Firstlinks
a Morningstar company

Edition 465, 8 July 2022

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Editorial

First up for a new financial year, many thanks to over 700 retirees who completed our survey on their retirement experiences, including thousands of comments. We have split the results into two articles: the first gives tips on how to make the most of a retirement, and the second shows the full results of the survey including charts. With so many comments across nine questions, highly informative but too numerous to put in one article, **Leisa Bell** has summarised the results into a downloadable document. It's worth taking the time to scroll through them, I found them fascinating.

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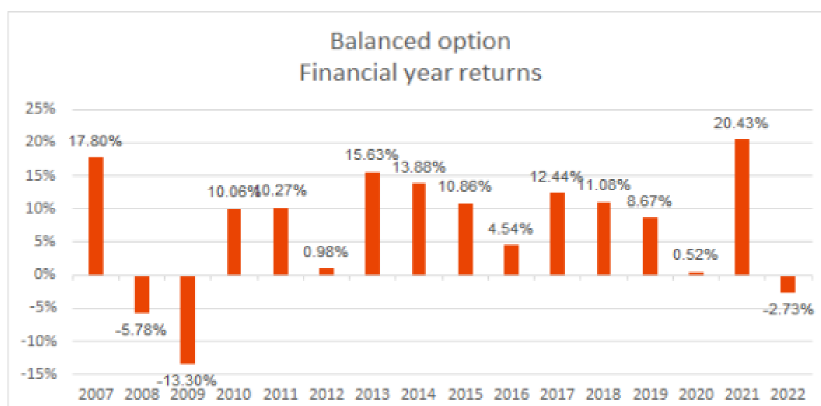
Behind the markets for last financial year delivering a fall in the S&P/ASX200 of 10% and a drop in the US S&P500 of nearly 20% lies every individual's personal experience. The US Treasury bond index lost 11%, offering none of the traditional bond protection. Even those who default into a balanced super fund will suffer their first negative returns since the GFC. Each investor must now decide whether to sit on their portfolio, sell to avoid further falls or invest more in bargain opportunities.

Howard Marks recently spoke about current market conditions on a Goldman Sachs podcast, saying:

> *"First of all, what is risk? It's the probability of a negative event in the future. What do we know about that? What does the past tell us about that? The past has relevance, but it's not absolute. I don't think risk can be measured. I don't think the past is absolutely applicable. In fact, the big money is lost at the juncture when the past stops being applicable, which happens eventually."*

The last six months feels like one of those junctures. We learn from the past but we are guessing about the future. **Mark Delaney**, CIO at Australia's biggest super fund, **AustralianSuper**, released a statement explaining a loss of 2.7% in its main balanced fund for last financial year. The same option was up 20.4% the previous year and 9.3% per annum in the last decade, a period of excellent returns for default super fund investors. It will be a long time before another decade is as good.



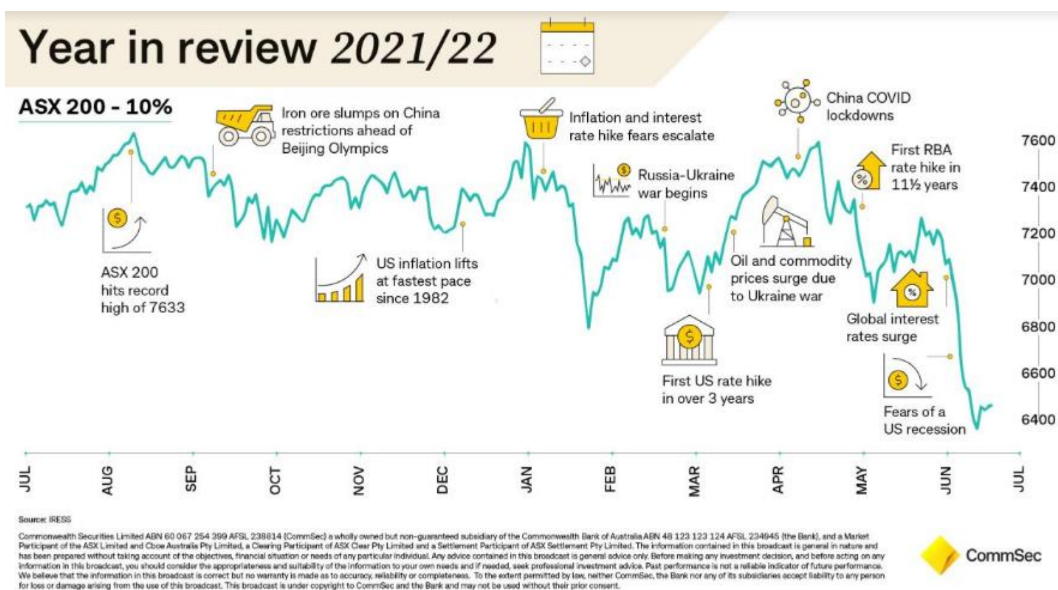
Delaney said of the results:

> *"After more than 10 years of economic growth our outlook suggests a possible shift from economic expansion to slowdown in the coming years. In response, we have started to readjust to a more defensive strategy, as conditions become less supportive of growth asset classes such as shares."*

He's a bit late to the game if he has just *"started to readjust"* as the signs were there in late 2021, as described in our editorials.

We all have different risk appetites and ways to think about investing. I have a friend who I've known for 40 years and he's been consistent in his strategy. He cares only about the income from his portfolio, and this is far less volatile than share prices. When **CIMIC** (formerly **Leighton**) was recently fully acquired by its German owner, he received a large cash payment which he wants to reinvest. What's his reaction to the recent sell off? *"Shares are for sale at a discount. It's fantastic,"* he told me last week.

Most investors nursing losses are not so happy, and this neat graphic from **CommSec** shows how the year unfolded to deliver the 10% loss in the ASX200. It highlights how poorly the year ended.



Hugh Dive of Atlas records the Dogs of the ASX each year, and here are the major losers. Wasn't everyone wearing gloves (**Ansell**), buying respiratory aids (**Fisher & Paykel Healthcare**) and buying pizza (**Domino's**) in the pandemic? **AfterPay** and BNPL rivals were replacing credit cards, **Xero** was driving business efficiency, job search was moving to **Seek**, **Reece** was riding the property boom. Hard to imagine anyone picked these 10 dogs during 2021.

Dogs of the ASX in 2022

Company	Industry	Return in 2022	Reason for Large fall
Block, Inc	Tech	-75%	Rising bad debts from AfterPay, tech sector de-rating
Ansell Limited	Healthcare	-47%	Higher raw material costs, weakening industrial demand for protective gloves.
Evolution Mining	Gold	-45%	Production downgrades
Xero Ltd	Tech	-44%	Tech sector de-rate
Domino Pizza	Consumer Discretionary	-42%	Slowing sales as CV-19 restrictions ease and higher raw material prices
Reece Limited	Industrials	-41%	Concerns about declining construction/renovations reduce sales
Virgin Money UK	Banks	-38%	Expectation of higher bad debts in the UK as recession bites.
Fisher & Paykel Healthcare	Healthcare	-37%	Falling earnings as a decade's worth of respiratory devices sold to hospitals over a 2 year period.
Seek	Media	-35%	High PE stocks de-rated
Nine Entertainment	Media	-33%	Increasing competition for advertising dollars as Netflix introduces a local ad-funded service

Source: iress & Atlas FM

The first-time, often younger, investors who jumped into the market in 2021 without the gains from prior years have found investing is difficult. It seemed like easy pickings when everything was up, from tech, Bitcoin, BNPL, online retail, NFTs, property. Interest rates lower than we'll ever see again pushed up the price of everything, and newbies bought on every tip in town. Now, late entrants to the greatest companies in the world are watching the red numbers with Amazon off 35% and Alphabet 22% in the June quarter.

For example, some tech-themed ETFs launched in Australia during the hype were ETFS Semiconductor (SEMI), down 33% last FY, BetaShares Crypto Innovators (CRYP) down 71% and Cosmos Global Digital Miners (DIGA), down 76%.

The debate is whether the losses suffered by younger people with a few thousand invested matters to them over the long term, as it is part of an investing journey and they have not lost much in dollar terms. **Rob Arnott and Research Affiliates** hold a view that is counter to traditional advice about risk appetite by age.

> *" ... we are told that the young are tolerant of risk and that, as retirement approaches, the average investor becomes intolerant of downside risk, fleeing after a serious drawdown ... Conventional wisdom suggests a percentage allocation to equities which is '100 minus your age' and the notion that the young can bear more risk than those of us who are middle aged (or older!). True, the young have more time to recover losses, but what losses are more insidious for retirees than inflation sapping the real income of a bond centric portfolio?*
>
> *If young workers have to deal with their volatile young human capital over a long horizon - with a heightened need to cash out when the portfolio values are depressed - then it makes even more sense for younger workers to begin with a less risky portfolio. This also helps shape their risk tolerance so that their attitudes about investing and riskbearing are not poisoned by a bad early experience."*

It's not a conventional view and bonds have not performed the protective role Arnott is writing about, but it's a legitimate challenge to the argument that equity exposure should reduce with age. Certainly, my mate, now in his 70s and fully exposed to equities, does not follow convention.

Our articles take the discussion further.

In this week's interview, **Chris Demasi** presents the case for ignoring short-term market falls when great long-term compounders are available at fair prices. This is not an argument to invest in just anything but the **Amazons, Microsofts** and **Alphabets** of the world that have strong future earnings. And he includes an Australian company in his portfolio.

Marcus Padley says investors should embrace the opportunities that come with fear in the market, and he describes five steps he has gone through in the recent selloff to decide the best way to respond.

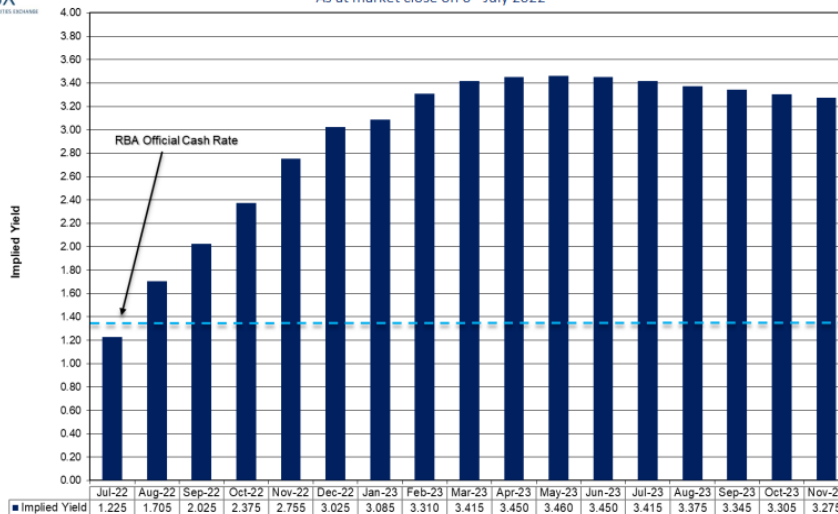
Then **Ian Rogers** chronicles the end of **Volt Bank**, which was one of the challenger banks that seemed more likely to survive. Volt did not fail due bad loans, but the current predicament facing many startups as capital becomes harder to access. It shows the benefits of scale of the majors and the difficult regulatory environment for new players.

Campbell Harvey and Rob Arnott paint a concerning picture of the US economy. They write that the Fed was late to the game, inflation is likely to keep rising and the result of the Fed's belated actions may push the economy into a recession.

Michael Collins explores how privacy-focused regulatory scrutiny is challenging the online-ad business that is built on the collection and dissemination of consumer data.

The **Reserve Bank** decision this week to increase the cash rate by 0.5% to 1.35% comes with the expectation of another increase next month. The decision was justified by high global inflation - boosted by supply chain restrictions and the war in Ukraine - strong demand for goods, a tight labour market and capacity constraints. But **Philip Lowe** expects inflation to peak late in 2022 and decline back to the 2–3% range in 2023. His comments sounded slightly more relaxed about the need for future rate rises.

Where do we stand now? We have featured this ASX chart several times over recent months, and close watchers will see a significant fall in cash rate expectations. The implied rate for early 2023 is 3.4% but it was over 4% in mid-June, a level we said was highly improbable. It still looks too high, requiring a hefty 1.55% of further increases for the rest of 2022. Lowe does not want to see what that would do to property prices.



How to enjoy your retirement

Graham Hand

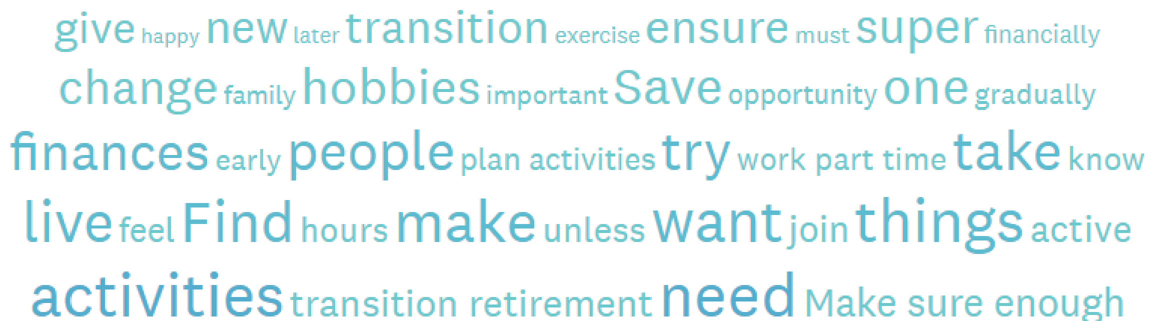
Coinciding with 30 years of compulsory superannuation, the start of a new financial year and the introduction of the Retirement Income Covenant, we surveyed our readers to find out how they spend their retirement.

As the survey was limited to retirees, the response from about 700 readers is excellent. Thanks for participating and sharing your wisdom from experience.

A complete analysis of the results with charts is in this article. Here we focus on one of the questions.

Do you have any tips for people approaching retirement?

The word cloud from this question neatly summarises important points:



One of the main messages concerns time management. Use it well. Retirees enjoy the freedom after a lifetime of work and the ability to spend more time with family and other interests but don't waste the opportunity. Make it a period without money troubles by owning your own house and using super well.

We received thousands of comments and it is impossible to feature them all in an article, so we have moved them all into a PDF. But here is a sample:

- Definitely plan something productive in your week. Gardening, volunteering, renovating or whatever helps maintain a sense of worth. Golfing and cycling are great but in my experience don't fulfill the need to feel productive in the long term. Also, if you are spending hours a day checking and researching your investments, just be aware that you are not doing it "for your retirement", you are making it your retirement. Which may be fine.

- Take one day at the time and all fall into place in time.
- Don't. The social aspect of work, the sense of purpose, can be hard to replace unless you have a serious set of interests or family to be involved with. Keep working - for many professionals it defines who you are.
- Be open minded to continue learning new things away from where your career took you. Give back to community where you can and ensure you have a big enough nest egg that pesky market fluctuations aren't an issue.
- Get out and enjoy. "SKI"…. (Spending the Kids Inheritance)
- Just do it if you can afford to...Life is short...make sure you retire debt free, especially with no mortgage
- Make the decisions together with your partner if you are lucky enough to have one, about where to live and how to accommodate the priorities of both of you.
- You need to break the work habit. After my wife and I retired, we went on 3 month world travel in year 1 and year 2. This broke the daily cycle which I found important.
- There's no magic moment or a time when one should retire
- Have a wide range of interests, care for others and do not let the 'Old Person' in.
- You have to keep busy even in retirement. Busy people are happy people. Find some hobbies. Do some exercise. Lots of people do gardening which is what I do. I enjoy it and it keeps me fit. I also go for a walk in the morning. I enjoy being outside. I go to the National Parks a lot. I only spend limited time inside at the computer. You need something that keeps you jump out of bed in the morning. Something to get up for. Everybody has things they like. Pursue something you love and just keep going until the end. Don't sit all day in the most comfortable chair. Do something. Challenge your brain every day to hopefully keep dementia away.
- Just do it. It is wonderful being fit enough to still be able to travel and do physical activities Don't wait too long
- Have a rough idea of how you will use your new found time. Plan a few years ahead, its great to work towards it, setting your goals. Live within your means.
- Do it gradually 2) Keep interested and involved 3) By all means help look after grandchildren but beware of committing to a regular schedule. It becomes a tiring routine and grandchildren may start taking you a little too much for granted.
- Do it in mid 60s. Speaking to lots of my older golfer friends when you hit 70, you won't be able to physically do a lot of things as well as before and health problems will start to set in-unless you are one of the lucky ones-but I don't like your chances.
- It took me about 2 years to fully appreciate retirement. If you can do some part-time work or voluntary work for that two years the transition can be easier. Work on keeping physically fit. Make sure that you retain a significant circle of friends and see them often. Regular catch-ups over a coffee at a cafe works for me.
- Look after your health in the years well before retirement and be financially secured.
- Develop new interests, reach out to meet new people, go and search for interesting and useful activities to participate in the community. Nobody will come looking for you.
- Ensure you make a list of things you want to do in the rest of your life. I'm still to take up fly fishing!
- Don't let yourself get confused by listening too much to all the wisdom of third parties who have not retired but want to give you advice what you need to do. Do what you want and think is best for you. Whether this is gardening, cycling cooking or tinkering with electronics or SW development does not matter as long as you and your partner give each other some free space and enjoy the majority of time together. Eat together speak to each other, enjoy your company. Happy days!!
- Talk to people who have retired. Transition. Educate yourself on potential pitfalls.
- Do the homework regarding the funding of retirement.
- Work out what you really enjoy about your current employment and do it on a smaller scale.
- Stay active in some role, either with sport or social activity, or volunteering, grand parenting, or in casual paid work - as these all add some structure and timetable to your week. Don't waste your days laying about or watching TV. Get out and about in some form and enjoy the freedom you have worked hard for!

- Don't stop work completely unless you have no choice. Keep you options open to continue working part time and take your time transitioning to full retirement. For most people, if you think you have enough funds to retire then you probably don't have enough funds without compromising your desired lifestyle excessively.
- Make sure you have enough money and maintain social and family ties, have some interests and keep fit.
- Corporate employment can deskill you for a life of independence. Approaching retirement pick up some individual skills that would enable you to pickup short term but well paid contract work.
- I took advantage of the pandemic to really scrutinize my spending habits and budget. I realised I didn't need as much money in retirement as I originally thought and therefore was able retire earlier than planned.
- Maximize your superannuation. Make sure you have plenty going on in your life outside of work.
- Pay off your house and top up your Super. Plan lots of travelling before you are in your 70's.
- Buy new stuff if required like fridges, cars, washing machines etc. They are expensive when you don't have an income coming in
- Look to your superannuation, because that will be the foundation on which you can live a comfortable life.
- Gradual if possible. Ensure money flow is more than adequate for what you plan. Think carefully about what you want to spend your time on. Ensure you have friends or join a group to make new friends. Volunteer using your talents
- Salary sacrifice. Being financially independent removes a huge worry.
- Keep in touch with your friends and family. Try to minimise debt before retiring, if possible. Have a go at a new interest, meeting new friends and contacts in the process.
- Save as much as you can while still working. If you have had a job where you work long hours, try going part time before stopping altogether. This will help with the transition.
- Have interests you really enjoy. Eg. My membership of outdoor group with many activities. I found it difficult to find a meaningful volunteer role due to my travel activities as many rely of frequent and regular attendance say 48 weeks per year.
- Become exposed to stock market investing (even in small way) ASAP. Join as many local activity groups before retiring (e.g. local politics, service and community interest clubs, Aust. Shareholders Assn., Sporting Clubs)
- Don't be a burden on others because you didn't arrange wills and get rid of excessive possessions
- Men are bad social animals, ring people, make lunch dates. Must have people.
- embrace the change and make a better place to live for yourself
- Wind down your spending as you near retirement to see how much money you can live on.
- Don't do nothing. Find things to do regularly even if they are very minor
- Keep yourself motivated. Step outside your comfort zone. Keep learning
- I tried to scale back from 5 days a week to 4 days a week but the project work kept on coming even on my days off. The scale back didn't really work but still got a pay cut.
- Plan and write your lists and then talk to those you know who have retired from your particular field. Think carefully about what you WILL do and then judge if this is practical for you. Visualize yourself as a retired person and then think about your lists of to do's and consider how practical they are depending on your health, finances, spouse's thoughts and aspirations
- Make sure you have enough money to avoid having to deal with Centrelink.
- Plan ahead and engage with your hobbies and any planned volunteer activities. Work part time near your retirement Have a financial plan.
- Retire early while still fit mentally and physically.
- Most people overestimate in their minds just how much money they need to retire comfortably. Whilst its not a small amount, its not a billion dollars either, so don't put yourself in an early grave trying to achieve a level of wealth that's unrealistic for the actual lifestyle you intend to live
- I strongly favour tapering into retirement: gradually reduce working hours and take on outside interests over time. Don't make a step change.
- Plan to ensure that you have things to do in retirement. If you having nothing to fill the vacuum, you will become bored and depressed.

- Staged retirement. Keep your friends, Do not go to live elsewhere, especially coastal holiday place.
- Prepare for what you will do on the Monday morning of the start of your retirement.
- Try to design a glide path of gradual move to no work. Secure some part time activity before making the jump. Retirement (even an active one) doesn't have to be expensive. Guard against relevance deprivation. It is not speed that kills, it is the sudden stop.
- I went to my first retirement seminar when I was 30 years old, not when I was 60 years old. Since that day I have been able to plan backwards from my planned retirement at 60yo. Unfortunately I had to medically retire at 57 but the plan was in place
- Keep yourself busy especially volunteering with a purpose. Keep yourself fit. Enjoy sleeping in some days. Walk the dog daily. Make sure you have enough money to retire comfortably without worry when the economy goes bad.
- Engage a financial planner even if it's only to ensure you are on the right track for retirement & the future ahead. Ideally educate yourself about your investments long before you retire. If possible go from full time to part time work to ease into retirement.
- Natural eating (no medicine, and alcohol is not medicine). Natural exercise (including climbing, swimming, jumping). Natural risk-taking (physiological, mental, financial).
- Read as much as you can on the issues, especially on funding and relationships. Having enough income helps adjust to the obstacles that will come sooner or later. I found 'The Barefoot Investor' an excellent guide to investing and it summarises my attitude after 40 plus years of investing. One of its concepts is to support charities as an integral part of your expenditure.
- Engage a financial adviser to plan your "portfolio" and mechanics of implementing a structure that can provide optimum financial benefits from the opportunities available.
- Contrary to the normal advice - I'd say don't overplan. I certainly didn't as I didn't intend to retire when I went on Christmas holidays but at the end said to my wife 'for the first time every I don't really feel like going back to work (I loved my job). Look for opportunities to do things you haven't done or have not been able to do while at work. Build new social networks (mine comes from the community transport volunteering).
- Don't feel guilty of just taking it easy and do not be pressured into doing things you don't want to.
- Read everything about planning for retirement. Join the Association of Independent Retirees (AIR) a national not for profit organisation advocating for those funding their own retirements. Do your homework - life in retirement can be cheaper than working life. Investigate where you live and why - no point spending huge money on a house and not having enough to live comfortably. Stay healthy so you can enjoy retirement - being a healthy weight and basic fitness extends your life and your enjoyment. Travel is easier if you are fit and healthy. Don't plan to retire and play golf everyday unless you have a plan B - what if you can't play golf because of injury? Bad weather? Don't become a slave to your children and spend your retirement looking after grandchildren at the expense of keeping in contact with friends.
- Prepare financially to the best of your ability have confidence in your decision and know what simple things in life you enjoy and do them it's your time do as you wish not others expectations.
- Unless super balance is very large try to continue part time work for a few years. This has advantaged me more than I realised at the time.
- Make sure you've paid off the house and can generate over $100k tax free income per annum and then enjoy!
- Plan ahead both in what lifestyle you want and how you will achieve it and fund it ongoing. Put money away for your travel aspirations.
- Retire at the same time as your partner.
- Do not think of retirement as just that short time between work and death. It can be a wonderful time of our life. We just need to re-invent ourselves. Our focus needs to be on mental and physical health, rather than career and building assets.
- Make a plan and potentially start an 'interest' that is viable in your senior years
- Plan for retirement a few years before, so that you have weighed out your options and make preparations. Finance is the area most covered but it is truly dependent on what you want to do with your time. Focus on family, health and spiritual areas.
- Life is too short, so do it while you have your health, sound mind. You can always find something to do. Even some trading if you have some spare disposable cash.

- Transition into it. Develop a hobby's and interests before retiring
- Make sure your finances are good. Get out of debt as quickly as possible and start compounding your money.
- Take an interest in your Super (now!). If you do not have many interest outside work, start looking for some. If possible scale back work or start taking Long Service on half pay, short term retirement also has economic benefits.
- Unless you will work part time, develop some hobbies before you retire
- Experience things like overseas travel early before health issues arise.
- Take it as it comes. Be frugal, look for value in your spend. Remember there is still much to smile about.
- Salary sacrifice as much as possible. (The govt will assist as a low income person) Consider selling home and moving to suitable country location, then invest proceeds in a suitable fund.
- Use it, or lose it. A good life is the attitude you bring to it. Every day is in your control - good or bad. Stay fit doing some form of regular exercise, eat a balanced diet, stay involved and connected to friends, family or acquaintances. Try and learn something new each day, no matter how small. Manage what is in your sphere and don't fret or worry about what you can't control or change. Stay informed and involved with your financial position.
- Pre retirement, start doing or learning things of interest that can be expanded in retirement (musical instrument, bridge, crafts, etc)
- I'm mostly invested in index funds with some sector funds I think will generate alpha (or at least very close to market returns in a worst case). I rarely buy individual shares unless i think I've found a no brainer- which the market doesn't throw up very often and most often simply reinforces the lessons of why low cost index investing allows you to beat most professional active managers over long time frames, assuming they're in business over a long time frame! I never sell because the market performs poorly. You can't successfully get a job by blindly picking a company and not knowing anything about it or understanding it's business. You can't successfully pick a stock/ etf/ fund by blindly picking a company and not knowing anything about it or understanding it's business.
- I think its obvious you need to get to the point where you don't have to think about money then you can do anything.
- Plan carefully, because earning money does make a big difference to your psychological state ... feeling free to spend / give money ... make sure you have enough to satisfy your individual lifestyle. Pay off your debts before you stop earning. Diversify your assets.
- Work as long as you can while you are enjoying it. You are retired a long time and there is no going back.
- Try to be without debt or make arrangements to make it happen soon after. Learn to cook and clean the house. Be prepared to de-clutter. Get financial advice if needed. Start looking at the share market at least 10 years before retirement.
- Try and prepare by having a good think about what it is you would enjoy. develop other interests. make sure to take the opportunity to join and enjoy new company and friends.
- It won't be as glorious and you think but it will be better than being at work (usually).
- you job title is not who you are. enter the final quarter with a spirit of enquiry, stay fit and healthy in body, mind and soul and kick with the wind
- Approaching 50's be ready things can change suddenly. Start realigning your personal wealth portfolio to ensure you have income generating assets. Cash flow is king.
- Keep active and involved in community and with family and friends.
- Keep as fit as you can, and remember that alcohol will pickle your brain and can encourage dementia.
- Manage life expectations well in advance of retirement so that the transition is seamless. Line up other things to do that don't cost money.
- Make sure you have the credit cards you want or similar as it becomes much harder to change banks when you are a self funded retiree even if your assets are in the millions.
- Plan ahead so that you have something active and stimulating to do - not just golf occasionally or walking the dog. If you just sit down in a chair (or at a holiday resort) and do nothing, you have set yourself on the downhill slope to losing muscle tone and mass, and losing brain sharpness, and consequently aging rapidly.

- research and be prepared to take up new activities. Never played bridge before but now have played in comps overseas
- Plan ahead. My retired brother-in-law has excellent advice. He says: "Keep trying new hobbies until you find ones you like." On a whim, I experimented making artworks out of beautiful, colourful fabrics. I've also taken some much admired photos and had them put on canvas. I found that creating things gives me satisfaction.
- Plan for retirement at least 10 years before to enable a comfortable lifestyle.
- The expectancy of life (in retirement) is a further 20 years of living. Health is a pressing concern, such as becoming overweight. The second essential is to have a plan for the ensuing 20 years.
- Go for it when you are ready as you don't know whats around the corner especially if you wish to travel or start new business venture
- Retirement is different for everyone, but think about how you will spend your day, and the next day and even for the next 20 years. Consider daily golf for twenty years.. Really?
- As much as possible, have a realistic plan for what will fill your time with worthwhile activities (and not just golf). Keep active, both mentally and physically (as health does become problematic for many) and contribute your time to what you consider to be some worthwhile causes. Financially, get good advice and stick to it (thanks Morningstar) and don't focus too much on short term market movements or sweat the small stuff.
- Start planning finances and attitudes so you slip into a pattern of your choice, not uncontrolled circumstances you may find yourself in.
- Try to transition gently so the change is not so abrupt. Consider a 3 or 4 day work week if that is possible. Have a plan for what you want to do in retirement and start to put it in place before you retire. Double check your financial position and if possible allocate more to retirement savings while you are still working. Start thinking about how it will be when you have no income from employment, and have to live off your savings only. That can be destabilising for some. Make sure you have realistic budgets and income expectations from your savings.
- Ensure your future income is sufficient. Invest in sustainable dividend producing shares. Get a dog.

Results from our retirement experiences survey

Leisa Bell

Our Reader Survey on retirement experiences drew about 700 responses, an excellent sample given it was limited to retirees.

We also received thousands of comments, and we are honoured that so many readers allowed a glimpse into their personal experiences. The comments are collected into this document. (Please note, this is a large document but we wanted to include all comments since people went to the effort to write them).

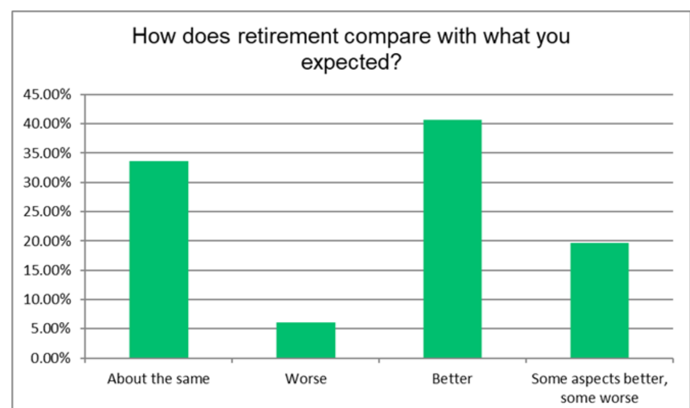
Of course, we must have a favourite comment, thanks for this:

"Reading and keeping informed is very crucial to good management. eg Firstlinks takes 30min~1hr per week. Thank you Firstlinks for a great, and free, informative, professional newsletter :)"

Here are the survey results. We include a chart for multiple response questions, and a word cloud for open questions.

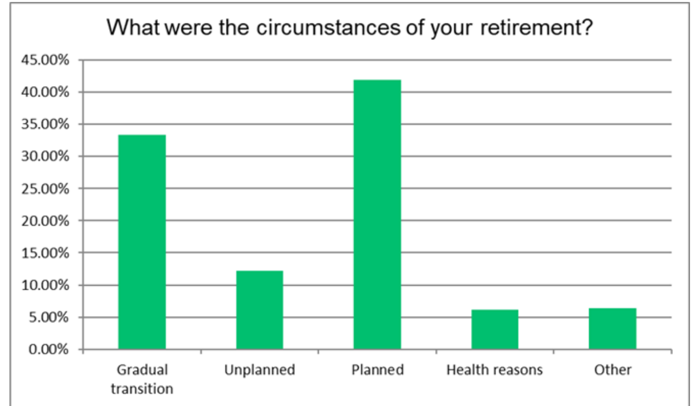
Q1. How does retirement compare with what you expected?

In an encouraging note, only 6% responded that retirement is worse than expected, while an optimistic 40% think it is better and 34% about as expected. Another 20% were more mixed, with some aspects better and some worse. See the full document for hundreds of explanatory comments.



Q2. What were the circumstances of your retirement?

It was good to see that 42% planned their move from paid employment and 34% enjoyed a gradual transition. Only 12% said it was unplanned due to loss of a paid job, while another 6% retired for health reasons. Another 6% had 'other' reasons for retirement, perhaps such as: *"Fed up with neighbours, noise and inconsiderate people and opted for 44 acres in the bush!".*



Q3. How do you spend the time previously occupied in paid employment?

An open-ended question, with a common reponse that there is now time for activities that were missed when working:

"Renovating, caring, animals, growing vegetables, relaxing dealing with day to day tasks."

"Live on small lifestyle property with large lawn/trees/garden. Reading books and articles non profession related. Manage SMSF funds and bookkeeping of such for accountant/auditor. Genealogical research and writing account of same."

"Working! But in different ways. We run an Air BNB inc doing maintenance and cleaning. Help with care of grandchildren , run two houses, do charity work and am doing a book of family history. No shortage of things to do."

took fitness Covid See retirement making studying week gym Lots fishing s
catching friends Catching help spend lot time cooking voluntary work things
coffee friends managing Research relaxing socialising going days week
interests know volunteer work much spending time bridge
grandchildren small investments managing investments
friends Also house want hobbies Mainly walking music
exercise spend volunteering managing SMSF
gardening management travel new reading
coffee time daily work Enjoying golf sailing family group
home family friends day financial activities run cycling local wife
long etc Renovating holidays maintain lunches playing bridge Looking
looking grandchildren maintenance Playing sport investing Probus projects kayaking
sport caring walking dog overseas swimming people now club plus children tennis
beach playing planning

Q4. What are the best aspects of retirement?

Another open-ended question, many of you find retirement liberating:

"No tax, no pressure, no being told what to do or what not to do and a said above freedom to make your own choices."

"Sleeping in in winter, playing golf 2 or 3 times a week, swimming in the pool in summer every day. Cameraderie of the golf club."

"Last minute decisions to see shows or travel etc."

"Introspection that is not employment focussed. Feels like I had an imagination budget, and the large part of that used to be spent on work thinking. Now that's so broad!"

schedule trying family look think commuting fit responsibilities needs years better exercise
plenty time lot reading Waking plan time constraints friends Control time less
Enjoying life live anything now week rush will time things early sleep hours
choose daily want want lifestyle go etc pressure meet able
every day enjoy make day free want people Freedom
boss time grandkids work bit things see travel spent
flexibility volunteer stress great Choice Free time activities
around Less stress control worry interests ability demands spend time
business take go work life Freedom choose long less pressure deadlines able want want
one s feel wife please regular Freedom choice morning relaxed set home
everything stress work rather without holidays grandchildren walks

Firstlinks
a Morningstar company

Q5. What are the worst aspects of retirement?

Although most people said there are no downsides to retiring (and many said there are not enough hours in the day), others report that it's not all 'smelling the roses', with some warnings, especially around health. Enjoy it while you can:

"Our golden years were cut short by health issues. Boredom is now my major problem."

"Dealing with doctors and all the time spent in waiting rooms."

"Some friends still work and not available. Also being single, I need to factor in friend's partners as well."

"Sometimes I feel a lack of mental stimulation."

"Knowing that this is it! When working it didn't matter if you were ill, thanks to sick pay it didn't feel like a dead loss. Likewise if the weather was foul you could still go to work and feel purposeful. When retired these days feel like lost opportunities."

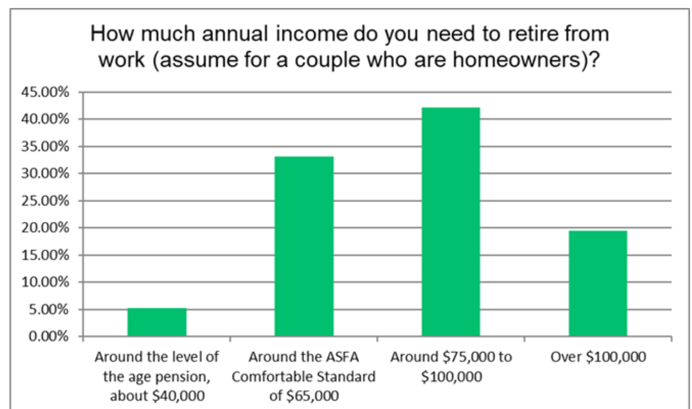
Q6. Do you have any tips for people approaching retirement?

This question is covered fully in its own article.

Q7. How much annual income do you need to retire from work (assume for a couple who are homeowners)?

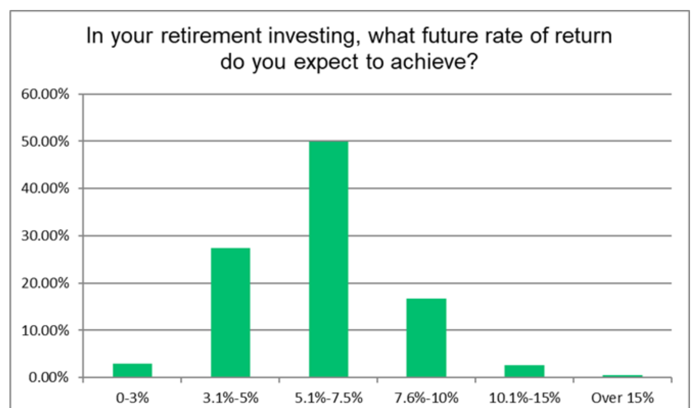
Firstlinks readers hold above-average wealth, and it is not surprising to see about 20% need over $100,000 a year in retirement, and another 42% are $75,000 to $100,000. That's almost two-thirds needing more than the ASFA Comfortable Standard which is sufficient for 33% of respondents. Only 6% accept the age pension level. All amounts assume home ownership.

There is a strong preference to self fund retirement, even if it means working longer or saving more, and seeing the retirement years as an opportunity rather than a post-work drag.



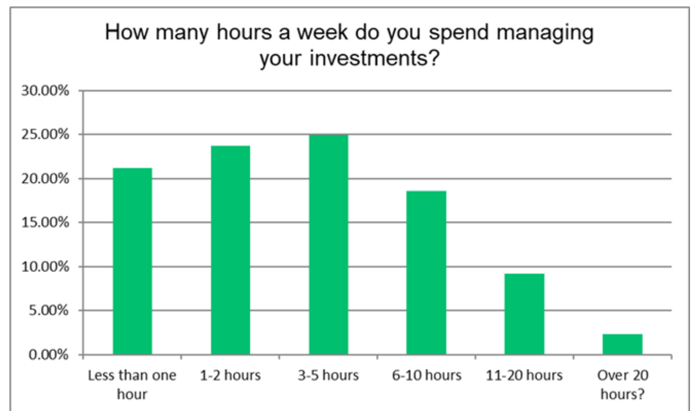
Q8. In your retirement investing, what future rate of return do you expect to achieve?

Most people expect a return on retirement savings of over 5%, with almost 20% aiming for a more optimistic 7.6% or more. Perhaps this question should have been asked in real terms, because if inflation hits 7%, strong returns may be flat in real terms, at least for the next year or so. High inflation is not expected to last forever, even if the days of ultra-low interest rates are gone.



Q9. How many hours a week do you spend managing your investments?

Managing investments occupies a decent chunk of the lives of many retirees, with 30% spending six or more hours a week on their portfolio. For a small minority at over 30 hours a week, it's a main activity. Some of the comments are:



"I enjoy economics and finance. I read and listen a lot but leave my investments alone. Inflation has eroded less of my cash position (30%) than the fall in my equities. Waiting for equities to approach fair value before buying selectively."

"Went to a financial adviser and got things sorted out just the way we like them. Doesn't require too much managing now."

"This includes reading the Australian Financial Review, Firstlinks, Morningstar."

"My partner loves doing this for our SMSF so I just keep up with my reading on financial affairs and attend monthly investment meetings."

Thanks again to everyone who participated.

Why short-termism is both a travesty and an opportunity

Graham Hand with Chris Demasi

Chris Demasi is a Founder and Portfolio Manager at Montaka Global Investments, a global equity manager with staff in Sydney, Melbourne and New York and managing about $300 million across two ASX-listed active ETFs and an unlisted fund.

GH: You've been writing on the need to invest and think long term. Would you describe short-termism in equity markets as the biggest problem facing investors?

CD: Absolutely. The myopic nature and increasingly short-term views mean investors are taking their cues from short-term movements in stock prices, and that's how they measure the success of their fund managers or the companies they invest in. The geopolitical and financial market uncertainty makes horizons shrink and it's a travesty, but it also creates a lot of opportunity for people who stay the course, pick up bargains and hang in for the long term. I say travesty because they forgo a lot of the extraordinary gains they could otherwise make by staying the course and focussing on a long-term view. They should be thinking about the fundamentals of the business and the opportunities in front of them rather than short-term share price fluctuations.

We use a chart which shows over the long term, the chance of a positive return on a daily hold of the S&P500 is only 53%. But go out to one year, and it's 75%, then five years is 88%, 10 years is 94% and there are no negatives over a 20-year period.

Stock market performance over different horizons

S&P500 return frequency, percent

Horizon	Total Periods	Positive Periods (%)	Negative Periods (%)
Daily	23,529	53%	47%
Monthly, calendar	1,104	63%	37%
Quarterly, calendar	368	69%	31%
1-year, rolling monthly	1,093	75%	25%
5-year, rolling monthly	1,044	88%	12%
10-year, rolling monthly	984	94%	6%
20-year, rolling monthly	864	100%	0%

Source: Fisher Investments; Global Financial Data, Inc. Daily return data begin on 31 January 1928 and are based on price appreciation only; all other data begin on 31 January 1926 and reflect total returns to 31 December 2017.

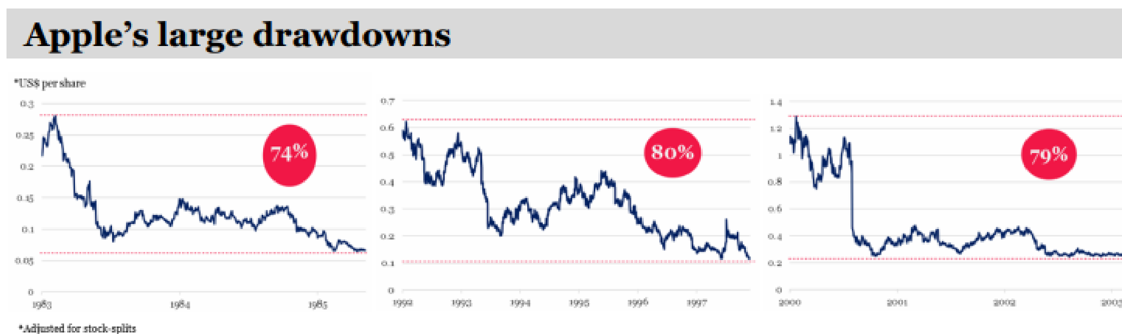
GH: Do you believe good opportunities still exist in today's market of inflation, rising rates and a fear of recession?

CD: Even today, we see many examples where excellent companies have expanded their addressable markets, they are growing their revenues, their earnings power is increasing, often exponentially. The business value is going one way but the share price is moving completely opposite. And therein lies the opportunity for investors that stay the course.

Go back to the experience of Alphabet over the last decade. It's a company that has grown earnings by seven times and over a decade, it's an eight-bagger, but few shareholders would have retained it over that time. They are too busy timing the buying and selling but if investors had simply followed the path of the earnings power and the business fundamentals, they would be rewarded handsomely. Alphabet's share price is down 22% in the last quarter. There have been periods where the stock has gone down by 30% and it's often fallen by 15% but that's the cost of entry to the opportunity.

GH: Yes, and the same with Amazon that had a 90% drop in the tech wreck, but how many people hung in through that experience?

CD: Yes, and we don't wish for falls like that, but Charlie Munger and Warren Buffett say that if you can't tolerate a 50% sell off, you shouldn't be investing in equity markets. Morgan Housel says in *The Psychology of Money* that volatility is the price of admission and the prize is superior compound returns. While some of these drawdowns can be painful and nobody wants them, the best performers have all had large drawdowns. In fact, Apple has had three.



Investors need to understand this to give them confidence to stay the course, but not in every company. It applies for excellent companies that have opportunities to grow exponentially for long periods of time when their leadership positions and moats are sustainable.

There are great examples of that not being the case. Peloton had a pull forward in demand during the pandemic for their digitally-enabled bikes but the fall in its stock price has been led by an earnings drop. The same is true for some bricks and mortar retailers such as Bed Bath & Beyond in the United States with unsustainable earnings estimates. But if you look at the best companies, such as Apple, Amazon and Microsoft, their future earnings potential continues to grow.

GH: You've also written about how long-term returns are driven by surprisingly few companies and the majority don't contribute over time. So it's not a matter of simply investing for the long term in anything.

CD: In our analysis over 10-year periods, most companies don't hold their value and only one in four stocks turn $1 into $5 and one in 16 turn $1 into $10 and it's those that create all the value in the stock market. So to deliver superior compound returns over a decade, we need to focus on finding outstanding businesses leading transformations in their markets, and buy them when they're undervalued.

GH: Is this message of accepting the inevitable drawdowns resonating with your clients?

CD: It's always a difficult message and that's a reflection of human nature, we just don't like to see prices go down. But, yes, the message resonates when we present the evidence as it builds a degree of confidence that this is the right way to approach equity markets.

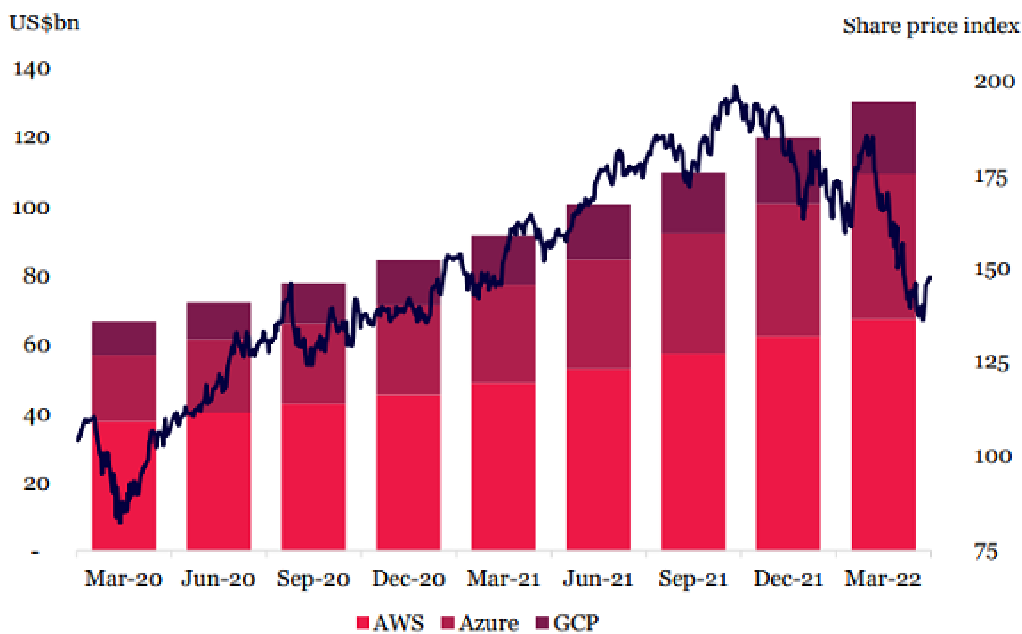
GH: But what might you also look for as an exit point for some of these companies, because if you if you look at an Alphabet or Microsoft, there's a case to own them forever?

CD: This is our playbook. If the thesis changes or something happens that we don't understand, that triggers a review of the position. It might be competition or regulatory change or something else that disrupts a leadership position. Or if the market size is not evolving as we expect and the growth potential is lower or riskier than we thought. And of course, the one that we like is if the price goes up a lot more than we can justify. We have a good example in Microsoft at around US$250 today. We think the business will reach a value of US$1,000 to US$1,200 over a decade based on growing cash flows into future, so we're playing for four or five times in 10 years for one of the highest-quality companies in the world. We take a 'private equity'-like approach to public markets, so if the public equity market takes Microsoft to US$1,000 by the end of the year with nothing else changing, that might trigger a sell because that was all of the upside we were playing for.

The flipside is that if we still believe in the thesis but the share price halves, now we're playing for a 10-bagger. We might have capacity to add to our position, and investor with money on the sidelines can improve the future return potential.

GH: How do you weigh up for the geopolitical and macroeconomic factors that also feed into the market, as well as the company specific?

CD: Because we focus on a concentrated portfolio of opportunities, we think less about geopolitical events and macro. We appreciate they can change the mood and sentiment in the market but if it doesn't change the drivers of business value and earnings power over time, then it's much less relevant in most cases. Extending the Microsoft example, virtually all the increase in value over the next 10 years will come from cloud computing and artificial intelligence, and that's not dependent on a war in the Ukraine or inflation or interest rates over that time. We don't typically change the portfolio to play the short term.



(Note, AWS (Amazon) holds 33% of public company cloud market share, Azure (Microsoft) holds 21% and GCP (Alphabet or Google) holds 10%).

GH: You're a global equity manager but do you have any Australian stocks in your portfolio?

CD: We've held REA Group for a while. It's one of the world's best businesses, which sounds funny because it's in a small pocket in a corner of the world but it's almost a monopolist in an industry that favours winner-takes-all, and it still has room to grow as we shift from offline to online. It will take a greater share of real estate marketing budgets. It's not a Microsoft or Alphabet but it's an excellent position and it's still a growth business.

GH: You have two ASX-listed vehicles, the Global Long Only (ASX:MOGL) and the Global Extension (ASX:MKAX). What does 'extension' mean and what's the difference between these two funds?

CD: They both invest in the same core portfolio of stocks and today there are 23 stocks so it's a concentrated portfolio with the top 10 making up about 70%. The extension allows us to run a small short portfolio of companies we believe are in trouble or in industries that will deteriorate over time, and that's about 30% worth of the portfolio. We use the proceeds from shorting to apply more exposure to the core portfolio of 23 on the long side.

GH: Okay, it's typically a 130/30 fund of your selected winners and losers. Can you give an example of a stock you like but has disappointed and it made you think about any lessons you might learn about your investment process?

CD: The biggest lesson is the other way around, where we have let go of one of these high-quality compounders too soon. We've been too sensitive to a run up in prices, for example, selling Apple and Microsoft. The trick is to recognise the difference between price and value and stay the course and not be tempted to sell out, either up or down. We're less inclined now to take shorter-term profits because we're playing for so much more in the future.

GH: Is there a company that you expect to own for the next 10 years or longer?

CD: Almost all the companies in the portfolio, unless the public market gives us an opportunity to reap the multiples we expect much sooner. An example is Blackstone, the private capital and alternative asset manager. We can see so many new market opportunities for them not captured in the current valuation. They're only just starting as far as money allocated to the alternatives sector is concerned. Institutions are underweight private capital and the retail market of private banks and clients is an US$80 trillion untapped opportunity. Blackstone's been building distribution and sales for the last 10 years. We expect them to manage many trillions of dollars in the years ahead but the macro themes and lumpiness of asset accumulation will test investor patience and staying power, while throwing up opportunities to buy more shares.

GH: Final question. If valuations are so good at the moment, what are doing with your own money?

CD: I can't understand the divergence between the business values created in the companies we hold in the portfolio and the selloff in their stock prices, so sharp and dramatic. Microsoft down over 20% year-to-date, Amazon even worse, 35%. We've been putting more and more of our own money into our funds and will continue to do so. We're eating our own cooking.

Graham Hand is Editor-At-Large for Firstlinks. Chris Demasi is a Portfolio Manager at Montaka Global Investments, a sponsor of Firstlinks. This article is general information and does not consider the personal circumstances of any investor.

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Fear is good if you are not part of the herd

Marcus Padley

No doubt a lot of you, scarred by the GFC or the 2020 pandemic-inspired drop in the market or by the current sell-off, are worried about a more significant market correction. It's no fun investing in 'fear' and if that's you then let me tell you about fear and in so doing rid yourself of the constant worry that the stock market is about to fall over and destroy your financial expectations.

Understanding and welcoming fear

Let's make a few points about fear.

First, there is always, always, always something to fear when to comes to the stock market and fear is good because it's the fear that creates opportunities. Rather than avoid fear, you should welcome it. It is in the grip of stockmarket fear and exuberance that the most money is made in the shortest timeframe.

Second, you should also understand that when fear starts, we will perpetuate it. Fear is great for us, for the financial media, the brokers, the financial planners, the fund managers, for financial advisers, in fact it's great

for the whole finance industry. Some commentators make a living out of fear, like Nouriel Roubini or Marc Faber with his Doom and Gloom report. Why? Because fear triggers insecurity which drives investors to us. Fear is the sheep dog of financial services. It rounds up the sheep so we can shear them.

Third, fear is also a powerful magnet that attracts eyeballs and in a competition for clicks, when investors are at their most fearful, the clicks and eyeball numbers explode. Everyone wants advice and we will provide. Advice is a Trojan Horse for commercial purposes, much more effective than common cheerfulness.

Click bait in its natural form starts with the words "5 things…". To capitalise on that, we in the financial media chuck in some of the top click bait keywords, and then, if the glorious moment (as now) presents, we throw in some fear. The most commercial headline includes keywords "Warren" and "Buffett" and a small sprinkling of fear, and it goes like this:

"5 reasons Warren Buffett thinks the stock market will crash"

Publish and wait for the clicks.

The bottom line is that fear is just part of the great game that is the stockmarket (or any market). It creates the lows, it creates the best opportunities and for the finance industry, it is gold. Whether it is a broker looking for an order, a media person looking for attention, or a financial planner looking to convince a client that they need them, fear gets more traction than optimism. Fear gets attention.

So when the stock market drops 5% in a day there are a few things you don't do. Don't join in. Fear makes you vulnerable as an investor. It distorts your normally objective state of mind. If you get fearful when the market loses its head, you become part of the herd. Far better you recognise it for what it is: an emotional 'moment' in other people's minds. Rather, think about how you can exploit it. It will vary depending on the sort of investor you are and the sort of risk appetite you have.

A plan of action when fear hits

When the market loses its head in fear:

- Stay cold, objective, logical. Look down on the fear. Emotion will not help you, it will cost you.
- Accept what your shares are worth now. Don't dwell for a moment on the highs and how much you *were* ahead. The highs are gone and there's nothing you can do about it. Anchoring yourself to yesterday's prices will deliver nothing but regret and a feeling of stupidity. Look at the bottom of the spreadsheet. That's what you're worth. Accept it.
- Get excited. The market only presents great opportunities occasionally. One is coming. It is from moments like these that quick money is made.
- Take an informed guess at what you think is going to happen next. The only thing that matters is what's *going* to happen not what has happened.
- Decide what to do, if anything. Understand that no-one knows. Do your best. Just decide and live with it. Accept the outcome right or wrong.

So, my thought process in the current sell-off has gone like this:

1. Take 10 seconds. Tiger Woods says you are allowed 10 seconds to express your emotion after a golf shot, but that's all. Take 10 seconds. It's good for you, but there's nothing to be done about the past now. Time to move on and decide what to do next.

2. Identify the core issues. I read a lot and quickly (it's pretty obvious) identified the core of the issues for the correction. Macro stuff. In this case inflation, interest rates and the fear of a US recession, with a sprinkling of China lockdowns and Russian risk.

3. Decide if it's a blip or a trend. I made an assessment of whether the main issues are likely to persist or turn on a sixpence. I decided this time they were more likely to persist.

4. Do something or decide to do nothing. I'm good at selling, which I did this time. You should learn to do it. It's cathartic. You wake up the next day *hoping* the market collapses rather than fearing it will. It's empowering having cash and being 'ready to go'.

5. Take it day by day until the bottom. Now the game is to watch and wait for 'Peak Fear'. The market will bottom one day. It could this week or it could be in a year. You must take it one day at a time. Wake up

> every morning and react. There's no predicting it. I know I'll make more money in the recovery from the bottom, and more quickly, than I lost in the last few days. If I can get it right, it will be fabulous.

And that's how you approach this moment. With the intention to exploit everyone else's fear.

I believe you can time the bottom. Commentators say it is impossible so they don't have to do it. For financial professionals, it's easier handling docile 'buy and hold' clients who can be convinced that timing can't be done.

Embrace the fear

You should welcome corrections and other people's fear. The most exploitable moments of the market are the fabulous exponential, irrational, exuberant bits at the top and the most fearful, despondent, capitulations at the bottom. They are the bits, the extremes, the opportunities, that make the market worthwhile. Those extremes, those moments of stupidity, absurdity, farce, ridiculousness and nonsense are brought on by other people's irrational fear and irrational exuberance. You should expect them, look forward to them, and use them, not avoid them.

A good investor watches and exploits the herd. Let that be you.

Marcus Padley is the author of the daily stock market newsletter Marcus Today, see marcustoday.com.au. This article is general information and does not consider the circumstances of any investor.

No excuses: Plan now for recession

Rob Arnott, Campbell Harvey

Recessions do not naturally begin in an economy with two job openings for every job seeker. That said, there's nothing natural about recessions. In 1998, MIT Economist Rudi Dornbusch in the US observed that "*none of the post-war expansions died of natural causes, they were all murdered by the Fed*." The motive for this murder is usually to save the economy from incipient inflation by killing the economy.

It is a time of heightened uncertainty, with many forces driving that uncertainty. The US has an inflation rate at a four-decade high. Most people don't remember the last time inflation was at this level. The Fed's responses adopted now will likely slow the economy. The Fed is very late to the game because the board members were in denial for a long time. In November 2021, the Fed finally officially retired the word *transitory* after dismissing the inflationary pressures with that description far too long. We might be surprised that the Fed did not see this coming, but the Fed's track record on forecasting, whether the economy or inflation, is rarely better than a Ouija board.

Inflation's causes, prospects, and the Fed's toolkit

Inflation is a simple consequence of a supply/demand imbalance. If demand exceeds supply, prices rise until balance is restored. The current surge in inflation has been caused mainly by blowout spending, supply chain disruptions - some related to Covid lockdowns and some to geopolitics - the Russia-Ukraine war, and working from home, which leaves people with more money to spend, even as many produce less goods and services.

Which of these can the Fed influence? None? Is the Fed powerless to rein in inflation? Not at all. Central bankers can decrease demand, albeit with serious lags, even if the problem is on the supply side.

To a person with a hammer, everything looks like a nail. With an echo-chamber guiding monetary policy all over the world, the only answer that seems to resonate with central bankers is to decrease demand. None of this is to say that the Fed should continue with a dozen years of negative real rates. Jerome Powell inherited a Fed after a half-dozen years of negative real interest rates, which he has continued to this day.

We liken real interest rates to a speed bump. Too high and traffic is stopped: innovation, long-horizon investment in new initiatives, entrepreneurial capitalism all slow markedly. Too low and reckless driving ensues: if we are among those able to borrow at negative real rates, we will, whether we have good ideas for the money or not. Misallocation of resources and malinvestment - at the individual, corporate, and government level - naturally will follow, along with propping up zombie companies that clog the runway for the innovators. All of this in turn inhibits innovation and entrepreneurial capitalism, both because risky projects cannot access

those ultra-low rates, and established enterprises and government may waste much of the free money at their disposal.

Being late to the game increases the probability that the Fed overreacts, because it didn't act soon enough. This increases uncertainty and elevates the probability of a hard landing, which is what everybody wants to avoid. Hard landing means we go into a serious recession, like the one associated with the GFC. There are huge economic as well as human costs associated with hard landings. Nobody wants to be laid off or to spend an extended amount of time on unemployment insurance. A soft-landing scenario is much more desirable. That could mean slower economic growth or maybe a mild recession before the economy moves into a recovery phase.

Will the Fed raising interest rates by 75 basis points make a difference to supply chain disruptions? No. To deal with inflation, we need to deal with the source of the problem and address it directly, not just hit it with a blunt instrument that sometimes worked in the past. The usual approach does not inspire confidence. We worry the Fed is going to mess it up.

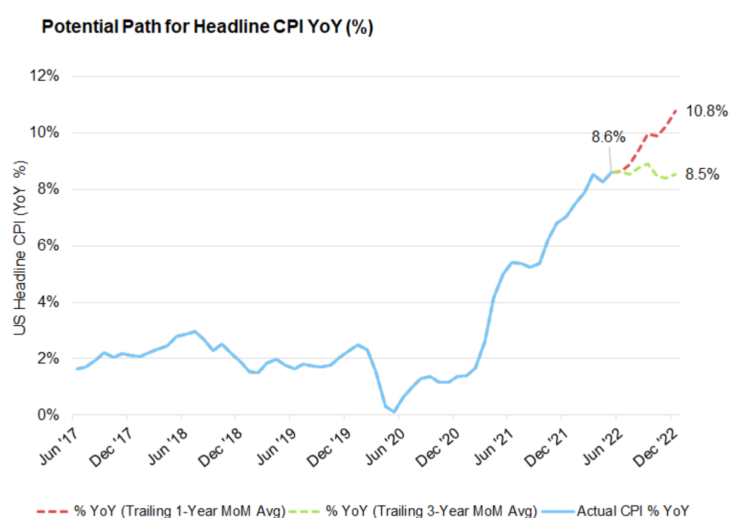
Step number one is to go through the individual components driving the 8.6% CPI inflation number. Consider housing, for example. Given that a homebuyer can get a mortgage for much less than 8.6% means that effectively the financing is free or being subsidized. In terms of real rates, this increases the demand for housing. So, for this component, raising rates appears to have some logic. But the housing issue is much more complex, encompassing not just the demand for mortgages, but the demand for materials, and the structural backlog caused because we have not been building enough housing over the last five years. The rise in housing prices has nothing to do with Covid.

The near-term prognosis for inflation is not good

Each month's 12-month inflation rate matches the previous month's inflation rate, plus a new month, minus the corresponding month dropped from the previous year. We can't know with any confidence what the new month's rate will be, but we know with precision the rate of the month being dropped. The next four months to be dropped from 2021 will be 0.9%, 0.5%, 0.2%, and 0.3%, respectively.

The Cleveland Fed produces an 'inflation nowcast' which estimates what the monthly inflation would be if the month ended today. If their nowcast is correct, the 0.9% from June 2021 will be replaced with 1.0% for June 2022. If inflation in each subsequent month through year-end 2022 matches the average inflation rate over the prior 12 months, we should finish the summer at 9.9% and finish the year at 10.8%.

If, alternatively, monthly inflation recedes to match the trailing 36-month average, then the current 8.6% inflation rate would remain steady through year-end. This simple analysis leads us to believe that inflation will likely get worse before it gets better.



There's another problem with the way CPI inflation is calculated. The largest component, shelter, is one-third of the total and is smoothed and lagged. According to the Bureau of Labor Statistics (BLS), their chosen measure for the cost of home ownership, owners' equivalent rent (OER), is up 7.3% in the last two years, while the S&P/Case-Shiller Home Price Index shows that US home prices have risen by 37% in the two years ended March. The BLS switched to OER after the last inflationary surge in 1979–81; indeed, if inflation was calculated today like it was in 1981, we would already be solidly into double digits.[1]

The one-third of CPI for shelter will be playing catch-up for some years to come. Empirically, most of that catch-up occurs over the subsequent two to three years. Note that this inflation has already happened; *it simply hasn't made its way into CPI quite yet.*

Preparing for recession versus reacting to recession

Uncertainty is a negative force and is a question of degree. When a war is going on, especially involving a nuclear power (as is the case now), that's a big deal, much different than a regional war that doesn't involve a nuclear power. The degree of uncertainty is key. An average level of uncertainty is always present, but the level can fluctuate. When the level of uncertainty is relatively high, as it is today, business leaders should actively manage their risk.

What does risk management look like? Let's say, for instance, that a corporation has a promising project which entails building a new plant. Management believes this investment will enhance its long-term value. It increases investment, employment, economic growth, all good things, but the corporation needs to finance the plant. At this point in time, do you want to bet on the company given the current uncertainties? This isn't theoretical. With inflation running at a 40-year high, major geopolitical disruptions around the world, monetary and fiscal policies in flux, the logical tactic is to exercise caution.

In his 1986 PhD dissertation, one of us (Cam Harvey) was the first to show that a yield-curve inversion has a perfect batting average in forecasting recessions since 1968. The other (Rob Arnott) has suggested that a yield-curve inversion doesn't *predict* recessions, it *causes* recessions. The long end of the yield curve is mainly a market rate set by the market's perception of the fair cost of long-term capital. The short end is largely managed by the central bank.

If the central bank raises the short-term cost of risk-free capital above the long end, it is choosing a rate the market *tells us* is too high. This isn't necessarily the case in an economy (Europe or Japan) where the central bank also controls the long end of the yield curve (in policy circles, this is called yield-curve control). But, when the free market determines the long end of the yield curve, the Fed should pay close attention!

On 30 June 30 2019, when the yield curve had inverted for a full quarter, Cam was frequently interviewed by the media, explaining that this signal was 'code red' for recession. All previous eight episodes since October 1968 of inverted yield curves were followed by recessions, with no false signals. Some criticized his statements as potentially causing a recession. No, his warning was risk management 101. Facing a red flag, a business would be ill-advised to bet the firm on that new plant.

Today, the yield curve is not inverted, so why worry? As with the recent two-fold surplus of job openings relative to job seekers, this too shall pass. Really? The forward markets do a pretty good job of forecasting near-term Fed decisions and they are suggesting a 90% likelihood of a 75 basis-point hike in July followed by another 50 to 75 basis points in September. Those moves would take the 3-month Treasury bill yield to about 3%, within hailing distance of the current 3.15% yield on the 10-year Treasury bond. Absent a run-up in long bond yields, one additional hike before year-end would leave us with an inverted yield curve. Further, Cam's analysis shows the slope of the yield curve is the key indicator. A flat curve is bad and an inverted curve is really bad for economic prospects.

Many companies took Cam's warning in 2019 seriously, and indeed when Covid hit, they were in reasonably good shape. No single industry faced an existential crisis as a result of Covid, although some industries, especially hospitality, restaurants, and retailers, were more negatively affected than most. But this was not like the GFC when a single industry, financials, faced a risk of collapse and/or nationalization. Some people were ready because they knew an inverted yield curve was a reliable red flag. Today the heightened uncertainty is obvious. We think that means people will be cautious and they will engage in risk management.

It's not too late to prepare

If we are not already slipping into recession, we see a substantial probability that a recession could start in late 2022 or 2023. If we are right, then the CEO of a company that gets into real trouble in the recession can't go on stage at the shareholders' meeting or on the quarterly earnings call and say management was blindsided by the recession. That's not good enough. People would laugh at them. The signs of recession are in your face. The way to deal with it is to be more conservative until some of the uncertainty is resolved.

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Footnote

1. In "The Coming Rise in Residential Inflation" available on SSRN, Bolhuis, Cramer, and Summers (2022) argue that "the current inflation regime is closer to that of the late 1970s than it may at first appear."

The fall of Volt Bank removes another bank competitor

Ian Rogers

The board and management of Volt Bank, in their bombshell decision in June 2022 to hand back their banking license, have underscored the fragility in so many fintech business models in Australia. Banking is an incredibly heavy consumer of capital and even in the best run organisations it chews through mountains of pricey executive and consultant time.

From the outside, it seemed Volt - which weathered the storm of Xinja Bank's chaotic demise in 2020 - was passing milestones and finding its footing, even the outline of a sustainable niche, in the crowded banking market in Australia.

The hard-working Volt board, fed up with the shrinking pools of capital worldwide for the briefly-fashionable fintech and neobank sectors, have resorted to retrieving whatever owner value they can, and carrying on with the remnants of its tech (via Volt Limited) that may challenge banks, without the unaffordable luxury of a banking licence.

Startups who plan to fund and flip

As unbelievable as it sounds, there was a period - let's say around 2019 - when all manner of schemers and dreamers and their advisers sat around devising banking business models that were never intended to be a proper business. The poorly-founded belief was that, once and if licensed, the plan was to cash in. Just flip the license pronto.

Proponents of this madness, of which there may have been dozens, must have thought the process was mainly a case of ticking APRA boxes, then cutting and pasting the absolute minimum risk, prudential, operational and governance documents to creep over the line.

With no more than vapourware, these schemers intended to rustle up the minimum capital to get the APRA green light. Then, these hopefuls believed, they'd pocket the profits from the sale of their non-existent bank via a trade sale.

Only equally desperate and even less well-capitalised fintechs could have been in the target market. Of course, none of these operators got anywhere near the starting line.

Judo Bank is kicking on, even flourishing. Two licenced RADIs doing not much are Alex Bank and Avenue Bank. Alex is up and running, or dawdling. The Alex balance sheet is constrained by the low ball cap on deposits. It has until July next year to progress to a full licence. Avenue, 20% owned by Liberty Financial, has no deposits, no loans and no known plans to make its debut.

Volt was different

Volt's management and board were never part of the ill-informed antics. A defining difference at Volt was the depth and experience among the top management team and on the board.

Only half a dozen or so neobanks ever secured a license from APRA during this strange era. And there won't be any more. Xinja self-destructed 18 months ago. Soon after Xinja tanked, Cuscal – the owner of 86 400 – astounded the industry with the well-considered (and highly profitable) sale of the bank to NAB, in January 2021.

Now Volt, less dramatically, is staging a strategic withdrawal.

Non-bank mortgage funder Resimac appears to be the buyer of the mortgage book of Volt Bank, which is exiting the industry. In a media release, Volt said it had "*executed a transaction to sell its mortgage portfolio*," but did not identify the buyer. Resimac declined to comment on a request to confirm or clarify its dealings with Volt. APRA data shows Volt had $80 million in housing loans at the end of April.

Through Volt Limited, which will continue trading even as the bank is wound up, Volt retains ownership of the intellectual property at the heart of the Australian Mortgage Management business, which it acquired a year ago.

Volt Bank clients - fintechs and others – are scrambling to identify and engage with alternative suppliers of a banking-as-a-service offering, and minimise damage to their own businesses. Volt devastated their BaaS clients by withdrawing their increasingly in-demand BaaS suite – including deposit products – effective immediately.

Volt had five BaaS clients in production and another half dozen ready to on-board. The number of prospects in the pipeline is unknown, but likely to be plenty.

For clients such as money management platform Parpera, which was reselling deposit and card payments product to sole traders and very small businesses, the sudden cancellation is compromising for a fintech emerging from its start-up phase. Parpera ceased onboarding new members immediately and providing its services to members by 5 July 2022.

Who might the likes of Parpera go to? There is little depth in the banking-as-a-service domain in Australia. BAAS is, nominally, a (recent) strength of Westpac, but there are doubts the bank is eager to serve small fry and its systems may be too clunky (the bank counts heavyweights such as Afterpay and SocietyOne as clients). CommBank? Maybe, but fintechs by and large plan to profit from attacking the market share of the biggest banks.

The drastically short notice imposed on clients by Volt had some asking: why not a few weeks longer? The reason may well be that this is a function of APRA's inflexible requirements, rather than any resolve of the Volt board for a hard stop.

Ian Rogers is a seasoned industry commentator with more than 30 years' experience and Founder of [Banking Day](). This article is general information.

Three main challenges to online ads and 'surveillance capitalism'

Michael Collins

In 2007, Jonathan Trenn of the US bought a diamond ring from Overstock.com so as to propose to his girlfriend in a few months' time on New Year's Eve. Within hours of buying the ring, Trenn received a 'shocking call' from a friend saying congratulations for getting engaged. He said:

"Imagine my horror when I learned Overstock.com had published the details of my purchase including a link to the item and its price to all my (Facebook) friends ... including my girlfriend and all of her friends."

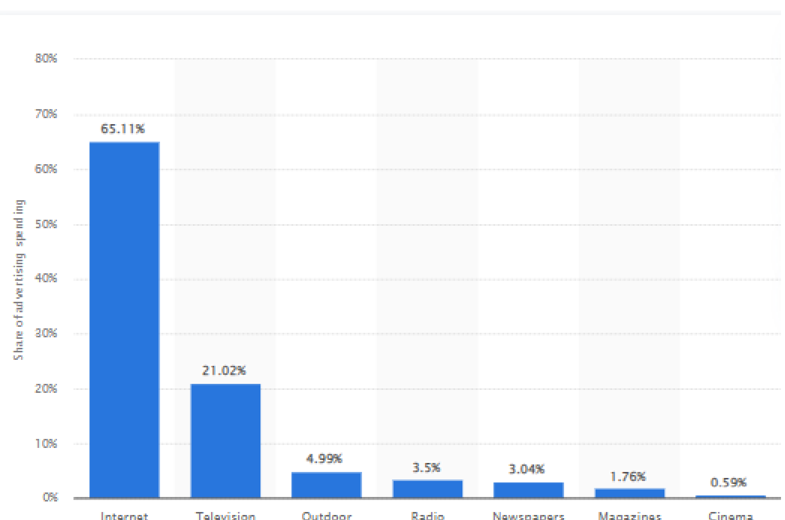
Such was the technical ability of Beacon that enabled Facebook publisher partners to reveal their customers' purchases to Facebook networks to drive engagement and sales.

While Beacon was shut down in 2009 due to user complaints about privacy violations, the gathering and commercialisation of user data on the internet has only intensified such that the phrase 'surveillance capitalism' was coined by US academic Shoshana Zuboff in her book of 2019 to describe the practice. The term represents how private companies, sometimes with questionable user consent, collect as much data as they can on their users with an objective to maximise profits. Controversially, they have enjoyed the ability to employ technology that can track users across the internet. Once they have enough data, the data harvesters then sell their ability to match these profiles against the type of people whom advertisers would like to reach.

The success of online ads

Targeted online advertising is among the world's most successful business models such that online advertising is expected to reach 65% of global advertising spending by 2024.

Online advertising's dominance
Distribution of advertising spending worldwide expected in 2024, by medium



Source: Statista. Published 17 February 2022

The sobering news, however, for companies that turn data into behavioural information is that the business model is coming under regulatory scrutiny and changing in ways that dent the money-making ability of the platforms that rely on off-site (or 'third-party') data for targeting, while strengthening the position of those platforms with significant on-site (or 'first-party') data.

The impact of regulators and Apple

The **biggest** challenge for the online-ad business model is the elevation of online privacy as a social concern. This has two strands.

The first strand is that EU policymakers are imposing tougher laws to restrict data use and make more transparent how data is used. The most worrying consequence for Big Tech? Such regulations spread worldwide, most worryingly for them to the US.

The second strand to the elevation of privacy concerns is that Big Tech companies – especially Apple – are offering privacy protections because, as Apple CEO Tim Cook says, the online privacy 'emergency' is making society 'less human'. An Apple update in 2021 installed a change whereby users must agree to being tracked across apps. The result is that Facebook and other platforms have suffered as their ad targeting has become less effective.

The **second** challenge to the online-ad business model is greater scrutiny of the unregulated ad exchanges on which prices for online ads are set in an auction. Texas and other US states have filed a lawsuit of collusion against Google that accuses the company of taking steps to prevent publishers from using 'header bidding'.

The term refers to when publishers insert code in the header of web pages to increase competition among online ad exchanges. The Texas filing said that when publishers used header bidding, they received up to 70% more for their ads than when using Google's ad exchange without header bidding.

The header-bidding revelations have aroused other policymakers. In the US, bipartisan-sponsored legislation is before Congress that aims to stop companies from playing more than one role in digital advertising. If enacted in its current form the legislation would force Google to spin off parts of its online-ad business.

A **third** challenge for the online-ad business model is the political question of the dominance of internet platforms in society; specifically, whether their data gathering and use of certain algorithm-promoted content to maximise engagement threaten democracy. Some demand that the ability of companies to collect data be restricted to the point of being abolished.

Hurdles to displaying ads, exposés on online-ad exchanges, industry restrictions on competitor data-gathering, and incremental government regulation might accelerate the decline in the effectiveness of display ads. But people will still see plenty of them. Businesses know that online advertising is a generally superior way to promote sales and brands thanks to its micro-targeting and measurement abilities. A mild rise in ad misfires won't matter much to them.

Advertising budgets still directed online

Governments and bad actors have the capabilities to abuse online privacy to a much greater extent. Irrespective of the harshness of laws preventing ad targeting, the personal information of device users will remain traceable. Privacy only flickers as a political problem because most people seem untroubled that Big Platforms and others track them online.

But enough care and more might, especially as TikTok is gathering data globally that many allege heads to China. While a drive is underway to ensure online privacy more matches offline privacy, nothing is likely to happen that stops advertisers from directing most of their budgets to online. But at least enough of a privacy push is underway that it's safer to buy an engagement ring before proposing.

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