

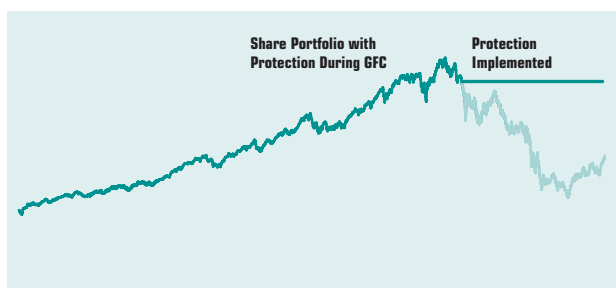
# Everyday Portfolio Protection for SMSFs

As you approach retirement it's prudent that SMSFs consider reducing their exposure to riskier assets like equities and increase exposure in safer assets like cash/bonds. However with current interest rates and the benefits franking credits provide via shares it is something that is seldom done.

Overweight holdings in shares exposes retirement savings to market corrections, a lesson learned the hard way for many during the GFC.

There is a valid alternative that continues to receive franking credits, benefits from future share price appreciation but protects the portfolio from large market corrections.

Purchasing protection from the options market can help!



The chart above shows an increasing share market until a market crash. Purchasing index put options returns cash to a well-diversified portfolio to help offset the decline in share prices whilst still ensuring the continued benefit of share ownership (dividends, franking credits, etc.)

## Implementing the Strategy

Like an insurance policy there are a number of factors that influence the premium paid for protection:

- Portfolio Value
- Excess (Protection level)
- Length of Protection
- Market Risk

The greater the level of excess (or protection level below the prevailing market) willing to be accepted the lower the premium. Obviously the longer the time frame the higher protection costs will be.

The following table helps identify the approximate percentage costs of insuring a well-diversified portfolio with index put options.

|            | 3 MONTHS | 6 MONTHS | 12 MONTHS |
|------------|----------|----------|-----------|
| 0% Excess  | 2.3%     | 3.0%     | 4.0%      |
| 5% Excess  | 0.7%     | 1.3%     | 2.2%      |
| 10% Excess | 0.2%     | 0.4%     | 0.8%      |

Note: The table assumes a market volatility level of 13% and S&P/ASX 200 Index Value of 5250

## How many options to buy?

Once the protection level and timeframe length is determined the final step before placing the options order with a broker is to determine how many options are need to protect the portfolio.

ASX index option contracts are worth \$10 per point if the protection level chosen is 5,000 points, 1 contract is worth \$50,000. For a portfolio worth around \$500,000 then 10 index options would need to be purchased. \$350,000 = 7; \$1,000,000 = 100 etc.

## What's the end result?

For every point the index falls below 5,000 points, the options contract returns \$10 cash. The following table shows as the market falls that losses are partially offset by cash you received from the options market. Whilst as the market rises the portfolio continues to benefit from share price rises, albeit less the premium paid for protection.

| INDEX VALUE | PROFIT/LOSS SHARES | PROFIT/LOSS OPTIONS | TOTAL     |
|-------------|--------------------|---------------------|-----------|
| 4250        | -\$100,000         | \$68,100            | -\$31,900 |
| 4750        | -\$50,000          | \$18,100            | -\$31,900 |
| 5250        | -                  | -\$6,900            | -\$6,900  |
| 5750        | \$50,000           | -\$6,900            | \$43,100  |
| 6250        | \$100,000          | -\$6,900            | \$93,100  |

Assume Index @ 5250 - 6 month 5% excess option bought. Portfolio Value = \$525,000

# Everyday Portfolio Protection Fact Sheet

## Where to from here?

ASX has a range of resources to help get advisers up to speed on employing options.

- [Online Protect Your Shares Course](#)
- [Pre-recorded Seminars & Podcasts](#)
- [Strategy Guide](#)

Visit [www.asx.com.au/options](http://www.asx.com.au/options) for more information.

Alternatively you may want to arrange an in-house training session. If so, contact:

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