Cuffelinks
Connecting investors with ideas

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Outperformance: unique skill or free gift?

Chris Cuffe

In my 25 years in wealth management, the best conference I have ever attended was the FTSE World Investment Forum in May 2011. The main presenters were world leaders and academics from the investment management industry, and in this article, I will be drawing on the findings of two of them: Elroy Dimson of the London Business School and Roger Ibbotson, founder of Ibbotson Associates and Professor at Yale School of Management.

Let's start with their conclusions. The sharemarket commonly measures the outperformance of active fund managers by the extent to which they beat an index, and refers to this as the *alpha*. The ability to produce alpha is generally attributed to the unique skill set of a fund manager. The presentations suggested this is not necessarily so. There are proven contributors to alpha which are persistent and systematic, and should not be attributed to manager skill, and hence are not alpha in the true sense of the word. These factors include:

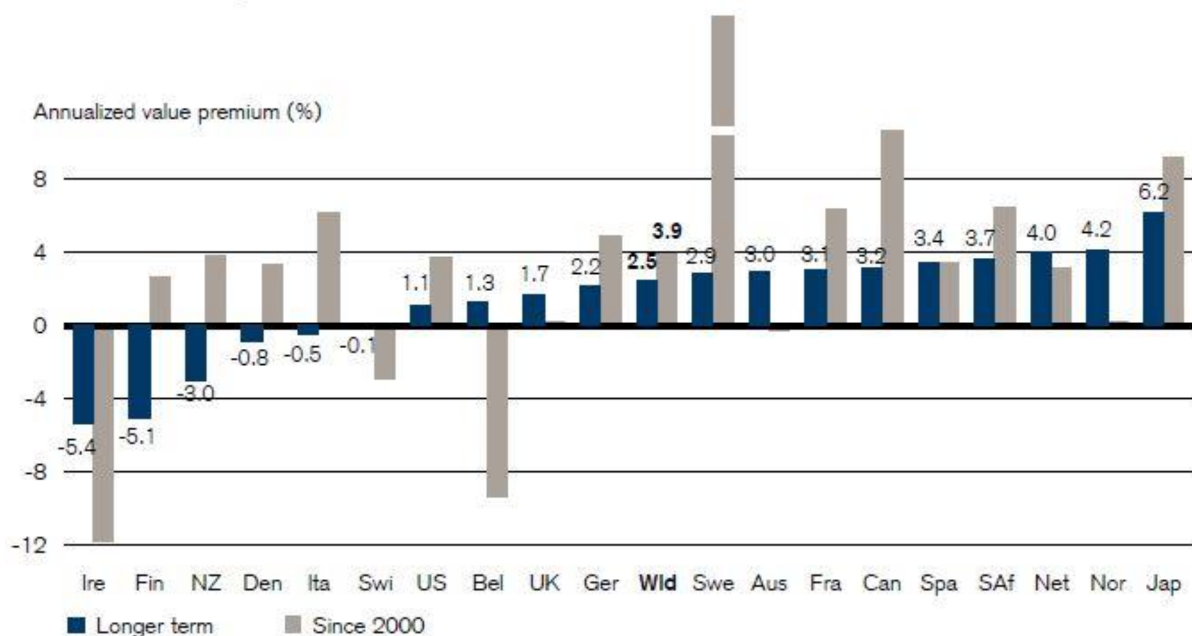
- value
- dividend yield
- small companies
- momentum
- liquidity

In other words, the 'alpha' from these factors can be systematically extracted at low cost without any particular stock-picking skills from the fund manager, and in my observation of markets and fund managers, I agree with the merits of this argument. Let's briefly examine each of these factors individually.

Value

Without becoming overly technical, a 'value stock' has a high ratio of its book value (that is, the net asset value of the company, calculated by total assets less intangibles and liabilities) to its sharemarket value. It is an indication whether a stock is under- or over-priced. A stock with a lower ratio is called a 'growth stock'. In Australia, similar studies use low P/E ratios to define a value stock.

Dimson reported on his studies based on markets in 22 countries and regions from 1900 to 2011, and showed that in the US, value stocks beat growth stocks by 3.1% per annum, and in the UK by 5.8% per annum. These percentages produce extraordinary return differences over long periods, although it does not occur over all time horizons. For example, the long term outperformance for Australian value stocks is 3% per annum, but a small negative (that is, growth outperformed value) since 2000, as shown below.



Source: '111 Years of Stock Market Regularities', Elroy Dimson, London Business School, May 2011.

Dividend yield

Again, Dimson found systemic outperformance for high dividend-paying stocks. In the USA, high-yielders beat low yielders by 1.9% per annum, in the UK by 2.7% per annum and in Australia by a healthy 5% per annum, although significantly less since 2000. Furthermore, when measured against the volatility of returns, high-yielders had lower risk and therefore delivered a better reward for risk.

Small companies

Dimson reported that small companies beat large companies on average around the world by 0.34% per month, and in Australia by 0.52% per month. Obviously, when the research combined size and value v growth, small-value is a major winner.

Momentum

It's almost embarrassing for an investment professional to explain momentum. It appears that many investors buy shares or commodities simply because they have recently risen in price, and

therefore have their own ‘momentum’. There are overlaps to behavioural theories such as ‘following the herd’ and ignoring one’s own better instincts. Dimson wrote, with colleagues from the London Business School, in a 2007 research paper,

Momentum, or the tendency for stock returns to trend in the same direction, is a major puzzle. In well functioning markets, it should not be possible to make money from the naïve strategy of simply buying winners and selling losers. Yet there is extensive evidence, across time and markets, that momentum profits have been large and pervasive.

Dimon’s research suggested past winners have beaten past losers for over 100 years, in the US by 7.7% per annum, and to a similar extent in Australia, although the returns come at a cost of higher turnover.

Liquidity

Roger Ibbotson argued that more liquid assets are priced at a premium, and less liquid are at a discount and therefore offer a higher return. He noted that liquid securities are easier to trade with lower market costs and are more desirable to high turnover investors, but as a result they are higher priced for the same expected cash flows. Thus, less liquid investments are better for longer term investors.

Ibbotson measured 3,500 US stocks from 1972-2010 and divided their liquidity (measured by daily trading volumes) in quartiles. The lowest quartile liquidity consistently outperformed. He applied the same reasoning to US equity funds and concluded that those with less liquid holdings also outperformed. He argued that as the liquidity (trading activity) of a stock rises, its valuation rises and investors pay too much for it.

His main message was do not pay for liquidity you do not need. Liquidity needs to be managed like any other risk, and changing stock liquidity creates return opportunities.

With trillions of dollars at stake in the investment management business, not to mention a few hundred thousand high-paying careers, these systemic advantages have been trawled over by analysts for decades. Some people devote their entire lives to one factor, and would probably be horrified by my one paragraph summary. In my mind’s eye, I can see a university academic with steam coming out of his ears as he waves around his 100-page thesis on momentum. Anyone is welcome to comment, and we will spend more time on each factor in other editions of *Cuffelinks*. My report on the conference is not an academic study of the literature, and no doubt an analyst can cut the data any way to produce other results.

The main conclusions I took from the presentations are that:

- there are highly-researched factors which have, over time, generated outperformance, although not over all time periods
- you should consider these factors when assessing whether an active fund manager really has any skill, or are they extracting a factor which should be more cheaply available
- there are some funds that do not need liquidity that may be able to extract a premium (for example, Listed Investment Companies traded on the market are closed-end and do not face redemptions, but do they extract a liquidity premium?).

Other presentations at the Forum focussed on keeping costs low and risk diversification, emphasising the need to access these factors at competitive costs and across many sectors.

Is defined contribution superannuation fit for retirement?

Jeremy Cooper

Many people ask me what I think about Stronger Super and the legislation based on the Cooper Review recommendations. Overall, it looks pretty good, although naturally, various compromises and changes of emphasis and approach have occurred here and there. Of course, we also need to see it work in practice.

The big disappointment, though, is retirement. Here, it seems super funds weren't ready or the changes looked too dramatic. Whatever the reason, we are left with an unfinished retirement system; just a continuation of the accumulation phase. Like the 401(k) regime in the United States, our defined contribution (DC) system was never designed to provide retirement income, but just a lump sum to retire with.

We now realise there is a lot more work to be done in building a proper retirement system. That said, I do acknowledge Bill Shorten's efforts in pursuing, through the Superannuation Roundtable, ways that new retirement income products could be brought to market. So, progress is being made.

But, what is wrong with DC retirement savings schemes? Well, think of the age pension. Its cash flows are fortnightly; it is AAA-rated; and it keeps up with price and wage inflation. It is the gold standard of retirement products, but the obvious problem is that it is only a safety net. Nobody aspires to live at the standard of living afforded by the age pension. But, the point is all about the design features.

Can the private sector create products that work like the age pension? The answer is that Australian life insurance companies can deliver private pensions that are effectively (apart from obvious differences) the same as the age pension. Okay, what then? Well these need to be integrated into both the super system and into our consciousness: a partial 're-intermediation' of super, accessing specialist balance sheets to provide the secure income in retirement that a purely DC approach cannot by itself deliver.

Governments and corporations around the world realised some time ago that defined benefit (DB) pensions that involved carrying market, inflation and longevity risk for people in retirement were simply too risky and expensive other than for some specialists.

DC seemed like the perfect solution. Because a DC super scheme does not aim to provide the retiree with a particular level of income in retirement, there is no target from which there can be a shortfall.

DB plans pool the risk related to an unknown length of life for each person across the pool, while DC plans leave it to the participants to deal with on their own. This makes most DC retirees like small insurance companies taking on their own longevity risk without any additional capital or the skills to do so. As a person ages, longevity risk overtakes even market risk as the key risk in retirement.

DC also tends to encourage a 'wealth management' mindset in retirement, as opposed to a 'retirement income' approach. Under the latter approach, retirees get regular income and protection from inflation and longevity risk as a 'floor'. Only after this floor has been secured and precautionary liquidity is available do they consider exposure to growth assets. There is quite a difference between the two approaches.

Are target date funds the solution? Partly, but it depends on what the retirement solution looks like. Asset allocation alone doesn't go the distance in protecting against all of the risks in retirement. If a target date fund is merely reducing exposure to volatile asset classes as a person ages, then it is helping with some of the issues – such as sequencing risk and portfolio size effect - but it does not address longevity risk or exposure to inflation.

What is it about retirement that makes a DC fund that is relying solely on asset allocation struggle to provide an adequate solution for retirees? In retirement:

- The 'financial dynamics' of accumulation are reversed. There is generally no regular wage or salary (or other income) and the retiree starts drawing down on their savings to fund consumption. This makes it a fundamentally different proposition from accumulating savings and introduces new risks. For example, dollar cost averaging works in reverse, against the retiree's interests.
- Retirees are exposed to longevity risk: the risk that they outlive their savings by reason of increasing life expectancies.
- The sustainability of retirement savings becomes a new and important concept. This has two elements: the probability of success of the retirement plan (expressed as a percentage of likelihood of reaching a particular age and still being able to access sufficient income) and the range of potential outcomes based on market returns that deviate from long term averages.
- Retirees' aversion to loss is greatly increased. In a large US study carried out in 2007, just under half the retirees surveyed said they would be unwilling to risk even $10 in a bet that offered a 50% chance of winning $100.
- Close to retirement, more of a retiree's money is exposed to potential losses and so negative market movements around that time have the most adverse impact on sustainability of cash flows.
- A retiree's ability to recover from poor investment returns (or take advantage of lower market prices) is generally limited.
- Inflation takes on a new dimension because the retiree is disconnected from wage rises and can generally only maintain purchasing power via the age pension or explicitly inflation-linked investments. Contrary to a widely-held view, equities do not provide an adequate hedge against inflation.
- Plans based on long term averages and notions like 'investing for the long term' are generally inappropriate in retirement. This is because approximately half of a typical retiree's savings are consumed in the first 10 years; later retirement spending is funded from dollars created by compounding returns during retirement.

- The financial needs of retirees differ. The spending profile for someone with $1,000,000 in super won't be the same as someone who has only $100,000, but it won't be ten times as much though. A different rate of outflow from the investment portfolio might require a completely different investment mix to get a suitable outcome. The shape of cash flow is important in retirement.

There are no universal solutions to funding a retirement, but it is critical that policy makers address these matters with the increasing number of baby boomers approaching retirement. Over 60% of the value of the superannuation system is owned by the 45-65 year-old cohort.

Part of the solution will lie in thinking about the partial re-intermediation of our DC super system so that retirees get a promise of a certain level of income above the age pension that will last as long as they do.

Jeremy Cooper is Chairman, Retirement Income at Challenger Limited.

Disclosure: Jeremy Cooper is a full-time employee of Challenger Limited and has interests in equity securities issued by Challenger, which is an issuer of annuities in Australia.

Superannuation is losing its lustre

Don Stammer

The framework for Australia's retirement policy set up in 1992 was original and even world-leading. It offered great promise that, once the new arrangements settled in, the retirement needs of our ageing population would be well-provided.

Alas, in recent years, our retirement arrangements, and particularly the superannuation component, have been losing their lustre, because of the many changes in regulation already made and in prospect.

The framework proposed twenty one years ago

The original framework had four components.

First, the taxpayer-funded age pension would continue to provide for a relatively frugal lifestyle and be means-tested. This was in line with the traditional approach in this country to the age pension, but stood in contrast with the higher, and universal, age pensions paid in much of western Europe which, in recent years, have contributed to government financial problems across a lot of Europe.

Second, there would be compulsory contributions into superannuation, mostly paid from employers, with recognition these payments would lessen the rate of increase in average wages. These compulsory contributions would start at 3% of wages and the required minimum would be raised, over time, so that a large proportion of the future retirement needs of middle Australia would come from the compulsory contributions and the accumulated earnings on them.

Third, there would be tax benefits provided for superannuation savings, to boost the return on compulsory contributions and to give some encouragement for voluntary savings in superannuation.

The fourth feature of the proposed retirement arrangements attracted surprisingly little attention at the time: most Australians would have defined contributions superannuation rather than the defined benefits superannuation that traditionally applied to the small proportion of the workforce who had participated in superannuation.

In the future, the amount of superannuation most of us would draw on in retirement would be defined by the amount of contributions paid into our superannuation accounts and the accumulated earnings on those funds.

The retirement framework is not working out as well as was hoped

But 21 years on, the goal of sustainability in Australia's retirement system is proving to be elusive.

In part, that's because we are, on average, living much longer and have more years of retirement to fund than was earlier expected. For the most part, that's a good problem to have. (As average longevity is likely to rise further in the future, let's make enough allowance for that, both in thinking about future strains in the retirement system and when individuals plan their own retirement).

But there are other and more deep-seated problems. The rules for superannuation keep changing, making it unnecessarily hard for people to plan for their retirement years. For example, there's the imposition of a cap of $25,000 on the annual tax-favoured contributions into an individual's superannuation fund (including, of course, the contributions paid by employers on behalf of their employees).

This will prevent many people, particularly parents in their late fifties and sixties who are better placed to save when their offspring have finally left home (some for the third time) from building up enough superannuation to carry them through what could be several decades in retirement.

There have been widespread suggestions that taxation of superannuation will be increased in this year's budget, in part because the government needs additional revenues to fund existing and proposed spending programmes and in part because the current tax treatment of superannuation is said to unreasonably favour high income groups.

Taxation of superannuation: the main options

Superannuation has four possible taxation points:

- contributions
- investment earnings
- benefits
- death of the superannuation member

My preference was always to have superannuation taxed when the benefits are paid, whether taken as lump sums or as superannuation pensions.

But the decisions of successive governments have left us with taxation arrangements that run as follows: there's taxation (at rates of 15% or 30% depending on the income of the contributor) of most money going into superannuation funds; also, investment earnings are taxed while the individual's superannuation is in accumulation phase; but superannuation benefits paid to people aged over 60 are untaxed; and tax applies to most undrawn, tax-benefited contributions left in the estate of superannuation members when they die (any taxable component of superannuation benefit not paid to a dependent spouse or minor child is taxed at 16.5%).

The exaggerated numbers of taxation foregone

The Federal Treasury publishes figures each year for 'taxation expenditures', or how much tax revenue is forgone by existing tax concessions. I have trouble accepting the Treasury's estimates that $30 billion (and soon to be $40 billion) a year of tax revenue is forgone because of the favoured taxation treatment of superannuation – estimates that the government is using to justify increased taxation of superannuation.

Those calculations make inadequate allowance for the front-ended taxation of superannuation. They assume the $1.5 trillion of assets currently held in superannuation funds would be invested elsewhere with all earnings taxed at marginal rates, and none would be spent or invested in tax-effective ways. In addition, the calculations ignore future collections of tax from estates.

Even without any further tax imposts on superannuation, superannuation isn't the preferred vehicle for additional retirement savings it was intended to be. Many Australians now find they'd be better off putting further saving for retirement outside rather than within their superannuation account.

An increasing number of Australians will even find they'd improve the after-tax returns on their investments by moving some current savings in superannuation to other categories of their wealth holdings.

What's needed?

It would be great to see a review and renewal of Australia's retirement system, with:

- caps on life-time contributions to superannuation set at a level that permits adequate self-financing of retirement
- taxation arrangements leaving superannuation as the preferred vehicle for retirement savings
- fewer year-by-year changes in the design of retirement arrangements
- the ages for various entitlements to the age pension and superannuation moving up in parallel with average longevity.

Sadly, breathing this new life into the structure of retirement policy would require standards of leadership and bi-partisanship lacking in Australia these days.

Don Stammer is an advisor to the Third Link Growth Fund, Altius Asset Management and Philo Capital Management. He writes a weekly column on investments for The Australian newspaper. The views expressed in this column are his alone.

Demographic insights: living longer with low growth

Bruce Gregor

Australia is at a critical point on four fronts - economic growth, capital allocation, public finance and personal management of retirement income. To see how this position has developed we need to look beyond the 2008 GFC and commodities booms and examine longer term demographic changes and their effect on markets. I will examine each of these four aspects in turn and make some comments on what actions could be taken by Australian governments and individuals to moderate potential problems.

Economic growth

For too long public policy in Australia has focused on headline (real) GDP growth (rather than GDP per capita). This disregards important changes in demographic composition. For example over the past 10 years, headline GDP growth was 3% pa while GDP growth per capita was only 1.4% pa (from RBA data to September 2012). This difference is due to population growth adding to the population faster than total GDP is growing. Australia is one of the highest net migration countries compared to other developed economies as a percent of population. Our population has also maintained higher headcount than some others because of extended lifetimes.

If we look at a country like Japan that has negligible migration but now has the most aged population in the developed world, its latest (OECD 2011) 10 year GDP growth rate and per capita GPD growth rate are equal at about 0.7% pa. Due to low fertility and an extreme aged structure, Japan is now producing negative annual population change.

Before we get to the future implications for Australia, we need to factor in one more demographic element in the mix. When a country's age structure becomes skewed towards older ages, the consumption mix in the economy changes. Income per capita is lower in older age groups and at lower income levels more spending occurs on food and essentials versus 'other' consumables. If there is a lesser demand for consumables, the size of the total market for domestic consumption (per capita) will reduce. The narrower range of consumables stimulates less demand.

At the present time Australia's ageing structure is an amber light stage with 14% of total population aged 65 plus. Japan reached this level in 1995 and is now at 24%. My population projections using ABS mid-range assumptions show that Australians aged 65 plus will be 24% of the population in 2055. To allow comparison to Japan, and allow for zero migration, the 24% figure is reached 20 years earlier in 2035.

So ignoring the short term surface ripples of mining cycles and financial volatility, my view is that demographically-driven domestic demand in Australia over the next 10 years will generate significantly lower growth in GDP per capita. This has little to do with labour productivity – it is pure demographics.

I now look to external factors and the long-term global investment markets outlook. The best recent examination of this by Elroy Dimson and his team at London Business School which has just been published in the 2013 Credit Suisse Investment Returns Year Book. Their conclusion for future average returns in major investment markets over the next 20 to 30 years is for 3 to 3.5% pa real equity market returns and for about 0.5% pa real return from bonds. This compares to the period since 1980 to date which averaged just over 6% pa real return in both equities and bonds.

In summary, economic text books and investment models based on the last 30 years are likely to be of little worth in charting the life course over the next 30 years.

Capital allocation

Australia's aggregate household balance sheet has two big capital items – superannuation assets and residential housing.

Superannuation assets were valued at $1,500 billion as at September 2012 – almost identical to both annual GDP and the value of the ASX-listed shares. The majority of superannuation assets (excluding a shrinking defined benefit component) can be allocated (and after age 60, spent) at the whim of households. These are assets which in the main were compulsorily acquired by superannuation guarantee contributions or involuntarily accumulated in conjunction with salaried employment.

I believe the job of administering and investing these assets with major funds is superior to putting them into federal government consolidated revenue. However, it seems to me we have reached a stage where some mandated investment allocation of part of these funds (say 30%) should be directed to balancing out the aforementioned adverse economic effects of ageing demographics. I support privately managed rather than using the Future Fund. Its investment mandate and governance has little relevance to the future.

How this directed investment is done needs more debate. It should not be too difficult to devise a scheme of targeted infrastructure development bonds and longevity reinsurance bonds backed by government guarantees (like we now have for bank deposits and flood and terrorist reinsurance). Left as it is, super assets will force up prices for domestic listed investments which will then offer lower long term returns than currently priced in.

With regard to housing, the average Australian house price is currently about 8 times annual wages whereas 30 years ago it was 4.5 times. Whilst maybe you get more house in the 'average' these days, young couples just want a modest initial residence close to work and child care. This is becoming an impossible dream that is stalling young people from settling into productive occupations and starting families. For older age workers in outer city suburbs living in their 1980's two storey McMansions, the position is also less than ideal. As they age and their children move out they are thinking single storey close to public transport. Apart from massive infrastructure spend, big migration increases and forced relocations, there appear to be few palatable solutions to facilitate redistribution of housing options between these two groups.

So in my view we have two major capital items not optimally allocated for the future, superannuation assets and residential housing.

Public finance

Income tax is collected by the federal government. It only really needs 75% of what it collects to cover its primary responsibilities in defence, social security, health and education and the rest should go to the states. States and local councils rely on the residual of federal collections as they have limited means of raising taxes to cover their responsibilities, although they do now get GST collections. In past high growth times, federal government has been able to gain a rising dividend from 'bracket creep'. This will not be available in a low growth environment. Also the GST will suffer lower growth in an ageing economy because of the exclusion of food and health expenditure.

Politicians need to sit down with local electors and have an adult town hall chat about this situation. Instead, the head in the sand is clear to see on the website of the Australian Office of Financial Management. Federal borrowings are now at $260 billion (February 2013) compared to a standing start at $50 billion five years ago. A number of states now have substantial borrowings, part of which must be covering shortfalls on regular expenditure.

Personal management of retirement income

Most people arrive at the end of full-time work having had someone else worry about how their pay reaches their bank account. Few are well prepared to manage this task when retirement arrives.

Whilst the $1,500 billion in superannuation assets is a big item, it is very unevenly distributed. About 60% of this 'belongs' to a well-endowed 20% of the population (SMSFs, public servants and military super). The majority of people retiring over the next 20 years will have modest balances. When we overlay this with the future low growth world and the variability of prospective life expectancy, retirement income planning is really 'mission impossible', despite the best efforts of financial planners.

One way to make this money go further is to 'recycle' part of what's left for the benefit of the surviving population when someone dies. There are two established ways of doing this. The best way is by compulsory annuitisation of part of superannuation at retirement. A less popular way of recycling is by applying a rate of death duties on super. There's another useful if unpopular topic for that local town hall meeting.

I am fairly pessimistic of this retirement income issue being resolved by public policy. I expect that the 20% higher socio economic group will be able to deal with this acceptably. For the remainder of the population, it will require a more innovative and diversified life planning approach to cope with retirement living. This may involve some continuing employment, renting out rooms in houses, multi-generation households and formal paid arrangements for grandchild and aged care. Public finances will not allow expansion of the age pension to cover this gap.

For further writings by Bruce Gregor on similar topics, see his website www.findem.com.au.

Is your super fund adequately diversified?

Rick Cosier

Before SMSFs took off, the vast majority of super fund members were in 'balanced funds' whose assets included sizeable allocations to bonds, global shares and listed property. According to the ATO December 2012 estimates, only 14% of SMSF assets are now in managed funds, with 29% in cash deposits, 32% in Australian shares and 15% in direct property. Another 4% is in listed trusts, likely to be mostly Australian shares.

Over the past few years, these percentages have not changed much, and the evidence is that these allocations have delivered better returns than most of the balanced funds on the market. SMSF investors have turned their backs on managed funds and global shares.

However, there are danger signals ahead. Firstly, cash rates are now barely covering inflation. Unless you have a lot of money and are only interested in wealth preservation, your superannuation could be going backwards in real terms. The costs of essentials such as housing, food, gas, electricity and healthcare may well rise faster than the CPI figures.

Secondly, we are a small country whose sharemarket consists of a few high profile sectors. History is full of commodity price booms and busts so BHP and Rio are not immune even though Chinese demand is unlikely to end any time soon. The top ten stocks include four banks whose share prices have rocketed in recent times due to the attractive dividend yields on offer.

The thinking seems to be that the banks are so secure that dividend yield is pretty much the same as term deposit interest. The potential problem is that they are completely different. Interest is a government guaranteed (on deposits below $250,000) payment in exchange for a 'loan'. Dividends

are payments made to shareholders based on the profits generated by the business. Sometimes these dividends are no more than confidence-boosting payments which have no relation to profits. If profits fall, then it is probable that dividends will fall, or possibly not get paid at all.

Australian banks appear to be well run, but are the most expensive in the world. You only have to look at the share price of Apple to realise that buying a good company at a bad price can turn ugly. On 19 September 2012, Apple's share price was $702. On 25 January 2013 sales were still rising, but the share price was $435, 38% lower.

'Direct' property is the third major asset class favoured by SMSFs. Despite all the media focus, residential property only represents 3.5% of SMSF assets, with the majority in 'business real property'. Owning your business premises via superannuation is a reasonable strategy, but can be very risky if it comprises most of your fund.

Where's all this going? Well, my points are these:

1. Based on current life expectancies, one spouse will probably live past 90. In the current low interest rate environment, having 29% in cash deposits could mean that your money runs out too soon.
2. Investing 30% of your super in Australian shares means that you are probably hanging your hat on the performance of a few companies in two or three sectors, if you have an index-like portfolio. The big four banks, BHP and Telstra account for almost 40% of the ASX200 and it's a fair bet that SMSFs are heavily exposed to these companies.
3. Having a high percentage of your super in property substantially reduces diversification and liquidity.

What assets are readily available that improve diversification and have the potential to deliver reasonable returns? There are three that spring to mind:

- hybrid securities issued by the major banks
- global infrastructure
- global shares

Hybrid securities are so called because they are a mixture of debt and equity. One of the attractions is that they generally pay a fixed margin above the bank bill rate. For example, the latest Westpac Note pays 3.2% above the 90 day bank bill rate, which at current rates is a yield of 6.12%. If the bank bill rate rises the investor receives more interest, if it falls they get less. This is different to buying a government or corporate bond where the rate is fixed. At the end of the term, investors receive their original investment back in cash or in shares. Note that different hybrid securities have different terms and conditions. Some of the latest offerings are less favourable than previous issues due to banking regulations imposed to prevent a repeat of the GFC.

The upside is that investors are receiving a decent return which is almost certainly going to be better than inflation, and if interest rates rise you don't miss out. The downside is that neither your capital nor the interest payments are guaranteed. Not even the major banks are immune from problems, but are less likely to default than other companies.

Global infrastructure (roads, railways, utilities, etc) improves a portfolio's defensive characteristics. Infrastructure assets won't save you entirely if investment markets tank, but history suggests they will not be as badly affected. The major benefits are that the world desperately needs infrastructure as populations and urban centres grow. These companies also have the ability to maintain profits (as they are 'necessities') and tend to deliver more income than shares.

Global shares have been on the nose for many years, and it's entirely understandable. In most Australian-based funds, returns were abysmal before a rally in the last 12 months. Many people will also question the logic of investing in countries that have high debts and lousy economic growth. My suggestion is based on these observations:

1. Investment in global corporations diversifies your fund, and accesses a much wider range of industries and corporations which are not well represented on the ASX. Look around your home or your office to see what you are missing - Microsoft, Google, Intel, Samsung, BMW, Toyota, Panasonic, Sony, Nestle, Canon, Kellogg, Glaxo, Coca Cola, for example.
2. Companies with strong brands do not just sell goods and services in their own countries. They manufacture and sell them all over the world, including the fast growing Asian economies. So to avoid them because their headquarters are in countries which are struggling economically is not logical.
3. Global shares are denominated in foreign currency so if the $A falls the returns from these investments can create potential currency gains. Of course this is a double-edged sword. If the $A rises, these investments will be negatively affected and you need to weigh up the risk of that happening.

These suggestions are made on the basis of increasing your super fund's diversification, not a prediction of which sectors will do better than others. Some may suit your objectives and risk profile, some will not. As always, seek independent financial advice on your particular situation.

Rick Cosier is the principal of Healthy Finances, AFSL 240026.