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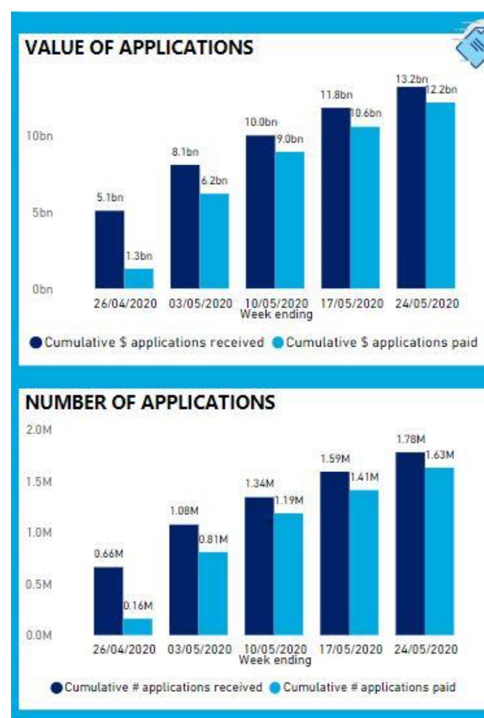
Editorial

Drought, bushfires and coronavirus ... even the Treasurer has admitted Australia is now in a recession after yesterday's fall in the March quarter GDP. The June quarter is certain to be worse. And such are the times we live in, despite blood and fires on the streets of dozens of US cities, the ASX200 rose 1.8% and is now 35% up from its 23 March low. The market has firmly factored in a V-shape recovery that still seems hard to fathom.

Much of the optimism is due to the stimulus packages. The withdrawal of up to $20,000 from superannuation is understandable for anyone struggling financially during the epidemic. A loss of retirement savings in 30 years is no match for a present-day need to put food on the table or pay the rent. But many young people who have accessed both JobKeeper and their super have more money during this crisis than ever before in their lives. Treasurer **Josh Frydenberg** actively encouraged it with statements such as "*this is the people's money and this is the time they need it most*".



Source: APRA Early Release Scheme statistics

There have always been rules that allow access to super for hardship, but it was previously difficult to qualify. Where the new policy falls down is the ease with which so many can withdraw. Although in theory it is targetted at people disadvantaged by the virus due to unemployment or a loss of hours, the guidelines say:

"You will not be required to attach evidence to support your application; however, you should retain records and documents to confirm your eligibility."

It's a low bar to jump over, and less than 1% of application have been rejected. There is no requirement to confirm the loss of hours is not compensated by government support. About 1.8 million people have applied for $13.2 billion already. Given there is a month to go on the first $10,000, with another $10,000 from 1 July, withdrawals could top $30 billion.

Most worrying is evidence (from a smallish sample of 13,000) from **AlphaBeta** (part of Accenture) that 40% of people who have withdrawn money have experienced no drop in income. The research suggests increased spending on discretionary items such as clothing, furniture, cars and alcohol, with about 12% spent on gambling. There's a lot of 'want' rather than 'need'.

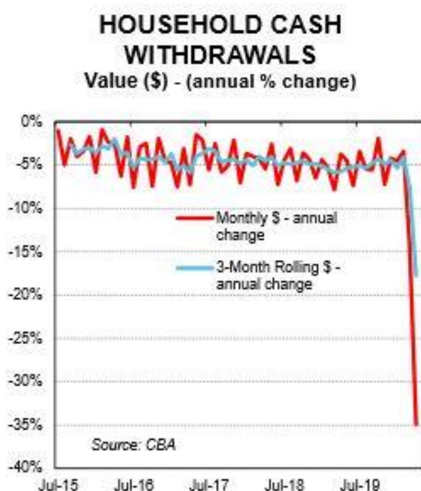
As a recent article by **David Bell** and the compounding article last week both show, the long-term consequence of early withdrawal is a major loss of retirement savings. **Scott Morrison** says the Government has no interest in what people are spending the money on, but consider these statements from retailers (courtesy of NAOS):

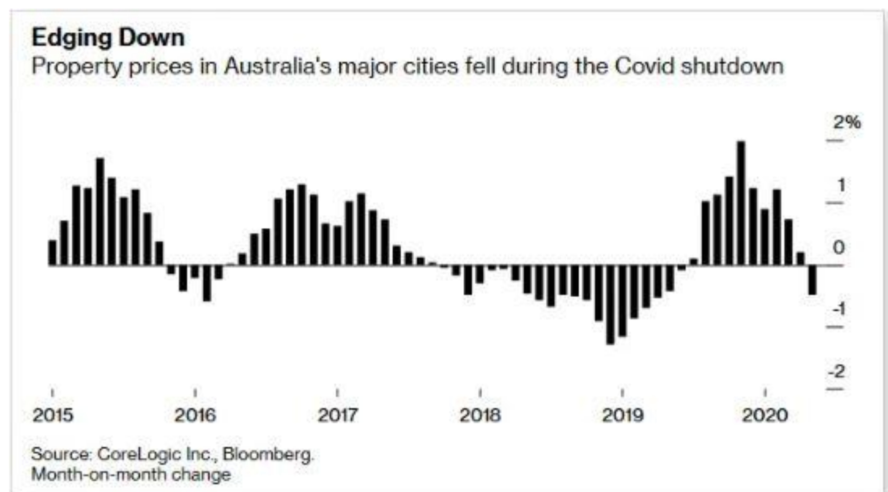
"*JobKeeper in our view is certainly fueling a lot of growth [in sneaker sales]. It really resonated with kids that they had some money."* Daniel Agostinelli, CEO, Accent Group, owner of high-end sneaker stores, HypeDC and Platypus.

"*Used vehicles have really taken off – much stronger than new cars – and actually better than pre-COVID. It's a lot of first-time younger buyers. In the past they would have caught the train or the bus – they're now planning to drive".* Anthony Altomonte, Managing Director, The Alto Group, car dealers

More cars on our clogged roads and less super in the accounts of young people with nice sneakers are two unwelcome, long-term impacts of COVID-19. The use of cash also has rapidly declined and this change will endure. Anyone who owns an ATM has become another victim of the virus.

However, with $7 trillion in Australian residential housing, there is no doubt which asset class delivers the biggest wealth impact across the nation, and the first signs of a reversal from the boom of late 2019 are now in **CoreLogic**'s numbers.





In Edition 360, a full 360 degree market review ...

Stephen Mayne is Australia's leading shareholder activist, and his analysis of Share Purchase Plans (SPP) shows how poorly retail shareholders are often treated. For example, in my own case, an allocation of only 672 shares with a refund of $27,048 on a $30,000 application for **Auckland Airport** was not worth the paperwork, and the **Cochlear** story in Stephen's article is as bad.

It's great to welcome back my co-founder **Chris Cuffe** who describes his use of private debt funds in managing the portfolio of the **APS Foundation.** Read about the tax advantage of charitable subfunds as we near the end of FY20.

Then updates from leading Australian investment managers. **Matt Reynolds** describes three market facts and three mistakes everyone should consider, **Anton Tagliaferro** shows the types of companies he is now looking for, and **Kej Somaia** manages a multi-asset portfolio and explains how his assets have changed since COVID-19 hit. Decades of experience from these fundies.

It's easy to think that all index funds are the same, but it is often not easy to replicate an index. **Duncan Burns** describes what to look for.

Pamela Hegarty says the pandemic has accelrerated digitial and disruptive changes, and she highlights the areas she is now watching closely.

The share price of **Afterpay** has moved from $8 to $50 in the space of only two months, and **Lex Hall** checks the fair value placed on the stock by Morningstar analysts.

Each month, **Jonathan Rochford** reviews global media and provides links to stories most people have missed. Provocative, quirky, unusual and plain weird.

This week's White Paper from **Capital Group** offers five quick tips for retirees hit by market falls while drawing down a pension.

Small investors miss out as institutions and banks cash in

Stephen Mayne

Last week, we received this request from a reader.

> *Dear Editor*
>
> *I'm hoping you might consider publishing a commentary on the recent spate of share purchase plans and placements. The mechanism seems anomalous and disadvantageous from a shareholder's point-of-view. What intrigues and annoys me is that in almost all cases retail shareholders are not given the first and biggest bite of the (often very attractive and profitable) cherry. What seems to be the case is that institutional investors are given the bulk of the issue and smaller shareholders the residue (the crumbs).*
>
> *Surely directors of a company are supposed to act in the best interests of all shareholders and yet they appear to ignore this by not giving preference to the company's owners - the people they are supposed to represent. The recent SPP/placement by Cochlear illustrates the point and inequities.*
>
> *Thanks for your publication.*

The biggest equity capital-raising binge since the GFC is showing no signs of abating. However, Australia’s retail shareholders are getting increasingly scaled back and diluted by boards and investment banks.

After raising $1 billion from institutional investors, Ramsay Health Care initially proposed limiting its follow-on share purchase plan (SPP) for retail investors to just $200 million. But when $695 million came through the door from more than 41,000 applicants, it expanded this to $300 million, refunding $395 million.

Medical device company Cochlear trod a similar path, raising $880 million from institutions and then proposing a derisory $50 million cap on its SPP for retail investors. This cap was then reluctantly lifted to $220 million after 16,651 shareholders applied for $417 million worth of stock.

Allocate according to ownership

Neither Ramsay Health Care or Cochlear, even after lifting their SPP caps, adhered to the principle of dividing up the capital raising to reflect the relative proportions of the company owned by institutional and retail shareholders before the capital raising was launched.

It’s not hard to comprehend. If retail shareholders own 30% of a company, the SPP should represent 30% of the overall capital raising.

National Australia Bank never respected that concept. It was 48% owned by its 615,000 retail shareholders before the board decided to launch an emergency $3 billion institutional share placement at the knockdown price of $14.15 in late April.

Retail shareholders were promised a compensatory $500 million SPP at the same price which was always going to be swamped, given that if all 615,000 shareholders applied for the $30,000 maximum, a whopping $18.45 billion would have come through the door.

The last 12 months have seen a step change in company disclosure about capital raisings, so we now have comprehensive data from 25 companies in terms of how many retail shareholders were sent capital raising offers and how many actually applied.

This is how NAB did it on Wednesday:

"The SPP offer was made to approximately 615,000 eligible shareholders, with valid applications received from approximately 155,000 eligible shareholders for a total value of approximately $2.9 billion. Valid applications received represented a participation rate of approximately 25% of eligible shareholders (representing 21% by shareholding), with an average application amount of approximately $18,500."

NAB's directors succumbed to pressure and used their discretion to increase the SPP from $500 million to $1.25 billion, meaning they are only refunding $1.65 billion.

Imagine if all retail investors participated

The Australian Securities and Investments Commission's (ASIC) move last year to double the maximum amount of an SPP offer for individual investors from $15,000 to $30,000 has turbo-charged the structure as a capital-raising option, but imagine if all retail shareholders acted rationally.

NAB shares were 8.5% above the offer price when the SPP closed on May 22 but 75% of them, or some 460,000, didn't bother applying at all.

One of the problems is that financial intermediaries such as brokers, financial advisers and accountants are not passing on the details of in-the-money SPP offers to their clients. Administrative incompetence has diluted retail shareholders out of billions of dollars over the years.

Sadly, the biggest losers in Australia's anything-goes capital raising system are the retail shareholders who ignore an in-the-money offer. That is usually a substantial majority of the share register, as occurred with NAB.

Handsome fees to investment banks

Investment banks have now pocketed more than $300 million worth of fees, underwriting almost $20 billion worth of capital raisings over the past 10 weeks. They rarely get paid to underwrite SPPs. For instance, NAB's $3 billion institutional placement generated $39 million worth of fees for underwriters Goldman Sachs and Macquarie, while the SPP generated nothing.

This is partly why boards should increasingly turn to their retail shareholders for fresh capital rather than listening to investment banks and tapping their institutional clients for excessive funds whilst not leaving enough cash on the table for the retail shareholders.

There's more to come on this front. Lend Lease did a $950 million institutional placement last month, followed by a $200 million SPP. Gold miner Newcrest has a similar dilemma after it too did a $1 billion institutional placement but then proposed limiting its SPP to just $100 million.

At least they've worked out that their circa-60,000 retail shareholders, who will still probably throw about $500 million at the SPP, only own about 6% of the company, whereas they are being offered 9% of the capital raising.

A rare example indeed of institutional investors getting diluted.

Stephen Mayne is the Founder of Crikey, where this article was first published. He also updates data and writes at The Mayne Report. The author has participated in some of the SPPs mentioned in this story. See also The Mayne Report's article on best practice capital raising outcome announcements.

Why private debt is a hidden gem

Chris Cuffe

Among my various investment activities, I am the Portfolio Manager of the $110 million Australian Philanthropic Services Foundation (APS Foundation). This article focuses on how I have navigated the uncertainties and wild gyrations of investment markets during the COVID-19 pandemic and benefited from a relatively-large holding in private debt securities.

What is a public ancillary fund?

The APS Foundation is a communal philanthropic structure called a public ancillary fund, a structure which is very efficient and tax effective for people interested in philanthropy. It is particular attractive to those who need a tax deduction now but want the flexibility to undertake a regular flow of charitable giving over time.

At this time of year, APS Foundation attracts a lot of attention as people think about philanthropy and do their tax planning and prepare for the close of another financial year. I feel the privilege, excitement and 'pressure' of managing this Foundation and take it very seriously. The onset of the COVID-19 pandemic and resultant negative economic and market consequences have given me plenty to think about. Sometimes the words 'cold sweat' come to mind when investment markets fall 20%-30% virtually overnight and I think about how that may impact the APS Foundation and in turn its impact on the community!

The APS Foundation comprises around 300 giving funds (also known as sub-funds) established by individuals, families and companies. They make a tax-deductible donation of at least $50,000 to the Foundation, which is set aside into their own-named giving fund. Each year at least 4% of the giving-fund balance is given to charities recommended by the fund holder. The giving funds are pooled and invested together, with investment returns accruing to the underlying giving funds. Returns are tax-free, so good investment management can see the balance grow, increasing the amount for charities over time.

Investment objectives and strategy

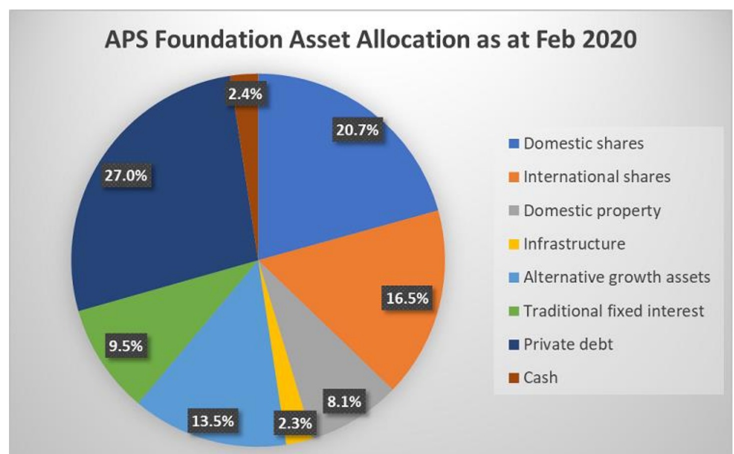
The investment objective for the APS Foundation is to achieve a return after fees at least equal to CPI inflation +4% per annum, measured over rolling seven-year periods. A lot of factors were taken into account before landing on this objective, including:

- the need to distribute a minimum of 4% per annum to charities
- the likelihood of inflation affecting the value of the investments and income generated
- the risk of capital or income loss
- the liquidity of the investments
- the costs of investment alternatives and transactions, and
- the benefits of diversification of investments.

With these investment objectives in mind, we set broad investment ranges to ensure we have plenty of flexibility.

I decided long ago that it was paramount that a charitable foundation, like APS Foundation, needed to have a well-diversified investment portfolio. That would be my best protection against unexpected negative surprises that investment markets have a habit of delivering more often than we sometimes think.

As at the end of February 2020 (just before COVID-19 started to hit hard) the asset allocation of the APS Foundation was as shown (right).



High allocation to private debt is an anomaly

Compared to say a typical balanced superannuation fund, the high allocation to private debt stands out. Private debt is a significant subset of broader credit markets, often resulting from private equity, securitisation and direct lending activities across various assets pools and corporate borrowers. Such exposures include leveraged loans, commercial, industrial and residential real estate loans, asset-backed loans and loans to businesses secured by their operating assets.

Generally speaking, private debt loans, as the name suggests, do not trade on open markets and hence are usually very illiquid (except for some asset-backed securities). Once a loan is made it is typically held to maturity, with terms generally ranging between one and five years, with varying repayment profiles.

Due to its illiquidity, private debt as an asset class will not suit all investors. But for a patient investor with a longer-term investment horizon, who is less concerned about liquidity and seeks attractive current income

returns, private debt funds can provide a good risk/return trade off versus high-yield bonds, for example. This suits APS Foundation.

Driven by changes to bank capital requirements

Since the GFC, changes in the bank regulatory capital environment in Australia have increased bank reserving requirements. Similarly, relatively buoyant equity markets and Australia's dividend imputation system have seen corporates and investors alike continue to favour equity over corporate bond issuances.

The **former** has led to a significant contraction in traditional bank lending to small and mid-sized businesses with limited real estate security for example.

The **latter** has perpetuated an underservicing of capital requirements for these and much larger enterprises through private credit.

This has created a 'funding gap' among Australia's major banks to these businesses, which has now been filled by a number of specialist non-bank lenders. This has greatly assisted the growth of the private debt market and the opportunity for investors like APS Foundation to participate in an area that was once only the domain of the banks. It is interesting to note that Australia's non-bank lending market is materially smaller as a percentage of the overall market relative to the US and Europe and is expected to continue to grow materially.

The nature of private debt markets

Typically, private debt funds, depending on their risk profile and security exposures, may yield between 5% - 15% per annum. While 'high yield' has generally been synonymous with high risk, this is mitigated if a focus is taken on senior secured investments. These rank in priority to other creditors or equity – particularly listed equity - for liquidity and payment and there is strong asset or cashflow backing to the loan. With a diversity of their underlying collateral, private debt markets deliver opportunities for experienced credit managers.

Australian-based providers of private debt who I have invested with include Revolution Asset Management, Realside Financial Group, PIMCO, Merricks Capital, Longreach Alternatives, Aquasia, Causeway Financial, Pure Asset Management, and Ventra Capital (of which I am also a shareholder and director). And there are many more in this growing market that I have not met.

Performance of the APS portfolio

So how has the APS Foundation investment performance fared of late? During the months of March and April 2020, when the pandemic hit hardest, the Foundation fell 6.1% in value. Although no one wants to see a negative result, this has been a credible performance relative to other multi-sector funds. During this same two-month period, Australian shares decreased 11.4%, unhedged international shares decreased 4.4%, listed property trusts decreased 21.5%, and fixed interest (as measured by the Bloomberg AusBond Composite Index) fell 0.3%.

I believe the private debt exposure has played a significant stabilising role in that result. We have carefully reviewed the value of all private debt in the portfolio to ensure they are realistic given the information currently known. This included a detailed enquiry with each underlying manager of the various private debt securities who in turn has done a granular review of each of their portfolios.

The investment objective of CPI inflation + 4% per annum after fees, measured over rolling seven-year periods, has been met to date, even taking into account the sharp falls over the last quarter. The returns since inception in mid-2012 are 10.1% compound per annum compared to the return objective of 5.9% compound per annum.

Apply these returns to a giving fund established seven years ago with a donation of $100,000 which has distributed the minimum 4% to charity each year. As at April 2020, the giving fund would have gifted $35,348 to charity and its balance grown to $140,949. The structure and its return deliver a compelling style of giving that allows a philanthropist to both give and grow money for charity.

Chris Cuffe is Chairman of Australian Philanthropic Services as well as Portfolio Manager of the APS Foundation. Anyone interested in knowing more about APS, including establishing a public ancillary fund before the end of the financial year, should check the APS website.

Chris is also involved with a number of other groups as a director, chairman and investment professional. Chris was one of the founders of Cuffelinks, the predecessor to Firstlinks. This article is general information and does not consider the circumstances fo any investors. Anyone wishing to know more about investments mentioned in this article should seek professional advice as private debts are not as secure as bank deposits or similar.

Three realities and three mistakes in market recoveries

Matt Reynolds

If market declines make you nervous, then you're not alone. Especially now, when COVID-19 and its economic impact are fuelling feelings of uncertainty around the world.

But while bear markets can be extraordinarily difficult, they also can be moments of great opportunity. Investors who find the courage and conviction to stick to their long-term plans are often rewarded as markets bounce back. To help put recent markets into perspective, we outline three facts about market recoveries and three mistakes that investors should avoid.

Three facts about market recoveries

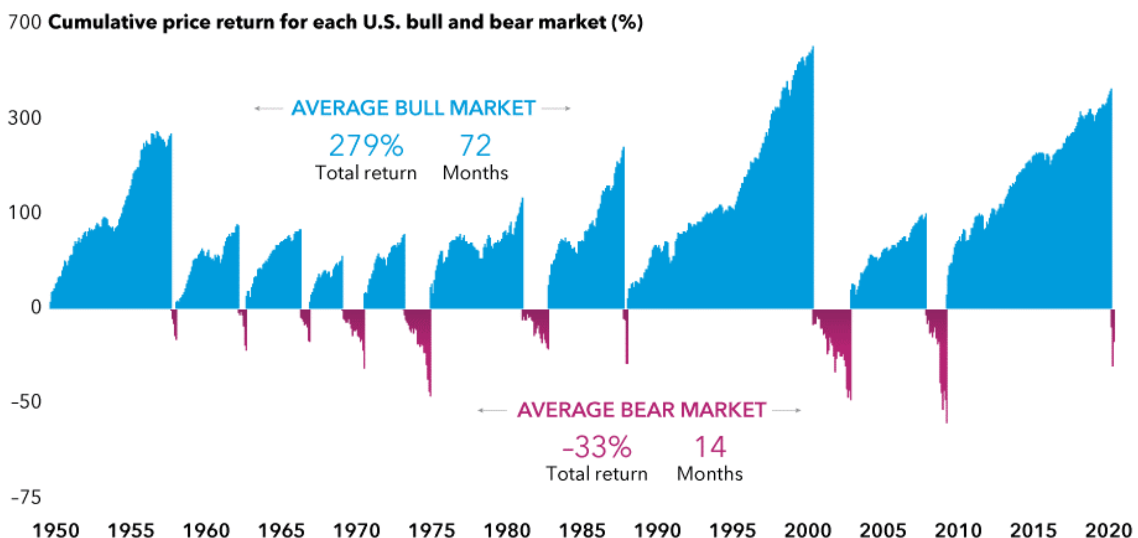
Fact #1: Recoveries have been much longer and stronger than downturns

The good news is bear markets have been relatively short compared with recoveries. They can feel like they last forever when we're in them but in reality, they are much less impactful compared to the long-term power of bull markets.

Although every market decline is unique, in the US, the average bear market since 1950 has lasted 14 months. The average bull market has been more than five times longer.

The difference in returns has been just as dramatic. Even though the average bull has averaged a 279% gain, recoveries are rarely a smooth ride. Investors must often withstand scary headlines, significant market volatility and additional equity declines along the way. But investors who remain focused on the long term are often better equipped to look past the noise and stick to their plan.

Fact #2: After large declines, markets have recovered quickly



Sources: Capital Group, RIMES, Standard & Poor's. As of 30/4/20. The 2020 bear market is considered current as of 30/4/20 and is not included in the "average bear market" calculations. In all other periods, bear markets are peak-to-trough price declines of 20% or more in the S&P 500. Bull markets are all other periods. Returns shown on a logarithmic scale. Returns are in USD.

Of course, we don't know exactly what the next recovery will look like, but history shows us that stocks have often recovered sharply following steep downturns. We tracked the 18 biggest US market declines since the Great Depression, and in each case the S&P 500 was higher five years later. Returns over those five-year periods averaged more than 18% per year.

Returns have often been strongest after the steepest declines, bouncing back quickly from market bottoms. The first year following the five biggest bear markets over the last 90 years averaged 71%, underscoring the importance of staying invested and avoiding the urge to abandon stocks during market volatility.

Five biggest market declines and subsequent five-year periods 1929-2019

Periods of decline	Decline	S&P 500 12-month returns (Positive periods (23) / Negative periods (2)): 1st year after low	2nd year	3rd year	4th year	5th year	Average annual total return for the 5-year period
7/9/29–1/6/32	-86.2%	137.6%	0.5%	6.4%	56.7%	16.5%	35.9%
6/3/37–28/4/42	-60.0	64.3	9.0	31.1	32.2	-19.9	20.0
11/1/73–3/10/74	-48.2	44.4	26.0	-2.9	11.8	12.8	17.4
24/3/00–9/10/02	-49.1	36.2	9.9	8.5	15.1	18.1	17.2
9/10/07–9/3/09	-56.8	72.3	18.1	6.1	15.7	23.6	25.3
Average		70.9	12.7	9.8	26.3	10.2	23.1

Sources: Capital Group, RIMES, Standard & Poor's. As of 30/4/20. Market downturns are based on the five largest declines in the S&P 500's value (excluding dividends and/or distributions) with 50% recovery after each decline. The return for each of the five years after a low is a 12-month return based on the date of the low. The percentage decline is based on the index value of the unmanaged S&P 500, excluding dividends and/or distributions. The average annual total returns include reinvested dividends and/or distributions but do not reflect the effect of sales charges, commissions, account fees, expenses or taxes. Investors cannot invest directly in an index. Past results are not predictive of results in future periods.

Fact #3: Some of the world's most influential companies were born during market recoveries

Many companies started during tough economic periods and have gone on to become household names.

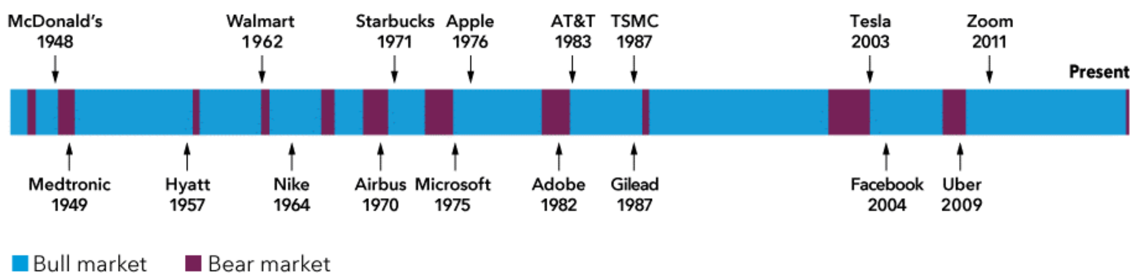
To highlight just a few in the US market:

- McDonald's emerged in 1948 following a downturn caused by the US government's demobilisation from a wartime economy.
- Walmart came along 14 years later, around the time of the 'Flash Crash of 1962', a period when the S&P 500 index declined more than 22%.
- Airbus, Microsoft and Starbucks were founded during the stagflation era of the 1970s, a decade marked by two recessions and one of the worst bear markets in US history.
- Not long after that, Steve Jobs walked into his garage and started a computer company called Apple.

History has shown that strong businesses find a way to survive and even thrive when times are tough. Those that can adapt to difficult conditions and become stronger often make attractive long-term investments.

Bottom-up, fundamental research is key to separating which companies may help lead a market recovery, and which are more likely to be left behind.

Notable companies, by year they were founded



Source: Capital Group. As of 30/4/20.

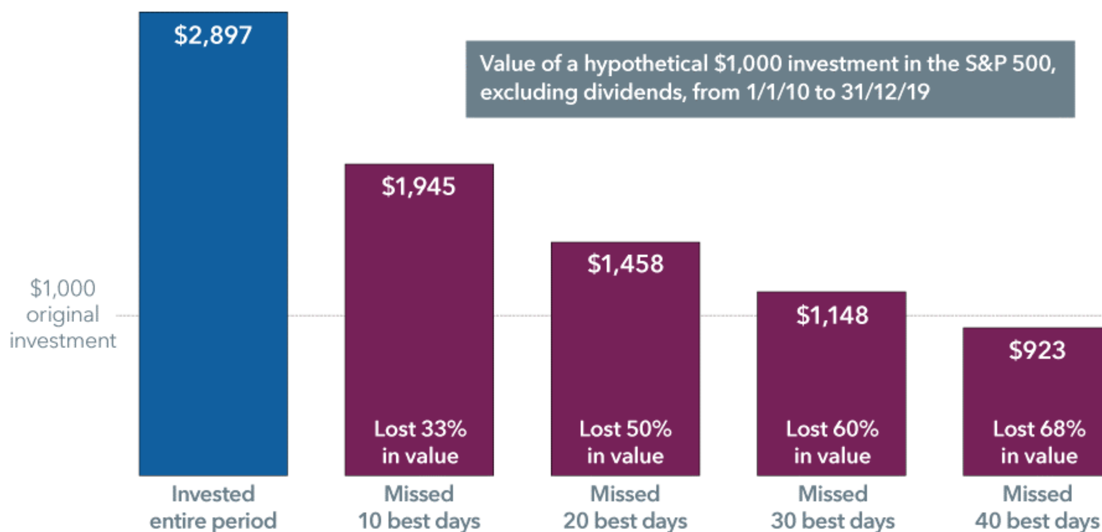
Three mistakes investors should avoid

Mistake #1: Trying to time markets

It's time, not timing, that matters in investing. Taking your money out of the market on the way down means that if you don't get back in at exactly the right time, you can't capture the full benefit of a recovery.

Consider an example of a hypothetical investor who sold stocks during the US market downturn of 2008–2009, and then tried to time the market, jumping back in when it showed signs of improvement. Missing even the 10 best days of the recovery would have significantly hurt that investor's long-term results. The more of the 'good' days were missed, the steeper the loss.

Investors who are more hesitant to put all their excess capital to work at once may want to consider dollar cost averaging, which often provides stability in volatile markets.



Mistake #2: Assuming today's negative headlines make it a bad time to invest

Today's economic and geopolitical challenges may seem unprecedented, but a look through history shows that there have always been reasons not to invest. Despite negative headlines, the market's long-term trend has always been higher.

Consider an investment in the S&P 500 on the day Pearl Harbour was bombed in 1941. Someone who stayed invested for the next 10 years would have averaged a 16% annual return. Likewise, a $10,000 investment in the S&P 500 Index on the day Lehman Brothers declared bankruptcy in 2008 would have grown to over $30,000 10 years later. History has provided numerous examples of this.

Great investment opportunities often emerge when investors are feeling most pessimistic. The coronavirus outbreak may be unlike anything we have faced before but uncertainty is nothing new to the market, which continues to be resilient over time.

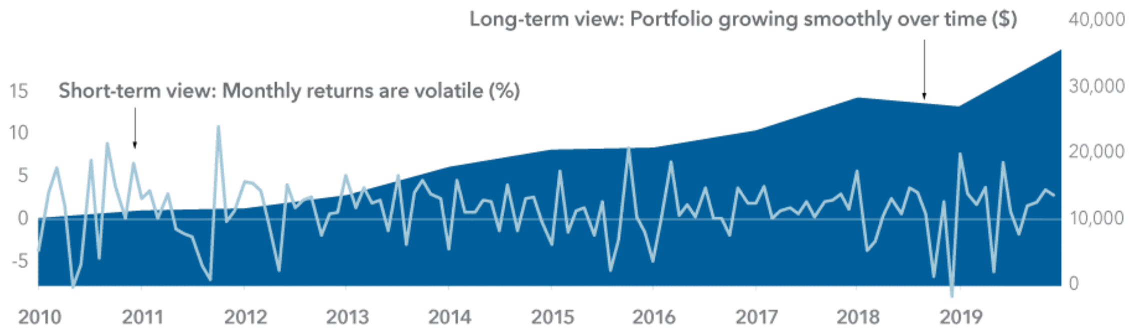
Mistake #3: Focusing too much on the short term

Market volatility is especially uncomfortable when you focus on short-term ups and downs. Instead, extend your time horizon to focus on the long-term growth of your investments and the progress you've made toward your goals.

Consider the chart below that shows contrasting perspectives of the same hypothetical investment. The short-term view is one that many investors have of their portfolios, tracing returns over short periods of time.

The long-term view plots the same investment over the same period, but shows annual change in the portfolio value invested instead. With this perspective, the short-term fluctuations have smoothed out over time, and the picture of a growing portfolio becomes clearer.

Bear markets don't last forever. Maintaining a long-term perspective can help investors to focus on the goals that matter most.



Matt Reynolds is an Investment Director at Capital Group, a sponsor of Firstlinks.

For more articles and papers from Capital Group, click here.

How COVID-19 prompted multi-asset portfolio shifts

Kej Somaia

Is asset allocation more important than stock selection? We certainly believe so, and the turbulence of markets in recent times has highlighted the need for a well-diversified portfolio with downside protection.

This is the goal of our multi-asset strategy. Every six months we pore over a raft of economic data, in order to review and reset our core asset allocation. The latest review, completed in April 2020, captured one of the most dramatic periods in recent economic history.

Here's what we made of it.

Raging bull meets ferocious bear

In our December 2019 review, the question on everybody's minds was: how long would this bull run last? Now, the question is: how long will this downturn last?

The conversation has flipped 180 degrees in a matter of months.

In our latest review, we tracked every market crash (a fall of 20% or more) since 1929, in terms of how long it took the United States' key stock market index, the S&P 500, to recover to the same level it had reached immediately before the crash.

While the Great Depression recovery blew out to 266 months, it took as little as three months for other crashes to make up lost ground. Excluding the Depression, however, the average recovery period was 27 months.

That means, if this is an 'average' crash, then it's likely that a recovery will take two years or more. But averages can be misleading. At this stage, we simply don't know the true scale of this downturn.

Our team took a somewhat sober view of the outlook, and incorporated a filter for highly-turbulent regimes in the recent asset allocation review.

Figure 1: Market falls and recoveries since 1929

Period	Decline of the S&P 500	Time to Recovery (months)
Sept 1929 - June 1932	-85%	266
Feb 1937 - Apr 1942	-57%	48
May 1946 - Feb 1948	-25%	27
Aug 1956 - Oct 1957	-22%	11
Dec 1961 - June 1962	-28%	14
Feb 1966 - Oct 1966	-22%	7
Nov 1968 - May 1970	-36%	21
Jan 1973 - Oct 1974	-48%	69
Nov 1980 - Aug 1982	-27%	3
Aug 1987 - Dec 1987	-32%	19
July 1990 - Oct 1990	-20%	4
Mar 2000 - Oct 2002	-49%	56
Oct 2007 - Mar 2009	-57%	49
Feb 2020 - Apr 2020	-34%	ongoing
Average	-39%	46
Average ex Great Depression	-35%	27

Source: Bloomberg and Goldman Sachs 30 April 2020

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This prompted us to make a significant cut to our equities exposure: the collective weight to Australian and global equities has gone from 50% to 29% (comprised of 19% global equities and 10% Australian).

The key reason is that we are cautious about the continued knock-on effects from the COVID-19 outbreak. While equity markets may be trying to look through into a more optimistic future, we think it could be premature.

Government support for fixed income: a gamechanger

A key difference between this and other downturns of the last 100 years is the unprecedented fiscal and monetary stimulus. Australia's fiscal stimulus is among the largest in the developed world, at 6.9% of GDP (in line with the UK and US, both at 6.9% - according to the International Monetary Fund (IMF) as at 8 April 2020). This has been adjusted from earlier higher estimates due to the $60 billion lower stimulus from JobKeeper.

Governments around the world have pumped money into the economy to try to stave off economic disaster. However, these initiatives will have an expiration date which may - or may not - align with the length of the downturn.

With this support in mind, a notable change to our portfolio is the increased exposure to bonds and credit. We increased Australian Government Bonds from 21% to 33% of the portfolio, investment-grade credit from 12% to 20%, while global bonds went from zero allocation to 8% and high-yield credit from zero to 5%.

We made this decision after taking a view on where we think the global economy is moving, and the likely long-term values for inflation, risk free rates, long-term bond yields and earnings growth. We then tilt the asset allocation based on this outlook.

Figure 2: CFS Multi-Asset Real Return Fund Neutral Asset Allocation (NAA) as at April 2020

Real Return Fund NAA	Nov 19		Apr 20	Change
Cash	5.0%	↔	5.0%	0.0%
Australian Government Bonds	21.0%	↑	33.0%	12.0%
Global Bonds (hedged)	0.0%	↑	8.0%	8.0%
Credit-Investment Grade	12.0%	↑	20.0%	8.0%
Credit-High Yield	0.0%	↑	5.0%	5.0%
Emerging Markets Bonds	10.0%	↓	0.0%	-10.0%
Australian Equities	20.0%	↓	10.0%	-10.0%
World Equities	30.0%	↓	19.0%	-11.0%
Emerging Markets Equities	0.0%	↔	0.0%	0.0%
Commodities	2.0%	↓	0.0%	-2.0%
Total	100.0%		100.0%	

Our team likes investment grade and high-yield credit at the moment, as we believe it delivers a lower risk portfolio at the aggregate level, especially with strong central bank support. The US Federal Reserve and the European Central Bank have indicated that they will not only be purchasing government bonds and investment grade credit, but for the first time, quality high-yield bonds too.

This is a game-changer for fixed income, particularly in a portfolio context, and it's one reason why we are reducing risk away from higher volatility equity allocations.

Although government bonds were occasionally caught up in the recent sell-off, alongside riskier assets like equities, we saw the traditional relationship between the two asset classes play out as we hoped: government bond exposures provided diversification to equity exposures during the increased volatility in March.

While liquidity was temporarily scarce, central bank initiatives to inject capital back into the economy subsequently eased anxieties. Given the need to manage risk in the portfolio, our allocation to Australian government bonds has increased significantly, but remains concentrated in shorter maturities.

Managing risk over time

We don't rely solely on the six-monthly neutral asset allocation (NAA) to construct our portfolio. We also have the benefit of dynamic asset allocation (DAA) which is reviewed weekly and allows us to make investment changes based on shorter-term market dynamics.

While individual investors would find it difficult to manage these two styles of asset allocation, the combination has allowed us to deliver additional returns and reduce portfolio risk, at the same time as meeting our real return objective. Having that flexibility built into our approach is helpful in times like these.

Even if you lack the firepower of a team of professional analysts, there are still lessons to be taken from our multi-asset strategy. In particular, the observation that macro events and economics have a significant impact on market and portfolio risk. As such, it can be appropriate to make asset allocation changes that reflect the current environment as well as the economic outlook.

Kej Somaia is Co-Head of Multi-Asset Solutions at First Sentier Investors (Australia), a sponsor of Firstlinks. This material contains general information only. It is not intended to provide you with financial product advice and does not take into account your objectives, financial situation or needs.

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Three key company features in assessing the outlook now

Anton Tagliaferro

Global sharemarkets have rallied strongly from their March lows thanks in the main to the huge fiscal and monetary actions by governments and central banks around the world. However, the economic outlook remains uncertain as the length and depth of the economic downturn as well as the strength and sustainability of the expected recovery remain difficult to forecast.

In Australia, the unemployment rate is likely to go over 10%, with activity at virtually zero in many sectors. Some of those unemployed people will return to work as we start seeing parts of the economy reopen such as restaurants and casinos.

Demand lower for longer

There are many differing theories and views about whether the recovery will be V-shaped, U-shaped, L-shaped or W-shaped. We believe we are moving into an environment where demand may be sustainably lower for many sectors. As the lockdown unwinds, we will get a fairly strong short-term recovery with a jump in spending as people rush out and spend things such as their JobKeeper allowance and government grants—the question then will be *how sustainable will demand be given potentially much higher unemployment?*

We believe that the Australian economy won't return to the same level as it was pre-COVID for some time. Some sectors which employ a lot of people—such as immigration-related activities, tourism, student travel and accommodation—look like they will take a fairly long time to recover. Meaning that certain parts of the economy could be subdued for a while.

Thus at IML, we are going through a stock-by-stock analysis to assess what we believe will be the ongoing, sustainable demand and revenue from various sectors of the economy. One factor that concerns us is the high level of household debt in Australia where in places like Sydney and Melbourne, it is not unusual to see mortgages of half a million to a million dollars or more.

While low interest rates will help people in jobs keep up with their mortgage payments, if unemployment goes up—especially in well-paid jobs such as airline pilots, hotel management and advertising agency staff and where some people probably have quite large mortgages—then it is probable that the overall level of demand will take a while to recover once the government stimulus fades.

Assessing companies and prices

Given the economic uncertainty, as well as reviewing the demand outlook for each industry, we are assessing the outlook for prices of goods and services within each industry. This is important as lower prices can have a big impact on the bottom line of companies, especially in a low-demand environment.

On the flip side, we are also looking for factors that may help certain companies improve their bottom-line outcomes. Initiatives such as increasing market share, if they have weak competitors or the ability to cut costs to drive productivity. It is also particularly important for companies to have a strong balance sheet given the current uncertainties.

And the last part of the puzzle is to assess whether a company’s share price is adequately pricing in the future outlook, and clearly we are looking for what we believe are undervalued companies.

Positioning our Australian equity portfolios for the current outlook

This is a period of time where virtually every business in the world has been impacted to some extent by the shutdowns and travel bans.

Some companies are adjusting quickly by tweaking their business model and many are being quite nimble. Most companies we talk to are cutting costs by cutting staff—which is unfortunate for the people involved—but in a lower demand environment, companies have to trim their organisational strcture.

We are mainly sticking to companies where the level of demand seems more transparent, in terms of where the economy is sitting today and where it will probably grow in future. Examples where demand is not easily forecast might include a building materials company or a company that supplies toilets for renovations. There is a question mark on the future level of home renovations given that unemployment may increase and demand for housing will slow as immigration reduces.

We feel fairly comfortable on the positioning of our portfolios for what we believe will probably be a recovery to a lower level of sustainable demand compared with the economy before the epidemic.

Three attributes we are seeking in our portfolios now

We are looking for the same attributes as always seek but referencing the more uncertain environment and subdued outlook.

We are looking for companies with:

1. a ***strong competitive advantage***, for example, companies that are number one or two in their industry, which gives them scale.

2. ***recurring, predictable earnings*** that will be relatively stable, even in a recessionary environment and that continue to pay healthy dividends to shareholders—examples are companies like Telstra, Amcor and Coles.

3. ***experienced and capable management teams*** as a recessionary environment is when good management stands out. We are looking for high quality management teams that have been around a while that have seen various cycles.

As mentioned earlier we are also focusing on companies' balance sheets as this is really important in times like these where many companies' earnings could be under some pressure. A strong balance sheet when competitors are weak could give an ability to take advantage of opportunities in the marketplace.

We want to buy these companies at a ***reasonable price***. In the current environment this means that we are looking to buy companies where a more cautious outlook is already priced in.

Anton Tagliaferro is Investment Director at Investors Mutual Limited. While the information contained in this article has been prepared with all reasonable care, Investors Mutual Limited (AFSL 229988) accepts no responsibility or liability for any errors, omissions or misstatements however caused. This information is not personal advice. This advice is general in nature and has been prepared without taking account of your objectives, financial situation or needs. The fact that shares in a particular company may have been mentioned should not be interpreted as a recommendation to buy, sell or hold that stock.

Is Afterpay really worth $50?

Lex Hall

Valuing a company is a difficult exercise at any time, but how do you pin down a stock that recently traded between $8 and $50 in the space of only two months? That's the Afterpay (ASX:APT) experience. The sellers at $8 are gnashing their teeth and the buyers at $50 are living in hope. It's been a wild ride for a business established only a few years ago in 2014 which does not yet make a profit.

A recent boost for the company with a market value of over $12 billion is the planned inclusion in the MSCI Australian Index. This Index measures large- and mid-cap performance and includes about 85% of the float-adjusted market capitalisation in Australia.

Like many fund managers, Morningstar analysts who cover Afterpay are ultimately required to put a fair value estimate on its price. On 1 April 2020, Analyst Mark Taylor wrote:

"We reduce our fair value estimate on Afterpay to $20.50 per share (from $23.50 previously) after reviewing its outlook following the COVID-19 outbreak ... We forecast the company to be profitable from fiscal 2022 onwards (roughly $100 million of NPAT), with scale benefits growing NPAT to about $300 million in fiscal 2024. Our modelling suggests only small changes to key drivers like financed sales growth, margins earned from merchants, receivable impairments are needed to materially impact its intrinsic value."

As the price of Afterpay moves around so much, Shaun Ler, Associate Equity Analyst at Morningstar who also covers the stock, gave an updated view at the end of May. He said:

"Afterpay has good growth potential but I'm cautious about how leveraged it is to consumer spending, especially the discretionary and fast fashion sectors that Afterpay focuses on. The COVID-19 economic downturn is driving up unemployment. There is also a variety of competition in this space, like Zip, Latitude, and the global Buy Now Pay later (BNPL) player Klarna.

"I feel the current share price is optimistic and is overlooking the near-term risks, which assumes that bad debts won't rise and discretionary spending will keep rising. To me it looks like another hyped-up FOMO rally."

Ler believes the main reasons Afterpay's share price has rallied so much are:

1. The recent third quarter update (in mid-April) flagged that COVID-19 has not yet impacted sales volume or impairments
2. It recently announced a partnership with eBay Australia
3. Tencent recently acquired a stake
4. It will be included in the MSCI Australia Index

The following chart from Morningstar shows the Afterpay share price since January 2020, with the 26 May 2020 peak of $50.01 highlighted (late update: at time of going to press, Afterpay surged another 5.5% on Wednesday 3 June to close at $52.26).

Reasons for the cut in the fair value price

The Australian Bureau of Statistics has tipped that 86% of Australian companies are vulnerable to the coronavirus-induced downturn. For Afterpay's demographic —which includes millennials and casual workers— the future is bleak: layoffs and cuts to working hours have eroded their purchasing power. Afterpay has about 7.3 million active customers and its business model is financing discrete purchases by four equal repayments.

On the reasons for the cuts to the fair value price, Afterpay carries a very high uncertainty rating and does not have a 'moat', in part because of the plethora of BNPL providers in the market. The price also factors in slower growth in customer numbers and spending activity as well as higher bad debt expenses.

Despite the immediate gloom, a few big factors weigh in favour of the company. The first is the online presence, which becomes even more meaningful in a world where shops are closed and consumers are confined to their homes. Another is the strength of their balance sheet, which should see it through the downturn.

The other factor is the government's gigantic rescue package, which is designed to act as a barrier to the avalanche of layoffs across sectors.

"We think Afterpay is in a position to weather the current pandemic. It is overweight online and should derive a partial offsetting benefit to the consumer downturn from retailers rushing to enhance their online presence," Taylor says.

"Fiscal stimulus and monetary easing should help to ease the severity of unemployment and bad debts. The balance sheet looks reasonable and it should withstand the current downturn."

The ability to maintain financing and focus on credit quality will be crucial, and is something Taylor thinks is possible. That will however mean a pause in growth plans.

"Doing the opposite significantly increases the risk of losing access to funding or being charged significantly higher rates. For example, Afterpay is currently creating a new feature to allow customers to pay a higher initial instalment and to transact higher amounts."

Taylor has trimmed his forecasts for Afterpay's fiscal 2020 total transaction volume (TTV) from $11 billion to about $10.5 billion. And he expects the full brunt of the downturn to be felt in fiscal 2021 and has cut his TTV forecast from $18.8 billion to $15.7 billion.

Temporary setback, rebound in spending

Despite the revised forecast, Taylor reckons the COVID-19 downturn will be temporary. Up to 75% of BNPL sales for Afterpay are processed online, and once a pandemic treatment arrives, sentiment and spending should follow suit.

"We also anticipate a rebound in spending activity starting fiscal 2022, driven by the likely availability of a coronavirus treatment which should help normalise consumer confidence, store footfall and subsequently economic conditions."

Further into the future, Taylor maintains Afterpay can exceed its targeted fiscal 2022 TTV of $20 billion, and forecasts TTV to grow to $25.1 billion for the year, rising to about $39.5 billion by fiscal 2024.

Lex Hall is Content Editor for Morningstar Australia. This article is general information and does not consider the circumstances of any investor.

A full report and free trial with instant access are available on Morningstar Premium at this link, including the portfolio management service, Sharesight.

Choosing an index fund is more than just the expense ratio

Duncan Burns

Index funds were initially labelled a 'sure path to mediocrity' in their quest to mirror benchmarks. But since the first index fund was launched some 45 years ago, millions of investors across the world have taken advantage of this easy-to-implement investment vehicle that offers transparency, diversification, low costs and tax efficiency.

Many investors have found the search for winning active managers an exciting but ultimately unrewarding experience. In contrast, index funds have regularly produced returns that are 1-2% above the average active managers.

(Having said this, even investors who clearly recognise the powerful case for index funds often find a place in their carefully-constructed portfolios for some favoured actively managed funds. At Vanguard, it is not a case of having index or active management to the exclusion of the other).

Let's talk about how to go about picking an index funds. When it comes to selecting a manager, there are a lot of options out there.

Costs are not the only differentiator

Driven in part by lower direct and indirect costs, which have benefited *all* investors, index products continue to grow in efficiency, popularity, and volume.

As a result, index fund expense ratios have compressed meaningfully across the industry and fee differences between funds have become less of a differentiator.

While this broad-based downward shift in index fund expense ratios has undoubtedly resulted in better investment outcomes and savings for all index investors, it has also created a new dilemma.

How does an index investor select managers and funds from the pack in this new 'everyone is a low-fee provider' environment? An investor might reasonably ask, how hard can indexing be?

Just like baking, all it takes is to follow a recipe precisely. Flour, water, yeast and a few hours later, the oven yields a lovely crisp loaf of sourdough. But as many have discovered on novice baking journeys brought on by the pandemic, the process is much more than throwing together a couple of ingredients and dropping it in the oven.

Indexing is not dissimilar. Resources, index expertise, investment sophistication and other factors can provide an edge. Investors should not merely pick the lowest cost index fund because, as with baking, the quality of the ingredients and the skills of the baker matter.

Looking beyond expense ratios

Prudent investment selection cannot be achieved by focusing on cost alone.

When searching for and selecting between index investment options, investors should use a decision-making framework that takes into account a range of factors, including expenses, portfolio management capabilities, securities lending programmes, pricing strategies and scale in more equal weights than in the past.

A recent whitepaper by Vanguard provides a framework to help investors select the best index fund managers. Below are some of the main points covered.

Exploring the factors that matter

Organisational incentives – Index fund managers come in all shapes and sizes. The details here are important because an asset manager's philosophy defines the incentives that drive the firm's business strategy. Does the investor's interest or the asset manager's interest come first?

Portfolio management track record – Despite the boiler plate warnings, "past performance, while not a guarantee of future performance", this is actually a great place to look. What historical track records do the index managers and funds have when it comes to performance after fees? Good index managers can track tightly and add incremental value to cover some or all of the management fees. Process frictions, inefficiencies and an inability to capture value add opportunities, like a thousand little papers cuts, will show up over time in long-term performance.

Buy/sell Spreads – When it comes to the total cost of ownership, buy/sell spreads must be factored in. What's the point of going with a low expense ratio fund if it is lost on high spread costs?

With great scale comes better returns – Scale is a key differentiator and one that is increasingly difficult for new entrants to achieve. Scale enables asset managers to lower fixed trading costs like commissions and ticket charges, track or replicate benchmarks with greater precision and strengthen relationships with trading partners.

Expense ratio – I know I said it did not matter anymore, but there are a few managers and funds still charging high active-type prices for index products. This is an obvious red flag.

Managing an index is harder than it looks

Index equity managers should produce returns that are, on average, approximately equal to their benchmark index minus the fund's expense ratio.

This concept applies broadly across markets, while the costs—and the consequent performance drag—range from minimal in developed markets to modest in emerging markets. For sophisticated index fund managers, opportunities exist to add value through the daily management of the portfolio.

Successfully taking advantage of these opportunities can effectively offset the expense ratio and increase investor returns.

Simple to understand, yes. Simple to execute, no.

Indexing is simple for investors to understand and use. It is this perception of indexing, of merely meeting a set benchmark, that has led to it being known as 'passive' or 'average' investing. Indexing certainly is simple for investors to understand and use but it is definitely not simple to execute. Heavy investment activity and resourcing is required.

Not all indexers are the same, and this framework shows where to look in an index fund search.

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Disruptive technology is fast-forwarding into the future

Pam Hegarty

Global lockdowns have accelerated the adoption of new technologies. The digitalisation trend has moved forward with a leap, benefiting from the stay-at-home measures to deal with the coronavirus pandemic and the boost these gave to e-commerce, remote working and other tech areas. Satya Nadella, Microsoft's chief executive officer, referred to "*two years of digital transformation in two months*".

We see several key trends:

- **Adoption of cloud computing**: Growth is driven by the need for remote working, online entertainment and telemedicine. Other factors include mass notification systems (MNS) and the remote provision of services. In terms of MNS, we have seen more and more governments use them to send emergency communications to one or many groups of people. And with much of the world in lockdown, services providers have been using augmented reality (AR) through customers' smartphones to identify and troubleshoot problems remotely.
- **Acceleration of e-commerce**: Visa recently reported that in Latin America, the number of people using Visa credit card online increased by 20% (13 million people) in one quarter.
- **Digital payments**: Similar to the above, there has been a rapid increase in 'card not present' transactions. This is a card transaction, made either online or by phone, where the card is not physically present.
- **Uptake of 3D printing**: Thanks to the often flexible and local nature of 3D printing, individuals and companies have taken to using it. As a case in point, Cisco employees have been producing face shields for healthcare workers.
- **Automation**: In addition to, say, robots in factories, there has been growing interesting in software to automate customer services and other business functions.

Future investment strategies

Uncertainty remains, both about the duration of the pandemic and the severity of the recession. Stock markets might be too optimistic about the timing and strength of an economic rebound. Our strategy is to stay focused on our secular growth themes of cloud computing, artificial intelligence, data analytics, automation and the Internet of Things (IoT).

We aim to maintain a balanced portfolio by owning defensive positions that could fare well during periods of heightened volatility and companies that have sustainable business models and exposure to long-term secular growth themes but may face a more challenging short-term outlook.

To this end, we hold slightly higher cash positions at the moment and remain flexible to buying stocks linked to the above themes should their valuations come down due to volatility.

The opportunities in coming months

The pandemic and resultant economic recession shine a spotlight on societal issues where technology can create solutions:

- **Inequality** – especially via better access to broadband and financial services and banking.
- **Renewable energy** – harnessing solar and wind energy to power the data centres behind the cloud.
- **Increasing the capacity of the healthcare system** – technology can monitor a patient's health at home while telemedicine can help to treat the sick at home.

We are currently going through a period of profound change that offers numerous opportunities for investors to position their investment portfolios for further growth in disruptive technology.

Innovation is not just technology

A promising strategy should interplay the latest developments from solid players across diverse sectors, and capture performance that is sustainable both in financial and ESG terms. For example:

- 'Disruptive technologies' do not all fall within the tech sector.
- Real innovations exceed sector barriers, providing investment opportunities that purely sector-based strategies may miss.
- Targeting companies that are sustainable in both the environmental, social and governance (ESG) and the financial sense, i.e. with high ESG standards as well as robust business models that ensure competitiveness and growth.

Our disruptive technology strategy looks for stock ideas throughout the economy and is not limited to the technology sector. For example, say we own Amazon because of its strong position in cloud computing, even though the stock is classified in the consumer discretionary sector like other retail companies. The stocks we would pick can be found in sectors as diverse as industrials, communications services, healthcare, financials, consumption and energy.

In addition, we monitor emerging technologies, such as 3D printing, blockchain and renewable energy. We can take exposure through stocks in related fields rather than directly targeting niches. So, cryptocurrencies can be represented by providers of powerful semiconductors that enable rapid calculations.

In cloud computing, we invest in both the large companies that provide cloud infrastructure services, as well as companies that provide software applications as a cloud service.

One can invest in artificial intelligence and data analysis via the financial services and healthcare sectors. Finally, the Internet of Things can involve sometimes unforeseen applications. Stories are proliferating of people saved by their internet-connected watch allowing for a rapid medical diagnosis.

A better world or the best of worlds?

We believe that the use of machine-learning algorithms will create economic value by making long and complex processes more efficient and by providing enhanced decision-making tools. However, there are pitfalls. The effectiveness of any algorithm depends on the quality of the data used to train the artificial intelligence.

For example, genetic data has historically been biased because it was primarily sourced from non-diverse populations of European descent. In addition, AI for facial recognition can be misused by governments and other actors to invade privacy or to create fraudulent videos. This illustrates the need for regulation to ensure proper use of these powerful tools.

Beyond moral and technical considerations, the question of abuse of dominance arises when one looks at (the giants of) technology. It has given rise to debate about the need to regulate or even dismantle companies. We are actively monitoring stocks that are exposed to the threat of tighter regulation.

Investment managers should take an active, fundamental approach to investing in disruptive technology trends. We meet companies, suppliers, customers, competitors, industry experts, academics and others to enhance our knowledge of the changing technology landscape.

The right time to invest?

Looking at valuations, technology stocks are currently trading at a 10% premium to the broader market based on a forward-looking 12-month P/E ratio. This is in line with the historical median since 1995. We believe this premium is justified by the superior growth prospects of the technology sector.

The current macroeconomic and geopolitical environment is highly uncertain. Most of the sectors we invest in, including technology, industrials and consumer discretionary, are cyclical. However, we believe investing in companies with strong secular growth drivers makes sense across cycles. Even in the event of a sharp slowdown, we expect companies not to freeze all of their technological investments but focus on the more innovative parts of the industry.

Accordingly, we view disruptive tech investing as a long-term (three-to-five-year) strategy, which involves keeping a close eye on the changes that can arise rapidly in this field.

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Media worth consuming - May 2020

Jonathan Rochford

A monthly look at dozens of local and global media articles that often do not receive mainstream coverage in Australia.

Finance

A cascade of bankruptcies is starting to hit the US economy. US auto dealers are overstocked with new cars and are having to rent space to park new arrivals. The real work for mortgage servicers will begin after the pandemic ends, when borrowers have to start repayments again. Credit markets point to more pain ahead for equities. Stanley Druckenmiller poured a bucket of cold water on asset prices and central banks.

Hertz has filed for bankruptcy with formerly AAA-rated bonds secured by its rental fleet at risk of taking a loss and its November corporate bond issue expected to default before making its first interest payment. America's largest shopping centre skipped its last two monthly debt repayments. WeWork's non-payment of rent is slamming CMBS transactions. A growing list of emerging market countries have their sovereign debt trading at distressed levels. Ten of the worst bond deals of the last decade. After four decades of strong real returns on bonds, history points to decades of negative real returns ahead.

Leveraged loan investors are regretting their purchases of covenant lite loans. The Federal Reserve is going to participate in leveraged loans with phony EBITDA calculations however sub-investment grade bonds are getting far less help from the Fed than the market is pricing in. UBS sees a world of pain for CLOs unless economies see a rapid recovery. Credit unions focussed on industries currently shutdown are suffering badly. Illinois pulled a bond issue after lacklustre demand. The state's investment grade rating is likely to be lost and the existing

debt is trading at emerging market yields. Deutsche Bank is going to struggle to find buyers for its bad bank assets. The US Government has gone from a deficit of $1 trillion per year to a deficit of $738 billion a month.

Bitcoin miners are getting extra income from load shedding agreements. Unicorns have done an extraordinary job of losing tons of money in industries where others were making decent profits. Bureaucracy is killing investment returns at many pension funds. The man making a small fortune betting against private equity. Michael Hintze's credit hedge fund is down 50% in two months. There's three parts to risk; the odds of failure, average consequences of failure and tail end consequences.

Politics and culture

The media castigated Florida's Covid-19 response whilst lionising New York's but the data shows Florida's response was far superior. Nursing homes in New York acquired Covid-19 after they were forced to accept infected residents discharged from hospitals. New York's Governor claimed they had a low level of deaths in nursing homes but the statistics had been deliberately doctored. New York City forced a hospital offering free care to close in the middle of the pandemic because of a debate over religious beliefs. New York's Governor begged for out of state health workers to help, then he slugged them with double taxation. San Francisco provided homeless people with free hotel accommodation and free drugs as part of its Covid-19 response.

The Governor of Kentucky called out an unemployment claim by Tupac Shakur (also a dead rapper) as a fraud, but it turned out to be a legitimate claim. In many cases, citizens reacted earlier and more rationally than governments to Covid-19. A series of US courts have ruled against government lockdowns, citing a lack of evidence of their necessity. A Texas salon owner who stayed open "in order to feed her children" was jailed by a judge for a week, but received $500,000 in donations. All workers are essential and leaving politicians to decide who is allowed to work is unwise. What if all the businesses forced to close just opened at the same time? Charity works best when people give voluntarily not forced by governments.

The mainstream media has treated similar accusations against Brett Kavanaugh and Joe Biden very differently. Euthanasia is a slippery slope, with several nations starting with voluntary and now moving to forced. The US is stepping up its support for Taiwan's involvement in the UN and other global organisations.

In the 1930's US taxpayers revolted, we could see the same thing again in coming years. If businesses and consumers must tighten their belts, governments should have to as well. Crony capitalists are using the Covid-19 crisis to beg for more government funding. The US Supreme Court is about to reconsider the doctrine of qualified immunity. American education institutions are dealing with a deluge of complaints of systemic discrimination against men.

Economics and work

In February Jerome Powell rubbished Modern Monetary Theory, now he is implementing it. Developed economies are now openly and directly using their central banks to finance government spending. Monetising debt brings long term problems, including skewing the way government works. The Federal Reserve needs to buy trillions of dollars in debt this year to keep up with Congress's spending plans. If the Fed didn't buy US Treasuries the lack of willing buyers for government debt would be exposed. The government answer to too much debt is more debt, so expect a lot more zombie borrowers.

The RBA has gone from 0% to 7% ownership of government bonds in less than two months. Germany's highest court finds part of the ECB's quantitative easing programme is unconstitutional. The Roaring Twenties were preceded by a pandemic and deep recession, with the economic cleansing a key part of the growth that followed.

Paying workers not to work looks a lot like Weimar Germany. The minimum wage in the US has been effectively increased to $25 an hour by large welfare payments. Less than half of the US population is employed, the lowest percentage since the Second World War. Many Americans have given up their independence and savings, living paycheque to paycheque and now needing government assistance to survive. The US government is using higher welfare payments as a way to sneak through a minimum wage increase.

Half of American small businesses had less than two weeks of cash on hand before the Covid-19 crisis, now one-third of small businesses aren't planning to reopen, citing an inability to meet rent and/or mortgage payments. The US government gave a ridiculously lavish bailout to its airlines.

Consumers are about to get some overdue price cuts. The fear of deflation by central banks is easily overcome by basic economics. Europe is facing its third financial crisis in 12 years with this one likely to be the worst of

them. Italy set a cap on the price of face masks and promptly had a problem securing supplies. The Michael Jordan documentary series contains a whole bunch of economic lessons.

Miscellaneous

After criticising Sweden for its Covid-19 response, many countries are now adopting its approach treating their citizens as adults capable of making decisions for themselves. Doctors in California are seeing an unprecedented surge in suicide attempts as a result of lockdowns. A clear explanation and examples of how Covid-19 is transmitted.

A thorough dismantling of the political spin and responses of both sides to Covid-19. There's still so much we don't know about the virus. One man is fighting to bring balance to the lockdown debate, but Silicon Valley wants to shut him down. Prisoners in Los Angeles deliberately infected themselves with Covid-19 in an attempt to gain early release. The vastly different reaction to the 1957 pandemic shows how we have changed our view of deadly viruses.

What it is like to be stung by a 'murder hornet'. A Californian man was arrested and released three times in a day, each time released without having to post bail. The intriguing story of how a young hacker saved the internet from the WannaCry computer virus after years of black hat misdeeds.

The man who feeds a remote Alaskan town with ingenuity and a Costco card. How one retail trader went from +$77,000 to -$9,000,000 betting on oil futures. Does Michael Jordan the owner care less about winning than he did as a player? How a pizza shop owner fought back against Doordash with a pizza arbitrage. American cannonball run enthusiasts have used Covid-19 to smash records.

Written by Jonathan Rochford of Narrow Road Capital. Comments and criticisms are welcome.

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