Safety, Risk & Scams

Financial Desk
National Seniors Australia

Safety When Investing

When choosing investments it is most important to consider your needs and objectives, your investment time frames and the security of the products being considered. While the level of security investors are comfortable with can vary from person to person, it is imperative to research potential products and strategies thoroughly before making decisions.

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An investor should be confident about the assets being purchased and, in the case of indirect (Managed) investments, the organisation/s through which the investments are made.

There are five asset classes in which investments can be made. The time the investments should be held to minimise the probability of financial loss varies with the asset class used.

As a general rule the following time frames can be suited to investments with the described volatility:

- shorter time frame - (up to 3 years), conservative low volatility investments are suitable (e.g. term deposits, bonds, high interest on-line bank accounts);
- medium time frame - (3 to 5 years), conservative low volatility investments together with a small amount of growth oriented investments are generally suitable (e.g. term deposits, listed property trusts, diversified balanced funds with shares in Blue Chip/ sound long standing public companies);
- longer time frame - (5 to 7 years and longer), a diversified portfolio is more likely to produce a strong result as the impact of short term fluctuations in value are averaged out. To minimise the probability of initial costs not being recouped growth investments are generally held for at least 5 to 7 years (e.g. residential property, property trusts, Australian and international shares).

To assist with understanding risk and time frames refer to our ‘Risk Meter’.

Different investments have characteristics that suit different time frames and individual objectives. Listed are the main investment sectors (asset classes) and the typical

characteristics they carry.

Cash & Term Deposits

The cash sector comprises products with the underlying assets in Financial Institutions. The investment term can be very short (overnight) through to 6 months. Typical products include at-call bank accounts, short term deposits, cash management accounts/trusts, bank bills and overnight money trading. These are considered low risk investment though liquidity risk could exist with some fixed term deposits.

Fixed Interest

> “…they have varied investment risk and liquidity risk factors to be considered..”

A number of different investment products form this market. Common assets in the sector include local and international Government Bonds, Corporate Bonds, Listed and Unlisted Debentures and Mortgage Trusts. The duration of these assets is greater than 6 months. Where the assets have a fixed term they have varied investment risk and liquidity risk factors to be considered. There is a market for trading these investments during their duration and values fluctuate with interest rate movements and the time remaining to maturity. These products may also be in the asset allocation of various managed investments.

Freezes on withdrawals and the suspension of distributions can occur in some circumstances.

Property

The property sector is traditionally considered by many to offer risk averse investors reliable capital growth over the medium to long term. Despite this often being the case, property asset values can be volatile and capital losses can occur. They do offer regular income but vacancies can affect this. Property can be purchased directly or indirectly via listed or unlisted trusts or property syndicates. Market and economic conditions can influence performance.

Australian Shares

The Australian share market historically offers opportunity for strong capital growth over the medium to long term. It is, however, volatile and losses can occur if assets have to be sold when the market is down.

Investors should be prepared to view investments in this market as long term in the face of extreme volatility. Investment can be made directly or indirectly via unit trusts or other derivatives.

International Shares

International shares, like Australian shares, offer the opportunity for long term capital growth. Investing offshore offers greater diversity due to access to larger markets. They can also be highly volatile in the short term and are therefore considered a long term investment. International share investments are subject to other risk factors such as currency fluctuations that can affect the risk/return equation.

Hybrid Securities

Hybrid Securities combine the Fixed Interest and Share markets. Convertible preference shares and convertible bonds are part of this option. The risk is higher than fixed interest investments but, in general, their volatility is not as great as shares.

Needs and Objectives

Investors should prioritise their needs and objectives so that they can choose investments with characteristics that can best achieve them. Those needs and objectives include:

- Security of capital
- Ability to generate income
- Protection from the impact of inflation
- Flexibility
- Tax effectiveness
- Access to Government Income Support
- Lifestyle
- Ease of investment management.

> “...all these objectives should be considered and the investor should be comfortable with their investment decision...”

At the end of the day all these objectives should be considered and the investor should be comfortable with their investment decision. To assist in determining if investors are comfortable with their investments they need to gauge their risk profile and understand the possible risks that can affect various investments.

There are many ways to determine a person’s risk profile or investment comfort level. Most are done by answering a questionnaire that is scored or rated. The questions revolve around what the investor wants to achieve from the investment and how comfortable they would be if the investment experienced one or more negative returns over the duration of the investment. Our Risk Meter can assist in understanding the timeframes, the markets and investments.

With any investment, there are many different types of risk - not just loss of capital. It is important to understand how these risks may impact the strategy being considered.

Main investment risks and typical characteristics

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Financial Markets Risk:

Markets are volatile and the value of investments may fall as well as rise. All investments (other than cash) can decline in value during adverse market conditions. This is particularly the case in the share and property markets.

For example, various reports show that while Share markets have experienced high volatility over the past 10 and 20 year periods, they have generally still outperformed other asset classes over the same period. A movement in the market price of an investment does not necessarily mean the investment is suddenly good or bad. While saying that Cash itself is not volatile, it must be remembered that its value fluctuates compared with other currencies. See Currency Risk.

Liquidity Risk:

Liquidity risk is where the investment may not easily be converted to cash, withdrawn or ‘cashed in’ without loss or penalty when access to the funds is required. For example a condition of release may need to be satisfied to access superannuation, a penalty applied if a fixed term investment is accessed or if shares are sold at a loss to satisfy a cash requirement.

Currency Risk:

The risk associated with the movement of a foreign currency in comparison to the Australian dollar (AUD) can have a major impact on the return from overseas investments (e.g. International shares) and is known as currency risk. This can also mean that it could take more cash to purchase imported items at a time when our currency has devalued against another.

Timing Risk:

Entering and exiting markets at the optimum time would achieve the best result for an investor. However, short term volatility can result in mistiming and paying more or receiving less for an asset than had been anticipated.

Price Risk:

This is the risk that the value of an asset will decline. This could result in a loss if the asset has to be sold at that time. For example paying the asking price or outbidding for a property when the market is falling and discovering the actual value is considerably less when seeking to re-sell it.

Manager Risk:

Past performance is no guarantee of future performance. Change of ownership, personnel and other factors could result in one year’s best performer being the next year’s worst.

Inflation Risk:

Inflation risk is when investments do not keep pace with inflation causing the real value of capital to fall. Risk averse investors who generally invest in cash and fixed term investments feel the full impact of inflation on the purchasing power of their savings. Because inflation and interest rates go hand in hand interest rates tend to be high in periods of high inflation and low in periods of low inflation.

Drivers of high inflation include high demand, rapid increases in wages and supply shortages. Easy access to low interest loans can also contribute.

Legislative Risk:

Rules and regulations governing superannuation, tax and other investment issues can be subject to considerable change.

Economic Risk:

Economic risk refers to the effects that the state of the economy has on the performance of an investment. If an economy is in recession, it means there is a slowdown in economic activity. Investment spending, household income, business profits, consumer confidence and inflation usually fall while bankruptcies and unemployment rise. All this usually impacts on share prices, property values and interest rates.

Major Event/Exceptional Circumstance Risk:

This includes events that occur naturally or those that are caused by humans. Whether they occur nationally or internationally they can affect investment performance. For example cyclones, bushfires, drought and floods can hurt or destroy businesses, farms and infrastructure affecting the economy on a local, state and national level. Events like these also affect insurance company profits and premiums. War and famine are examples of events that can affect economies on a global scale.

Illegal Activity Risk:

This risk includes improper use of the funds and fraud. To reduce risk investors should investigate all aspects of the investment and find out as much as possible about the promoter and the product.

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Whether dealing with a major fund, a well-known Financial Service provider, or a relatively small or unknown provider, thorough research is suggested before investing.

To minimise the risk of fraud or other illegal activity all paperwork and documentation e.g. Product Disclosure Statements (PDS)/Prospectus or Offer Document should be checked carefully and understood before being signed. Investors should ensure they receive acknowledgement of investments from the organisations concerned within a reasonable time.

Deal only with staff of product providers who hold an Australian Financial Services (AFS) Licence or are authorised representatives of licensees. Investors can check on an organisation’s licence by visiting the Australian Securities & Investments Commission’s (ASIC) consumer website, www.moneysmart.gov.au, or by telephoning 1300 300 630. To check for registered Financial Planners visit ASIC’s Financial Advisers Register at https://www.moneysmart.gov.au/investing/financial-advice/financial-advisers-register. After completing the necessary investigations a good rule of thumb to follow is ‘if in doubt ask more questions, if still in doubt then don’t invest.

Special care should be taken when making investments ‘on-line’. Often people accept the terms and conditions without reading and understanding them.

Scams, Schemes, Fraud and Dodgy Dealings

Many consumers lose money each year to dodgy investments or 'get rich quick' schemes that promise everything and deliver nothing. Often, the lure of making a lot of money can cloud a consumer's judgement when considering investment opportunities. Scam artists are continually coming up with new ways to lure consumers into giving up their money, some reinventing old scams but having the same result of the consumer losing out.

> "... it comes back to that old saying 'If it sounds too good to be true, it probably is'..."

Careful planning goes into marketing and presenting these scams and they are designed to touch the emotional desires of consumers. They may offer a 'free gift', a 'one off favour that is available to no-one else' or a 'special discount if bought now'. Documentation can also be presented in a fashion that looks legitimate, often with glossy images of luxury cars and homes that seem okay on the surface but an in depth look may reveal little detail on the investment and who is offering it. Some scams even offer testimonials given by so-called investors saying how 'wonderful the investment is' or that 'they made lots of money' and would 'recommend it to anyone'. Again it comes back to that old saying 'If it sounds too good to be true, it probably is'.

There have been many scams where consumers have lost money such as:

- Dodgy lottery schemes – the sale of tickets to lottery schemes that are not registered and have no prizes (often overseas lotteries);
- Gambling systems that guarantee success – these can include a book subscription or computer programs that promise success in picking winning race horses, lottery numbers or share prices;
- Offers from people claiming to have special or psychic powers – claims that they can offer wealth, love, happiness or health by paying fees, subscriptions or calling expensive phone numbers;
- Pyramid Schemes – the principal idea is that an operator recruits people who pay a fee or payment of some kind and then they recruit more people who also pay a fee, the majority of which is passed up the line to the original operator. The more people recruited the more money is made by the operator often with little chance of anyone else making money;
- The offer of free prizes by calling certain phone numbers or attending seminars – where pressure is then applied to sign up immediately for questionable investments with little or no opportunity to investigate or seek a second opinion;
- Cash payments offered from overseas if certain instructions are followed – with promises of large amounts of money to be paid on providing bank/credit card details and/or certain costs are met (e.g. Nigerian Scams);
- Requests to update or provide bank account details – letters or emails purporting to be from the financial institution requesting account and security details to be updated;
- Bogus charities – requests for donations to charities that do not exist or by people claiming they are from a legitimate charity but they pocket the donations;
- Financial scams – offers to invest in schemes that provide high returns from an unknown source, often overseas. This can include emails and letters sent to thousands of consumers suggesting they buy certain shares resulting in the share price increasing. The scammer then sells the shares at the higher price leaving investors with shares of little value. This is commonly called ramping.

- Requests from people claiming to be from government departments wanting payment or financial information. Recent cases include chasing up so-called unclaimed tax money or overcharged fees that the victim is owed. They then demand payment of money or charge a 'fee' to claim the funds and request the money be paid, often to an overseas bank account;
- Potions and lotions – scammers that often prey on the sick and vulnerable offering secret cures, weight loss, increased vitality or intelligence. Unlike legitimate alternative medicine there are no results or proof showing that they actually work although they are often marketed as alternative medicine;
- Offers to buy shares – Letters sent to shareholders offering to buy their share holdings at greatly reduced prices. This practice is not illegal but is considered to be morally improper as it is often the elderly or uninformed that agree to sell the shares without researching or understanding the consequences. The offer is usually on an official looking document, which adds to its authenticity. It has seen many investors agree to sell their shares at, in some cases, about 50% or less of the actual value and often with the payment being in instalments over a long period of time. It also means that the investor misses out on future dividends and potential gains.

*Note the examples given are not an exhaustive list.

Avoiding Scams

The most prudent action to take when there is any doubt at all about the investment or purchase is to not be pressured into anything. Don't let emotions override the decision and be confident to say no. Even if the offer is genuine, if there is any doubt, it is better to say no at first so that time is taken to consider the offer, understand it and be comfortable with it before deciding to accept it. Legitimate financial service providers will not demand an immediate answer.

> "... if there is any doubt, it is better to say no at first so that time is taken to consider the offer..."

Some tips to help protect against being a victim of a scam or dodgy scheme

- Ignore and delete emails, letters and chain mail offering lump sum payments or get rich quick offers
- Take the time to examine the offer carefully and do not commit to anything until fully satisfied with its validity. If in doubt check with the Australian Competition and Consumer Commission's (ACCC) 'Scamwatch' website at http://www.scamwatch.gov.au/ , visit the Australian Securities and Investment Commission's (ASIC) 'Moneysmart' website https://www.moneysmart.gov.au/ and contact your state's Office of Fair Trading
- Ask for identification from people offering investments, requesting payments or asking for donations
- Ask for proof that the business or charity is registered and that the person is employed or registered with them
- Don't accept testimonials without proof they are real as they can often be made up or dressed up to look good
- Ask if there is a cooling off period and how easily the investment can be redeemed
- Don't accept offers from unknown sources over the phone. Ask how they got your details and refuse to commit to anything as verbal agreements often can be enforced legally
- Ask for details of all costs, fees and payments that are involved in the offer or request
- Requests by letter or email for banking details and money (e.g. Nigerian Scams) should be reported to ASIC and/or ACCC
- You can minimise marketing calls by registering mobile and land line numbers with the Australian Government's 'Do Not Call Register' by phoning 1300 792 958 or visiting the website www.donotcall.gov.au.

'The Higher the Return, the Higher the Risk'

This is an important investment principle. Managing the level of risk is a vital part of investing. There is no investment without some risk and this includes depositing money in the bank. Always check potential risks when quoted returns are unusually high.

For more information:

Australian Securities & Investments Commission (ASIC)

moneysmart.gov.au
1300 300 630

Australian Competition & Consumer Commission (ACCC) Scamwatch (ACCC Information Centre)

scamwatch.gov.au
1300 795 995

National Seniors Australia (National Seniors) is a not-for-profit organisation that gives voice to issues that affect Australians aged 50 years and over. It is the largest membership organisation of its type in Australia with more than 200,000 members and is the fourth largest in the world.

The Financial Information Desk (FID) is an independent, confidential service funded by National Seniors that aims to improve the investment information available to older Australians

Our Objectives

- To provide an accessible, independent and trustworthy source of information for older Australians - particularly those with modest means.
- To promote industry and community awareness of consumer investment issues - particularly amongst older Australians.
- To promote industry understanding of consumer investment issues and to contribute to the raising of industry standards.
- To examine any unfairness in the market between consumers and providers of investment services and to provide information to consumers on dispute resolution processes.
- To represent the views of consumers on investment issues to industry and government organisations.
- To research and publish items on consumer issues relevant to the financial welfare of older Australians.
- To liaise with relevant consumer, community, academic and industry groups, as well as government organisations, to further these objectives.

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