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Three personal lessons from my European trip

Graham Hand

I have just spent a month in Europe, mainly Malta and Sicily. Don't worry, I won't bore you with holiday snaps, although it's hard to beat these countries for ancient temples, ornate churches and more sacred ruins than Julius Caesar could point a dagger at.

Rather, with head space freed from reading about the sad state of Australian politics and a declining stock market, here are three lessons that spring to mind as the sun sets over the Milanese skyline in front of me.

1. Contrast the 'remembering' versus the 'experiencing'

In his bestseller, *Thinking Fast and Slow*, Nobel Laureate, Daniel Kahneman, writes about the difference between a life 'experienced' and a life 'remembered'. He summarises his views in this [20-minute youtube video](#).

We experience life moment by moment. Kahneman says a 'moment' last about three seconds, so a life is made up of hundreds of millions of moments. The vast majority are forgotten, but the memories we choose to remember build a picture of how we feel about our lives. It's vital, says Kahneman, to understand this to realise why we are happy or not about our lives.

It's a fascinating insight which applies to holidays as much as any event. Consider the riddle of a holiday which is experienced in thousands of moments, versus how it is remembered in an overall rating of the entire trip. Let's face it, much international travel is exhausting and unpleasant. Waiting around for flights after security checks, catching transport to airports while facing flight deadlines, finding accommodation and checking into a room not as good as expected, looking for places to eat at every meal, searching for toilets in busy cities ... you know the drill.

Moment by moment, as I walk around yet another art gallery or temple, I am drawn to ask myself whether I am actually enjoying that moment. Okay, I know I am fortunate to be in Rome or Tuscany, but often I'm not really enjoying the moment, or at least, no more than I enjoy my everyday life in Australia. With obvious exceptions during a great meal, some good laughs, a stunning view over a landscape or the first look at a famous building, it's often hard work. This is the 'experiencing' self.

And yet global travel is one of the main goals of retirement, often a chance to travel in style with more time and money.

What is happening when I return from a trip with wonderful memories? My wife compiles fantastic photobooks, and we read them and reminisce about our amazing holidays. This is the 'remembering' self, and we have shared memories. I can relive an entire month-long holiday in 15 minutes ... what happened to the rest of the time? They were the tired and hungry (hangry?) moments I choose to forget.

Increasingly, I realise that significant overseas holidays are about building memories and remembering shared good times. The mind can turn events such as being ripped off by the Italian souvenir seller into great stories. In fact, Kahneman says the remembering self is a storyteller rather than the experiencing self who wanted nothing more than a sleep rather than another Roman ruin.

Kahneman extends the value of this insight far beyond holidays. He says it's essential to understanding happiness and personal judgement of a life well-lived.

Here are some of his quotations:

"We have a confusion between experience and memory. It's between being happy in your life versus being happy with your life ... The remembering self is the one that keeps score and maintains the story of our life."

"Our memory tells us stories and what we get to keep from our experiences ... Most of the moments of our life are lost forever, yet somehow you get the sense that they should count."

"The remembering self is the one that makes decisions. We don't choose between experiences, we choose between memories of experiences."

"We go on vacations to a very large extent in the service of our remembering self."

"You can know how satisfied someone is with their life but it does not teach you anything about how happily they are living their life. And vice versa. The correlation is low, about 0.5."

He suggests the following test to observe your attitude to your remembering self. What if you are told that, at the end of a holiday, all photographs of the trip will be destroyed. Furthermore, you will swallow a potion which will wipe out all memories of the vacation.

Would you still want to go on the holiday? How much less is the value of such a holiday? The elimination of the memories greatly reduces the value of the experience.

2. Prepare for medical emergencies

I travelled around Europe for a year when I was in my twenties, and I don't recall thinking about illness or doctors at any time. At that age, we're indestructible. A few decades later, this is not good enough, and Sicily taught me a lesson.

After we'd been on the road for three weeks, including a complete circumnavigation of Sicily, we returned the hire car to the airport at Palermo, ready for a few days in the island's largest city. On a Sunday morning, my wife slipped a disc, resulting in a severe sciatica attack. She now says it was the worst pain of her life, including childbirth.

Suddenly, we had an urgent medical crisis, and I had not given any thought to what we would do. She was sweating and groaning with pain, and desperately needed immediate relief. In her agony, she suggested all manner of actions like calling the Australian Embassy, phoning an ambulance or finding an English-speaking doctor. We were staying in an apartment so there was no hotel staff to assist us.

From a frantic Google search, I found a couple of doctors who looked suitable, but either the contact details were old or they were not answering their phones. I tried what I thought was the number for an ambulance, but the receptionist could not speak English. Another lesson – don't assume the world speaks your language.

Meanwhile, my wife could not find a comfortable position, and the pain had moved down her right side and her leg felt like it was on fire.

Our travel insurance was not specifically purchased for the trip but was one of the features of our credit card, an HSBC Qantas card. I recalled it had an emergency medical number, so I checked the internet. Here is what it says:

"Overseas. To make an emergency overseas claim, call Allianz Global Assistance on +61 7 3305 7499 (reverse charges from overseas). You will need to provide your policy number as well as proof that you paid for your travel tickets with your eligible HSBC credit card."

Policy number? Do I have a policy? I thought it was part of the card. Prove I spent 90% of travel tickets on the card? Is that flights only or accommodation? My wife is in agony and they want me to find policy numbers and details of a flight booking made over six months previously.

In fact, the HSBC's travel insurance conditions say:

"In order for Allianz Global Assistance to confirm your eligibility for International Travel Insurance, you will need to have copies of the documents listed under 'Documents to take with you'." This includes, "copies of their Card account statement and HSBC Card receipt to confirm the purchase of their overseas return travel ticket(s)."

I did not have the documents with me, and with my wife screaming in pain, a more direct approach was needed.

We decided to go out to the street and seek help calling an ambulance. We found someone who seemed to understand what we wanted, and he kindly called the Sicilian emergency number. We tried to explain the problem to him, and he translated, but despite several attempts, the operator said the condition was not severe enough for an ambulance. It was later explained that because ambulances are free and taxis expensive, many Sicilians call the service to visit the hospital, resulting in incorrect usage and cost.

So I ran off to find a taxi. We were staying in the centre of the old part of town, and most of the streets were closed for Sunday morning festivities. Reluctant to leave my wife, and worried about becoming lost in the tiny and intricate street network, I soon abandoned the taxi idea.

I returned to find her standing outside our apartment with four people, obviously attracted by her moaning in pain, trying to help. They called the ambulance again, and this person was more insistent. About 30 minutes later, the ambulance arrived.

I never want to see the inside of a Sicilian hospital again. It was nine hours of communication problems, x-rays and queues to see doctors before she received any pain relief and a drug prescription. It included a weird instruction to inject vitamins into her buttock, an exercise we attempted only once as it was so painful that we later dumped all the vials and needles bought at considerable expense. We were later told that some Italian doctors believe vitamins are a significant part of almost every treatment process.

Next day, the pain was reduced but significant. With less urgency than before, but still needing help, we tried the Allianz Global Assistance line. The call took about 45 minutes, including establishing whether we had coverage and the nature of the problem. They were unable to supply numbers of local doctors because "the contact details change so much". I don't see how they could have speeded up the ambulance with a phone call from Australia in English.

To their credit, Allianz subsequently stayed in contact and wrote to confirm we had full cover for expenses (less a \$200 excess) which might have included return business class seats and cancellations at many hotels. A nurse later also called with good advice on pain management for the return trip.

We managed to catch the relatively short flight from Palermo to Milan but the pain returned in northern Italy. Finally, during a night in a hospital in Alba in Piedmont, a doctor tried three different pain killing medications before we found one that worked. Hundreds of dollars worth of anti-inflammatory, anti-spasm, painkillers and vitamins later, we had a management plan for the long return of Milan-Rome-Abu Dhabi-Sydney.

I offer this detail to suggest you decide in advance what you would do. In recent years, we have travelled to Burma, Sri Lanka, Indonesia, Brazil, Peru and Argentina, as well as other European and Asian countries. The health system in many of these places is worse than the one in Sicily.

In future, I will attempt to clear my 'qualification' for cover with HSBC before leaving, to make the initial call as short as possible. Even then, I'm not sure how they could have expedited assistance, as they did not have local contact numbers for Palermo. For less developed countries, I'll check the state of the health system in advance. Perhaps I will take out cover specific to the trip to remove any doubts about coverage, especially where medical costs can be sky-high like the United States. But now there's a problem that my wife probably has a 'pre-existing condition'.

3. There are different worlds within one country (or how football explains Italy)

Nobody should judge a country after a brief visit or seeing only part of it, and Italy is a great example of such a diverse place. Amazingly, while most Australians think of Italy as an old country, the formation of the modern Italian state only began in 1861.

Italians talk openly about the cultural and economic differences between the north and the south, with Rome on the dividing line. A visit to Naples and Sicily shows an Italy rich in history, architecture and scenery, but it's often untidy and in disrepair, with poor garbage services and graffiti common in many towns. There is not enough money to maintain some great historical sights, and while the roads are generally good, the footpaths are no place for less-mobile people.

When we told an Italian friend from Milan of our experience in the Sicilian hospital system, she said it was notoriously underfunded compared with resources allocated in the north. Milan itself is one of the classiest cities in the world, with the Duomo spectacular after a recent clean. It also has an excellent public transport system, one that leaves Sydney for dead. Towns like Alba and Acqui Terme feel sophisticated, and of course, the Italian lakes area around Como and places like Tuscany and Venice are great destinations in the north.

Even the fantastic city of Rome is now called 'an open sewer' by its residents, with protestors hitting the streets last week to complain about the neglect of a city in disarray. They say roads are riddled with potholes, while strikes by garbage collectors leave bins overflowing, and public transport is in permanent crisis. More than 20 buses have caught fire in the city so far this year due to poor maintenance.

There's an excellent book, written by American journalist Franklin Foer, called *How Soccer Explains The World*. Judging from my attendance at Serie A matches in the south in Naples (Napoli versus Parma) and the north (the Milan derby, Inter v AC Milan), there are obvious differences.

The Napoli experience felt threatening. As a security measure, they do not sell tickets before the game at the ground, even when the stadium is half-empty. There is no ticket office. All tickets are bought in advance via full identification, and the tickets include a name, date of birth and address to prevent on-sale. The stadium looks more like a maximum security prison, with rows of high steel fences around the outside. There was a massive police presence externally, but none inside, where it felt like a colosseum.

On entry, police check tickets against everyone's ID, so imagine what a mad scramble that is before kick-off. Fans are herded through tight, single-file barriers and frisked by officials, although this did not prevent the regular firing of flares inside. At the end, whether or not the extreme fans, the 'ultras', chant, everybody is standing up, most are smoking and many of the so-called seats are wrecked or filthy. There are high fences and a wide, deep moat around the pitch.

Yet Napoli is not some hick team. Currently second in Serie A behind the all-conquering Juventus (now home to Cristiano Ronaldo), they are coached by Carlo Ancelotti, one of only three managers to have won the UEFA Champions League three times. It's a top quality side which the following week drew with Liverpool. And yet the passionate fans are treated like animals in a tense and intimidating experience.

Milan's San Siro is one of the world's great stadiums, sold out at a capacity of 86,000 for the derby game I attended. It's purpose-built for football with high sides to maximise noise and atmosphere. Fans are close to the pitch, and I've never experienced 90 minutes of such intense noise. I've been to three World Cups and great stadiums like Manchester United's Old Trafford, Liverpool's Anfield, Wembley and many others in London, but this was among the best. It was an exciting, non-threatening experience. Most fans sat down for the whole game, except at the two ends, and there was surprisingly little smoking. It was a world away from Naples.

We also visited Italy to attend two food festivals. The best pistachios in the world are supposed to come from Bronte in Sicily, but the weekend of the pistachio festival was a letdown. Modest stalls lined the main street of Bronte selling cakes and icecream featuring the nut, but it was low key, poorly attended and hardly worthy of the festival name.

In complete contrast, the white truffle festival in Alba to the north was amazing. Now in its 88th year, the city was packed and the festival itself was a mad scramble by thousands to taste and spend. Some individual truffles cost over Euro 1,000, and just to have a modest shaving on a plate of pasta added \$60 to the dish. As my wife is a serious foodie, it was like standing in the middle of a crowd tearing up dollar bills. Knowing they are on to a good thing, this festival runs over consecutive weekends for six weeks, and must have a multi-million dollar turnover.

And not one overflowing garbage bin in sight.

Building memories

Experienced moment by moment, these wonderful trips are often tiring and repetitive. Really, how many temples, museums or art galleries does anyone want to see in a month? After daily pizza, pasta, panini and pepperoni, we craved salads and Asian food.

But I know exactly what Kahneman means when he says:

"We go on vacations to a very large extent in the service of our remembering self."

Graham Hand is Managing Editor of Cuffelinks.

Are there profits from the 5G revolution?

Roger Montgomery

Wireless technology for mobile telecommunications commenced with analog and voice-only 1G in 1981. In the early 1990s, 2G enabled users to send SMS and MMS messages between two mobile devices. In 1998, 3G brought faster transmission speeds allowing internet browsing and video calls, and in 2008, 4G enhanced prior capabilities while also providing the ability to download and upload larger files such as video. It seems a new generation is developed every decade.

Who benefits from 5G?

The advent of fifth generation (5G) technology now has the world on the precipice of a major communication and mobile internet revolution. We were recent investors in Telstra at around \$2.70, and much earlier in Apple below US\$100, so we cannot ignore the implications of a 5G-connected world.

As providers switch to offering radically faster 5G speeds, an acceleration in the adoption of Internet of Things (IoT) devices and virtual and augmented reality will occur. We will probably move into edge computing (where computation is performed on distributed 'smart' devices or 'edge devices' as opposed to primarily taking place in a centralized cloud environment), smart cities, efficient energy usage and autonomous vehicles. I say 'probably' only because cheap interest rates have hitherto played a part in the willingness of investors to fund loss-making start-ups. Higher rates could curtail investor enthusiasm.

Investors should also avoid being blinded by the promises of new technology changing the world because history shows it is the consumer that benefits from such changes, more so than shareholders. By way of example, airlines, television manufacturers and car makers have indeed changed the course of human history but it has often been to the detriment of their shareholders.

That said, telcos, equipment makers, chip manufacturers, network utilities and data centre operators are just some of the businesses that may benefit or be disrupted. 5G will produce some winners and many losers.

The 5G opportunities

In June 2018, the 3rd Generation Partnership Program (3GPP), a global telecommunications standards partnership, announced a final standardisation for the first phase of 5G for new, standalone 5G deployments. The previous standardisation, finalised in December last year, covered non-standalone deployments, where 5G's dramatically-faster internet speeds are achieved using existing 4G infrastructure.

The June standardisation will permit high-speed connections for much more than just mobile phones. Cars, trucks, digital concierges, autonomous robots, and hitherto unimaginable devices will be given rein to literally change the course of human history again. Verizon and Nokia jointly recently achieved throughput speeds of up to 1.8Gbps through carrier aggregation, where an individual device, such as a smartphone, connects to multiple cellular frequencies at once. By comparison, 4G can deliver 450Mbps in Sydney's CBD but the average is about 33Mbps. According to another report, "Verizon and Nokia transmitted nearly seven times faster than 4G's latency ..."

Here's how Balázs Bertényi, Chairman of 3GPP, painted the accomplishment of the second standardisation:

"5G NR Standalone systems not only dramatically increase the mobile broadband speeds and capacity, but also open the door for new industries beyond telecommunications that are looking to revolutionize their ecosystem through 5G".

Today, decreasing latency – the delay prior to the transfer of data beginning after its request – is the goal, and sub-one millisecond is the aim currently required for satisfactory reaction times of autonomous vehicles. The demand for private vehicle connections is accelerating rapidly. 5G will enable vehicle-to-vehicle and vehicle-to-infrastructure communications at speeds allowing cars to anticipate and react to dangers much faster than the organic matter that sits between the driver's seat and the steering wheel (humans).

The 5G spectrum ultimately adopted will depend on the carrier, country, application, spectrum auction results and the user's location. But multiple radio spectrum frequencies and shorter wavelengths will allow 5G to support an estimated one thousand more devices per square meter than 4G. This is essential, for example, for seamless communication between and among multiple autonomous vehicles in crowded urban environments.

Unsurprisingly, countries around the world are racing to deploy the networks that would make all of this possible. In South Korea, the major carriers, including SK Telecom, KT, and LG Uplus, agreed to work together to build a single 5G network, keeping capex down and accelerating its roll out, which begins in December 2018 and is expected to be completed by 2022. In India, the government-owned telecom department is pressing ahead on its 5G rollout as early as 2020, while expanding the size of its spectrum releases. From Japan to Serbia, the desire to deploy 5G and take advantage of its benefits is unbounded.

Investors now have many ways to invest in this space. In addition to the usual telco suspects such as China Mobile, SingTel, Vodafone, AT&T, Verizon, T-Mobile, Sprint and Orange, there's a global telecoms ETF managed by iShares (IXP) and a US Telecoms ETF also run by iShares (IYZ). Fidelity run a MSCI Telecoms Service Index ETF (FCOM) and there is also the S&P Telecom ETF SPDR (XTL).

Nearly 80% of the estimated US\$350 billion spend on 5G infrastructure will be on hardware and network transformation projects. Cisco (CSCO), DellEMC, Hewlett Packard Enterprise (HPE), IBM (IBM), Lenovo (LNVGY) as well as Nokia (NOK) and Ericsson (ERIC) are expected to benefit. Tower cells will be required and owners include American Tower Corp (AMT) (20,954 towers including US, India, UK, Mexico), Crown Castle Corp. (CCI) (22,231 towers, US and Australia) and AT&T Towers (10,792 towers in the US). There are long lists available for each country.

Upgrades and adoption periods

When the current 4G standard was released in 2008, it didn't become a commercial reality until 2010, and a sharp 75% jump in smartphone sales, to over 300 million units a year, occurred. While newer generations of phones are backward compatible – a 4G phone can communicate through a 3G – a 4G phone will not be able to communicate through the 5G network. Each new generation typically requires cell phone providers to make upgrades on their towers, requiring end users to upgrade devices such as phones so that signals through the new infrastructure can be received and sent. In its 2018 Mobility Report, Swedish telecom equipment manufacturer, Ericsson, estimated 1 billion 5G devices will be in use by 2023, accounting for approximately 20% of mobile data traffic. Apple, Samsung, Sony, OnePlus, Huawei are leading mobile device manufacturers.

In turn, these devices, which include mobile phones and PCs, will need 5G chips. Intel (INTC) is currently seen as the leader in chips, while Samsung, Nokia, Huawei, Ericsson and ZTE are also major 5G participants described as leading 5G development.

Investors however should again be reminded not to get too excited or blindly believe that the benefits to consumers and society will automatically translate to huge profits for providers and suppliers. The requirement, for example, of thousands of small cells (on towers and sides of buildings) as well as 'beamforming' – an important highly directive feature for base station antennas – will be essential to maximize 5G's capabilities and these will be a huge capex burden for providers.

More of Moore's Law

In 1965, the semiconductor pioneer and cofounder of Intel, Gordon Moore, observed that the number of components that could be mounted economically on a standard computer chip was doubling every year. Similar laws can be observed in everything from photovoltaic cells to broadband capacity and they have important implications for investors. Back in 1954, the average price of a transistor was about US\$5. Over the following 50 years, the price of computing power steadily dropped and today an integrated circuit is worth a billionth of a dollar. The consequence is that manufacturers and suppliers need to run faster and do more just to stand still.

As power or capacity increases and costs fall, markets open, competition increases and the consequence is slimmer margins.

Investors excited about the prospects of 5G need to keep this dynamic in mind, along with the knowledge that 6G will be rolling out by 2030.

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Five factors to check for Nervous Investors

Tim Fuller

You wanted shares to buy last year but didn't get around to it, then prices rose and so you were waiting until prices fell, but now that they have fallen you are worried they will fall further.

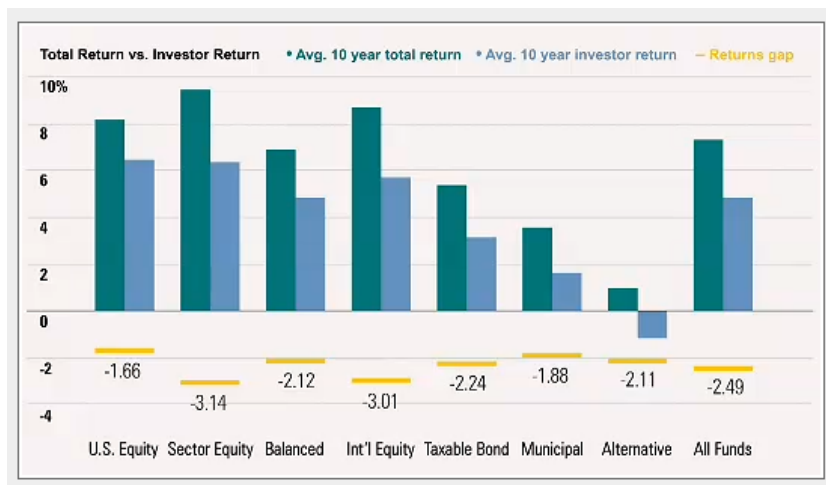
I have good news and bad news for you. The bad news is as a 'Nervous Investor', you will never find a perfect time to invest, when everyone agrees markets are going to go up. The good news is I think I can help.

Let's look at why retail investors often underperform, what assets are available and five tips on what to do.

Why retail investors underperform professionals

Morningstar regularly publishes studies showing retail investors underperform by around 2% (and others think the gap is larger):

Figure 1: Returns gap



Source: Morningstar

The main factor is behaviour. When markets wobble, investors tend to sell or sit on their cash. When markets have been performing well, investors tend to invest their cash. From a risk perspective, this might seem reasonable to the Nervous Investor – buy when risks seem low and sell when risks seem high. But, from a return perspective, it is exactly the wrong strategy: buy high, and then sell low.

Your brain is actively working against you. The average Nervous Investor makes poor investment decisions in the heat of the moment.

Getting perspective is difficult, especially if you rely on newspapers, financial TV or stock brokers. The first

two are in the entertainment business and so creating an exciting story trumps any obligation to give you a realistic perspective. Stockbrokers make money from turnover, so convincing you to buy one day and sell a few weeks later trumps the obligation to give you long-term advice.

Some of the many biases include:

- **Loss aversion:** The hurt from losses is more than the joy from gains. For a Nervous Investor, this might mean being overly conservative rather than taking calculated (and diversified) risks.
- **Confirmation bias:** searching out facts supporting our view rather than challenging it. For a Nervous Investor, it means looking for reasons to invest later. And, as the internet is a big place, I'm sure you'll find someone who agrees with you.

- **Planning fallacy:** our tendency to underestimate the time, costs, and risks of future actions and overestimate the benefits. For the Nervous Investor, this means “I’ll invest later after I learn the entire financial system and all its risks”. But life gets in the way.
- **Choice paralysis:** too many choices overload. For the Nervous Investor, this is a never-ending excuse – you just need to research the choices more.
- **Bias blind spot:** we can see everyone else’s biases but not our own.

To overcome these biases, create a plan and stick to it.

One of the most dangerous biases is judging a past decision by the outcome instead of the quality of the decision at the time it was made, given what was known. Humans are constantly rewriting history, such as these two staples of investment prediction:

- “Last year was much easier, all you needed to know was [insert theme that is known now but wasn’t 12 months ago] – this year will be more difficult.”
- “Last year was all about [insert growth / value / quality / momentum]. This year will be a stock pickers market.”

The reality is, investing is never riskless and there are always reasons for markets to fall or to rise.

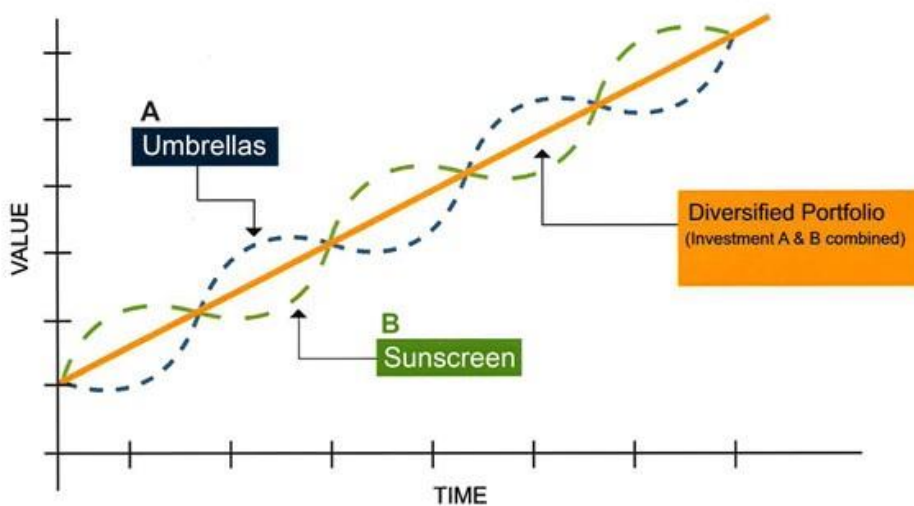
Typical assets, and how they usually perform

First, you want to diversify to smooth your returns. Consider the apocryphal portfolio owning an umbrella seller and a sunscreen seller. Some days one does well, other days the other does well. An investment in only one gives a volatile return, an investment in both smooths the return:

How Diversification Works

A Simplified Example

By owning a portfolio specifically designed to take advantage of asset categories with **dissimilar price movements**, an investor can minimize volatility while continuing to pursue positive returns.



Investment A and B have a negative correlation.

The four traditional asset classes are:

1. Cash/term deposits: the big advantage of cash is the value doesn’t fall in times of stress. The disadvantages are that cash gives a poor return relative to other assets, and in times of trouble, central banks cut interest rates which flow through income immediately. If you are relying on interest payments for living expenses, then this can create problems at the worst possible point of the economic cycle. While you can mitigate somewhat by term deposits, you then lose the liquidity of cash. The danger is you own too much.

2. Government bonds: The big advantage of government bonds is in times of stress the value often (but not always, depending on the type of crisis) rises. This provides diversification and income when you want it most. The main downside is the value of the bond does change, and so bonds are riskier than cash. Over the long term, bonds perform better than cash, but not as well as stocks.

3. Corporate bonds: Corporate bonds provide a higher interest rate than government bonds. The downside is there is a much larger chance the company you are investing in goes broke, which manifests itself as a poorer level of diversification. This makes the returns for corporate debt more similar to stock market returns – meaning for the Nervous Investor corporate debt is less useful.

4. Stocks: Stocks are the most volatile – in boom times they return the most, in bust times lose the most. Over the long term they return the most. As a Nervous Investor you want to have a diversified weighting to stocks over the long term, but keep this exposure to a level you feel comfortable with.

Five areas of focus for the Nervous Investor

1. Asset allocation

Get your strategy right and then stick to it. Write it down. Put it somewhere safe and refer to it before you make any investments. As a Nervous Investor, don't let your emotions rule.

Diversify. Diversify. Diversify. Useful for ordinary investors, doubly so for a Nervous Investor.

2. Regret minimisation

Realise every investor is wrong at some stage. Your goal as an investor is not to make zero mistakes, it is to make sure mistakes don't ruin your overall portfolio.

First, evaluate the fear versus greed trade-off. If you really want to be the person at the BBQ talking about how much you made on the stock market, then you must take risks. And some years you will have big losses. For many Nervous Investors, this is unrealistic. Abandon your dreams of being the hare and embrace the role of the tortoise.

Second, don't invest all at once. Make a plan, and for some this will mean gradually investing over a few months, for others, it will mean gradually investing over a few years. You will be alternatively kicking yourself for not investing earlier and then berating yourself for not waiting for the market to fall. Accept that now and move on.

3. Self-evaluation

Do you have the knowledge to make investment decisions? If not, get a professional to do it. If you "just need to read up on a few more things", then get a professional to do it for you in the meantime, in case it takes you a few years longer than you expect.

Do you have the temperament to make investment timing decisions? If not, get a professional to do it. You need to stick to your plan as a Nervous Investor, and if you are unsure of your ability, leave it to the professionals.

4. Self-control

Rebalance regularly. As a Nervous Investor, this will be a painful process because it will entail selling assets that are doing well and buying assets that have done poorly. Do it anyway. For many investors, near the end of the tax year is a good time.

Don't watch every market tick. Once your plan is set up and running, turn off the live prices and financial news. As a Nervous Investor, they are going to pander to your worst instincts.

5. Analysis paralysis

As a Nervous Investor, you are probably already a few years overdue to do something. A longer-term plan might take years to be fully invested if that is what you feel comfortable with. But start now and don't keep making excuses.

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The impact of negative Australian versus US rate spreads

Stephen Cooper

Australian sovereign bond yields have typically traded above many global counterparts, particularly those in the US. This has reflected a number of fundamental factors, including Australia’s higher long-term average economic growth and inflation. Australia’s inflation target of between 2.0% and 3.0% per annum is slightly higher than the Federal Reserve’s 2.0%. Higher Commonwealth Government Securities (CGS) yields have also arguably reflected Australia’s higher term premium, given the economy is relatively small and largely influenced by commodity exports.

A reversal of historical norms

Accordingly, the Australian economy can be susceptible to fluctuating fortunes. The current desynchronised global growth environment, in which the Australian economy is lagging the US, has seen a reversal in this historical relativity. The spread between Australian and US 10-year sovereign bond yields has moved materially into negative territory for the first time in over 30 years, although CGS spreads relative to German bunds, UK gilts and Japanese government bonds are little changed this year. This raises questions over the sustainability of this negative spread and, in turn, whether it might affect offshore demand for Australian bonds in the future.



An additional issue is the impact of front end interest rate differentials on hedged returns. Historically, hedged exposures have been the norm, but in a world of negative returns from hedging, this default setting needs revisiting.

The sustainability of negative Australian versus US spreads

From a fundamental economic perspective, most would argue that equilibrium interest rates in Australia should be somewhat higher than those in the major G3 countries. A medium-term view of the key drivers of 10-year yields – potential growth, long run inflation outcomes, and term premia – are all consistent with higher yields locally. Consider:

- Australia’s population growth rate (through both natural increases and immigration) remains higher than in the US.
- Productivity has been higher in Australia than the US historically, and while this is less certain going forward, the balance of risks remains skewed towards higher Australian outcomes.

- The inflation target is higher than in the US, Europe and Japan.
- As a small open economy, Australia is subject to volatility in domestic and external demand so term premia should be structurally higher for Australia than other markets.

Notwithstanding, Australia’s sustained economic prosperity and credit rating stability has historically supported demand for Australian paper, particularly against a background of sub-par economic outcomes, deteriorating fiscal positions and declining credit quality globally. Indeed, Australian CGS have become a core diversifying holding for many central banks, sovereign wealth funds and other large institutional investors worldwide. The case for diversifying into Australia in such an environment is a logical one from a default risk perspective, and makes even more sense when there’s also a clear return benefit in making the allocation.

Although the return advantage of Australian bonds has been removed, the diversification benefits remain, particularly when considered against Japanese and European alternatives. We believe demand for Australian paper will persist, potentially allowing local yields to trade below comparable US Treasuries for sustained periods of time, albeit with an average ‘over the cycle’ profile that continues to show a positive spread relative to the US.

Short end differentials and implications for hedging

Front end (cash and money market) rates have also recently fallen below their US equivalents. With the Federal Reserve committed to a path of monetary policy tightening while the Reserve Bank of Australia (RBA) is expected to keep local rates unchanged for an extended period, this differential could widen further and persist for an extended period of time.



This environment represents a different dynamic from a hedging perspective for AUD-based global fixed income investors. Historically, hedging global fixed income exposures back to AUD provided a higher yield and lower volatility in total returns. However, there is now a distinct trade-off between return and volatility, on at least part of the portfolio.

Hedging policy considerations must factor in expected total returns of a hedged exposure, as well as the hedging costs themselves. We believe Australian investors will continue to favour hedged offshore exposures due to:

- The diversity benefit that global fixed income provides, and
- The continued positive hedge benefits from the non-US elements of these exposures.

Where specific US-only exposures are included, hedging appears likely to remain the default option to help mitigate the potential portfolio impact of currency volatility. Overarching currency views, as well as a focus on the forces that may influence them beyond interest rate differentials, will undoubtedly continue to drive hedging decisions.

Could persistent negative spreads have long-term implications for Australia?

We do not believe negative spreads alone will have any significant adverse impacts on Australia, or on the domestic bond market in general. Supported by AAA ratings, lower rates are favourable for the Commonwealth Government and state issuers from a cost perspective. They also reflect confidence among the international investment community in Australia's long-term economic prospects. Lower rates might also be expected to be supportive of domestic economic activity and should make it more comfortable to fund current account deficits.

Perhaps a more interesting question is whether the RBA could miss out on participating in a global rate hiking cycle altogether and, in turn, what risks this might present over time.

The RBA continues to suggest the next move in domestic rates will be upward. But with inflationary forces under control and with lenders increasing variable mortgage rates independently of moves in official policy, we are unlikely to see a rate hike in Australia in the foreseeable future, potentially not until 2020. There's some risk that the global interest rate cycle will have turned before domestic conditions justify an increase in Australia and the RBA could therefore miss an entire hiking cycle globally. If that were the case, with local rates staying lower for longer, current policy settings would increasingly be perceived as the norm by both fixed income investors and Australian households. In turn, this would potentially increase the vulnerability of the local economy to future rate increases, as businesses and households had structured their activity and spending based on current settings.

A balanced risk approach

Relative yield differentials and duration positioning are by no means the only drivers of performance in our fixed income strategies. To varying extents, our Australian and global fixed income portfolios maintain exposure to a wide range of alpha sources globally. Australian and US signals including rates, curve, country spreads and FX are just a subset of the return sources that are utilised globally. The 'balanced risk' approach employed in the management of all portfolios ensures they are constructed in a diversified manner. No individual risk position or view has the ability to dominate the return profile, increasing the likelihood of accomplishing portfolio objectives and providing investors with better risk-adjusted returns over time.

Stephen Cooper is the Head of Australian Fixed Income at [Colonial First State Global Asset Management](#), a sponsor of Cuffelinks. This article is for general information only and does not consider the circumstances of any individual. For more articles and papers from CFSGAM, please [click here](#).

Investment flows and the trifecta of desire

Douglas Isles

I started my current role as Platinum's investment specialist in 2013, representing the investment team I had previously been a part of, to advisers. I spoke to a wide range of clients trying to determine their needs. After a process of collation and reduction of countless notes into lists of words, headings and subheadings it struck me that three things came up again and again – Performance, Connection and Simplicity – the "trifecta of desire".

We all now know that our biases affect investment decisions. But they also affect investment communication and a simple question captures this for me. A lot of meetings begin with advisers enquiring: "How are your flows?" It's simple, and it's about connection. It's the herd mentality in action, and they are really asking, "What are others doing?", almost as if others' endorsement is a critical requirement. Less obviously, it's all about performance.

1. Performance

Strong performance is desirable and should be sought, but not chased. Finding a rare and genuine edge in delivering long term performance for clients is the goal of fund selection.

But, flows do not and cannot predict future performance. This is recency bias at its worst; industry surveys and our own data confirm that collectively consumers chase past performance. The relationship is alarming.

Recent past performance is a very strong predictor of flows. I use an algorithm^[1] to track this as it helps me empathise with clients. I know when people are likely to take money away, or give us more. It's an emotional rollercoaster.

The simple fact is that the best managers are not always the best short-term performers. Staying the course is the challenge. Discerning between process and outcome is hard. The industry ('sales and marketing') focus is on outcomes; good outcomes sell funds, processes remain conceptual. Despite its triteness, it's right to disclaim that "[recent] past performance is not a reliable indicator of future performance".

Performance is based on a single sequence of events. No one can measure a portfolio in advance yet risk analysis uses realised historic outcomes to model possible future ones. Successful managers buy cheap stocks and sell expensive ones but expensive stocks can rise and cheap stocks can fall (witness 2018!). So sound processes will often deliver poor outcomes and vice versa.

But at softer times, clients ask the tough questions, and Connection and Simplicity become important. The risk is that these are 'tools of selling' at odds with 'tools of investing'. They open us up to exploitation.

2. Connection

Connection is a basic human need. We feel exclusion as acutely as physical pain so fitting in is very important. The herd mentality is well documented.

Influence guru Cialdini cites seven 'weapons of influence' with four directly relate to connection – reciprocity, liking, social proof and unity. Strong connections are essential for the persuader.

Salespeople know 'How to win friends and influence people': Listen, take an interest, smile and use peoples' names but above all, avoid disagreement. Yet most successful fund managers are contrarian. Bringing an opposing message is a tough starting point. But unless active managers take on the market, they will be replaced by index funds, which naturally attract flows in rising markets according to my algorithm, and the evidence of recent years!

Motherhood statements like "Apple is a good company" could be exploited as sales tricks. No one can disagree and subtly most equate good companies with good investments. By making statements that can't be challenged, we win people over but may not make them money (ironically, Apple has!). Connection is aided by agreement but successful investing is about challenging consensus thinking.

3. Simplicity

Simplicity is helpful – the world is a complex place. Portfolios are hard to distill down to key drivers, so stereotypes make life easier. We can't model all possible outcomes but they can lead us astray.

Remember that if your business could be written as a set of simple steps, a computer will eventually replace you. That's robo-advice for advisers, that's smart-beta for fund managers.

But look around you today – simple slogans, logos, promises, hopes and dreams. Just do It! Make America Great Again! We are all easy prey, for manipulative marketers, predatory politicians and mercenary media moguls. Our industry exploits this via personification (celebrating individual star fund managers despite teams producing better results), slogans (such as disruption), familiarity (the cause of home-bias) and storytelling (usually about stocks that have already performed).

People like asking questions that can be answered and tracked. "What's your economic view?" is easier than examining useful but more abstract portfolio characteristics.

Simplicity misses the psychology of successful investing. The best investment decisions are the most uncomfortable, and at the time, they often sound crazy. If tough ideas are presented coherently, we don't convey this angst. The entire existence of active managers relies on rare talent for exploiting uncertainty, disagreement and complexity. Machines will replace the simple and those who simply agree with the market.

In my view, 'tools of selling' are at odds with the 'tools of investing'.

To balance the trifecta of desire, investors will benefit from remembering to consider the following two points:

- Acknowledge the relationships between luck and the short-term versus skill and the long-term
- When meeting fund managers, replace questions such as “How are your flows?” and “What’s your economic view?” with the critical “What is your edge?” and “Why will it persist?”

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[1] I simply average 4 numbers – the 1 and 3 year absolute returns of the fund, and the 1 and 3 year returns of the fund relative to the appropriate index. The correlation with net flows over the next six months is striking.

Keating’s super versus disengaged millennials

Leisa Bell

Can the superannuation system designed a generation ago still be fit for purpose for the modern workplace and our ageing population? This was the question put to 80 business executives across a wide range of industries in Mercer’s recent survey and report: [Keating’s super meets the digital natives/the next generation of super](#).

Changes in the modern workplace

Nine of the ten organisations surveyed agree that as the workplace transforms, so too must super. Mercer’s CEO, Ben Walsh said:

“The results indicate a seismic shift from the workplace of 1992, when full-time jobs were predominantly filled by men with few job changes. Contrast that with Generation Z, digital natives who will not only have multiple jobs, but multiple careers.”

Demographer, Bernard Salt, added:

“The nature of work has changed, as has the gender mix, the ethnic mix and the technology skills of the workforce. And yet, throughout these profound changes, the essence of superannuation has not changed substantially. Superannuation of the future needs to be portable both within Australian workplaces and even globally. It needs to be ‘pauseable’ so that women, and men, can come into and out of the workforce as they deem appropriate to their life choices. The next generation of super needs to reflect the agility, the diversity, the globalness, the lifestyle choices of Australians today, that indeed the workplace now recognises.”

The changes in the future labour force predicted by the 80 business leaders include 54% forecasting an increase in contractors at the expense of permanent staff and a sharp spike in part-time workers, both men and women.



Lack of engagement

The Mercer Report also highlights the differences in superannuation engagement by age. About 89% of employers think employees aged 60 years and over regard super as **very important**, compared with only with 8% of employees under 30 years. In fact, the reported 56% didn't think super was important and 23% only somewhat important. The Report provides many quotations from young people showing a complete lack of interest in super.

The following is predominantly extracted from Mercer's report.

Despite super now having served a generation of workers, there is broad agreement that the system has failed to engage employees. According to those surveyed, employees don't view super contributions as 'their money', with many unable to identify their fund or what it invests in. Not surprisingly, they fail to undertake any forward planning or consider super as part of their broader investment approach to retirement.

This trend will worsen in time, with younger workers in particular found to have little interest or engagement with the super system. Engagement only appears to occur closer to retirement, when it can be too late to optimise super savings. Competing financial priorities, a sense of a lack of empowerment in dealing with finances and financial institutions and difficulty in navigating a 'complex' system are among the main reasons cited for people's disengagement with super.

Failure is an opportunity in disguise

While failure to engage super fund members is acknowledged as a major issue, it is an opportunity for vast improvement.

Survey participants think super is an underutilised lever when it comes to staff recruitment and retention, with the majority of employers not recognising its value when negotiating staff contracts, such as offering higher contributions or paying administration fees. Integrating super into staff entitlements can also serve to better educate and empower staff to actively manage their financial assets.

Communications to members are also viewed as opportunities to better engage members, particularly young workers, with current interactions criticised for being text heavy and lacking dynamism. While other industries had successfully used video, social media and humour to interact with their target audiences, the super industry is lagging.

While the bulk of members' interactions with super funds shifts to online platforms, technology can further enhance member experiences through more widespread adoption of AI to anticipate and meet member needs, such as matching callers to customer service staff by age. AI is also seen as a way to trigger discussion about investment needs based on members' life stages.

Linking super accounts to online bank accounts was considered another opportunity to keep super front of mind and incentivise saving and contribution targets. However, more traditional forms of communication still have their place. One suggested solution included employee workshops to demystify super and encourage members to be more active participants in their future saving strategy. Financial literacy should start earlier than the workplace, with widespread agreement that the government should update school curriculums to include 'financial health' alongside health and fitness, and sex education.

Distrust and disruption

The recent scrutiny of the financial services sector could further embed a sense of skepticism and detachment among fund members already feeling overwhelmed by a multi-faceted and regulated system. Current industry practices are partly responsible for contributing to wide-scale disengagement and apathy towards super.

The future workforce profile will not be a big enough impetus to trigger change in the system on its own. They also doubt recent 'disruptors' targeting millennial members through social channels and simpler product options can reshape an essentially government-controlled system, and that it would likely take the big-name funds to have large-scale impact and force significant change.

Businesses see a growing need for a new superannuation system to cater for the next generation. Superannuation providers, in turn, should view this as an opportunity to break away from an outdated system and lead the change.

Go to mercer.com.au/NextGenSuper to learn more. Leisa Bell is Assistant Editor at Cuffelinks.

How to access terminal illness benefits

Julie Steed

If a super fund member is terminally ill, they may be able to receive a tax-free lump sum from their super fund. Many funds also allow a death insurance benefit to be paid early too.

In this article we explain some of the pros and cons of terminal illness benefits.

Early release

A member's benefit can be released early if the member has a terminal medical condition which meets the following conditions of release:

- Two registered medical practitioners certify that the member suffers from an illness, or has incurred an injury, that is likely to result in the member's death within 24 months or less (the Certification Period)
- At least one of the medical practitioners is a specialist practicing in an area related to the illness or injury
- The Certification Periods have not ended

Preservation

The member benefits that exist at the time of meeting the condition of release or accrue during the Certification Period become 'unpreserved' which means they can be accessed. Any benefits that accrue after the Certification Period ends remain 'preserved' and cannot be accessed until the member meets a further condition of release.

Insurance

Many insurance policies allow a member to claim a death insurance amount if they meet the terminal medical condition of release. Generally a member can only claim a death or permanent disability benefit once.

Prior to 1 July 2015, the terminal medical condition certification period was 12 months. Although the condition of release extended the period to 24 months, many insurance policies are only increasing the period in their policy definitions when policies are renewed. This means some members with a 24-month certification period may not be able to claim insurance benefits.

Payments

The tax treatment of a terminal illness benefit depends upon how the benefit is paid.

If a lump sum payment is made during the certification period it is tax free, regardless of the member's age. Any balance remaining after the Certification Period ends will be taxed as an ordinary member benefit where tax will depend upon the member's age. If a member previously applied for a benefit under another condition of release and PAYG tax was deducted, the member may provide the trustee with the terminal illness medical certificates. The certificates must state that the member satisfied the terminal medical condition definition at the time the original payment was made or within 90 days from receiving the payment. The trustee may then request a refund of the PAYG tax deducted from the ATO and make an additional payment to the member.

Claiming a tax-free terminal illness benefit can help members who have non-tax dependant adult children as the likely recipients of a death benefit. A death benefit paid to an adult child will be taxed at 17% of the taxable component. An amount paid as a terminal illness benefit can be withdrawn tax free and gifted to the children before death or paid as non-super monies via the estate (and therefore not subject to tax).

If the member chooses to receive a pension benefit, the benefit is taxed as a normal superannuation pension, there are no tax concessions for a terminal illness pension.

Rolling over

Although superannuation law allows a terminal illness benefit to be rolled over to another fund, such rollovers are not rollover superannuation benefits under tax law. This means if a terminal illness benefit is rolled over, the transfer is not treated as a rollover but as a personal member contribution.

The paying fund is treated as having paid a benefit to the member for tax purposes and the member is deemed to have been paid a tax-free lump sum. The receiving fund is then treated as having received a personal contribution from the member.

The amount will therefore count towards the member's concessional and/or non-concessional contributions cap, depending on whether they may have been eligible to claim a tax deduction for some of the contribution.

Summary

Understanding the requirements to claim a terminal illness benefit may help members with their tax planning and avoid potential pitfalls of rolling over. For more information, please speak with your financial adviser.

Julie Steed is Senior Technical Services Manager at [Australian Executor Trustees](#). This article is in the nature of general information and does not consider the circumstances of any individual.

Airports as defensive assets for Australian investors

Nicole Connolly

Mounting uncertainty surrounding the outlook for the global economy and investment markets is highlighting the benefits of holding defensive assets, such as infrastructure, in a portfolio. Unlisted airports have especially attractive features.

While typically thought of as an investment for large superannuation funds, more private investors are adding unlisted infrastructure to their portfolios. Infrastructure assets provide essential services such as gas, water, electricity transmission and distribution networks, as well as transport infrastructure including airports, rail and toll roads. These assets are considered to be defensive as they provide reliable income given the prices they charge are often regulated by governments and their cash flows are predictable.

The airport attraction

Airports provide numerous sources of revenue from a diversity of stakeholders such as airlines, passengers, visitors, retail tenants and government agencies.

In fact, airports should be considered as two separate businesses – airside and landside. The airside operations include the management of the runways of the airport. Revenue is generated by either a charge levied per passenger or a charge levied on the weight of the plane or a combination of both. This side of the operations behaves much like a regulated utility. The landside operations involve the non-air aspects of the airport such as retail shops, car parking and property development and maintenance.

Airports have been a strong driver of returns for unlisted infrastructure portfolios. The sector in Australia has delivered long-term growth, with only one year of negative passenger growth over the last 25 years. This compares to four years of negative growth for Australian equities over the same period. The airport sector performed relatively well through the GFC, with airlines managing the down cycle through a range of initiatives including discounted ticket prices and reduced services for example.

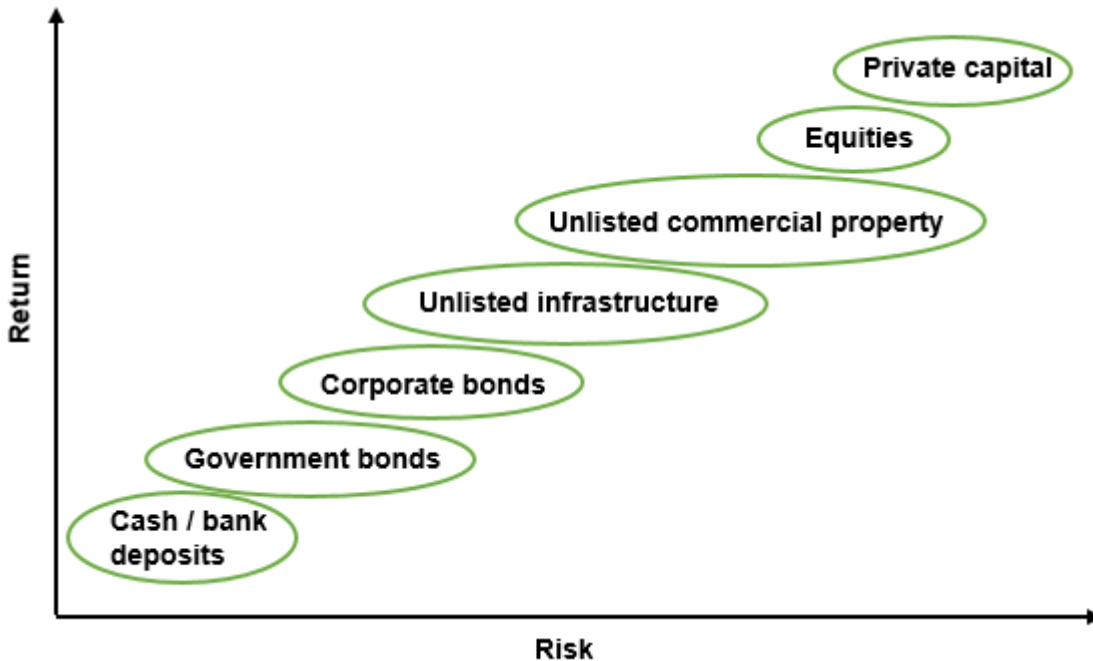
In FY 2017, Melbourne Airport generated a return of 25%, Perth Airport returned 13.2%, Brisbane Airport returned 14% and Adelaide generated 23.2% for investors.

The value of unlisted infrastructure in a portfolio

Unlisted infrastructure in a portfolio sits between government bonds and equities in terms of risk return, making it strong portfolio diversifier, as shown in the chart below. Infrastructure's potential for stable, reliable income and capital growth is derived from long-term, stable and predictable cash flows, typically underpinned by long-term contracts or a regulated asset base. High visibility of income and revenues are often linked to inflation.

Unlisted infrastructure investments accounts for between 7- 12% of major institutional investor portfolios, with the Future Fund having allocated around 7% to infrastructure and Australian Super 12%, as at the end of 2017.

Risk return profile of unlisted infrastructure



Source: IPIF August 2018

The key is to determine which assets and projects will provide the greatest, and most consistent, returns.

Our investment strategy focuses on providing exposure to a diversified portfolio of mature, stable and cash-generating infrastructure assets. This includes exposure to transport assets including Perth, Adelaide, Melbourne and Brisbane Airports and Interlink Roads, and a number of energy and utilities assets including TransGrid, the UK's South East Water and PowerCo and First Gas in New Zealand.

In infrastructure funds generally, it's worth checking on the type of assets held and the particular merits of airports.

Nicole Connolly is executive director at Infrastructure [Partners Investment Fund Management Pty Ltd \(IPIFM\)](#). This article is for general information only and does not consider the circumstances of any investor.

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