Edition 384, 20 November 2020

Contents

Graeme Shaw on why investing is at a pivotal moment *Graham Hand*

Offices will live on in a post-COVID world *Adrian Harrington*

11 key findings on retirement dreams during the pandemic *Matt Rady*

Bond basics and four messages in the search for yield *Nathan Boon*

Bank scorecard 2020: when will the mojo return? *Hugh Dive*

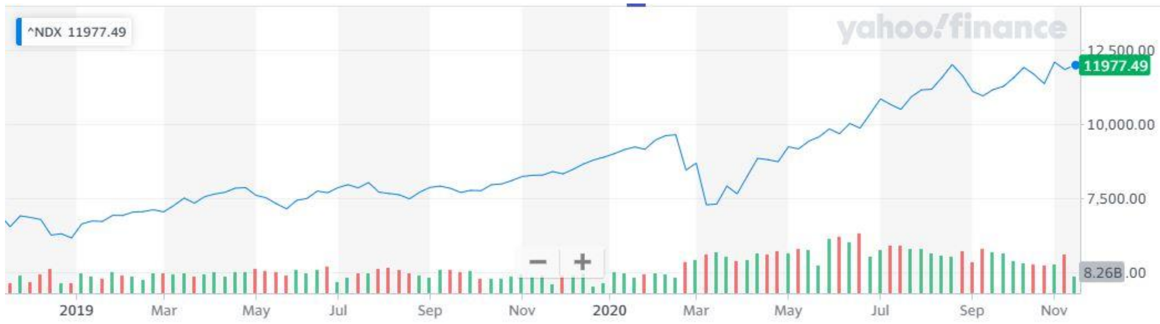
Generational wealth transfers will affect all investors *Max Pacella*

How real-time data keeps investors engaged *Ash J Hart*

Editorial

Underperforming asset managers receive little sympathy from critics and investors, but what does 'underperforming' mean? It's normally a reference to not matching a benchmark, but what should a fund manager do if the market is behaving in a way that is totally anathema to a belief in how companies should be priced? Change their style or tough it out? Most supporters want style consistency, even if it does not work in the short term. Adverse behaviour can last for years, which means investors choosing a manager should consider it a long-term commitment, at least seven years.

More than ever, this is where many of our highest-profile fund managers find themselves. For example, the tech-heavy NASDAQ index has doubled in the last two years, as shown below in the blue line. If earnings had doubled in the same period, then many 'value' managers who focus on fundamentals such as quality earnings would have invested more in tech companies.



Source: Yahoo Finance

But NASDAQ company earnings have been flat for at least two years, as shown below highlighted in red. This is called 'multiple expansion', because buyers are paying higher prices as a multiple of the earnings. The NASDAQ price gains are driven by reductions in interest rates and excess liquidity, not higher profits. Yes, the period from 2009 to 2015 was excellent for tech earnings, but not more recently, and yet prices continue to run.

Our interview with [Graeme Shaw of Orbis](#) explores what has happened and why he thinks we are at a critical moment in investing history. As he says:

"But if you look in the last three years, the multiples applied to those businesses have expanded much faster than the underlying earnings. That's where a lot of the overvaluation has come from as everyone gets over excited and things start getting silly and that's what's happened."

On the other side of the coin, many managers have benefitted from the tech theme, including some featured in **Hearts and Minds Investments** (ASX:HM1), chaired by **Chris Cuffe**. Its portfolio is constructed around the recommendations from core and other selected fund managers who present at the annual Sohn Hearts & Minds Investment Leaders Conference, held last week. The additions to the portfolio for 2020 are listed below. Instead of charging an investment management fee, a donation is made by HM1 to medical research.

Company	Ticker	1-line Description
Bill.com	BILL US	Improving back office processes for SME's
CSL Limited	CSL AX	Develops pharmaceutical and diagnostic products from human plasma
DISH Network Corp	DISH US	Satellite and interactive television services
Fisher and Paykel Healthcare	FPH AX	Designs humidification products/systems for use in respiratory care
Hello Fresh	HFG GY	Fresh food delivery
Nintendo	7974 JP	Video game developer in Japan (you've all heard of this one!)
Ping An Healthcare and Technology	1833 HK	Chinese mobile platform for healthcare and hospital referrals
Shenzhou International	2313 HK	Chinese textile manufacturer with Nike, Adidas, Uniqlo and Puma as its main customers
Slack Technologies	WORK US	New age email/real time messaging platform
T-Mobile	TMUS US	National wireless carrier in the US
Target Corporation	TGT US	Discount retailer with a very strong e-commerce platform
Teladoc	TDOC US	Phone/video consultations for visits to the doctor
Temple and Webster	TPW AX	Online furniture and homeware business
Treasury Wine Estates	TWE AX	Manufacture and selling of Aussie wine around the world
Yeahka	9923 HK	A Chinese mobile/app payment service, that uses QR (and other) codes that allow merchants to capture the various payment alternatives

In this week's other articles, **Adrian Harrington** explains why there is life in the office market in a post-COVID world as businesses assign more space per employee. Anyone who has worked with me knows I was never a fan of activity-based working so it's good to see the end of that counterproductive idea.

Matt Rady reports on mid-pandemic research on retiree reactions to the investment climate, experiencing doubt about how long money will last and their ability to withstand further losses. On a related theme, **Max Pacella** looks at intergenerational wealth transfers, especially as the Baby Boomers age and pass money to people with different spending and investing habits.

Many retirees expected to rely on bank dividends to compensate for negligible rates on cash and term deposits, and the surprise cancellation or reduction in dividends in 2020 was a shock. **Hugh Dive** checks the recent bank results and their potential to restore profits and dividends. Who will win in 2021?

While more investors are looking to bonds and bond funds for the defensive allocation in their portfolio, some of the terms are still confusing. I dislike references to running yield because it ignores the capital loss when a bond is purchased at a premium. **Nathan Boon** goes back to basics including four tips on the outlook.

Finally, in the week when the ASX has been plagued by service disruptions which also affected its competitor, Chi-X, **Ash Hart** expains the value of real-time data and how Application Programming Interfaces (APIs) have become crucial to our investing, and what is required in a good software interaction.

This week's White Paper from **Shane Oliver** of **AMP Capital** gives five reasons why Australian shares are likely to outperform in the next year. Most Australian feel lucky to live here during the pandemic, and Shane suggests it also a good place to invest.

According the **The Australian** today, the Government will release the Retirement Income Review tomorrow. The article claims the Review:

- warns that tax concessions for superannuation will exceed the cost of the age pension by 2050
- increasing super guarantee to 12% by 2025 would widen the equity gap between genders
- wage earners and women would pay for the increase from the current 9.5%.

The newspaper also says that the Government will delay a decision on the scheduled increase to 10% until the May 2021 Budget.

Graeme Shaw on why investing is at a pivotal moment

Graham Hand

Graeme Shaw is a Director at Orbis Investments and has worked at Orbis as an Investment Analyst on global equities since 1997.

GH: Orbis's contrarian investing approach is a difficult style of management and as your own website says, you often find "boring, overlooked and even hated companies". What are the challenges and does it require a certain personality to invest this way?

GS: Yes it does. You're often buying things that other people say are terrible. The brokers don't like them, your own clients might look at you like you're a little bit mad and they start questioning whether they should have hired you. Society conspires to make you feel like you've done something wrong.

You need to have an independence about the way you think and a willingness to analyse the evidence and come to a fact-based decision on what a company is worth, rather than getting caught up in the emotion.

GH: And just because it's unloved doesn't mean that you can pick the low point, so you can still have pain buying a cheap stock.

GS: Absolutely. Look at Simon Mawhinney from Allan Gray.

GH: Yes, he's been toughing it out holding AMP.

GS: The team at Allan Gray has observed that there are two differences between our style and other value-oriented investors. One is we buy the stocks that are so uncomfortable to own that even the analysts recommending them feel uncomfortable. And second, when others buy a stock and it's gone down a lot, they come under a lot of pressure to sell and absolutely not buy more. History shows that a large part of our outperformance comes from those two categories.

GH: Is there an uncomfortable stock that you've bought in the last few months.

GS: BMW. It was already cheap along with most other global automakers on the fear that electric cars will disrupt the industry or that self-driving cars means nobody needs to own a car again. Then when coronavirus hit, nobody wanted to own a company that sells expensive cars to rich people. We spent a lot of time with the company. We calculated BMW could shut down all its factories, tell its staff not to come to work but continue paying them and not sell any new cars for about a year and a half before they would need to tap the debt markets. It's a resilient business that gives us confidence it will ride out this pandemic well.

GH: Has that thesis played out yet?

GS: It's well off its lows, especially since people are nervous about catching public transport or using Uber. Owning a car is something many urban dwellers decided they needed to do for the first time. Plus, China has dealt with the pandemic and its car sales are growing again and that's a big market for BMW. Many people have tried to break into the luxury car market, mostly unsuccessfully, leaving the market to Audi and Mercedes and BMW with high barriers to entry and good margins.

GH: Looking long term at your Global Equity Strategy Fund, the numbers are good, but more recently, it has struggled. Is this the 'value versus growth' story?

GS: That's a big part of why the last three years have been tough. If you go back to 2006, value had been doing well for years after the tech bubble burst in 2000. In 2006, everyone wanted to be a value manager. It wasn't 'growth', it was 'growth at a reasonable price'.

GH. Ah yes, I remember the old GARP, you don't hear that much these days.

GS: And in 2006, we were finding high quality growth stocks that were very attractive, such as Microsoft and Cisco and Google. We were picking up those companies on P/Es of 10 to 12 and yet the more cyclical, value-oriented companies were not cheap and many of them were expensive. So, in 2007, there was a strong signal from the market that it was a really good time to be a growth/quality investor as the gap in valuation between growth and value was near the bottom of it historical range.

Look at that same valuation metric today using something simple like the ratio of price to book or price to sales. Whichever way you slice and dice the data, the valuation gap between value and growth is historically incredibly wide. It's the most extreme period for value investing in 200 years, according to a recent FT article.

Here's a graph showing the difference in expected returns between the cheaper, more value-oriented stocks and the more expensive, growth-oriented stocks, calculated over time using a dividend discount model. There are periods where growth stocks are relatively cheap and other periods where value stocks are relatively cheap. The style that has done well becomes more popular at points in the cycle. A contrarian approach to the weighting of value and growth makes sense.

Some people will say value investing is broken but it can never be broken. You outperform in the stockmarket, which is a zero-sum game before costs, when somebody else makes the mistake of selling you a stock too cheaply and therefore they underperform. What type of mistakes do people make? Well, they make all the usual human ones. When things are bad, they get emotional, they get pessimistic, they give up. They want to deal with their mistakes by selling them so they don't have to look at them anymore.

And all of those characteristics are still true, and vice versa when something's going really well, they get over optimistic, they get emotional, they start cheering for Team Amazon ...

GH: Or in Australia, Team BNPL.

GS: And they only look at the good news and they ignore the bad news and they push it and overpay, and human beings haven't changed. If you look at the last 13 years, growth stocks had great valuations in 2007 and it was definitely a good time to be a growth manager. And then for a decade, many of those growth companies genuinely added value and deserved to go up. These are the Amazons and Facebooks and Apples of this world - high-quality businesses with great cash flow, high barriers to entry.

But if you look in the last three years, the multiples applied to those businesses have expanded much faster than the underlying earnings. That's where a lot of the overvaluation has come from as everyone gets over excited and things start getting silly and that's what's happened.

GH: So you've owned those stocks in the past but you've exited in recent years?

GS: Yes. If you look at this what people call the FANGAMs to include Microsoft, they're about 15% of the MSCI World Index and we have about 3% in those stocks, predominantly Facebook and a little bit of Google. We struggle to find value but they're not 'tech bubble crazy'. We'd be happy to own more if they fell by 50% whereas in the tech bubble, there were plenty of stocks that we didn't want if they fell 90%. They were not good businesses.

But we also avoided the fall out in retail. We knew online would be the dominant format so we stayed away from most of those value traps in the traditional retailers. In the past, we owned Rakuten in Japan, which is the dominant online retailer and MercadoLibre in South America, we have owned Amazon twice and we owned PayPal. But at some point, these stocks reached valuations where we could find better places to put money. Today we are seeing a scenario where a lot of tech companies are trading on FANG-like multiples even though

it is unlikely their businesses will be as successful. We call them 'imitation valuations without imitation businesses'.

GH: And on the other side, what are some sectors or companies that look cheap?

GS: The market tends to look back at the last war where companies have done well off the expansion of smartphones or online, but what's the key theme for the next 10 years?

Green energy could be one. We've had a good look at solar power, but there's over-capacity and too much competition. We like the world's largest maker of wind turbines, Vestas, as wind power has become low cost and doesn't require subsidies. Even if the world leaves all its all its hydrocarbon burning generation in place but only grows new generation through green initiatives, then that alone is enough for solar and wind to grow massively. A Biden win is a bonus. Vestas is a company whose economic profits are higher than its accounting profits, because its accounting profits reflect service contracts signed in the past, whereas economic profits are new wind turbine sales plus new service contracts. It's cheaper than it looks with multi decades of growth.

GH: What are your three favorite stocks at the moment?

GS: If I look at the top five stocks in the fund, there are three I'd highlight. BMW is on about five times its normal earnings capability. Typically, it trades at more than 10 times so BMW is at half price. People look at Tesla but BMW has a huge number of electric vehicles and hybrids coming out. We like hybrids because it makes more sense for a large number of people to have a small battery that does 60 kilometres then kicks into a small petrol engine rather than a small number of people having a large, expensive battery in an all-electric car. Hybrids are cheaper to make so people can afford to buy them, unlike Teslas.

The market makes the mistake of dismissing value stocks as low quality. But the higher quality value names include Anthem, a US health insurance company. It's operating an oligopoly, it's a business the US can't do without as it sits in the middle of the healthcare system and coordinates everything. If someone gets sick they manage the relationship with the hospitals and with the drug companies. An oligopoly priced at 12 times earnings and its earnings have grown faster than the market historically.

And a third one is Naspers which is a way of buying TenCent at a discount. While Naspers is a South African company, its biggest asset is a stake in TenCent. The price of Naspers is so low relative to TenCent that it allows you to buy China's best internet company at half price.

We also like a Chinese online gaming company called NetEase. If you strip out the cash on its balance sheet and the losses in its startup businesses, it's only trading at around 19 times core earnings, so a similar P/E to the market while it is growing much quicker. These entrepreneurial companies often include many start-ups under one umbrella and the losses of the start-ups can hide high much higher profits and free cash flow in the core business.

GH: What's your biggest portfolio disappointment?

GS: We sold our FANG stocks too soon. We've also been surprised how low value stocks have gone. For example Japan has stocks trading at 4% to 6% dividend yields, solid businesses such as KDDI, a Japanese mobile phone operator. They've never missed a dividend in 20 years, they've grown at a reasonable rate and they're well managed. A lot of these companies have low payout ratios so they can grow their dividends simply by raising their payout ratios from the low 30s to 50s. Warren Buffett recently bought a basket of Japanese trading companies.

GH: Why do you only have one Australian stock, Newcrest, in your global portfolio?

GS: The general reason is that Australia represents only 2%-3% of global opportunities. There are about 5,000 stocks we can buy, and historically, about 15% of them beat the market by 10% or more. So that means 750 stocks we would be happy to own and we need 50 of them. There are thus always a lot of good stocks that we don't buy. So if we miss out on Australia, it's because we have found something a bit better or a bit safer. We do like Alumina as it looks incredibly cheap and the world will always want aluminium.

GH: What's the biggest investment theme on your mind at the moment?

GS: It's recognising where we are in the long span of investing. I think we are at a very unusual fringe point. Investors should take care believing in many of the things they believed in the past. For example, I'm not a huge fan of balanced funds, but if ever there was a time to spread things out and diversify widely, this is one of

those times. Spread investments across different equity management styles and different asset classes and don't expect the growth style to continue forever.

Graham Hand is Managing Editor of Firstlinks. Graeme Shaw is a Director at [Orbis Investment] and has worked at Orbis as an investment analyst since 1997. Orbis is a sponsor of Firstlinks.

Past performance is not a reliable indicator of future results. The value of investments in the Orbis Funds may fall as well as rise and you may get back less than you originally invested. It is therefore important that you understand the risks involved before investing. This report represents Orbis' view at a point in time and provides reasoning or rationale on why we bought or sold a particular security for the Orbis Funds. We may take the opposite view/position from that stated in this report. This is because our view may change as facts or circumstances change. This report constitutes general advice only and not personal financial product, tax, legal, or investment advice, and does not take into account the specific investment objectives, financial situation or individual needs of any particular person. This report does not prohibit the Orbis Funds from dealing in the securities before or after the report is published.

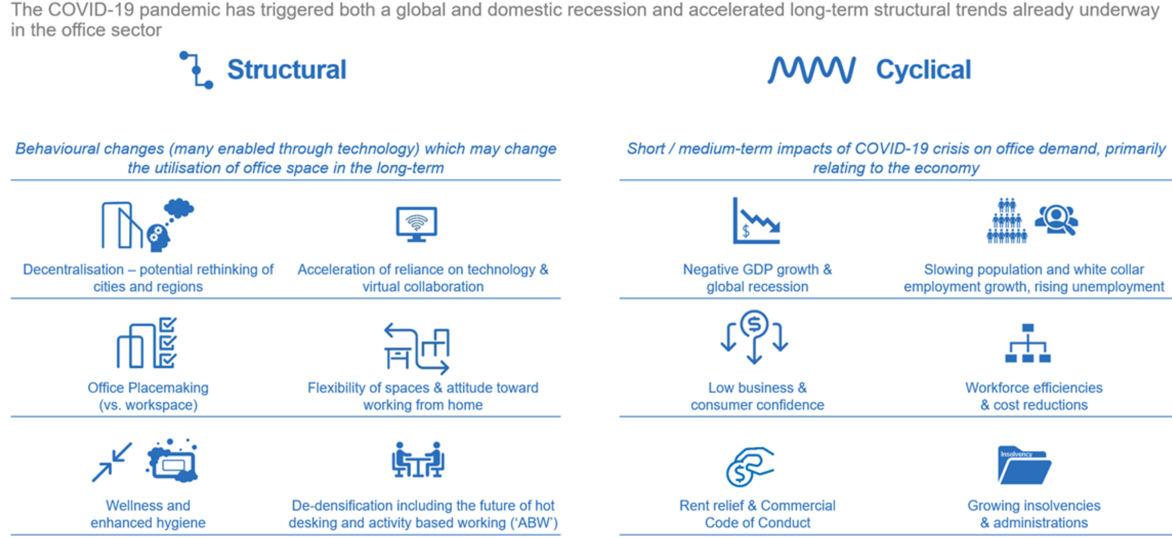
Offices will live on in a post-COVID world

Adrian Harrington

COVID-19 has put the spotlight on all asset classes, and commercial property is no exception. David Harrison, Charter Hall's CEO & Managing Director, recently spoke at the Morningstar Individual Investor Conference and explained why quality office buildings are still an attractive investment. Here is a summary of the reasons David is still optimistic on the outlook for the office sector.

Structural vs cyclical change

There is a lot of media hype on the office sector. The million-dollar question is whether COVID-19 will create a structural change or a cyclical change, as we have witnessed with other past economic downturns.



Charter Hall's view is that this is another example of a cyclical correction. While there will be a short-term reduction in demand and vacancy factors will go up, we entered this crisis with some of the lowest vacancy rates we have seen in both the Sydney (3.9%) and Melbourne (3.2%) CBD markets. Compare this to cities like Chicago (16.2%), LA (13.0%) and New York (7.7%). This will buffer any short-term reduction in demand.

Clearly, we are already seeing companies announcing cutbacks in headcount in response to the economic downturn. But an offsetting trend is an increase in the amount of space per person in occupying in a building. Go back 30 years, it was 25sqm per person but pre-COVID, it went as low as 10sqm per person. The pendulum had swung too far - you cannot have that sort of density and operate efficiently.

The end of 'activity-based working' extremes

The concept of 'activity-based working', where two or three people might occupy one seat on a particular day, and as people went to a meeting or left the office, their seat was occupied by some else, is unlikely to be the predominate workplace system in future. There will be a move back to fixed seats with some clustering in neighbourhoods and there might be some movement in those neighbourhoods on a weekly basis but not on an hourly or daily basis.

With the emphasis on workplace health, the densification of workplaces will return towards 14-16sqm per person. As a result, businesses will need more space for the same amount of people in our offices and this will help offset the cyclical change in demand.

CEO and business leaders need to deal with productivity and risk management. One of the problems that has arisen out of COVID-19 and working from home is that risk goes up. It is difficult to have a detached workforce no matter what the business. There will be a desire, particularly over the medium term, for staff to return into an office environment. Yes, there will be flexible arrangements, and in some industries, like call centres, they may be able to work efficiently from home 100% of the time. Most people will spend more time in the office and it is unlikely that we are going to see a long-term structural change in mass working from home.

Health and wellness in the office

In response to concerns about the workplace environment, there will be more focus on technology in buildings and a flight to quality by tenants. New buildings that provide the latest in health and hygiene facilities (such as ultraviolet hand rail sanitiser on building escalators and in air handling units, touch-free technology for doors and lifts and temperature scanners in the entrance) will be in demand. Buildings that fall short will not be able to compete.

We've seen a lot of change over the past 30 years. The office will continue to evolve and adapt. We'll see more flexible working hours, more shared information, and more innovative technology. But at the same time, there will be a greater focus on collaboration and empowerment. Whether in the CBD or the suburbs, a well-designed, productive, connected workplace environment will allow a company to attract and retain talent at the same time helping to foster the company's identity and culture.

The way people work is constantly evolving, enabled by technology…COVID-19 has accelerated this evolution

The evolution of work

The past	The now / future
Hierarchy	Flattened structure
Fixed work hours	Flexible working hours
Hoarded information	Shared information
Command & control	Engaging & empowering leaders
On premises technology	Cloud technology
Email primary communication form	Email is secondary
Siloed & fragmented company	Connected & engaged company
Work at office	Workplace ecosystem

CBD vs the suburbs: It's not one or the other

Another refrain is the death of the CBD and the rise of suburban office markets. We are believers in both CBD and metropolitan markets. Charter Hall is one of the largest owners of office property in Parramatta. We recently bought a 34,947 sqm office property in Macquarie Park in suburban Sydney that is leased to the NSW Government for 12 years.

The CBD is, and will continue to be, the dominant office market. Across Australia, there is 11 million sqm of quality (Premium and Grade A) CBD space and circa 3 million sqm in non-CBD areas.

To meet the needs of staff, businesses want a quality retail amenity and good public transport. It is difficult to have a suburban location in any state that has the convenience and centralised public transport system of a CBD. Apart from Parramatta and North Sydney in Sydney, most states have little in the way of mature suburban markets. There are some exceptions, but there will not be a massive structural change in office demand moving from the CBD to the suburban market.

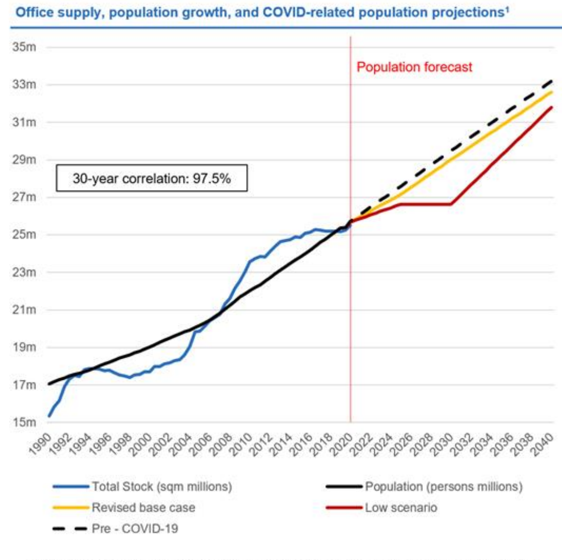
Population growth drives demand and it will again

There is a strong correlation between office demand and population growth. Obviously, COVID-19 has driven a short-term reduction in net migration. Hopefully, after the health crisis, we will see a return to pre-COVID net migration levels, which in turn will drive office demand. Population growth is essential if Australia is to continue above average economic growth compared with Europe and North America and many other parts of the world.

Office demand is very closely correlated to population growth

Australia's population is forecast to exceed 30m in the next 20 years, potentially generating 6m+ sqm of office requirement

Office supply, population growth, and COVID-related population projections[1]



Source: JLL, ABS, Australian Government Treasury, PCA, Queensland Centre for Population Research. At August 2020.
1. Queensland Centre for Population Research.

Projected growth in office space requirements

	Pre – COVID-19	Revised base case	Low scenario
Projected change in stock (sqm)	7,735,688	7,156,358	6,347,381
Projected growth in stock (CAGR)	1.35%	1.26%	1.13%

- Office stock is substantially driven by Australia's total population level
- Australia's population is forecast to reach between 31.7 million and 33.0 million by 2040
- This equates to a requirement of stock between 6.3 million and 7.6 million sqm over the next 20 years based on long-term historical correlation
- Given the ongoing transition towards a greater services based sector output, the proportion of white collar employment will increase over time, but the correlation may change due to increased adoption of working from home

Capital continues to chase office assets

Some of the largest global institutional investors are investing in Australian office buildings and this will continue. Two recent examples include Peakstone, a Singaporean investor, acquiring a Sydney CBD office building in June 2020 for $530 million while in October 2020, Deka Immobilien, a German investor, paid $452 million for a Melbourne CBD office building.

One of the key reasons they are choosing Australia is because of the lease structures that allow 3.5% to 3.75% annual fixed rental growth. Investors want a growing distribution yield in a low inflation, low interest rate environment. Australian commercial real estate offers an attractive relative investment return compared with other major global markets. We expect office transaction pricing to remain firm and reflect the large gap between office yields and the 10-year bond rate.

Winners and losers

We are not as concerned about the office market as some. Clearly, industrial and logistics will be the stand-out performer for the next five years driven by the explosion in e-commerce while the supermarket and convenience end of the retail market will be more stable.

While there will be winners and losers in the office market, modern buildings with long leases to quality tenants will perform well. Older buildings with shorter leases will underperform.

Adrian Harrington is Head of Capital and Product Development at Charter Hall, a sponsor of Firstlinks. This article is for general information and does not consider the circumstances of any investor.

For more articles and papers from Charter Hall, please click here.

11 key findings on retirement dreams during the pandemic

Matt Rady

COVID-19 is taking a harsh toll on the economic wellbeing of many retirees with research showing it has shaken their confidence in the quality of their retirement and how long their money will last. Notwithstanding the recovery in many share prices over recent months, returns on cash and term deposits are negligible.

Here are 11 key findings from the Allianz Retire+ research during the pandemic, conducted a few months ago. A more comprehensive summary of the research follows the list.

1. Money is a recurring worry for retirees
Almost one in four retirees (24% of survey respondents) said they worried about making ends meet. One in five (20%) said money was a constant worry.

2. Spending even less on necessities, luxuries
Three quarters (75%) of surveyed retirees said they were spending less on luxuries due to COVID-19. Two thirds (68%) of retirees said they were only buying necessities.

3. Many retirees did not feel financially secure
Half (51%) of surveyed retirees said they did not feel secure in their financial position.

4. Wealth destruction
A third (36%) of surveyed retirees said they had lost money during the COVID-19 market downturn. One in 10 (13%) believed they had experienced financial losses that would not be recovered during their retirement.

5. Vulnerable to another financial shock
Almost two-thirds of respondents (61%) did not believe their financial situation was safe in the event of another economic downturn.

6. Lack of control
Just under half of surveyed retirees (45%) did not feel in control of their financial future. Higher sharemarket volatility was making many retirees feel they were at the mercy of global financial markets and unable to control their financial future.

7. Quality of life worries
Recurring worries about day-to-day bills, financial security and the risk of another economic shock was fuelling concerns about life quality in retirement. A third (34%) of retirees said they worried about whether their finances would allow them to have a good quality of life.

8. Illness, market uncertainty top concerns
The top five retiree concerns were:

- becoming ill (55%)
- unexpected costs (45%)
- losing a loved one (44%)
- not having enough money to live the life they wanted in retirement (34%)
- the risk of one-off market downturns such as COVID-19 and the GFC (32%).

9. More conservative approach
Almost two-thirds (62%) of surveyed retirees said they were taking a more conservative approach to their retirement because of COVID-19. Given that many retirees already live conservatively, the finding added to the broader survey theme of retirees cutting back even further and taking fewer financial risks during the pandemic.

10. Retirement expectations being downgraded
Almost a quarter of current retirees (23%) now had more negative expectations of their retirement due to COVID-19.

11. Wary of financial advice
Less than a quarter (23%) of surveyed respondents sought financial advice, even though they were feeling less financially secure. Allianz Retire+ research consistently finds that retirees who used professional investment advice feel more confident in their financial position.

Here is more detail on the research:

Shortcomings in retirement outcomes

Many Australian retirees are downgrading their retirement expectations, spending less on luxuries, and are fearful and confused about the safety of their investments.

The Allianz Retire+ survey collated the views of over 1,000 current and prospective retirees nationwide in May 2020, to understand how COVID-19 was affecting their lifestyle, investment actions and retirement perceptions.

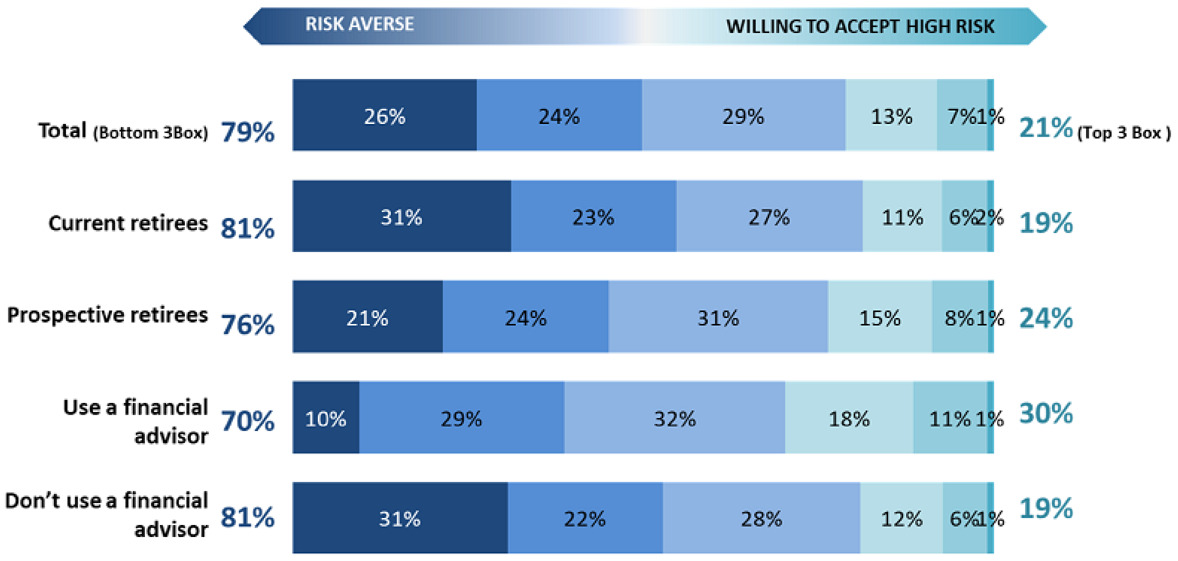
Only one-third of retirees feel confident in their financial position. In addition to health concerns about the virus and not being able to see family and friends as much, retirees are yet again suffering the sharemarket rollercoaster.

A total of 66% do not agree that Australia's superannuation system will provide them with a dignified retirement. It suggests the Australian superannuation system, which is lauded as one of the best globally, is not working for a great deal of the people it's designed for.

Moreover, COVID-19's impact has exposed systemic issues in the drawdown phase of retirement, highlighting shortcomings in retirement product design, access to financial advice and superannuation education.

In a previous study, 'The Next Chapter' undertaken by Allianz Retire+ in 2019, retirees reported feeling nervous and uncertain about what's ahead and lacked in investing confidence. Unfortunately, COVID-19 has taken that to a new level. On both occasions the research indicated retirees want safe, simple, low-cost retirement products with certainty a key feature. Unfortunately, the investment industry is not generally meeting that need.

The current survey found that three in four retirees are not confident about how long their money will last in retirement and when asked about their investments during the pandemic, only 18% felt their investments would be safe in case of economic downturn. They also reported being largely risk averse, seemingly exacerbated by the pandemic.



Source: Allianz Retire+, 'Black Swan Research', May 2020

Nearly half of respondents said they were monitoring their investments much closer due to COVID-19 and just under a third of those surveyed were happy with the federal government's response to COVID-19 policies that affect their retirement.

The pandemic has brought many of the systemic issues back to the surface and there needs to be a greater sense of urgency in delivering change to the system.

Prospective retirees most at risk

The economic impact of COVID-19 was greater on prospective retirees (within seven years to retirement) than current retirees, the survey found.

Source: Allianz Retire+, 'Black Swan Research', May 2020

Vulnerability close to retirement

About 40% of prospective retirees said they lost money to date during COVID-19. Just over one in five said their employment status has (or may) change due to the economic downturn.

Falling retirement savings and rising job insecurity is a toxic combination. Around one in three prospective retirees now have more negative expectations of their retirement. And 77% of prospective retirees do not believe superannuation will provide them with enough money in retirement.

Those nearing retirement have been particularly hurt by the downturn. These investors tend to have more funds allocated to shares, so have higher susceptibility to market crashes. Typically, they are still working and need that income to build retirement savings.

This is where the impact of COVID-19 has shown the danger of 'sequencing risk', where the timing of poor market returns can permanently damage retirement savings. Prospective retiree investors can ill afford to have the share component of their superannuation crushed by market volatility. Many do not have enough time left in the workforce to rebuild their wealth.

With COVID-19 reinforcing the need for retirement-savings products that have a low-cost protection mechanism, around one in three prospective retirees said they would consider an investment product that 'insured them from market downturns'. Investing in retirement is very different to accumulation and retirees are realising diversification and asset allocation is no panacea to protect wealth during crises.

Lack of advice during the pandemic

Remarkably, the survey found 79% of retirees did not seek financial advice during COVID-19.

Only one in five retirees felt that they had easy access to professional financial advice and approximately a third felt financial advisers were 'for the rich'. Almost two-thirds of those without an adviser said they would not use one because the service was too costly.

The advice proposition is proven to be an integral part of providing individuals with confidence and certainty in retirement, with those who use an adviser stating more confidence and security in their financial position. And 68% of those who were advised during COVID-19 said they are sticking to their financial plan, meaning advice is definitely deterring people from making sub-optimal investment decisions based on fear or a lack of understanding. That fact alone proves there is a clear need to change the perception of financial advice among retirees and increase access to affordable advice.

About the survey

Allianz Retire+ commissioned research surveying 1,007 retirees in May 2020 to understand how the economic impact of COVID-19 was affecting them. The sample was split equally between current and prospective (retiring in the next seven years) retirees, and equally between men and women. Most respondents were aged 60 to 75 or over. The survey included responses from retirees in each State and Territory. About two thirds of respondents had an annual household income below $79,000.

Innovative retirement income products with in-built protection from sharemarket losses include Future Safe from Allianz Retire +.

Matt Rady is Chief Executive Officer of [Allianz Retire+](). This material is for general information purposes only. It is not comprehensive or intended to give financial product advice and does not take into account your objectives, financial situation or needs.

Bond basics and four messages in the search for yield

Nathan Boon

Bonds have been strong performers over more than a decade in the lead-up to the current crisis, and we believe they could play an important part in defensively-positioned portfolios in future. While there is a certain lack of understanding about bonds on the part of many investors, relative to equities, but the principles are quite simple. Here are a few things we bear in mind when considering a role for bonds in a portfolio:

1. Income and defensive positioning

An important part of building a defensive position into a portfolio is the inclusion of securities with cash flows that are resistant to market downturns. Considering the credit risk of the issuer, bonds can offer an opportunity to harvest regular and reliable income streams with lower risk of capital instability.

2. Returns are typically driven by interest rate sensitivity

As interest rates fall, the discount factor used to value income streams is reduced, increasing the value of those cash streams today. The yield on issued bonds becomes more attractive, driving up prices and returns.

The sensitivity of a fixed income security's price to changes in yield increases the further a bond is from its maturity. When measuring how sensitive a bond's price is to changes in interest rates, we refer to its duration (as explained below).

The strong performance of bond markets over the past decade has been driven by a falling interest rate environment, fuelled by a series of financial crises and the lack of ability on the part of most major economies to generate significant inflation, in turn necessitating monetary stimulus in the form of lower interest rates. In this environment, portfolios with higher duration have tended to perform strongest.

The gains on offer from interest rate risk have plateaued in recent years as interest rates across most of the developed world have effectively bottomed out, and it's important for investors holding these assets to understand the specific role they play in their portfolio structure.

3. Investment-grade credit can play a defensive income role

Credit spreads are the difference between yields on non-government bonds such as corporate bonds and government bonds, and represent the additional credit risk premium allocated to the issuer of the bond. Credit spreads widened dramatically during the first stages of COVID-19, as passive bond funds underwent forced selling and introduced excess liquidity into the market. Over the past few months, however, spreads have largely stabilised towards pre-COVID levels, particularly in investment-grade bonds.

Despite this, investment-grade credit spreads tend to have a fairly low volatility, and well-constructed portfolios may provide access to this credit risk premium for a low level of downside risk. We find that through the cycle, investors in Australian investment-grade bonds tend to be overcompensated for the credit risk they are taking. By investing into a diversified portfolio of stable investment-grade bond issuers, investors may earn superior risk-adjusted returns, and do so without seeing undue volatility in the total returns they earn from these investments. In an environment of very low yields globally and where investors are being tempted down the quality spectrum to earn moderate returns, we view this as a key means of earning defensively oriented income in an uncertain environment.

4. The outlook for Australian investment-grade bonds remains positive

Australian companies were better prepared for this crisis than their counterparts in countries such as the US. We believe Australian corporates entered the recession with stronger and more conservatively positioned balance sheets and were quick to raise equity where they faced uncertainty. This supportive attitude has been reflected in ratings, and our corporate sector has for the most part avoided the ballooning leverage witnessed in other markets.

That said, there are still considerable downside risks ahead relating to the future evolution of the pandemic and the capacity for our economy to recover. Uncertainty is likely to persist for some time, especially with the risk of further waves and lockdown.

Despite this potential volatility, inflation and interest rates are likely to remain low in the short to medium term, and future stimulus programs should remain highly supportive of credit markets. We view a well-constructed portfolio of defensive income in this space as being a critical component for weathering this uncertain economic environment.

Decoding the corporate bond discussion

The key to understanding bonds is becoming fluent in the terminology used to describe the various attributes of fixed income securities. Let's take a run through a few of the more important concepts.

Types of yield

Current yield, also known as **running yield**, refers to the annual payout as a percentage of the current market price. For example, the current yield on a bond with a market price of $1,000 that pays $80 per year in interest is 8%. Running yield is a similar concept to the dividend yield for equities.

Yield to maturity, or **gross redemption yield**, is a yield that represents the total coupon payments for that bond if held to maturity, plus interest on interest (the reinvestment), and the gain or loss realised from the security at maturity.

A **yield curve** is a function that traces relative yields on a type of security against a spectrum of maturities ranging from three months to 30 years or longer.

The next consideration is the way that yield responds to interest rate movements and credit risk.

Interest rate sensitivity

We use the term **duration** to broadly refer to the extent to which a bond's pricing responds to interest rate movements. Technically, it's a weighted measure of the amount of time until the cashflows of the bond are received **(Macaulay duration)**. As such, it reflects the timing and magnitude of each cash flow, and the extent to which changes in the discount rate for those cash flows (at the prevailing interest rate) will affect the price of the bond.

Modified duration is an extension of the Macaulay duration concept, whereby it directly expresses the percentage change in the price of a bond for a given change in interest rates.

Credit sensitivity

Credit risk is the expected risk of loss due to the issuer delaying or defaulting on interest or principal payments. Credit risk is assessed by agencies who issue **credit ratings** on the quality of debt securities.

Bond issuers with lower credit ratings must pay a premium to investors who purchase their bonds. The difference between the yield on a bond and a government bond of the same maturity (effectively a risk-free rate of return) is known as the **credit spread**, measured in basis points.

Credit spreads are affected by factors such as the financial strength of the issuer, broader macroeconomic conditions and the demand and supply amongst investors for the issuer's securities. After purchasing a corporate bond, the bondholder may benefit from a narrowing of the credit spread which all else being equal, should drive up the price of the bond, delivering a capital gain.

In a similar fashion to interest-rate sensitivity, the term **credit spread duration** is used to refer to the sensitivity of a bond's price to movements in credit spread. Typically, the higher the credit spread duration in a portfolio, the greater the credit risk that investors are exposed to.

Understanding corporate bonds, or fixed income generally, does not need to be complicated. Once the basic principles are broken down, investors can better understand how corporate bonds may perform in a changing interest rate and macroeconomic environment.

Nathan Boon is Head of Credit Portfolio Management and Co-Portfolio Manager at AMP Capital, a sponsor of Firstlinks. This document has been prepared for the purpose of providing general information, without taking account of any investor's individual objectives. For more articles and papers from AMP Capital, click here.

Bank scorecard 2020: when will the mojo return?

Hugh Dive

In early 2020, it seemed that this year the banks would get their mojo back. Rising profits were expected with the 2018 Royal Commission passing into the rear vision mirror along with falling compliance and remediation costs. After Commonwealth Bank reported their first-half 2020 earnings in early February, the bank's share price surged over $90 after delivering 11% profit growth. The only cloud on the horizon was the question as to how the banks would maintain profit margins with interest rates so low.

How wrong we were! In late March, a mere five weeks after reporting solid profit results, Commonwealth Bank's share price had fallen 40% (like all banks) to $54. The financial press was wondering whether the mulit billion dollar provisions each bank had taken for bad debts stemming from Covid-19 shutdowns will be enough.

In this piece, we are going to look at the themes in the approximately 800 pages of financial results released over the past two weeks including Commonwealth Bank's 1st Quarter 2021 Update, awarding gold stars based on performance over the past six months.

Reporting season scorecard November 2020

Company	Share Price	Market Cap $B	Cash earnings per share growth	Dividends Paid	Net interest margin	Credit Impairment charge as % of loans	Capital Ratio	Return on Equity	Forward PE Ratio	Forward dividend yield	2020 total return
Westpac	$ 18.60	$ 64.1	-36.0%	$ 0.31	2.1% ★	0.45%	11.2%	3.9%	14.9	3.8% ★	-19.9%
ANZ	$ 21.13	$ 54.6	-42.0%	$ 0.60	1.6%	0.43%	11.3%	6.2%	16.3	3.5% ★	-9.5%
NAB	$ 21.59	$ 65.0	-33.0%	$ 0.60	1.77%	0.46%	11.5%	6.3%	18.0	3.2%	-8.5%
Commonwealth (1QFY21 trading update)	$ 74.49	$ 124.7	-16.0% ★	$ 2.98 ★	2.07%	0.28% ★	11.8%	10.3% ★	21.3	3.4%	-2.0%
Macquarie (1H21)	$ 140.43	$ 49.3	-23.0%	$ 1.35	2.07%	0.44%	13.5% ★	9.5%	22.7	2.8%	4.6% ★

Source: Company reports, IRESS, Atlas Funds Management

Uncertainty falling

In May 2020, the base case for the banks was unemployment between 10-12% and house prices falling by between 15-20% throughout 2020, with further deterioration expected in 2021. This cautious stance saw Westpac taking $1.8 billion and ANZ $1 billion in provisions and most banks declining to pay a dividend. The lack of dividends surprised many investors as Westpac even paid a dividend during its near-death experience in 1992.

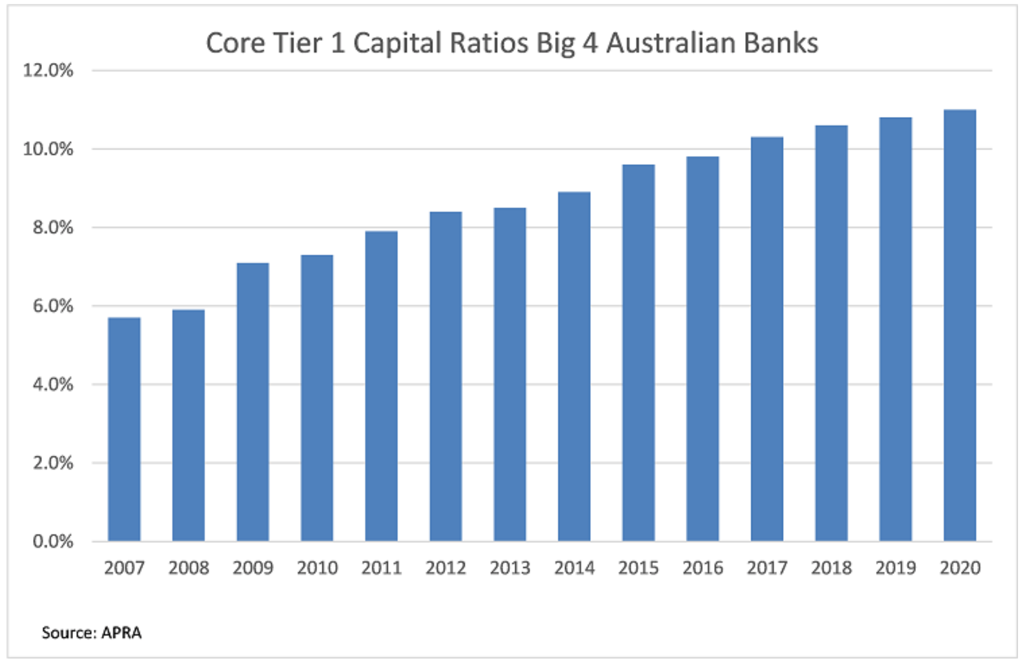
November revealed cautious optimism due to the high levels of fiscal stimulus, falling levels of Covid-19 transmission and historically low interest rates. The economy in late 2020 is in better shape than was expected six months ago. Indeed instead of seeing a steep fall in house prices which could have exposed the banks to losses on their mortgage books, in October CoreLogic revealed that house prices across the five main capital cities were up +4% over the past year, with Sydney leading the pack gaining +7%.

Furthermore, in November, the banks showed that the number of stressed customers had been falling steadily. In June, Commonwealth Bank had 210,000 loans on their book deferring payments, this fell to 129,000 in September and again to 52,000 in October as borrowers returned to making full payments.

Strong capital positions

All banks have core Tier 1 capital ratios above the Australian Prudential Regulation Authority (APRA) 'unquestionably strong' benchmark of 10.5%, despite the billions of dollars of provisions taken and in the case of Westpac, a $1.3 billion-dollar AUSTRAC fine. This allowed Australia's banks to enter 2020 with a greater ability to withstand an external shock than was present in 2006 going into the GFC.

From the below table you can see that the banks have been building capital particularly since 2015 when APRA required that the banks be "*unquestionably strong and have capital ratios in the top quartile of internationally active banks*".



Furthermore, in the lead up to the Financial Services Royal Commission, the banks have divested their wealth management and insurance businesses to varying degrees. This resulted in the banking sector remaining well capitalised despite taking heavy provisions due to expected loan losses from Covid-19.

In the November management presentations, there was again a tone of self-congratulation from bank executives at their prudence for having such high levels of capital in 2020. In the GFC all banks raised several billion dollars each, whereas in 2020 only NAB raised capital and may not have had to do so if they had been able to divest MLC Wealth in a timelier fashion. Among the banks, Macquarie came out ahead in November with the strongest capital ratio, though in fairness to the trading banks, Macquarie's business model which has a high weighting to annuity funds management income will see lower loan loss provisions that erode capital.

Net interest margins holding

Gold Star

Before the pandemic, the biggest issue facing the banks was maintaining net interest margins as the cash rate moved towards zero. Banks earn a net interest margin [(Interest Received - Interest Paid) / Average Invested Assets] by lending out funds at a higher rate than which they can borrow at. When the prevailing cash rate is 6%, it is much easier for a bank to maintain a profit margin of 2% than when the cash rate is 0.1% and there is nowhere to go in lowering deposit rates further. Also, falling interest rates reduce the benefit that banks get from the billions of dollars held in zero or near-zero interest transaction accounts that can be lent out.

Westpac revealed in September 2020 that it held $196 billion in accounts earning less than 0.25%, an increase of $39 billion over the previous six months that indicates that a portion of the stimulus payments is being saved and not spent. Net interest margins remained stable at between 1.6% and 2.1%, with the banks more heavily exposed to mortgages (CBA and Westpac) traditionally having higher margins. The business banks (NAB and ANZ) generally have lower margins as they face competition from international banks when lending to large

corporates. In aggregate net interest margins for the banks only reduced by 0.06% over the past year, a solid outcome given falling interest rates over the past year.

Dividends

While ANZ, Westpac and NAB cut their dividends during the depression, both World Wars, the 1991 recession and the GFC, investors need to look back to the banking crisis of the 1890s to see the last time the major banks declined to pay dividends to shareholders, as they did in May 2020.

The banking crisis of 1893 was arguably more severe than what the banks faced earlier this year. After the collapse of the Melbourne land boom in 1888, a large number of Australian banks were unable to pay depositors, who saw access to their funds locked up for several years. This stressed situation saw the English, Scottish & Australian Bank and London (Chartered) Bank of Australia (precursor banks of ANZ) and National Bank of Australia suspend dividends between four and nine years. In fairness, Westpac (née Bank of New South Wales) could claim to have paid dividends during this period.

In November most of the banks returned to paying dividends from profits, following APRA's guidance of limiting dividends to 50% of statutory profits. However, Westpac's final dividend payout was underwritten by an investment bank issuing new shares, which dilutes shareholders. CBA wins the gold star for the smallest decline in the dividend and by not resorting to financial gymnastics to make the payment.

The road back to pre-COVID-19 levels of profits

While the banks will eventually see profits from banking return to pre-COVID-19 levels, the road back to the same dividends per share that we saw in 2019 will be slow. NAB and Westpac have both conducted significant equity issues over the past 12 months, which have expanded the share count. Commonwealth and ANZ are in a more fortunate position, as they entered 2020 with excess capital, courtesy of the sale of their wealth management and insurance businesses over the past year. As a result, neither of these banks issued shares at depressed prices during 2020.

We expect dividends to increase across the banking sector in 2021, as APRA has indicated that it will relax its stance on limiting bank dividends if the economy continues to improve.

History provides some clues on when the banks will return to their 2019 levels of profitability. After the GFC, the banks took roughly three years until 2011 to regain their pre-GFC level of dividends per share. Less encouraging is the historical example of bank dividends in the 1990s and the 1890s. Westpac took until 2000 to reinstate the same dividend per share that it paid shareholders in 1990.

Atlas believes that the path to restoring dividends is likely to be closer to the post-GFC experience than the 1990s. Today the banks have higher credit quality in their loan books, and no Quintex, Bond Group, ABC Learning nor poorly supervised foreign adventures. Additionally, their customers face interest rates in the low single digits, not the 18-20% mortgage rates seen in the early 1990s and enjoy high levels of fiscal stimulus. Unlike the GFC, in 2020, the banking system is not the cause of the problems we face, and the banks themselves are carrying increased levels of capital to absorb losses.

Hugh Dive is Chief Investment Officer of [Atlas Funds Management](). This article is for general information only and does not consider the circumstances of any investor. The author would like to recognise Ashley Owen's assistance in looking at historical Australian banking crises.

Generational wealth transfers will affect all investors

Max Pacella

And as he hung up the phone it occurred to me
He'd grown up just like me,
My boy was just like me.

Harry Chapin, 'Cat's in the Cradle'

One of the largest transferrals of wealth in history will occur in the next few years, depending on the health and goodwill of the Baby Boomer generation.

Referencing American demographic figures, Boomers are the wealthiest generation in US history and are currently the custodians of circa USD68 trillion in assets says Cerulli Associates, a US research firm that specialises in global asset management and distribution analytics. According to Forbes, Boomers control roughly 70% of all disposable income and have vastly differing attitudes to their parents and their heirs.

What happens when the time comes for this generation to pass down these titanic asset holdings, who will receive them and what impact will this transfer have on the world as a whole?

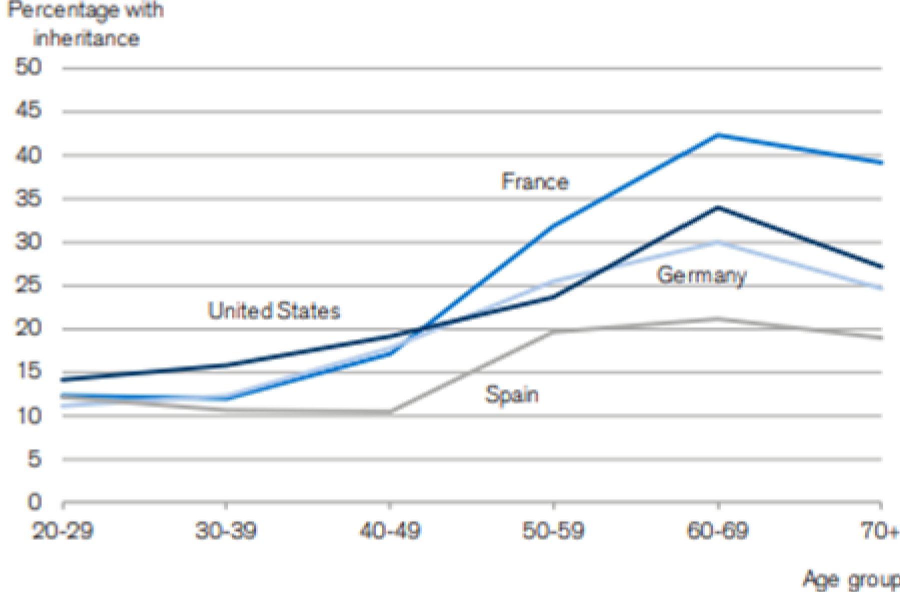
Who will receive this wealth?

The question now looms, who will receive all of that money?

The first suggestion is Millennials, the heirs of the Baby Boomers, presently aged around 25 to 40 years. The numbers vary, but the most consistent estimate is that Millennials will be five times richer in 2030 than they are today due to this transfer of wealth between generations. And that figure is just for the US. In Australia, Millennials will inherit AUD3.5 trillion over the next 20 years, an average of $320,000 per person.

But there is uncertainty around if all, if not most, of Boomers' wealth will go to their children. The reason is quite simple: Boomers want to spend their hard-earned cash.

Figure 1: Incidence of inheritance by age, selected OECD countries



Source: Citi Group

Consistent across OECD countries (and most developed nations), more than half of the Baby Boomers do not have an estate allocated to their children. In fact, estimates by CNBC suggest that only 57% of total assets are going to be transferred to Millennials over the next 20 years.

The Boomer generation more than any other has a penchant for spending their own money rather than acting as a walking piggy bank for the next-in- line generation.

An interesting observation from a Citi Private Bank commentator was that since Baby Boomers are on balance living in a more peaceful and prosperous time than their parents, many don't consider the same drive to 'set up' the next generation. In the absence of war or decades-long financial collapse, the status quo of leaving a nest egg to protect children has been disrupted somewhat.

So where will the money go, if not to their children?

For the most part, back into the economy.

Boomers are living longer, and 65-70 is no longer the twilight years of life. It's not only that 60 is the new 40, but 80 is the new 60. Plus funding must be put towards retirement living, senior living accommodation, holiday homes and much more.

A lot will remain in the stock market as well, with Baby Boomers having the second lowest average allocation of wealth to 'cash' in the last 100 years (according to BlackRock).

Figure 2: Cash allocation

65%
59%
54%
47%
58%
Millennials (Age 25-35)
Gen X (Age 36-51)
Baby Boomers (Age 52-70)
Silent Generation (Age 71-74)
Global Average

Source: BlackRock

What will be the aftermath of the Great Wealth Transfer?

For any Baby Boomers reading this, you'll almost certainly see that your children's outlook on the world and investing is vastly different to your own. The result of this divide in perspective will have consequences for the global economy, and particularly in the realm of financial advice and investing.

Studies reported by CNBC show that over 80% of children who inherit their parents' wealth will look for a new financial adviser. This represents tens of trillions which will shift between different advisories over the next few decades.

Millennials also prefer to invest into physical assets such as real estate and gold much more heavily than their forebears. On average Millennials report investing over 65% of their portfolio into more defensive assets (including cash), and less than 20% report having an allocation of over 25% of their wealth towards stocks. We may see an outflow from equity markets in the next few decades and the bulk of global wealth shift to other sources of investment.

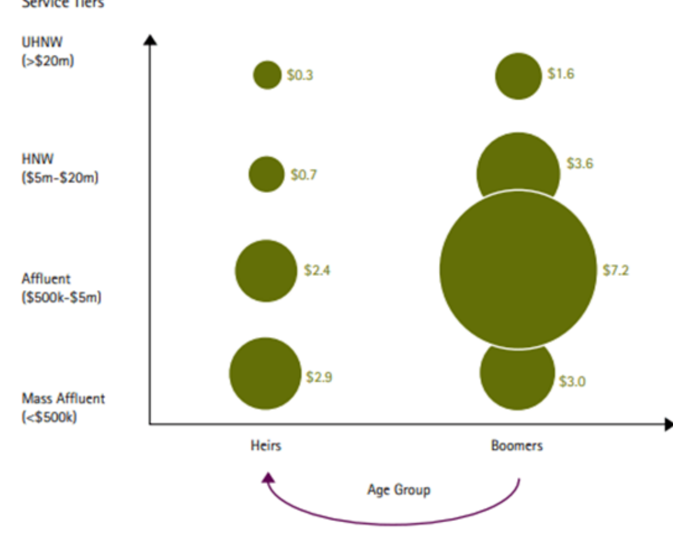
We may also see a shift in the balance of wealth classes, as the influence of the generational transfer inflates demographics within the heirs of these trillions.

Figure 3 shows the discrepancy not just in total wealth, but also in demographic distribution. The two largest groups amongst Boomers are Affluent and High Net Worths, whilst Mass Affluent and Affluent are the two largest groups of their heirs.

When this wealth moves down a generation, we will likely see a greater weighting towards higher tiers of wealth amongst the Millennial benefactors of their parent's inheritance.

As for economic consequences, it's a big question to tackle, but we can surmise that there will be overall less economic activity in the mid-term.

Figure 3: Demographic distribution of wealth



Source: Accenture, Federal Reserve

Millennials have a 10% retirement savings rate, more than double that of their parents. They also avoid debt, holding approximately 15% less mortgage debt than Baby Boomers. And as we established earlier, they are not as active in the stock market.

Looking to tomorrow

There will always be question marks around this level of wealth transfer being almost exclusively tied to human behaviour and social preference. Maybe some adult children should be a little kinder to their parents, or maybe those parents will buy another jet ski out of some planned inheritance.

As members of the global investing ecosystem, the Great Wealth Transfer will inevitably affect us all. Investors need to look over the next few decades to consider how the consumption and spending preferences of the two generations differ.

It seems likely that Millennials will not seek to imitate the behaviour or style of their parents, and we will walk blindly into the future not knowing where $68 trillion will end up.

Max Pacella is a Relationship Executive, Partnerships at Mason Stevens. The views expressed in this article are the views of the stated author as at the date published and are subject to change based on markets and other conditions. Mason Stevens is only providing general advice in providing this information.

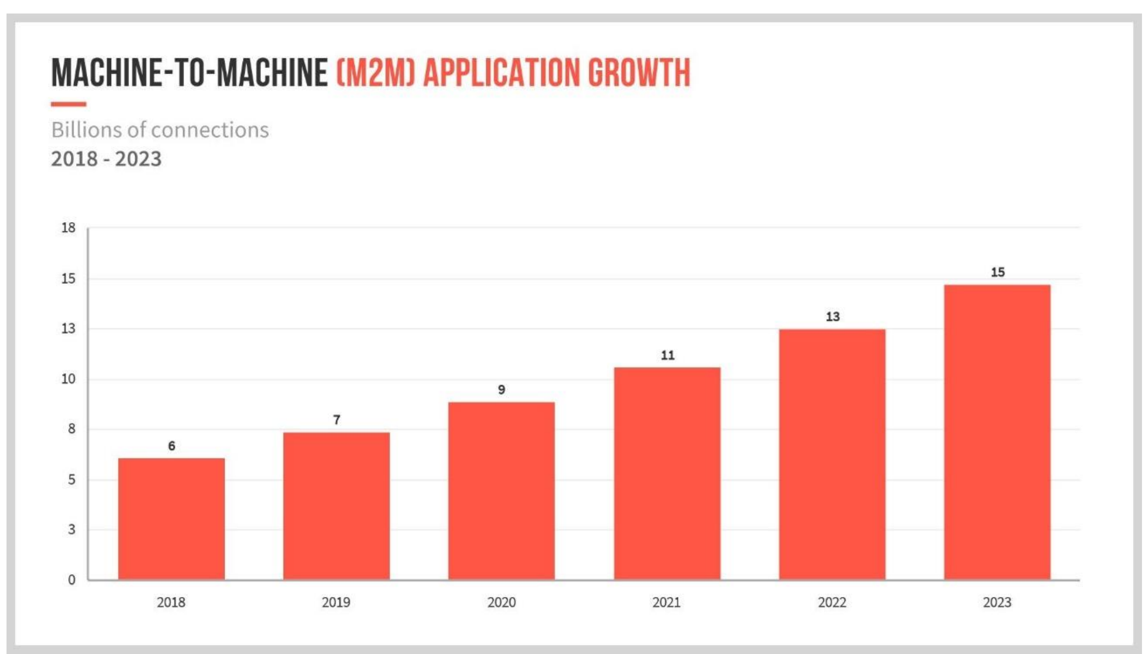
How real-time data keeps investors engaged

Ash J Hart

Data is everything. Even with a pandemic causing shockwaves in capital markets, data is a driving force. It powers modern, interactive technology, and the personalised services that attract consumers.

However, it also does something more. Data produces data. The information that comes from people using technology is vital. In some ways, that data is better than content in this digital era. The difference is that it incorporates real-time events.

Look at the world of finance. People watch the markets closely and follow the subtlest movements that sway financial predictions. They pay attention to industry and company news. Then, they make their investments accordingly. In this climate, providing investors with real-time data is no longer an exception but a rule. As shown below, machine-to-machine data applications will continue to increase rapidly.



Machine to Machine connections will grow 2.4-fold, from 6.1 billion in 2018 to 14.7 billion by 2023. Source: Cisco Annual Internet Report, 2018–2023.

Understanding data and potential problems

But what is data?

By itself, the word is an umbrella term. It can include confidential personally identifiable information (PII). For investors, data refers to resourceful information. It includes any information that can shape sound investment strategies. Data may include stock indicators or company news.

Unfortunately, not all data is created equal. The common problems with traditional data management are:

- Human input is prone to errors and inaccuracy, which can cause severe losses in the market.
- Organisations usually need accurate data from many sources at any given time. Manual measures are not cost-effective and sometimes impossible.
- Data needs to be automatically updated to remain relevant. 'Real-time data' is useful because it is timely.

For capital markets, each piece of data has the potential to move the market. In turn, each market movement has the potential to cascade into a more significant shift.

Understanding real-time data

Real-time data refers to market information that is reported as it happens. Before the advent of real-time data, investors relied on analysing stocks at the end of a trading day. The old method prevented investors from responding to short transactional opportunities. Today, real-time data informs investors of potential losses and gains, and lets them gain greater control over their portfolios.

The trade stock volume is a guide to how much interest other market players are showing toward a stock. Technical traders and analysts compile volume data according to stock movement trends.

Real-time data goes through APIs (application programming interfaces). In turn, they connect to centralised backend databases.

What are APIs?

API software effectively functions as the 'middle-man' in the stock monitoring process. It exists between the applications used by investors and the platforms powering backend operations. Each API solution supplies data according to what is wanted and when it is needed. To enjoy the full benefit of APIs, investors need to be specific about their goals. Data glide paths and other reference points can streamline that process.

Effective API solutions minimise delays in the transfer of information across the channels. The right API can help investment firms build more robust and productive relations with their investors. Offering tighter surveillance over market movements is a powerful benefit.

Open Banking in the UK and PSD2 in the EU prompted Australia to follow suit. Nations are passing new regulations that improve transparency and offer data protection. This resulted in the creation of more open API frameworks that support greater user control in data management. Progressive API standards started with the banking sector involving four of Australia's biggest banks in 2019, which have permeated other aspects of the market.

Real-time data in Australia

Australia, the UK, and the USA are currently seeing real-time data advantages through API frameworks. For example, the ASX processes its information from the Australian Liquidity Centre through advanced analytic systems. The ASX provides flexibility for investors who may opt between real-time data or end of day licensing. This arrangement allows investors to adapt to the rapid pace of real-time data analytics gradually.

But exchanges driven by real-time data are not without their hazards. On Monday this week, the ASX saw its biggest outage since 2016. Trading halted at 10.24 am and did not resume that day. According to the Exchange, the cause was a software issue that affected only the trading of multiple securities in a single order (combination trading) and created inaccurate market data on bid and offer prices.

Even though the bug only directly affected a limited number of orders, any inaccurate data in a market is unacceptable, as its effects can ripple rapidly outward. Investors must be able to trust that all the data they see, and any data driving the market's movements, is accurate.

The ASX is not the only exchange in Australia. Another lesson learnt from the ASX halting was that equity exchanges are in an interconnected ecosystem. Chi-X, a leading alternative securities and derivatives exchange, continued to trade after the ASX halted but trades on Chi-X were a trickle at best. Chi-X said the ASX put the market in 'enquire status', freezing all trades, where it should have put the market in the 'adjust phase' to allow brokers to cancel trades and move liquidity to Chi-X. The ASX said that brokers could have cancelled their trades while the market was in 'enquire status' but chose not to. Investigations into the glitch by market regulator ASIC should tell us more.

Real-time data moving forward

Real-time data is an essential aspect of modern investment strategies but an API is only as good as its integrity. The quality of real-time data determines the accuracy of investment potential. Investors should always opt for a platform that is certified and accredited by leading market experts.

An API coupled with real-time data can supercharge data management by:

- Easily integrating many sources of data
- Improving the speed of data transfer
- Automating otherwise tedious processes
- Eliminating the risk of user entry error
- Improved quality of investment services
- Constant innovation in data monitoring and investments

Sticking to delayed and conflated analytics can hurt investors. It deprives people of being able to make informed decisions. Investors need solutions that support the quickest, most reliable responses and interventions. A comprehensive API can achieve that through the implementation of smart real-time data.

Ash J Hart is the CEO of CGD Digital. For over a decade, the company has served NZ's top-performing asset management firms by creating applications to support client goals. This article is general information.

Disclaimer

This message is from Morningstar Australasia Pty Ltd, ABN 95 090 665 544, AFSL 240892, Level 3, International Tower 1, 100 Barangaroo Avenue, Barangaroo NSW 2000, Australia.

Any general advice or 'class service' have been prepared by Morningstar Australasia Pty Ltd and/or Morningstar Research Ltd, subsidiaries of Morningstar, Inc, without reference to your objectives, financial situation or needs. Refer to our Financial Services Guide (FSG) for more information at www.morningstar.com.au/s/fsg.pdf. You should consider the advice in light of these matters and if applicable, the relevant Product Disclosure Statement before making any decision to invest. To obtain advice tailored to your situation, contact a professional financial advisor. Past performance does not necessarily indicate a financial product's future performance.

For complete details of this Disclaimer, see www.firstlinks.com.au/terms-and-conditions. All readers of this Newsletter are subject to these Terms and Conditions.