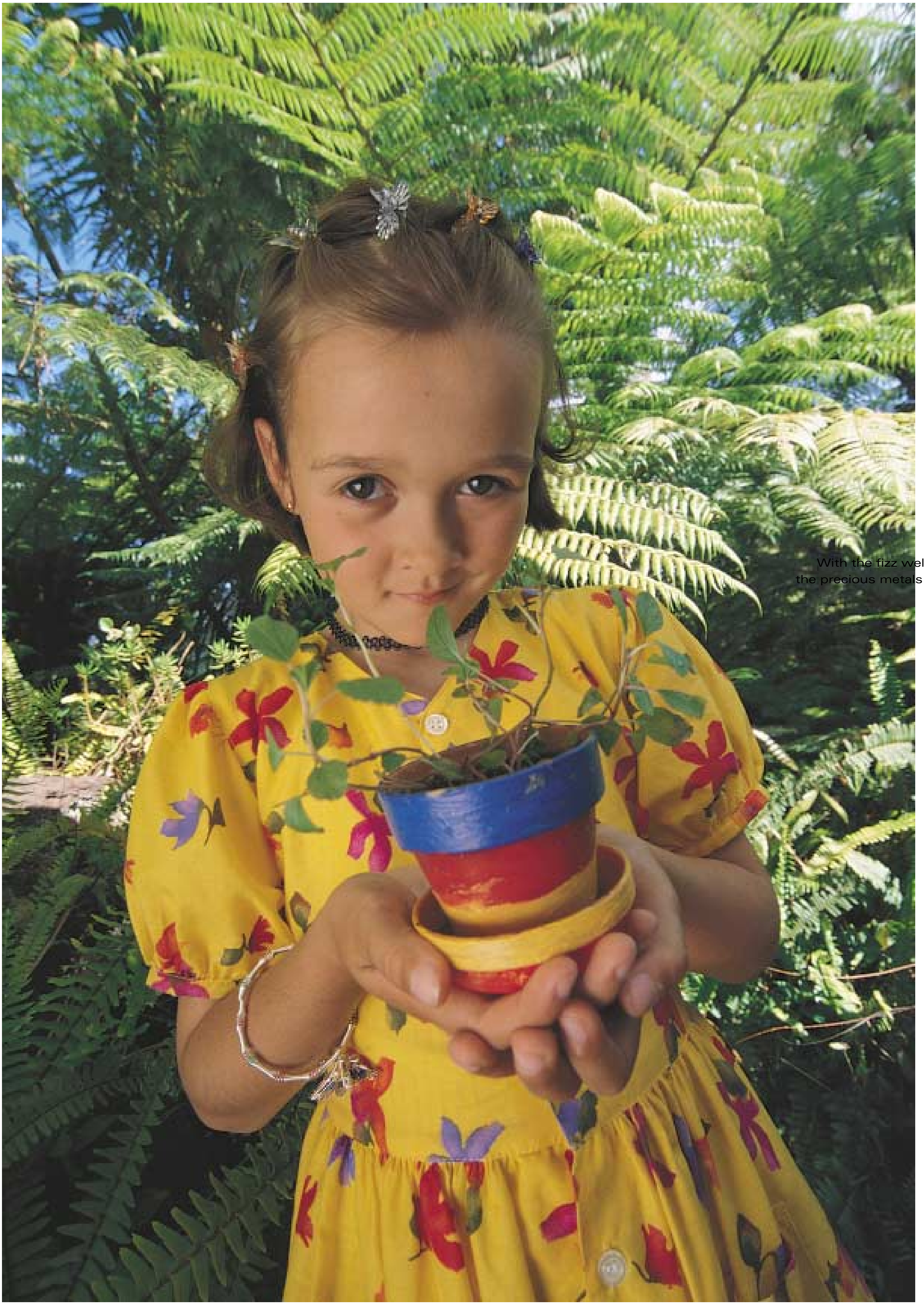


With the fizz well and tr
the precious metals to keep

NEXT GENERATION INVESTMENTS

What's on offer

Believe it or not, but there is life beyond fixed interest, equities and managed funds. Although having perused the entrails of fund inflow in recent years you might think otherwise. Cynics may argue that local investors exist within a vortex where the range of investment products is severely limited. While this view is unwarranted, it is true that local investors are comparatively unsophisticated in their understanding of different investment products compared with investors in Australia or the US.

The trouble is, local investor willingness to embrace less traditional investment vehicles is severely limited by a lack of knowledge. It's only natural that investors should steer well clear of investment vehicles they don't understand. But if the New Zealand Stock Exchange (NZSE) can negotiate some sort of merger with it's Australian counterpart (the ASX) as expected, local investors are likely to end up with a much greater exposure to different investment options. So wouldn't it worth finding out them now?

Investors who are prepared to trade higher risk in the pursuit of better returns will find investment vehicles featured in this issue of interest. Many of these investment vehicles have been around a long time, but as far as most local investors are concerned, they belong to a brave new investment frontier they know little about. Here's a few you might want to explore in greater detail.

Second-guessing tomorrow

Trade futures

Surfers and futures traders share that same dream, the chance to catch just one perfect wave. But instead of surviving the cold and possible shark attacks, futures traders have to ride-out small and regular loses so that they're around to enjoy the upside when it finally arrives.

Typically the domain of the speculative investor, futures unlike other forms of investment can offer almost instant returns. But professional futures investor Mark Sleeman says uninitiated investors looking merely to regain the excitement that the equities market once offered, should be prepared to take the associated risks that go with it.

Sleeman is one of around 1000 local private investors and high net worth individuals who buy and sell futures contracts internationally. These contracts are traded locally by 10 brokers who are members of the New Zealand Futures and Options Exchange (NZFOE), a limited liability company owned by the Sydney Futures Exchange.

During Sleeman's first year of full-time trading in 1998, he made a 31% return by successfully reading fluctuations in world markets spurred by currency crises in Asia and Russia. Not a bad gamble for the ex-engineer who sold his house to become a fulltime trader back in September 1997.

At any one time, Sleeman has between four to 10 positions on anything from one to 15 contracts. Successfully anticipating future trends in short-term interest rates (bank bills) in Europe, Australia and the US and long-term interest rates (bonds) in the US and the UK has earned Sleeman a net return of between 19% and 30% last year. And with several hundred thousand dollars in the market, that's a nice return. Also contributing to Sleeman's returns last year was the bull run in the precious metal palladium where prices have rallied from US$450/oz to US$900/oz and the falling NZ$ against the US$ which has moved from US$.50 to US$.39 at the low.

Another commodity that Sleeman has done well on this year is natural gas. Arguably the most volatile commodity right now, natural gas recently put on 1066 points in one night. At $10 a point, (US.01c per so much of natural gas) a trader with a natural gas contract would have made a profit of US$10,660. But there's a flipside, in fact for every trader who wins at futures, there's always a corresponding loser.

So how do futures markets work exactly? Conceptually it's really simple. Investors make money on the ups and downs of commodity prices.

Modern futures-trading has its roots in the Chicago of the late 1800s, where farmers, known as hedgers, would secure future prices on their grain and other commodities from future buyers. The market worked because it pro vided revenue certainty for the seller and price stability for the end user, for arguments sake a baker who would use the grain to make bread.

Since then, private investors like Sleeman have been able to get in on the act. Although the commodity range has widened to include metals, grains, crops, other scarce resources, plus bond and equity markets, today's futures work pretty much on similar lines.

In other words, today's price is the market's best guess on what the commodity's price will be on delivery date. Factors determining price fluctuations include anything from climate, natural disasters to wars and economic booms and busts.

"I prefer futures markets because they're so much more diverse than equities. When the Dow Jones or the NZSE goes down, most stocks are effected. When sugar is down, it has effect no on oil and coffee. That gives me more opportunity for profit.

The art of futures trading, says Sleeman is anticipating future trends. For example, had he known that Gold prices in september 1999 would rise from around $US260 to more than US$300 an ounce, he would have bought gold futures. What he didn't know was plunging gold prices would be suddenly reversed by an agreement among 15 European central banks to limit gold sales to 400 tonnes a year for the next five years. And with crude oil having jumped from $12 to $36/barrel many a fortune has been made on black gold over the last 18 months. And those who can accurately time the drop in oil prices stand to do the same.

Cash flow

One advantage of futures is they don't require huge cash flow. Here's how it works, because buyers and sellers contract to do business at some time in the future, they're only required to pay a deposit. A futures trader contracts to buy 100 troy ounces of gold on December 15. At US$300 an ounce this will cost the trader US$30,000, but they pay only a 5% deposit of around US$1500.

If the price of gold moves to US$295 the trader is down US$500 ($5/oz times 100 oz) for the day and would have to put up additional funds to hold the margin at a constant level. But had the trader contracted to sell, not buy, at US$300 an ounce, they'd have had US$500 credited to their account that night.

The way Sleeman sees it, smart futures traders limit how much they'll lose on any single trade by placing stop-loss orders when the contract's entered. This means they limit how much they're prepared to lose by bailing out on the contract. Small loses tend to be more frequent, but these are usually offset by larger, yet rarer gains. And in the case of coffee, which went up 300% three years ago, gains can be huge.

"I limit my losses over a two-day price range and keep them to 1% of my total assets. By all means have a crack at futures, but do it first through a managed fund. It has taken me 10 years to feel like I know what I'm doing, and even then, there have times when every market seems to move against me."

Seven tips for would-be traders

Sleeman recommends investors dip their toes into the futures market via a (futures-based) managed fund. For those investors compelled to have a go themselves, he shares the following tips.

1) Hard Yakka: If you're keen on trading futures you must be prepared to do your homework. Taking money off fulltime traders has more to do with skill than luck.
2) Play money: Only invest money you can afford to lose.
3) Survival tools: Because of the unlimited loss profile associated with leveraged markets like futures, you can't afford to be wrong for very long. So remember to cut your losses on every position.
4) Let profits run: Often a market will go up well beyond expectations. So if the market is in your favour, you need a strategy that lets you run with it.
5) Manage your money: Recognise that as a rookie trader you'll have losses and probably lots of them. The trick is to ride out small losses so you're still in the game when markets turn in your favour.
6) Trading plan: A totally defined trading plan should include tactics for entering and exiting the market and controlling downside risk.
7) Examine your motives: If you're not trading in futures with the singular aim of making money, don't do it.

HCM Global Asset Fund

Share price $15.52 (30 November 2000)

Established in 1994 by renowned Auckland-based futures guru Robert Holroyd, this is New Zealand's only commodity-based futures fund. As an open-ended, specialist limited liability company, the fund trades in international commodities markets utilising the expertise of skilled commodity trading advisers, these include local fulltime trader Mark Sleeman, and associated fund advisers in Australia and the US.

The fund has been structured to diversify risks. This means only 0.2% of the fund's total value ($12 million at October 2000) is risked in any one trade.

Commodity Tip

Listen up, there's a small fortune to be made buying futures contracts based on industrial commodities in 2001. At least that's the view of UK-based Fleming Global Mining Group. Titled "Riding Out the Storm", author of the report, from Fleming's London office Nick Moore, concludes that base metals will rebound from lethargic and oversold levels.

His favoured based metal picks are aluminium, copper, lead and tin. Aluminium, the premier base metal in terms of overall world metal consumption, remains one of Moore's flagship bull calls. He now envisages a peak in the aluminium cycle in first quarter 2002, and expects prices to rise sharply in the

With the fizz well and truly out of the gold and silver markets. Moore expects palladium and platinum to be the precious metals to keep an eye on 2001

coming months, to average 2001 at US$80c/lb, before peaking out at a 2002 price average of US$86c/lb. Similarly with copper, peak cycle prices averaging US$1.03/lb are now projected in 2002. And set to average US$21c/lb in 2000, lead is expected to rally to US$26c/lb in 2001 before peaking at US$28c/lb in 2002. Meantime, Moore projects the price of tin to progressively rally from US$2.50/lb in 2000 to US$3.00 in 2003.

With the fizz well and truly out of the gold and silver markets, Moore expects palladium and platinum to be the precious metals to keep an eye on 2001. "We expect more of the same from gold and silver. The outlook for the palladium price remains positive, although the peak has probably passed. Meantime, the platinum group metal markets remain hostage to the vagaries of Russian exports."

Compared with 1999, one of the best years on record for world mining share performance, 2000 has been an annus mirabilis. But on balance, Moore still believes the peak in the commodity cycle has not yet been seen. "Robust demand, high capacity utilisation rates, deep market deficits plus stock:consumption ratios at or below critical levels... all bode well for another 12-18 months of price excitement."

METAL PRICE FORECASTS 1999-2003

Source: Flemings Global Mining Group London

Metal	99	00E	01E	02E	03E	LongTerm	
OECD IP	(YoY%)	2.3	5.0	3.5	3.2	3.0	
Aluminium	c/lb	61.7	71	80	86	78	70
Copper	c/lb	71.3	84	98	103	90	85
Lead	c/lb	22.8	21	26	28	22	25
Zinc	c/lb	48.8	52	55	58	52	52
Nickel	c/lb	2.73	3.95	3.40	3.15	2.75	3.00
Tin	c/lb	2.45	2.50	2.60	2.80	3.00	2.50
Gold	c/lb	278	280	280	285	290	300
Silver	c/lb	5.22	5.00	5.00	5.10	5.20	5.00
Platinum	c/lb	374	540	530	490	450	360
Palladium	c/lb	360	650	625	580	520	325
BMPI	US$	93.8	109	120	126	113	106

APPROXIMATE PORTFOLIO HOLDINGS

Sector	%	Description
Interest rates	20-30%	Long and short term rates in US, NZ, Australia and Europe.
Currencies	20-30%	NZ$, AU$, European, Yen,CAN$
Commodities	40-50%	Metal, grains, softs (cocoa..)
Cash	5-15%	Bank deposits any currency

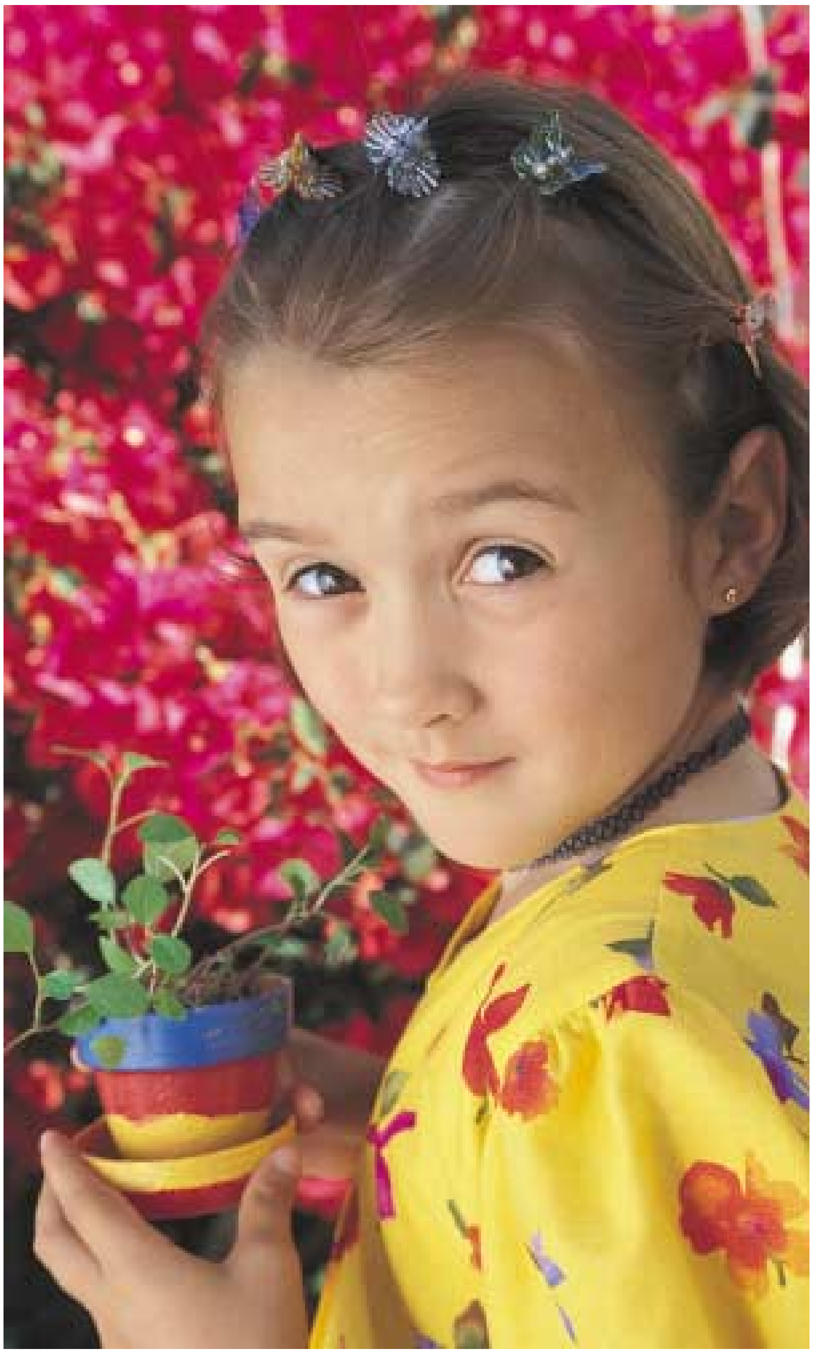
FUND PERFORMANCE

Five years	one year	Six months	Three months	YTD (11/11/00)
55.5%	9.2%	3.95%	-2.02%	16%

Wealth creator

Geared Equities Investment (GEI)

Chances are if you borrowed from the bank three years ago to invest in real estate, you're currently sitting on a net loss due to falling housing prices. What Macquarie Bank (in Australia) has done is take the philosophy of borrowing money to buy and hold property to grow wealth



and offset tax (through negative gearing) and successfully apply it to the stock market.

The bank lends investors a minimum of A$50,000 to buy Australian shares. Investors can chose from 25 (predominantly) large-cap stocks identified by the bank based on risk and liquidity. But unlike the property example (where housing prices can and do fall), the 100% finance offered by Macquarie Bank to buy share also comes with 100% capital protection.

By guaranteeing 100% of the loan capital, the Macquarie Bank's GEI programme limits the investor's risk to net interest costs over the life of the five year loan. In other words, if the investor buys (for arguments sake) National Australia Bank at $29 share, the bank guarantees to honour that minimum price (if after five years the share price has fallen below that level). The bank looks to recover its costs after five years, and the interest charged is relative to the investor's limited risk.

Capital protected loans like Macquarie's GEI are by no means new. In fact, Macquarie Bank started offering the GEI product in Australia around ten years ago. In recent years, around eight other providers were offering similar products in Australia. But unlike the Macquarie product, most other providers were offering shortÄterm (typically one year) frontÄend loaded, preÄpaid interest deals. And when the Australian Tax Office jumped on these products by putting a cap on the interest, all of Macquarie's competitors, including broking firms, Ord Minnett and JB Were in Australia decided to jump ship.

Auckland-based firm Geared Equities were charged with managing Macquarie Bank's GEI programme in New Zealand five years ago. "Aucklanders tend to leverage themselves for lifestyle costs as opposed to investment purposes. As a result, most of the (several hundred) Kiwi we have under the Macquarie GEI programme are from the deep south," says Murray Simpson managing director of Geared Equities.

Tax breaks

So exactly what kinds of investors are being attracted to GEI? "Most GEI investors are less interested in managed funds. They tend to be higher income earners, especially senior executives and accountants (who understand the numbers) with the disposable cash-flow to be able to leverage their taxable income. This product should attract any high income earner who wants exposure to international equities in a tax-efficient way."

What attracts them to this investment vehicle, says Simpson is the tax deductibility available on income producing assets. In fact despite the gearing aspect, he says the geared equities programme also complements investors with a risk averse profile. "We find that because an investor does not suffer capital losses, they tend to outÄperform the market. For example, during the Asian crisis the market went up 6% while investors portfolios under the programme were up (on average) around 18%, and with gearing their returns were multiplied," says Simpson.

Under the programme, investors receive direct ownership of shares, and as such, are entitled to the full benefits of full dividend imputation credits. The underlying "buy and hold" strategy means that after five years the capital gains on this investment will be tax free (established traders excluded). In addition to receiving dividends, investors (as registered owners of the shares) also have access to any rights issues or other offers extended to ordinary shareholders.

Outgoing charges

Macquarie Bank establishes an account for all New Zealand investors when they enter the GEI programme. Based on the current interest rate, an investor who borrowed an minimum $50,000 pays NZ$900 a month servicing the loan. What offsets these payments are dividend payouts (estimated at 3.5% in the first year). "It's our view that in subsequent years, this cash cost will reduce, based on dividend payments and prevailing interest rates and exchange rate movements," says Simpson.

Annual loan payments	A$8,000
Less dividend payments	A$1,750 (year one only)
Net cash cost for year	A$6,250
Less 39% claimed as tax losses	A$2,437
Actual cost year one	A$3,813

After five years

At the end of the five year term, investors can either sell up their shares and payÄoff their loan, sell part of their portfo-

lio or roll over the loan for another five years. Simpson says most investors chose to "re-jig" their portfolio by rolling it over and taking the surplus as unmortgaged shares. In other words, instead of accumulating an asset with the bank's money, they take the capital that's been gained and put it aside.

For example, one investor who borrowed $80,000 to buy shares (under the programme) found that their market value was worth $125,000 after three years. "After paying off the loan in full at the end of the term by selling part of the portfolio, the investor was left with a remaining $45,000 in shares that were not encumbered by a mortgage. This investor then rolled over the loan to acquire additional shares to expand and further diversify their portfolio. In practise, this investor would have paid only around 25% of the $80,000 loan in costs. And with that $20,000 now worth $45,000 he effectively received around 50% per annum compounded".

Investors should note, because Macquarie Bank is only offering a loan facility, the GEI programme is governed by the Fair Trading Act as opposed to the Securities Act, and as such is not obliged to issue a prospectus.

Knock on wood

Hardwood Forests Issue

Perceived by many as a scary investment at the best of times, the Hardwood Investment Series II adds some curious short-term dynamics to the traditional 25 to 30 year yield cycle and ownership structure on most forestry investments.

Assuming average selling price forecasts ($78/tonne) are met, the offer expects to return a tax-paid internal rate of return of 11.5% (equivalent to an 18.8% pre-tax return) after seven to eight years. As with other forestry investments, expenditure is tax deductable and 84% of an investor's contributions can be written off against other source income. And assuming 84% is tax deductable and a 39c/tax rate, the forecast net after tax cost will be $10,337. Tax benefits will be available each year as a proportion of the forestry costs expended.

The promoter of the Hardwood Investment Series II,

Risk premiums: GEIs vs

Portfolio Endowment Warrants (PEWs)

Following table is based on a "best guess" scenario as to where interest rates and margins are likely to be in future.

	GEI	PEW
TERM	**5 years**	**10 years**
Debt	100%	40%
Capital Protection	100%	40%
Premium for Risk	35%	35%
Premium subject to interest charge	No	Yes
Premium tax deductible	Yes	No