



Bitcoin to infinity and beyond...again!

BY DR SHANE OLIVER

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KEY POINTS

- Bitcoin has made it to new record highs, helped recently by the advent of ETFs that invest directly into it.
- While blockchain technology has promise, the use case for Bitcoin is hard to determine making it impossible to value.
- Bitcoin could have lots more upside if it displaces gold as an independent of government “asset”, but this depends on having faith new buyers will come & pay ever higher prices.
- The key for investors is to recognise that: it’s highly volatile; very speculative; a poor diversifier; & there’s no free lunch.

BEFORE YOU GET STARTED

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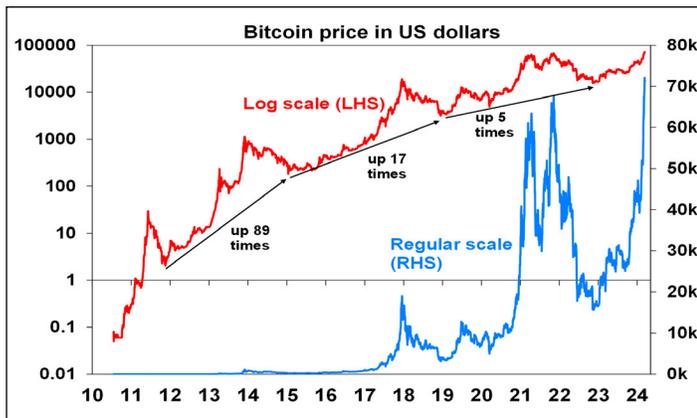
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Introduction

After another 80% or so plunge from its high in 2021 to its low in 2022, Bitcoin has rebounded again to a new record high. The next chart shows Bitcoin's price relative to the \$US since 2010, both on a regular scale and on a log scale to show perspective. From its 2022 low it's up more than fourfold. This is naturally sparking a new round of questions as to "what's driving it" and "should we invest in it"? The answer not simple. Bitcoin attracts extreme views - evangelists on the one hand and agnostics and atheists on the other in contrast to other things where the debate is between bulls and bears. This note looks at what it means for investors.



Source: Bloomberg, AMP

Bitcoin basics

Bitcoin was invented in 2008 by a person or group named Satoshi Nakamoto and the first "genesis block" was created in 2009. Trying to explain it and cryptocurrencies generally (and the blockchain technology that underpins them) is very complicated! The blockchain basically means that transactions in Bitcoin are verified and recorded in a public ledger (the blockchain) by a network of nodes (or databases) on the internet. New Bitcoins are created as a reward for an intensive computational record keeping process called mining, that groups new transactions into a block which is added to the chain. This requires significant computing power to show what is called "proof of work". The supply of Bitcoins is limited to 21 million, but because of a process called "halving" which occurs roughly every four years and sees miners compensated by less Bitcoins over time the limit will only be reached around 2140 after which transactions fees will be the only reward for record keeping. Because each node stores its own copy, there is no need for a trusted central authority like a central bank. Bitcoin is also anonymous with funds tied to Bitcoin addresses which require a private key (a long password) to access.

Because of Bitcoin's limited supply and independence from government it's seen as a hedge against the debasement of paper currencies (through inflation), the failure of

central banks or outright seizure. This has made it attractive to supporters of the Austrian school of economics (which advocates a free market in money), libertarians and anarchists.

As with most technologies, the more that use it the greater its appeal. So news that various groups will accept transactions in it, El Salvador's 2021 move to allow it as legal tender and various financial organisations allowing customer access via their platforms have aided its growth. The recent approval of Bitcoin ETFs and regulation of it, along with a coming halving (around April) have helped propel the recent surge in its price.

The number of cryptocurrencies blew out to more than 10,000 at the end 2023. Some started as jokes (eg, Dogecoin); some prioritise underpinning smart contracts (like Ethereum); some prioritise transactions (stablecoins that link to the value of a paper currency, eg, Tether); whereas others prioritise being a store of value independent of government (eg, Bitcoin). Of course, there is a lot of overlap. The focus for most remains on Bitcoin which is the oldest and biggest with a near 50% crypto market share.

Reasons for scepticism

Bitcoin enthusiasts see it as the future currency and as a way to riches with rapid price gains since inception seen as confirmation. The counter view is that it's just another bubble. Reasons for caution are as follows:

- First, it's not suitable for everyday transactions: Bitcoin transactions are not cheap costing \$US9 at present; they can take 8 minutes or so to complete; its price is very volatile (being roughly 13 times greater than US shares, 12 times greater than gold, 26 times greater than the \$US and 17 times greater than the \$A/\$US exchange rate) suffering 80% plunges in price every few years (in 2011, 2013-15, 2017-18 and 2021-22) rendering it unreliable as a short term store of value. Its limited value for use as a means of payment explains why most Bitcoin transactions are by speculators, not merchants. This is not to say Bitcoin may not have a role in some countries - eg, El Salvador - where the government is not trusted and much of the population lives in the US and faces high transaction costs sending money home. But even in El Salvador merchants have not rushed into using Bitcoin and the US, Europe & Australia are not banana republics!
- Second, there may be a role for cryptocurrency in payments systems (either stablecoins or Ethereum that have moved to speed up their processing), but who knows which one it will be and governments are likely to want to provide it themselves. But even here work on Central Bank Digital Currencies has slowed as its not clear people want to use them as we can already do digital transactions instantly & cheaply. There is almost certainly a role

“ Bitcoins longevity, its ability to rebound to new highs after each setback (so far), the potential use value from blockchain technology in smart contracts and decentralised finance and progress to greater respectability (with regulation on the rise) suggests Bitcoin and cryptocurrencies can't simply be dismissed as just another bubble. ”

for blockchain technology in smart contracts but it's hard to work out which cryptocurrencies it will be.

- Third, given the uncertainty around the use case for cryptocurrencies and particularly Bitcoin (which is less amenable for smart contracts and payments), it's very hard if not impossible to value. Unlike property or shares, it is not a capital asset and so does not generate rents or earnings. Unlike most commodities, it is not used to make things. Most of the major positive news about its value (eg the introduction of Bitcoin ETFs) have nothing to do with its fundamental use or value. Some claim it can generate a “yield” if you lend (or stake) your Bitcoin to traders...but this is relying on them actually making money trading crypto currencies. This makes it impossible to put a price on what it's worth - it could go to \$1,000,000 or \$100.
- Fourth, cryptocurrencies have had various issues with illegal activity and a lack of integrity. While there have been no cases of the Bitcoin or Ethereum blockchains being hacked, there have been high profile cases of people having their private keys hacked, people losing their holding via crypto exchanges and people simply losing their keys. Cryptocurrencies, notably Bitcoin, are also used for criminal activity. One benefit of using a bank to hold your cash is that it provides protection in the event your account is compromised, or you lose your password. Of course, wild west behaviour can be common at the start of new asset classes which may settle with regulation.
- Fifth, the computing power involved in mining for Bitcoin requires significant electricity, just below that of Denmark. This makes it bad for the environment. A single Bitcoin transaction consumes as much energy as 500,000 Visa transactions. Of course, not all cryptos are the same with those using a “proof of stake” (or proof of ownership of a currency) being less energy intensive (but arguably also less secure).
- Finally, Bitcoin and other crypto currencies face numerous threats from governments. Many governments have

been looking at doing CBDCs although progress has been slow. Government's may also crack down on illicit use of crypto currencies, its energy use and regulation is on the rise - although some see this as strengthening it.

Is Bitcoin “digital gold”?

Bitcoins longevity, its ability to rebound to new highs after each setback (so far), the potential use value from blockchain technology in smart contracts and decentralised finance and progress to greater respectability (with regulation on the rise) suggests Bitcoin and cryptocurrencies can't simply be dismissed as just another bubble.

However, the question remains that if Bitcoin is not really digital cash and it's not a capital asset suitable for normal valuation, what is it? The short answer is that it's something to speculate on. The strongest argument for its existence is that it's a digital version of gold and is displacing some of the demand that would have gone into gold. For millennia there has been demand for precious metals, like gold. While gold has a fall-back use as jewellery, its use for this does not explain movements in its price. Rather it has value because enough people have faith in it as a store of wealth which is independent of government - and people buy it not because they see jewellery demand going up but if they believe someone will pay a higher price for it. Some call this the “greater fool” theory.

Apart from not having the fall back of jewellery demand and not being able to see and touch, Bitcoin has many of the characteristics of gold - notably limited supply and independence of government. Bitcoin's resistance to relaxing its proof of work approach has by limiting its ability to be used as cash effectively strengthened its decentralisation and immutability characteristics - making it more gold like (unlike many other cryptos). Like gold bugs it has a similar demand base of people who don't trust central banks and governments. Which partly explains why Bitcoin resembles “more of a cult than a currency” - with a god (the mysterious Satoshi Nakamoto), a belief set and defined behaviours. Critical amongst the latter is to hodl (buy and “hold on for

dear life”) and have faith that new buyers will come along to keep it going to the moon, Of course many might describe this as a giant Ponzi scheme (without the illegality).

Of course, Bitcoin has arguably failed its first big test as a hedge against inflation because as inflation surged in 2022 Bitcoin saw a near 80% fall in value. Gold has also failed as an inflation hedge at various points though, but this has not stopped faith in it. Bitcoin’s rising sensitivity to movements in interest rates suggest its becoming more gold like as rising rates increase the opportunity cost of holding gold or Bitcoin and vice versa for falling rates - like now which has pushed both to record highs.

If Bitcoin is digital gold it could have lots more upside as younger digital savvy buyers favour it over gold. Rough estimates suggest that if Bitcoin were to approach say 25% of the market value of gold its price could rise to \$US160,000. Increasing ease of exposure via vehicles like ETF’s could see it pushed beyond that as buyers extrapolate past gains. But just be aware that owes to an assumption that enough have faith. If investors decide to move on to a new next best thing then watch out below!

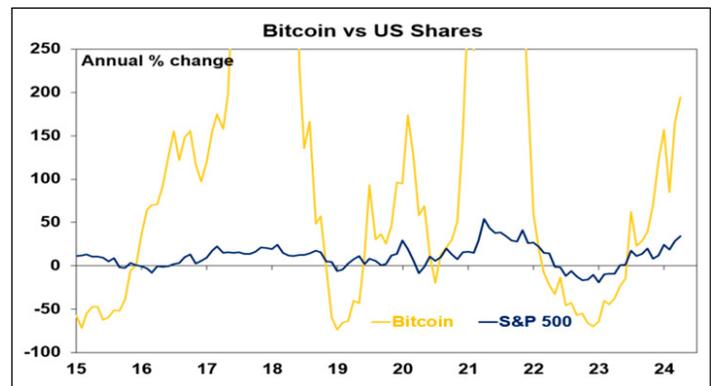
So what does all this mean for investors?

There are five key things to be aware of when considering an investment in Bitcoin or crypto currencies. First, Bitcoin may have a lot more upside: its very momentum driven so its recent gains will attract new buyers; new demand via ETFs and the next “halving” are giving it a push; it tends to run to a four-year cycle which would run into next year; and displacement of gold may have further to go. So far we are yet to see all the crypto ads like in late 2021/early 2022 which suggests its yet to hit a manic phase. It is worth cautioning though that as more own crypos their returns appear to be slowing (as highlighted by the arrows in first chart).

Second, none of this has anything to do with a fundamental assessment as to Bitcoin’s worth which is impossible.

Like gold it depends on faith that more buyers will arrive to push its price ever higher.

Third, it’s hard to work out where to put Bitcoin in a portfolio. It’s too volatile to be a defensive asset like cash. It’s impossible to get any reasonable idea as to what it may be worth or return (unlike shares, property, bonds or regular cash). And since its inception its seen a rising positive correlation with shares (averaging 40% over the last five years) with a beta of 2.3 times shares - so if US shares move 1% it moves by more than twice as much in the same direction - so its a poor diversifier.

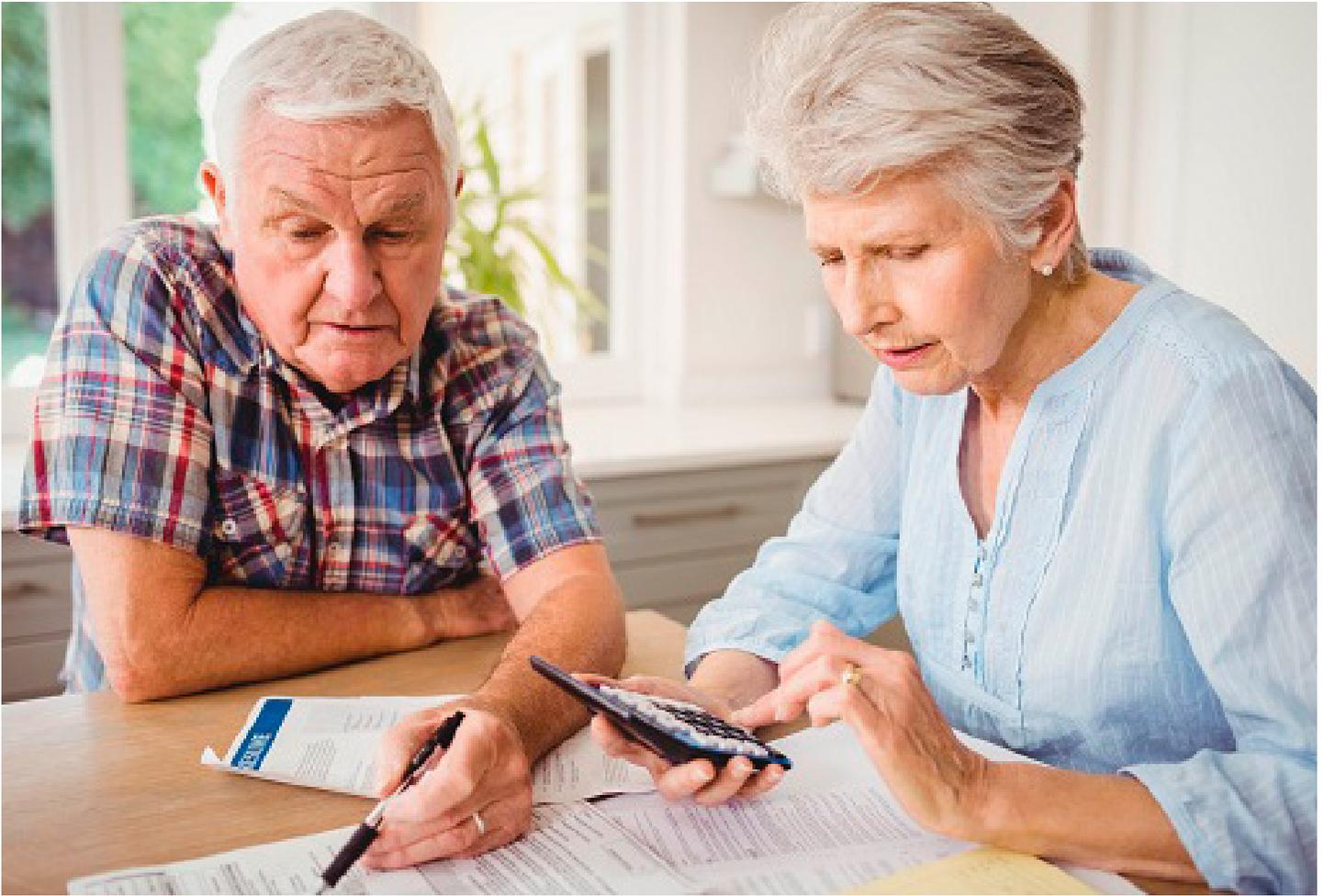


Source: Bloomberg, AMP

Fourth, its extreme volatility means investors should expect a wild ride.

Finally, don’t forget the basic principles of investing - there is no free lunch (high returns mean high risk); past returns are a poor guide to future returns; and if you don’t understand something, don’t invest in it.

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The aged care recommendations that will cost you more

BY RACHEL LANE

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In a significant development for Australia’s aged care sector, the Aged Care Taskforce recently unveiled its Final Report, comprising 23 recommendations aimed at reshaping the fees and funding arrangements governing aged care. While there has been a lot of coverage of the official Recommendations, the devil is in the detail. In the Aged Care Taskforce report, there are a number of unofficial recommendations that could cost you substantially more for aged care. There is also a pivotal question that the report doesn’t answer.

Refundable Accommodation Deposits to rise

Among the recommendations that didn’t make it on to the official list of 23 is an immediate increase in the Refundable Accommodation Deposit (RAD) price threshold

of \$200,000 to \$750,000 from its current level of \$550,000. The report says:

“The Tune Review in 2017 recommended an immediate increase to \$750,000 and indexation over time. While the Taskforce has not recommended a new maximum room price, it considers there is a need for an immediate increase in the rate and indexation over time to ensure it remains constant in real terms. The Taskforce considers implementing the prior recommendation from the Tune review is a prudent first step.”

Presently, aged care facilities must obtain approval for RADs exceeding \$550,000, effectively setting the benchmark for most beds at this price point. This small but significant change could take effect as early as July 1st, with the anticipated introduction of the new Aged Care Act and could see

the price of many beds increase by \$200,000 as a lump sum or around \$16,500 per year for those who elect to pay their accommodation cost by Daily Payment.

Adding to this, the official recommendation from the Taskforce of imposing a 3% per annum levy on Refundable Accommodation Deposits (RADs), capped at 15%, would see the cost of the levy go from \$16,500 per year, culminating in a deduction of \$82,500 over five years, to \$22,500 per year or \$112,500 over five years.

RAD	Annual deduction 3%	Capped at 15%	Refundable amount after 5 years
\$550,000	\$16,500	\$82,500	\$467,500
\$750,000	\$22,500	\$112,500	\$637,500

Presently, the government shoulders 94% of residential aged care costs (\$13 billion), with residents contributing 6% (\$800 million) through means-tested care fees. In contemplating strategies for individual contributions to aged care costs, the Taskforce considered that the government could assume all care-related expenses, with individuals only responsible for accommodation and living expenses.

Means-testing won't just impact the wealthy

While not explicitly recommending the removal of current caps on means-tested care fees, the Taskforce suggested that the government might consider such a measure if it opts against fully funding care. Currently the amount you can contribute towards your cost of care is capped at a daily amount of \$415 with an annual cap of \$32,700 and a lifetime limit (across home care and residential aged care) of \$78,500. Removing the annual and lifetime caps could see someone paying more than \$151,000 per year in means-tested care fees, almost five times more.

The initial response to the Aged Care Taskforce Final Report has, on the whole, been very positive - after all, how could the media or the public disagree with the very simple premise that “Wealthy Australians should pay more for

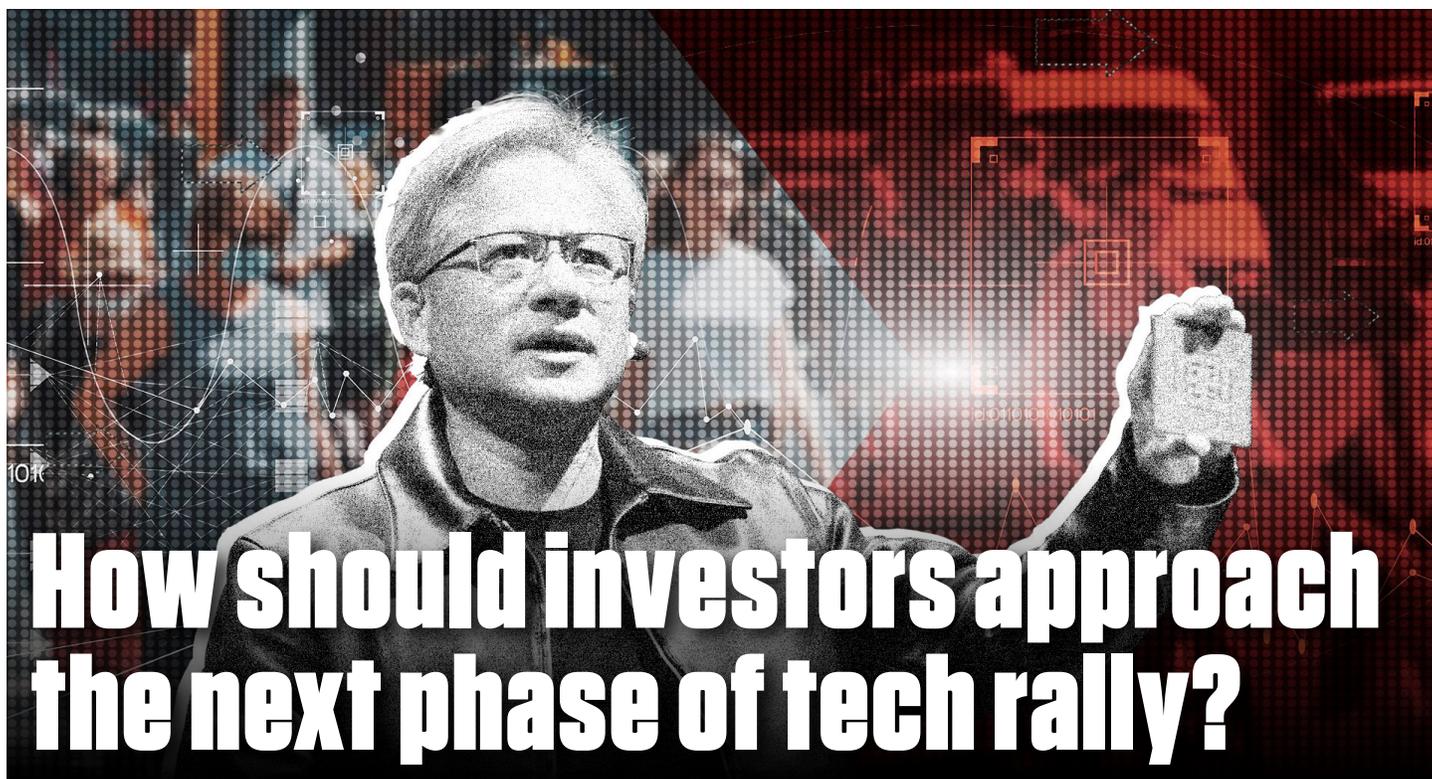
their Aged Care”? But who are these “wealthy Australians”? Under the current means testing arrangements, in order to be considered wealthy you simply need to have assets above \$197,735. This relatively low benchmark of wealth creates what I call “aged care no man’s land” for people with \$200,000 or \$300,000 needing to pay \$550,000 for their aged care accommodation.

The Taskforce didn’t provide details on the means testing for aged care, rather it hinted at a tiered approach based on pension qualification (full pension, part pension, or self-funded) and homeownership for those moving into residential aged care. The Taskforce also raised the prospect of aligning aged care means testing with pension arrangements which could see significant implications for carers and close relatives of aged care recipients, who could lose the ability to exempt the home they live in. Currently the home is an exempt asset while a ‘protected person’ lives there and is included in your aged care assessable assets up to a capped value of \$197,735 when it is assessed.

Who pays what?

Ultimately, the funding of aged care in Australia hinges on a binary equation: how much should the government bear the burden (through taxpayer funds) versus how much should individuals foot the bill. As the government deliberates over which recommendations to adopt, it appears inevitable that the cost of aged care will go up. Ensuring that the higher price equates to better care is crucial, so is ensuring that there is equitable access, and that aged care is affordable.

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How should investors approach the next phase of tech rally?

BY PATRICK POKE

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For over a decade, backyard barbecues and dinner gatherings have been dominated by conversations about the relentless surge in house prices. However, this enduring narrative now finds itself in competition with an equally pressing question: how best to approach the tech rally?

With interest rates seeming to have stabilised and investors awakening to the immense potential of artificial intelligence (AI), the ‘Magnificent Seven’ stocks drove an impressive 53.8% surge in the Nasdaq-100 Index in 2023¹ and propelled the S&P 500 past 5,000 for the first time in February 2024.

Nevertheless, amid the massive gains and optimistic projections, a number of key questions have emerged. Has the ‘easy money’ been made? Is it prudent to overweight Nvidia and other AI leaders among the Magnificent Seven? Is there better value elsewhere in the market?

In this blog, we assess the pros and cons of the tech sector’s performance and look at ETF ideas for investors looking to gain exposure to the sector.

Weighing the positives

The surge in ‘Big Tech’ stocks has been remarkable, with some stocks experiencing significant gains. For instance, Nvidia’s stock has more than tripled in the 12 months to

29 February 2023, while Meta Platforms has more than doubled. Amazon, Microsoft, and Alphabet are up over 50% over the same period.

If we consider where we were this time last year, arguments could be made that the tech sector’s surge appears justified.

First, after a period of intense interest rate hikes and recession fears, the sector was undervalued. However, the strong structural growth story and key themes like AI, digital advertising and cybersecurity, have so far remained intact.

Second, as indications of a halt in rate increases emerged from central banks in late 2023, many investors sought to capitalise on relatively appealing valuations, particularly among AI leaders such as Amazon, Apple, Alphabet, Microsoft, Meta, and Nvidia.

Third, tech stocks’ earnings in Q1 2024 showed significant growth and bullish outlooks, with Nvidia’s revenue soaring by 217%² over the 12 months to Q4 FY24, prompting the company’s CEO Jensen Huang to declare that “accelerated computing and generative AI have hit the tipping point.”

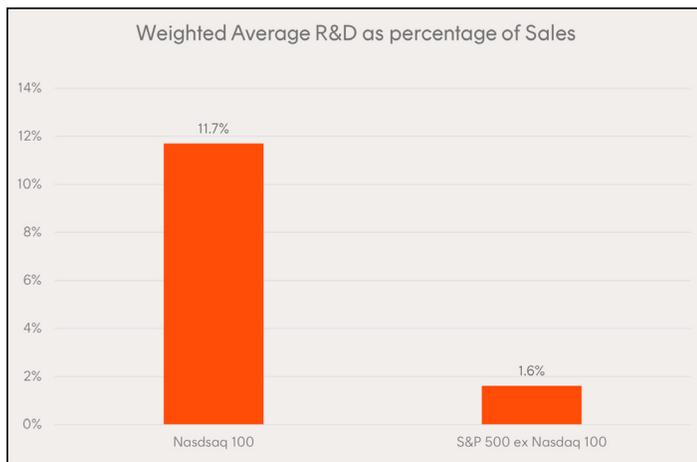
Lastly, companies in the Nasdaq-100 Index invested far more in research and development (R&D) than their peers in the S&P 500 Index (as of 30 June 2023), as shown in the chart below. R&D is a key driver of growth, and high spending may reflect tech-oriented companies’ intention to keep innovating with the aim of creating more and bigger revenue streams.

Annualised historical earnings growth (for the 20 years to

“When considering both the upsides and downsides, it’s clear that the tech sector, particularly the AI market, presents significant long-term growth potential. However, investors should be mindful of the risks and how much has already been factored into share prices when determining their allocation.”

31 December 2022)³:

- Nasdaq-100: 19.7% p.a.
- S&P 500: 9.5% p.a.



Nasdaq-100 companies and S&P 500 excluding Nasdaq-100 companies. S&P 500 weighted average R&D inclusive of Nasdaq-100 companies as a percentage of sales is 8.1%.

Weighing the negatives

Despite the prevailing optimism, there are risks on the horizon.

First, the sustainability of the current market rally heavily relies on central banks cutting rates and achieving a soft landing, a scenario already factored into current share prices. However, if central banks fail to meet economists’ expectations due to lingering inflation, it could potentially undermine the ongoing rally.

Second, geopolitical events pose a significant concern. Case in point, the US has imposed bans on Nvidia, Intel and AMD, preventing them from selling their top-tier chips to China⁴. Should these restrictions escalate into a full-blown trade conflict, it may significantly hamper the revenue streams of chipmakers and other tech firms, potentially sparking volatility.

Third, a case can be constructed for a shift from growth

to value stocks amid economic uncertainty. The chart below shows the ‘Magnificent Seven’ contributed to almost half of the S&P 500’s returns in 2023, indicating a disparity where non-tech stocks have trailed.



Source: Bloomberg, Betashares. As at 29 February 2024. Past performance is not indicative of future performance of any index or fund.

How should investors approach the tech rally?

When considering both the upsides and downsides, it’s clear that the tech sector, particularly the AI market, presents significant long-term growth potential. However, investors should be mindful of the risks and how much has already been factored into share prices when determining their allocation.

For investors seeking a strong emphasis on AI or aiming to integrate this theme as a satellite position, Betashares Global Robotics and Artificial Intelligence ETF (ASX: RBTZ) presents an option. While Nvidia currently holds the top spot in the fund’s portfolio, it also provides exposure to a variety of other significant players in the AI and robotics sector, including medical devices company Intuitive Surgical and factory automations leader Keyence.

Betashares Nasdaq 100 Equal Weight ETF (ASX: QNDQ) offers investors a more diversified exposure overall to non-financial US equities listed on the Nasdaq market. With each stock allocated a 1% weighting at every rebalance, there is low stock concentration, mitigating overexposure to the ‘Magnificent Seven’.

Alternatively, investors seeking to diversify their global equity exposure may consider Betashares Global Cash Flow

Kings ETF (ASX: CFLO). This ETF focuses on companies known for their robust free cash flow (FCF) generation and relatively low levels of debt, serving as an option for a core global equity allocation.

CFLO's holdings encompass not only tech giants with strong FCF like Microsoft but also notable non-tech firms such as Procter & Gamble, American Express, and Novartis.

Top 10 holdings of RBTZ, QNDQ and CFLO

The following table offers further insight into the level of diversification within the above-mentioned ETFs' top 10 holdings. It's important to keep in mind that a higher concentration could yield greater returns if those stocks with large weightings continue to perform strongly, whereas a lower concentration may potentially result in reduced volatility.

RBTZ	WEIGHT	QNDQ	WEIGHT	CFLO	WEIGHT
Nvidia	22.30%	Nvidia	1.70%	Costco Wholesale	4.50%
Intuitive Surgical	10.20%	Constellation Energy	1.40%	Microsoft	4.30%
Abb	8.30%	Advanced Micro Devices	1.40%	Visa	4.20%
Keyence	7.00%	Meta Platforms	1.40%	Novo Nordisk A/S	3.90%
Fanuc	5.30%	Marvell Technology	1.30%	Accenture Plc	3.50%
Uipath	4.00%	Doordash	1.20%	Adobe	3.40%
Smc	4.00%	Netflix	1.20%	Alphabet	3.40%
Dynatrace	3.80%	Applied Materials	1.20%	Unitedhealth Group	3.20%
Yaskawa Electric	3.70%	Asml Holding	1.20%	Procter & Gamble	3.10%
Daifuku	3.30%	Lam Research	1.20%	Cisco Systems	2.80%

Source: Betashares (as at 6 March 2024). Excludes cash. Subject to change.

Final thoughts

Whether you've already benefited from the tech rally or are considering investing in the sector, it's prudent to plan your next move carefully.

One approach is to consider thematic ETFs for satellite exposure or choose funds that offer diversification across the broader tech industry and global equities. This strategy allows the integration of the tech theme while mitigating concentration risk within your portfolio.

BetaShares is a leading Australian fund manager specialising in exchange traded funds (ETFs) and other Funds traded on the Australian Securities Exchange (ASX). Since launching their first ETF more than a decade ago, BetaShares has grown to become one of Australia's largest managers of ETFs.

1. Source: Bloomberg. Past performance is not indicative of future performance of any index or fund. Reflects performance of the index, and not any fund. Does not take into account any fund fees and costs. You cannot invest directly in an index.
2. Source: Nvidia
3. Source: Nasdaq. Past performance is not indicative of future performance of any index or fund. You cannot invest directly in an index.
4. Source: CNN

Q&A: Ask a Question

Question 1

My friend who have a financial adviser have told me they are investing through wrap accounts. What is a wrap account and what are the benefits of using one?

A wrap account is a centralised investment account offered by financial institutions or investment firms. It allows you to consolidate your various investment holdings, including shares, managed funds, ETFs, and term deposits, into a single platform. The benefits of using wrap accounts are significant. Firstly, they offer diversification across different asset classes and geographic regions, facilitated by access to a wide range of investment options. Additionally, wrap accounts can provide professional investment management services, reporting and customisation, which can help you construct tailored portfolios.

While these features can be useful for many investors, the platforms generally cost more than other investment options such as a share broker and the features may not be valuable for all investors.

Overall, wrap accounts can offer you a convenient, customisable, and efficient way to manage your investments while giving you access to professional expertise and diversification opportunities. Please discuss the appropriateness of using one with your financial adviser.

Question 2

Everyone including my financial adviser keeps telling me to get my Will sorted out with an estate planning lawyer. Why is it so important for me to have a will?

Having a Will grants you control over how your assets and possessions are distributed after your death, ensuring that your wishes are followed. If you pass away without a Will, you are considered dying 'intestate' and your family must apply to the state court who will then determine how your assets are split.

Clearly outlining your wishes, you can minimise family disputes and conflicts that may arise regarding the distribution of your estate, providing clarity and reducing the likelihood of legal challenges. Additionally, a Will enables you to appoint executors and trustees to administer your estate and manage trusts for beneficiaries, ensuring that your affairs are handled according to your instructions. Through tax planning strategies incorporated into your Will, you can also minimise estate taxes and maximise the value of assets passed onto your beneficiaries, ultimately providing peace of mind knowing that your affairs are in order and your loved ones will be taken care of according to your wishes.

Question 3

I'm considering winding up my Self-Managed Superannuation Fund (SMSF). I am wondering what are some valid reasons to wind up my SMSF?

Winding up a Self-Managed Superannuation Fund (SMSF) may be appropriate for several reasons. Significant changes in your circumstances, such as shifts in your financial situation or investment objectives, could make the SMSF structure impractical or no longer suitable. Additionally, if the costs associated with managing the SMSF outweigh the benefits, winding up the SMSF can alleviate ongoing financial strain.

Moreover, the complexity and administrative burden of managing an SMSF may become overwhelming, prompting the decision to wind up the fund if you are unable or unwilling to fulfill your responsibilities effectively. Lack of investment diversity or the inability to manage investments may also lead you to consider winding up the SMSF and consolidating assets into a professionally managed superannuation fund. Lastly, regulatory changes, retirement planning considerations, and estate planning goals are other factors that may influence your decision to wind up an SMSF.

We strongly advise you see your financial adviser before making any decision to wind up your SMSF.

If you have a question that you would like to see answered in **Wealth Adviser**, please send it through to centraladvice@wtfglimited.com.