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Editorial

The Cheesecake Factory is a US chain restaurant with a 21-page menu. Diners can choose between more than 250 options. The restaurant prides itself on making each dish from scratch. As you can imagine that takes a large kitchen staff.

Each day there are between 60 and 100 people who work in the kitchen with each chef responsible for overseeing the production of 30 menu items. The Nashville branch of the Cheesecake Factory has 18,000 kilos of ingredients delivered per week. It is an impressive logistical achievement.

On a trip to Japan in April I went to Sushi Kobikicho Tomoki for a 24-course omakase. There is no menu and you eat the fish that is in season. The meal was prepared and served by chef Kobikicho Tomoki, his wife and a dishwasher.

These are two very different experiences. At least I think they are – I'm yet to grace any of the 215 Cheesecake Factory locations.

There is a point to my restaurant juxtaposition. The difference between producing food at the Cheesecake Factory and Sushi Kobikicho Tomoki is the difference between mass production and a craft.

This doesn't make one good and the other bad. But if you want to be successful in either kitchen you need to be clear about what you are doing – practicing a craft or working the assembly line.

I've been thinking a lot about the term craft. I wrote an article for Morningstar last week and referred to investing as a craft. Several readers disagreed by pointing out that all it takes to be successful is dollar cost averaging into a broad-based index fund for the next few decades. They view investing as mass production. That isn't how I see it.

Is investing a craft?

A broad-based index fund is an investment. And there is a significant amount of research showing the merits of this approach.

But there is a big difference between an investment and investing. The craft isn't what you buy – it is the process you go through to build wealth. That is investing.

A craft requires judgement derived from knowledge and experience. It requires careful and persistent execution.

Building wealth takes the foresight and discipline needed to save money over decades.

It takes patience so that compounding can do its work.

Building wealth requires the emotional fortitude to not panic in a bear market.

It takes conviction to stick to the same strategy when some other investment will always perform better over the short term – especially if you use a broad-based index fund.

You must ignore the naysayers and resist the compelling pitches for alternate approaches.

Final thoughts

Working in the kitchen of the Cheesecake Factory requires basic culinary skills and the ability to follow a recipe. You need to know your role in a crowded kitchen and execute the same tasks repeatedly. Each staff member is part of an assembly line. That is how mass production works.

Chef Kobikicho Tomoki trained for ten years before opening his own restaurant. Four of those years were spent learning to make rice. Once the restaurant opened it took twelve years to be recognized by Michelin.

This seems like a lot of work to cut a piece of fish and stick it on rice. But what sets a craft apart is how hard it is to do something well. Just dollar cost average into an index fund over decades is easy to say and hard to do.

I've never seen a study that suggests the average person is good at investing.

Dalbar and J.P. Morgan looked at the average performance of individual investors in the US between 1998 and 2017. They estimated that the average investor achieved a 2.60% return per year when the average balanced fund returned 6.80%.

Morningstar shows a persistent gap between the returns of investments and the returns investors achieve. This isn't about what is in your portfolio – it is about you.

Call investing whatever you want. Just don't pretend it is easy.

Mark LaMonica

Also in this week's edition...

Globalization continues to reverse in the face of geo-political strife. **Arcadian Asset Management** puts forward the case for cross boarder diversification to take advantage of this environment.

Inequality continues to dominate political commentary in Australian and overseas. **Roger Wilkins** and **Peter Siminski** take a look at the role housing plays.

Many investors have been burned by lithium. **David Tuckwell** argues that investors shouldn't dismiss the current rally.

Inflation is again in the news with the RBA rate hike this week. **Quay Global Investors** looks at why inflation is so entrenched in the Australian economy.

Around the world, democracy as a system of government is backsliding. **Kate Griffiths**, **Aruna Sathanapally** and **Matthew Bowes** outline how Australia can keep democracy alive.

Tony Dillon explores an area of the federal budget that is routinely ignored - off-budget accounting.

Ashley Owen's abridged monthly snapshot uncovers what is front of mind for investors around the world and his view on the likely outcome of the stand-off in the Middle East.

This week's white paper from VanEck looks at the limitations of the 'quality factor' in Australia's equity market when compared to global options.

Curated by Mark LaMonica and Leisa Bell

Putting portfolios together when the world is falling apart

Acadian Asset Management

For decades, the world economy became increasingly integrated across product, labor, and capital markets—in a word, globalization. One of the many consequences of globalization was higher cross-market correlations. For example, the correlation between U.S. and German equities rose from 0.35 in the period 1970-1997 to 0.81 in the period 1998-2026.

In recent years, globalization has stalled and we now face the prospect of deglobalization. Nations are erecting barriers to the free movement of goods, labor, and capital across borders. If globalization goes into reverse, we would expect equity markets to decorrelate.

Perhaps counterintuitively, as the world deglobalizes, risk-minimizing investors should respond by making their portfolios as global as possible. A world of less-correlated equity markets is a world in which the benefits of global diversification are higher.

Globalization raised correlations

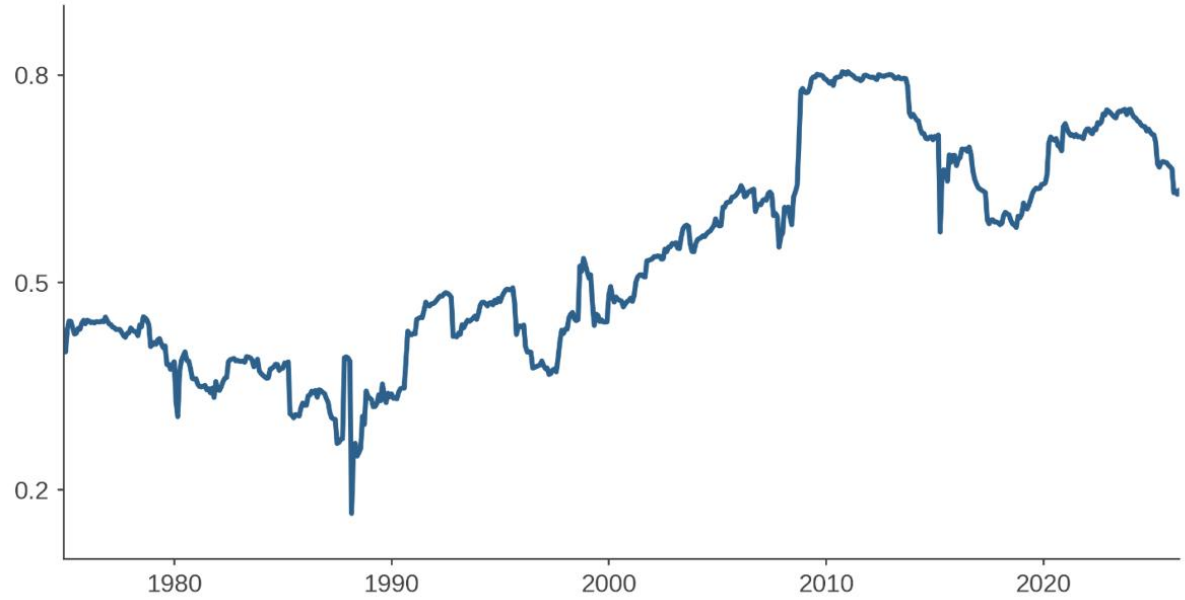
Globalization was a decades-long process involving falling trade barriers, increased migration, reduction in capital controls, financial liberalization, and regulatory harmonization. Milestones included the fall of the Berlin Wall (1989), NAFTA (1994), China's entry into the WTO (2001), and the expansion of the EU (2000s).

Figure 1 shows the resulting change in cross-country equity correlations from 1970 to 2026. It shows average pairwise correlations of the 23 developed market (DM) countries currently in the MSCI World Index, calculated from trailing 60-month windows of gross USD returns.[1] After globalization accelerated during the 1990s, average correlations rose substantially.

The pattern is representative of the broader sweep of history. Looking at global stock returns from 1850 to 2000, Goetzmann, Li, and Rouwenhorst (2005) find that "correlations vary considerably over time and are highest during periods of economic and financial integration such as the late 19th and 20th centuries."

Globalization seems to have stalled sometime after the Global Financial Crisis (GFC). Significant retrenchments included the Brexit vote (June 2016), Russia's full-scale invasion of Ukraine (February 2022), and tariffs announced by the Trump administration (April 2025). It remains unclear whether globalization has actually reversed in recent years ('deglobalization') or whether it has merely slowed ('slowbalization').[2]

Figure 1: Average DM cross-country correlation



Sources: Acadian Asset Management LLC and MSCI. Average pairwise correlations are calculated using a rolling five-year window of gross total USD returns across DM countries from January 1970 to March 2026. DM reflects countries in the MSCI World Index as of December 31, 2025. MSCI data copyright MSCI 2026. All Rights Reserved. Unpublished. PROPRIETARY TO MSCI. For illustrative purposes only. Past results are not indicative of future results.

Higher correlations, lower diversification benefit

Suppose that, going forward, we see unambiguous deglobalization and the world economy returns to the lower levels of integration observed from 1970 to 1997. What would this world look like?

First, we would expect lower corporate profit growth as the global economy is impacted. Second, we would expect lower cross-country correlations. While there is little that shareholders can do to insulate themselves from weaker fundamentals, they can benefit from decorrelating markets by diversifying as much as possible.

We define the diversification benefit as the reduction in portfolio volatility achieved by holding a diversified portfolio instead of a single country. Under simplifying assumptions, this benefit is a straightforward function of correlation.

Table 1: Benefits of diversification – Developed Market Equities

	1970 to 1997	1998 to 2026	
Correlations			
Average pairwise among all DM countries	0.39	0.65	a
U.S. and Germany	0.35	0.81	b
Volatilities			
MSCI World Index	14%	15%	c
U.S.	16%	15%	d
Germany	20%	23%	e
Average among all DM countries	22%	22%	f
Volatility diversification benefit	37%	28%	$g = \frac{f-c}{f}$
Maximum Drawdowns			
MSCI World Index	-40%	-54%	h
U.S.	-45%	-51%	i
Germany	-36%	-64%	j
Average among all DM countries	-51%	-62%	k
Drawdown diversification benefit	22%	14%	$l = \frac{k-h}{k}$

Sources: Acadian Asset Management LLC and MSCI. Diversification benefit is the percent reduction in risk going from the average to the world. Gross total USD returns across DM countries from January 1970 to March 2026. Sub-periods inclusive of starting and ending years. DM reflects 23 countries in the MSCI World Index as of December 31, 2025. MSCI data copyright MSCI 2026. All Rights Reserved. Unpublished. PROPRIETARY TO MSCI. It is not possible to invest in any index. Past results are not indicative of future results. For illustrative purposes only.

Average developed market correlation rose from 0.39 before 1998 to 0.65 after 1998 (Table 1, row a). This increase implies that the diversification benefit was about 1.9 times greater before 1998 than after 1998.

Table 1 fleshes out this change. Before 1998, the MSCI World portfolio had a return volatility of 14% (row c), 37% lower than the 22% average volatility of its constituent countries (rows f and g). After 1998, the benefit of diversification declined to 28%. While not the full 1.9x implied by the correlations, the earlier period still shows a meaningfully larger benefit (1.3x). [3]

Another way to measure diversification is through its impact on drawdowns, which we would expect to be roughly proportional to volatility. Table 1 shows that diversification reduced maximum drawdowns by 22% before 1998 and 14% after (row l). Again, the benefits of diversification were substantially larger in the earlier period (1.6x greater).

Table 1 also highlights results for the U.S. and Germany. Investors sometimes argue that global diversification is useless, and that it is sufficient to hold only U.S. equities. At first glance, the post-1998 data in Table 1 appears to support this claim, since during that period the U.S. had a smaller maximum drawdown (51%, row i) than the world portfolio (54%, row h) and similar volatility.

However, it would be a mistake to hold a portfolio that is 100% U.S. equities. It is not a law of nature that the U.S. always has lower risk than the world index. Before 1997, Table 1 shows the U.S. had drawdowns and volatility that were higher than the world index. Trailing performance can be a misleading guide to the future. For example, before 1998, the country with the mildest drawdown was Germany (-36%, row j). But after 1998, Germany had a drawdown that was worse than average DM country and worse than the world index.

Conclusion

Deglobalization, if it occurs, will produce winners and losers. Which countries will be the winners? We don't know. The appropriate response, therefore, is to diversify across countries.[4]

Will deglobalization lead to a collapse of dollar dominance and wild fluctuations in exchange rates? Again, we don't know. By holding a world portfolio, we diversify across currencies, helping to protect wealth from monetary disruption.

It has been said that diversification is the only free lunch in finance. While the free lunch of global diversification is always valuable, it becomes especially nutritious when markets fragment and correlations decline. If you want to minimize risk, then you should diversify more—not less—when markets decorrelate.

Endnotes

[1]Similar results are shown in "Polarizing Views: China's Impact on EM Investing," Acadian, December 2021.
[2]See Mohr and Trebesch (2025) for a literature review. Fernández-Villaverde, Mineyama, and Song (2024) argue that deglobalization has already begun while Altman and Bastian (2026) say that "deglobalization is a clear risk, but at least for now, the world's connectedness is holding steady at a historically high level."
[3]The substantial benefit of international diversification prior to 1998 was highlighted by Bergstrom (1975) and Michaud, Bergstrom, Frashure, and Wolahan (1996). In fact, the observation helped to motivate Bergstrom's founding of Acadian Asset Management in 1986.
[4]In addition to deglobalization, another source of uncertainty is AI. Which countries will be AI winners? Since we don't know the answer, the risk-minimizing choice is to hold all countries.

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Housing belongs in the inequality story

Roger Wilkins, Peter Siminski

Housing is crucial to economic wellbeing, yet it is still often ignored or treated incompletely in the analysis of income inequality. In our new research, we argue that this omission creates a distorted picture of the levels and trends of inequality in Australia.

Owner-occupied housing delivers two major economic benefits: imputed rent (the rental value that owner-occupiers receive by living in their own home) and capital gains that accrue as housing values rise. Neither is usually included in standard measures of household income, and neither is taxed in Australia. Our results show that this matters a great deal for how we understand inequality and redistribution.

While equivalised disposable household income remains a useful benchmark for inequality analysis, it is incomplete. By adopting a broad Haig-Simons concept of income—defined as consumption plus change in net wealth—it is clear that both imputed rent and accrued capital gains from owner-occupied housing belong in the income measure. This is not just a conceptual point. In an economy like Australia's, where housing has appreciated strongly over a long period and owner-occupied housing receives concessional treatment in both the tax and transfer systems, excluding these forms of housing income can substantially distort our picture of inequality.

The importance of a long-run perspective

A key contribution of our study is the focus on long-run income, rather than relying solely on annual snapshots. This matters because housing-related income is volatile from year to year, and annual measures are heavily influenced by life-cycle factors. Older Australians, for example, often have relatively low cash incomes but high housing incomes because they own their homes outright. Looking only at annual income can therefore make imputed rent appear equalising. However, when we take a longer-run perspective, that result reverses.

To examine income from owner-occupied housing, we constructed new measures of imputed rent and accrued capital gains using HILDA data from 2001 to 2023, combined with external data sources including the national accounts, the ABS Survey of Income and Housing, Reserve Bank mortgage rate data and CoreLogic hedonic housing price indices. We also improved on simpler methods used in earlier work. For example, we found that the median net return from imputed rent is around 2% in most years, far below the 5% assumption built into some commonly used measures. We also showed that annual capital gains are extremely volatile, so we developed a preferred smoothed measure that preserves differences across households while avoiding excessive year-to-year instability.

Striking findings on inequality

The substantive findings are striking. Including housing income shifts people within the income distribution by an average of 8 to 9 percentiles. Using standard disposable income, the mean income for outright homeowners is 34% higher than for renters, but 86% higher once housing income is included.

Over a 23-year horizon, adding imputed rent and capital gains raises the Gini coefficient by 0.02, or 7.9%. To give a sense of scale, that is roughly equivalent to shifting Australia from the 16th most unequal OECD country to the 10th most unequal. Housing income also tends to amplify the apparent increase in inequality over time, especially when looking at medium-run measures such as five-year income.

The inclusion of housing income also reshapes the demographic profile of poverty and affluence. Renters appear much more disadvantaged once housing income is counted. On annual disposable income, 15.6% of renters are in the bottom decile, compared with 7.5% of owner-occupiers. Once housing income is included, the gap widens dramatically: 24% of renters are in the bottom decile, compared with just 3.9% of owner-occupiers. At the top of the distribution, owner-occupiers are already more likely than renters to appear rich, but the disparity becomes much larger when housing income is factored in. The age profile also changes: housing income tends to lower measured poverty among older outright owners, while raising the relative poverty risk of younger households and children, who are much less likely to benefit from owner-occupied housing.

Implications for tax and transfer policy

Perhaps the most important implication concerns the tax and transfer system. Because imputed rent and accrued capital gains on owner-occupied housing remain untaxed, including them in the income base reveals a system that looks far less redistributive than standard measures suggest. On our long-run measure of income, the redistributive impact of income tax drops by about 40% when housing income is included. The redistributive effect of transfers falls by 18.9%, and the combined redistributive impact of taxes and transfers falls by 26.7%. In annual data, the same pattern appears: the measured

redistributive impact of income tax is, on average, 36% smaller once housing income is taken into account.

The concessional treatment of owner-occupied housing materially weakens the redistributive role of taxes and transfers. In effect, a large and growing source of economic advantage sits outside the state's main redistributive architecture. That should matter deeply for tax policy debates. We are not claiming that housing income should automatically be taxed in full, nor that measurement challenges disappear once a broader income concept is adopted. But if we want a more accurate account of inequality and redistribution in Australia, housing cannot remain offstage.

Conclusion

Housing is not just a backdrop to inequality: it is one of its central mechanisms. In countries like Australia, where owner-occupation is widespread but increasingly unequal, and where house prices have risen dramatically over time, omitting housing income provides an incomplete, and in some respects misleading picture of who is rich, who is poor, and how redistributive the fiscal system truly is.

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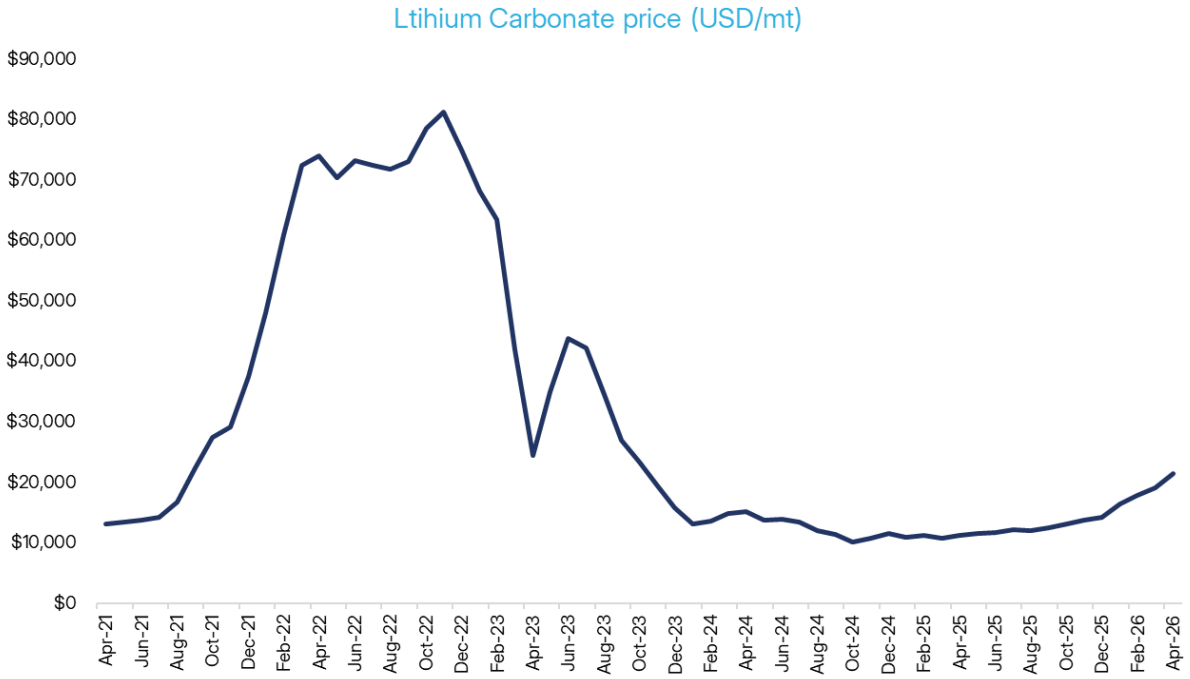
Lithium's rally is real this time – but no-one trusts it

David Tuckwell

Today's lithium rally has the look and feel of the tech stock rally in the early-2010s.

In those years, Amazon, Google and Netflix had proven business models and were household names. Their stocks were rising but no-one fully trusted it given the experience of the dotcom crash 10 years earlier.

Lithium today is rallying as major investment banks forecast sustained deficits. Demand for lithium is forecast by some industry figures to double between now 2030. Adding to potential demand are up-and-coming technologies like humanoid robotics and solid-state batteries, which are lithium intensive. Despite the strong demand picture, no new lithium projects have been launched since 2024, curtailments are everywhere and feasibility studies have greatly stagnated.



We believe that lithium remains out of favour due to the experience of 2022, when carbonate prices crashed 80%. Given this, it's worth unpacking why this time is genuinely different.

Lithium demand is forecast to double within three years

The guts of lithium demand come from electric cars, which are continuing their steady surge. Because Australians focus primarily on Australian and US car sales, they often miss the global picture.

Electric vehicles accounted for roughly one in four new cars sold worldwide in 2025. In China, they outsell combustion-engine cars. In Europe, sales grew 33% last year, faster than in China. And European vehicles tend to have larger batteries, requiring more lithium.

Industrial batteries for energy storage – increasingly linked to AI-driven power demand – have emerged as a major new demand category and are growing faster than EV batteries.

Data centres require enormous amounts of reliable power. That helped drive energy-storage battery demand up 51% in 2025, outpacing the 26% growth in EV batteries. JPMorgan projects energy storage will represent 30% of global lithium demand in 2026, rising to 36% by 2030. This category of demand barely existed during the 2022 bubble and is a major differentiator in today's rally.

Albemarle, the world's largest lithium producer, confirmed the scale of this shift in its February 2026 results. Global lithium demand reached 1.6 million tonnes of lithium carbonate equivalent in 2025, a 30% year-on-year increase. For 2026, Albemarle projects demand of between 1.8 and 2.2 million tonnes, and by 2030 it forecasts demand of 3.7 million tonnes annually – a doubling, in other words. SQM, the second-largest producer, has published broadly similar forecasts, with demand roughly doubling between 2025 and 2030 on its numbers as well.

Supply isn't ramping the way it did in 2022

Supply is not ramping up the way it did in 2022.

After the bubble burst, lithium prices remained below incentive levels for almost two years. Feasibility studies for new lithium projects fell from more than 30% annually to fewer than ten in 2025. No major new projects have commenced since 2024. Compounding the problem has been a wave of production curtailments, reflected in the table below.

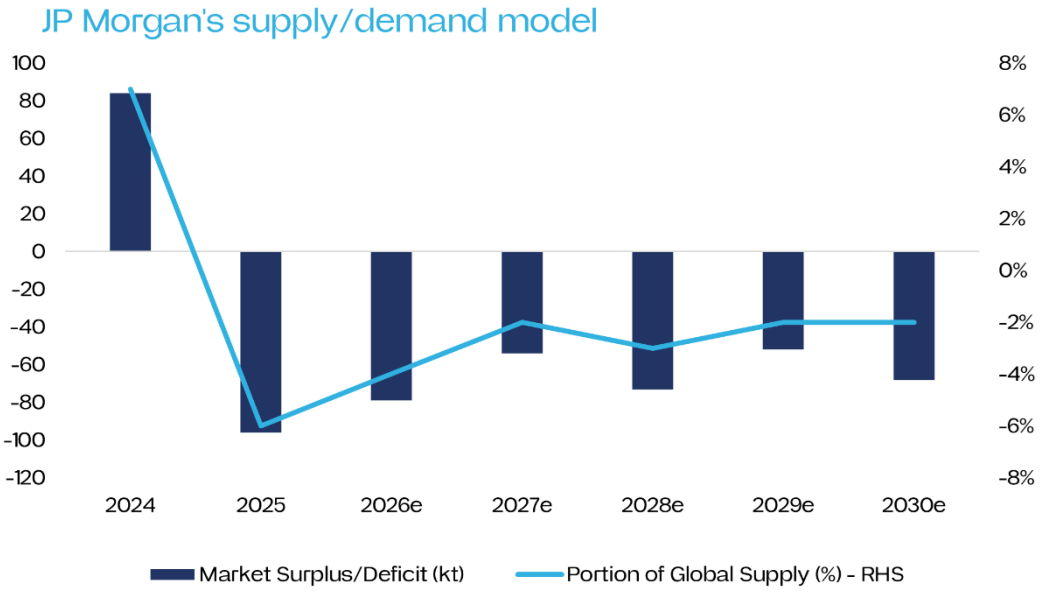
Curtailments table

Curtailment	Detail
Albemarle, Australia	The US producer idled its Kemerton lithium hydroxide processing facility in Western Australia in response to low prices.
CATL, China	CATL's Jianxiawo lepidolite mine in Jiangxi Province – representing roughly 3% of global supply – was suspended after its mining permit expired.
China regulatory reform	Beijing has delayed mining permits across Chinese lepidolite operations, estimated to effect up to 17% of projected 2026 global supply.
Zimbabwe	Zimbabwe requires foreign miners to invest in domestic processing infrastructure before resuming extraction, stalling supply.

Source: Financial Times, Bloomberg, Benchmark Minerals Intelligence. Data as of April 2026.

Miners that survived the downturn are in no hurry to flood the market. They have adopted a 'value over volume' philosophy similar to what has occurred in uranium recently with Kazatomprom. Even if prices rise above incentive levels, supply responses are likely to remain slow.

JP Morgan now forecasts a lithium market deficit persisting through 2030, even under conservative assumptions. Morgan Stanley projects a deficit of 80,000 tonnes of lithium carbonate equivalent in 2026 alone. UBS, while more conservative, still estimates a 22,000-tonne shortfall. Forecasts differ in magnitude, not direction. The broad consensus among major banks is that the era of chronic oversupply is over.



Source: JP Morgan. Data as of April 2026.

Lithium has optionality on future tech

Future tech like humanoid robotics, solid-state batteries, wearable computing and electrified aviation could also greatly benefit lithium. While these are widely understood by engineers and technologists to be 'on their way', most broker models still do not incorporate these demand sources.

Humanoid robotics may ultimately prove the most significant. Morgan Stanley has estimated that each humanoid robot could require around two kilograms of lithium. If its projection of more than one billion robots by 2050 proves even partially correct, incremental lithium demand by 2040 alone could push the market into a deficit approaching 80% of current supply. Morgan Stanley analysts have described lithium as an "Achilles' heel" of the humanoid robotics buildout.

Solid-state batteries are the second major wildcard. They are more lithium-intensive because they use lithium anodes instead of graphite ones. Commercial production is beginning to scale as technological breakthroughs accumulate. The consensus within the automotive industry increasingly appears to be that it is a question of when, not if, solid-state batteries become mainstream.

Lithium: how to invest?

For investors interested in lithium, the natural question becomes how to gain exposure. The most obvious approach is to buy ASX-listed lithium miners such as Pilbara, Liontown or IGO.

The challenge is that Australian lithium miners are narrow businesses and only mine spodumene (hard rock). This is a problem because spodumene is at risk of long-term disruption from cheaper and more environmentally friendly direct lithium extraction. This is where lithium is taken directly from brine without an evaporating pond. Aussie spodumene miners do not do refining either, unlike their Chinese counterparts Ganfeng and Tianqi. This too is a problem because refining can be higher margin.

A more balanced approach, in our view, is to diversify globally across lithium producers rather than trying to pick individual ASX lithium stocks. This allows investors to be more agnostic about the lithium extraction techniques, tap into higher margin refining, and avoid the risks that can come with betting on a single company.

Conclusion

Many investors burned by the dotcom crash in 2000 avoided technology stocks for years afterwards and missed one of the greatest equity rallies.

Something similar could be true for lithium. The energy transition is continuing. AI is accelerating global power infrastructure investment. Robotics is emerging as a genuine industrial category. And lithium continues connecting all these themes.

Whether the current opportunity persists will depend on how quickly supply responds and whether demand forecasts are realised.

ETF Shares provides the ETFS Global Lithium Miners ETF (ASX: VOLT) which began trading on the ASX in April 2026. For more information click here.

David Tuckwell is the Chief Investment Officer at ETF Shares, a sponsor of Firstlinks. He is also a journalist and researcher specialising in finance and international politics. The information provided in this article is general in nature. Before acting on any information in this article, you should consider the appropriateness of the of the information having regards to your objectives, financial situation or needs and consider seeking independent financial, legal, tax and other relevant advice. Past performance is no guarantee of future performance.

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Why is Aussie inflation so stubborn?

Quay Global Investors

In response to the re-emergence of inflation (core / trimmed mean) which has dogged Australian policy makers since COVID, this month the Reserve Bank of Australia (RBA) raised interest rates for the third time this year to 4.35%.

The increase in the official cash rate contrasts with almost every other developed country in the world (excluding Japan). Canada, UK, Europe, and the US (at the time of writing) have not reversed recent cuts while their inflation issues appear to be contained.

Why is Australia having such a difficult time reining in inflation?

Too much money chasing too few goods

The idea inflation reflected 'too much money chasing too few goods' was coined by Milton Friedman, the father of monetarism. It simplified inflation to the idea that money supply growth relative to real supply growth is inflationary. The idea is as seductive as it is simple. The complexity arises when one tries to define 'money', how it's issued, and who are the responsible issuers.

While we recognise the causes of inflation are many and complex, here we zero in on one of the issues that seems to be blamed the most. Money printing.

Refresher: Quantitative Easing is not money printing

After the global financial crisis (2008) most developed economies embarked on a new monetary policy instrument, Quantitative Easing (QE). In simple terms, QE allows the central bank (CB) to acquire high quality assets, usually government bonds, for cash. When first introduced in the US (2009) an open letter from prominent economists and historians to the Fed chair, Ben Bernanke, warned against such policy seeing it as leading to currency debasement and inflation[1].

But QE is one policy where there is no money printing. QE is a swap of one asset (bond) for another (cash). No new net financial assets are created with such a policy[2]. It is analogous to moving one's savings from a term deposit to an at call account.

It was therefore no real surprise that despite various forms of QE in the US, Japan, and Europe between 2001 and 2020, no developed country met their inflation target due to constant levels of disinflation.

How real money is created

The latest bogeyman blamed for inflation has been government spending. And here the critics have a point. Net government spending (deficits) literally prints money. When governments spend, treasury departments instruct banks to mark-up recipient private bank accounts (deposits). These new liabilities

for banks are paid for by the treasury transferring reserves to banks (an asset for the banks). Banks use these reserves to buy bonds. The net result? Banks own bonds, and the bank accounts of the private sector have swelled from government transfers reflecting new money ready to spend[3].

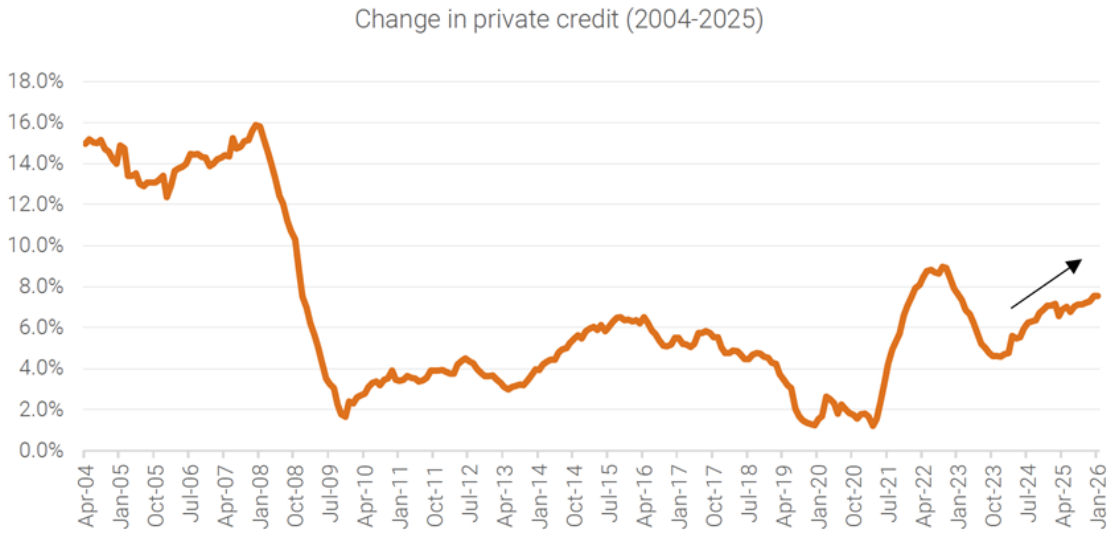
The second method of creating money is rarely discussed. Credit creation.

As discussed in part 2 of our Modern Monetary Theory series, private credit growth creates new money. New loans create new deposits and hence new money. For readers who are sceptical of this process, this Bank of England video provides an excellent summary.

Is the creation of new money via private credit growth causing our inflation ills? Let's dig in.

The data

The following chart highlights Australian credit growth since 2004. The recent re-acceleration of growth since 2023 can be clearly identified

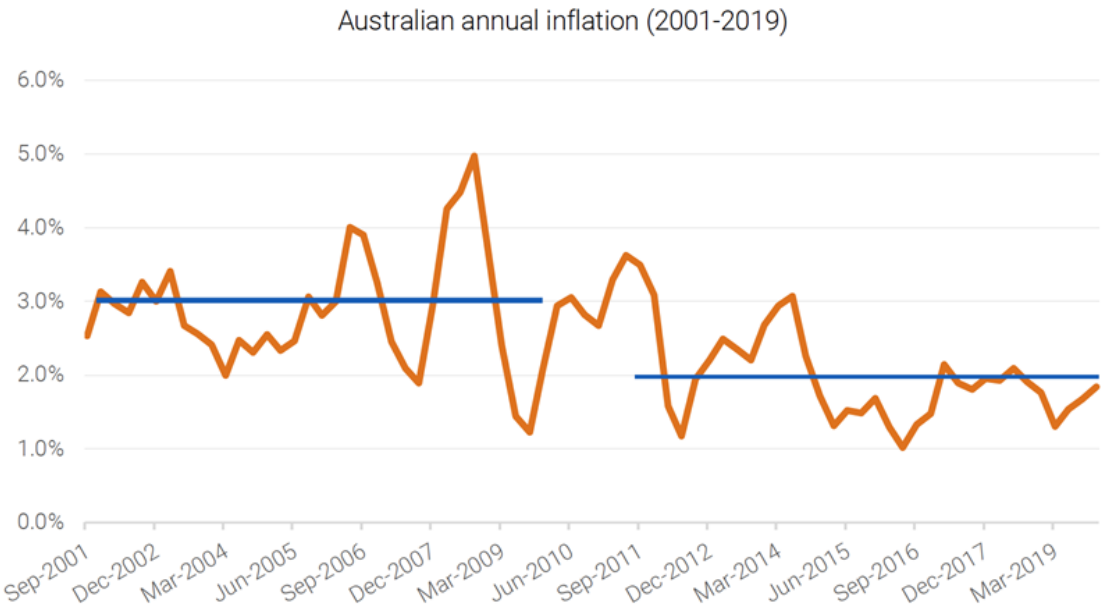


Source: RBA credit aggregates, Quay Global

A closer look at the above chart identifies a few other observations:

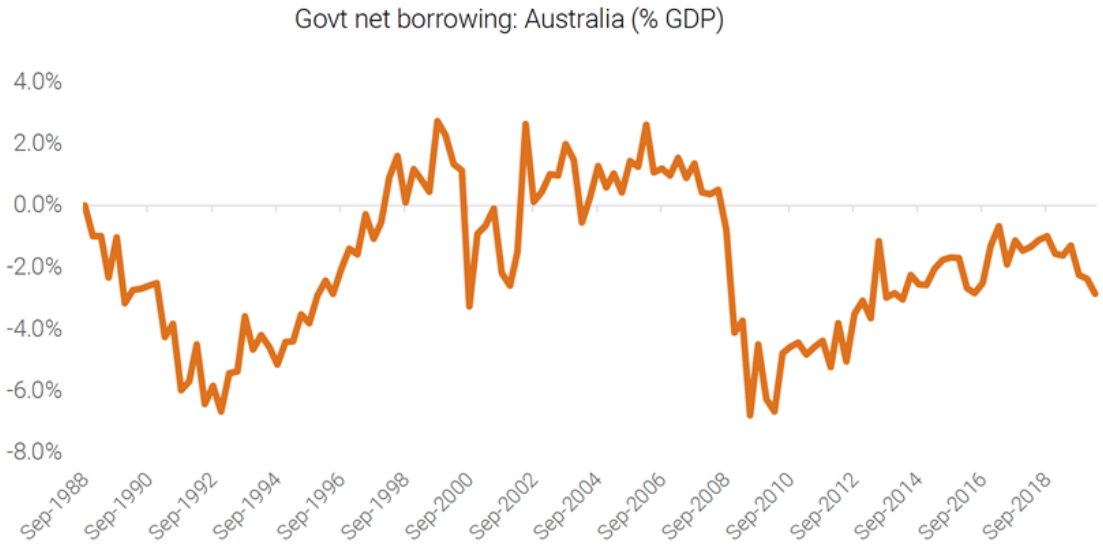
- Pre-financial crisis (2008), Australian credit growth was booming. This was despite the fact the RBA was aggressively increasing the cash rate from 4.75% (Oct 2003) to 7.25% (March 2008)[4].
- Post financial crisis, credit growth remained relatively subdued and in fact decelerated between 2016 to 2019 despite the RBA reducing the cash rate from 2.0% (April 2016) to 0.75% (October 2019).
- The strong rebound in credit in 2021-2022 (post COVID) coincided with post COVID inflation.

If private credit growth has a role to play in inflation, the above chart would suggest Australia had more of an inflation problem pre-GFC rather than post GFC. And that is exactly what the data supports, as per the following chart.



Source: ABS, Quay Global

And the relatively high inflation pre-GFC cannot be blamed on government spending. In fact, the opposite was true. Australia ran persistent surpluses in the early 2000's compared to persistent deficits post GFC.



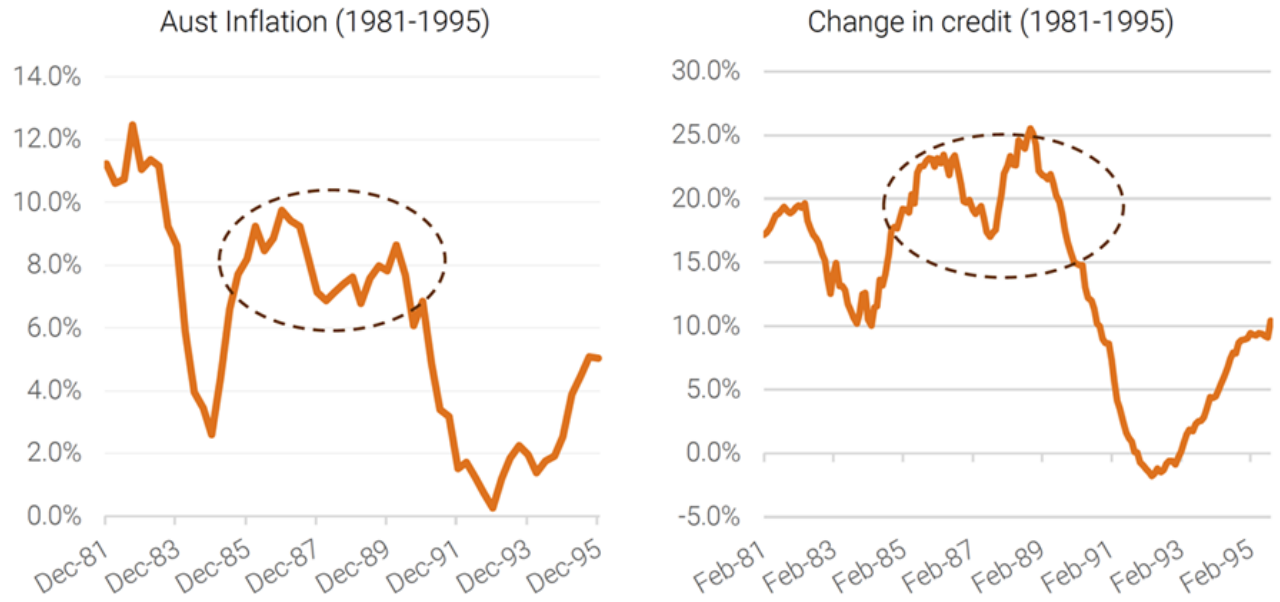
Source: ABS, Australian Treasury, Quay Global

We have been here before: The 1980s

The difference in Australian inflation pre and post GFC is difficult to explain by reference to government spending and interest rate policy alone. Relative credit growth appears to fill in the missing piece.

The same was true in the late 1980s, an era that saw high inflation along with:

- a balanced federal budget (1988-89),
- rising interest rates (peaked at 17.5-18.5% in Jan 1990), and
- very strong private credit growth (~20% per annum).



Source: RBA, ABS, Quay Global

Higher interest rates may not slow credit growth

Most central banks and market practitioners work on the assumption higher interest rates curb credit appetites and hence act as a brake on inflation. However, history often suggests otherwise. Strong credit growth in Australia is often associated with rising interest rates (1980s, early 2000s). And this is not just an Aussie characteristic:

- The US famously had a credit boom between 2002-2007 as the Fed increased cash rates from 1% in 2004 to 5.25% in 2006.
- The Japanese credit bubble emerged in the 1980s as the cash rate varied between 3 and 6%.
- Pre GFC, European credit growth averaged 9-10% while the cash rate increased from 2% in 2005 to 4.25% by July 2008.

This is where one could argue central bank models fail. Credit growth is more than just about price – it also reflects risk appetite. And risk appetite can be highly correlated with rising asset values (real estate / stocks) independent of the price of credit.

In addition, non-monetary policy changes can also have an impact. For example, recent housing policies have encouraged higher risk tolerance via the federal government's 5% home loan deposit scheme which came into effect in October 2025. Is it any wonder residential credit growth has since accelerated from 5.7% in July 2025 to 6.7% by January 2026[5]. There can be no better example of Australia's broken policy framework where the federal government is working to make home ownership easier, while the RBA is working to make it harder.

Conversely, macroprudential tools, such as limiting credit growth via regulation can be disinflationary even in a low-interest rate environment.

Concluding thoughts

Australian inflation has been sticky post COVID, which has encouraged the RBA to increase interest rates for the second time this year.

However, one source of inflation (private credit growth) is re-accelerating. And history shows that monetary policy alone cannot quell private sector demand for credit.

Worryingly for the RBA, the current environment of rising inflation, rising interest rates and accelerating credit growth has historically ended in a meaningful economic correction; the same conditions that were prevalent in Japan (1989), Australia (1990), and the US (2008) all ended in vicious recessions.

Forced by its narrow policy toolkit, the RBA may need to keep raising interest rates until the private sector 'cracks' or until some other exogenous event derails Australia's economic fortunes causing the private sector to meaningfully reassess its appetite for risk.

[1] https://www.hoover.org/research/open-letter-ben-bernanke
[2] For more on the mechanics of QE, please refer to our 2019 paper QE is coming but will probably do nothing
[3] For more on the mechanical process of government spending refer to our paper MMT and why you're going to hear a lot more about it
[4] Source: RBA https://www.rba.gov.au/statistics/cash-rate/
[5] Source: RBA Credit aggregates

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How to stop Australian democracy going the way of the US

Kate Griffiths, Aruna Sathanapally, Matthew Bowes

Around the world, democracy as a system of government is backsliding. After more than 50 years of liberal democracy in ascendancy, democratic progress plateaued around the turn of the century and is now going backwards.

In 2025, there were only 31 liberal democracies out of 179 countries assessed. And the United States – once the poster child for democracy – was downgraded from "liberal democracy" to "electoral democracy" because of declining checks and balances on power, freedom of expression and civil rights and equality before the law.

Australia is one of the few remaining liberal democracies, and a leading one at that. But we are not immune to anti-democratic forces or the fraying international rules-based order.

A new Grattan Institute report, For the people: Future-proofing Australia's democracy, identifies the main vulnerabilities for Australia's democracy and opportunities to build a better, more resilient democratic system.

A bright light in a dark landscape

Australia comes from a place of strength. We are one of the world's leading democracies, consistently ranking highly on international measures of democratic health, as well as on a suite of economic and social measures – including life expectancy, human development, employment, and GDP (gross domestic product) per capita.

This is no coincidence. Our democracy underpins our prosperity and safeguards our rights and freedoms. International evidence shows democracy supports peace and economic growth, while delivering longer lives and more education.

Social trust matters too. Countries with higher interpersonal trust – like Australia – tend to have higher economic growth and lower income inequality, which in turn support democratic resilience.

But the world order in which Australia has flourished is now being seriously tested. These are more turbulent times not just for our economy or standard of living, but for liberal democracies themselves.

Fuel for discontent is building

Our report takes stock of Australia's greatest asset: the health of our democracy.

The good news is that Australians' support for democracy has been consistently strong – even growing over time. Only a small share of the population is discontent or disengaged with the system, and the data do not suggest either have been spreading.

The bad news is that our social compact is under pressure. This is showing up in growing economic pessimism, worry for future generations, concern about unfairness, declining sense of belonging, and low trust in political actors.

While support for democracy remains high in Australia, satisfaction with how our democracy actually works is more fragile.

Satisfaction with democracy is typically lower among groups who are less well served by the status quo. Most obviously, our institutions have persistently failed First Nations Australians, and don't fully support new migrants.

Lower-income Australians and those with financial concerns tend to report lower trust and satisfaction with democracy.

Renters are less satisfied than homeowners, and people in regional areas tend to be less satisfied than people in cities.

Migrants are an interesting exception here. Migrants (except for those from the United Kingdom) are typically more satisfied than people born in Australia with the way democracy works here, despite the disadvantages they often face living here. This may, at least in part, be due to direct experience with other systems.

Everyone needs confidence that the system can work for them, even if it doesn't always. Groups who persistently lack security, opportunity, or solidarity under the current system cannot reasonably be expected to trust or defend it.

3 big risks

Where there is fuel for discontent, there is increasing risk that global challenges could spark a blaze. Three inter-related global risks are particularly testing for democracies.

First, the decline in traditional news media and the rise of online and social news sources are fragmenting our fact base, and making misinformation and extreme views more salient in people's daily lives.

Second, global political tensions and the rise of anti-democratic forces overseas are testing Australia's social cohesion at home.

And third, the heightened probability of economic, social, and environmental shocks increases the challenges democratic governments face to deliver better outcomes for their people.

These are risks – not eventualities. The resilience of our democracy is in its capacity to recognise challenges and collectively respond.

And 5 ways forward

Our research and consultation identified five priorities for Australia to build a better and more resilient democracy:

1. Make the most of our parliament

Our elected federal parliament sits at the centre of Australia's democracy. An independent review should consider how to make it more representative and better functioning – to rebuild trust in politics, improve administration of government and enable better long-term decision-making.

2. Nurture belonging and engagement

We need more ways to have a say and be heard and clearer pathways to citizenship. Our public sector leaders should also be actively stitching public engagement into the fabric of our existing institutions.

3. Protect our public sphere

A healthier public sphere requires ensuring the sustainability of our news media and investing in institutions that produce trusted information. We should also experiment with responses to misinformation, to work out which approaches are effective at scale.

4. Tackle the known policy challenges

In a democracy, process matters, but so do outcomes. Australians need confidence that our system of government can work for them and build something better than the status quo.

5. Prepare for the future

Crises are the moments that build trust, or lose it, and the future will almost certainly be more volatile. Governments can prepare by reducing our vulnerability to known risks, building fiscal buffers and calibrating expectations about what governments can reasonably do to cushion the blow.

Governments can and should lead on this. But we mustn't forget that in a democracy, we govern ourselves. This is a task for all of us.

The Conversation. Kate Griffiths, Democracy Deputy Program Director, Grattan Institute; Aruna Sathanapally, Chief Executive, Grattan Institute, and Matthew Bowes, Senior Associate, Economic Prosperity and Democracy, Grattan Institute

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Off-budget, but not off-the hook

Tony Dillon

As anticipation grows for the upcoming federal budget, financial commentators will fixate on two words: debt and deficit. These will be the measures by which the government's fiscal performance will be judged. But there is a growing disconnect between debt and spending, with the culprit being 'off-budget' accounting.

Where typical government expenditure flows through to the 'underlying' cash balance, cash flow into financial assets for policy purposes that are deemed off-budget 'investments', does not. Such expenditure does however add to gross debt, and is recorded in the 'headline' cash balance.

The problem is, and in muddled terminology, the headline figure around budget time is the 'underlying' cash balance, while the 'headline' cash balance is paid scant regard by the media.

But with the December 2025 Mid-Year Economic Fiscal Outlook (MYEFO) revealing 'underlying' cash balance deficits totalling $143 billion in the four years to 2028-29, the equivalent 'headline' deficits total $237 billion. That represents anticipated off-budget spending of $94 billion, which is by no means trivial and warrants clear understanding.

Included in the $94 billion going to 'financial assets':

- Additional equity injections (including in the NBN, Snowy Hydro, Clean Energy Finance Corporation)
- Loans (including to Snowy Hydro, write down of HECS loans)

And since the Albanese government came to office, fund capitalisations to the tune of some $50 billon have arrived off-budget, including Rewiring the Nation Corporation ($20 billion), the National Reconstruction Fund ($15 billion), and the $10 billion Housing Australia Future Fund.

As we shall see, these items alter the scale of the government's balance sheet, shifting attention away from direct spending. But they represent real cash outflows.

To understand how off-budget accounting works, consider the Housing Australia Future Fund (HAFF).

It was set up like a mini sovereign wealth fund, with an initial $10 billion capital injection that was raised by the government issuing bonds, adding to gross debt. Under the Future Fund Board, the $10 billion is invested in financial markets, with up to $500 million per year of investment earnings earmarked for social housing projects and affordable housing programs.

Housing Australia Future Fund - Financial performance since inception to 31 December 2025

	$millions[1]
Total Credits	10,000
(Plus) Net Earnings[2]	1,932
***(Equals)* Total Credits and Earnings**	**11,932**
(Less) Debits (drawings)[3]	500
***(Equals)* Balance**	**11,432**

Notes:

1. Data may not sum due to rounding.
2. Earnings are net of investment and administration fees incurred by the Board.
3. This amount represents debits made for policy purposes under the relevant Act.

Source: Australian Government Department of Finance

How this is all accounted for is key.

The $10 billion outlay was deemed an investment, not expenditure, and therefore was not counted in the 'underlying' cash deficit. It does, however, sit in the less scrutinised 'headline' cash deficit. The government's balance sheet expanded, with the $10 billion fund a financial asset, and gross debt increasing by the same amount.

Once in place, distributions from the fund are taken up as revenue in the 'underlying' cash balance, offset by corresponding housing spending. With little net impact on the cash balance. And the government pays interest on the borrowings used to establish the fund, also recorded in the 'underlying' cash balance.

So what has happened here?

As well as altering the fiscal presentation, policy programs moving off-budget introduce investment risk. While the HAFF $10 billion doesn't register in the 'underlying' cash balance, it is a leveraged position borrowing at a fixed cost with fiscal outcomes determined by market returns. The sustainability of this approach is dependent on a positive spread between return on investment and cost of debt. The process represents a shift from income statement to balance sheet, with the most closely watched budget metric not capturing this economic reality.

The HAFF was established in November 2023, and as of December 2025, its balance was $11,432 million. Breaking this down: $10,000 million capital injection + $1,932 million investment earnings - $500 million disbursement = $11,432 million. This represents investment performance well above the benchmark rate of return of CPI + 2-3%.

But there was also interest paid on the start-up capital, which since inception would be of the order of $900 million. A budget cost. This highlights the mismatch of the capital being excluded from the underlying balance, while the cost of funding it is not.

Compare the off-budget HAFF approach to a more conventional arrangement. The government would not set up an investment fund with borrowed money. Rather, it would simply fund the housing program directly each year by up to $500 million, recorded as expenditure in the budget. The costs would be visible with no differences recorded between the 'underlying' and 'headline' cash measures.

This is where things become blurred. Is the HAFF a policy program or an investment? If the fund was created to deliver a policy outcome first, and to earn a commercial rate of return second, then it is basically spending with risk attached. It amounts to spending via markets as opposed to spending via a budget.

And the larger the difference between the 'underlying' and 'headline' cash measures, the bigger the fiscal spending off-budget and the size of program invisibility, compounded if follow-up equity injections occur like with the NBN and Snowy Hydro. Focus ends up not so much on the scale of the initial decision, but more on the smaller cashflows it generates. The conversation shifts from one of $billions up front to $millions per year, because of the lesser scrutiny around cash deployed for 'investment'. In the end though, taxpayers carry not only the program cost, but the investment risk as well.

So why transform a straightforward spending program into a leveraged investment position?

The establishment of a fund is less about having a punt, and more about bringing forward a commitment to spending. And even though there could be commitment without a fund structure, the government is basically capitalising an annual budget in the balance sheet. In that sense, it removes the annual argy-bargy for funding when the intention is locked in for future years.

Governments like this approach because it creates future funding that would be harder for future governments to unwind or to make program cuts. It is a signal that the program is not temporary. The trade-off is the loss of annual scrutiny and flexibility.

Overall, off-budget accounting doesn't reduce the cost of policy. Rather, it changes its visibility, risk, and the timing of financing. And the extent to which it is now deployed warrants greater scrutiny and challenge. Particularly around budget time.

Tony Dillon is a freelance writer and former actuary. This article is general information and does not consider the circumstances of any investor.

Shares rebound on hopes of war ending, but stalemate the likely outcome

Ashley Owen

The following is an abridged version of Ashley Owen's monthly snapshot. You can read the full version here.

Here's my quick wrap-up on global markets for serious long-term Aussie investors – including shares markets, interest rates, inflation, bonds, currencies, commodities, and more, including portfolio implications.

Key points:

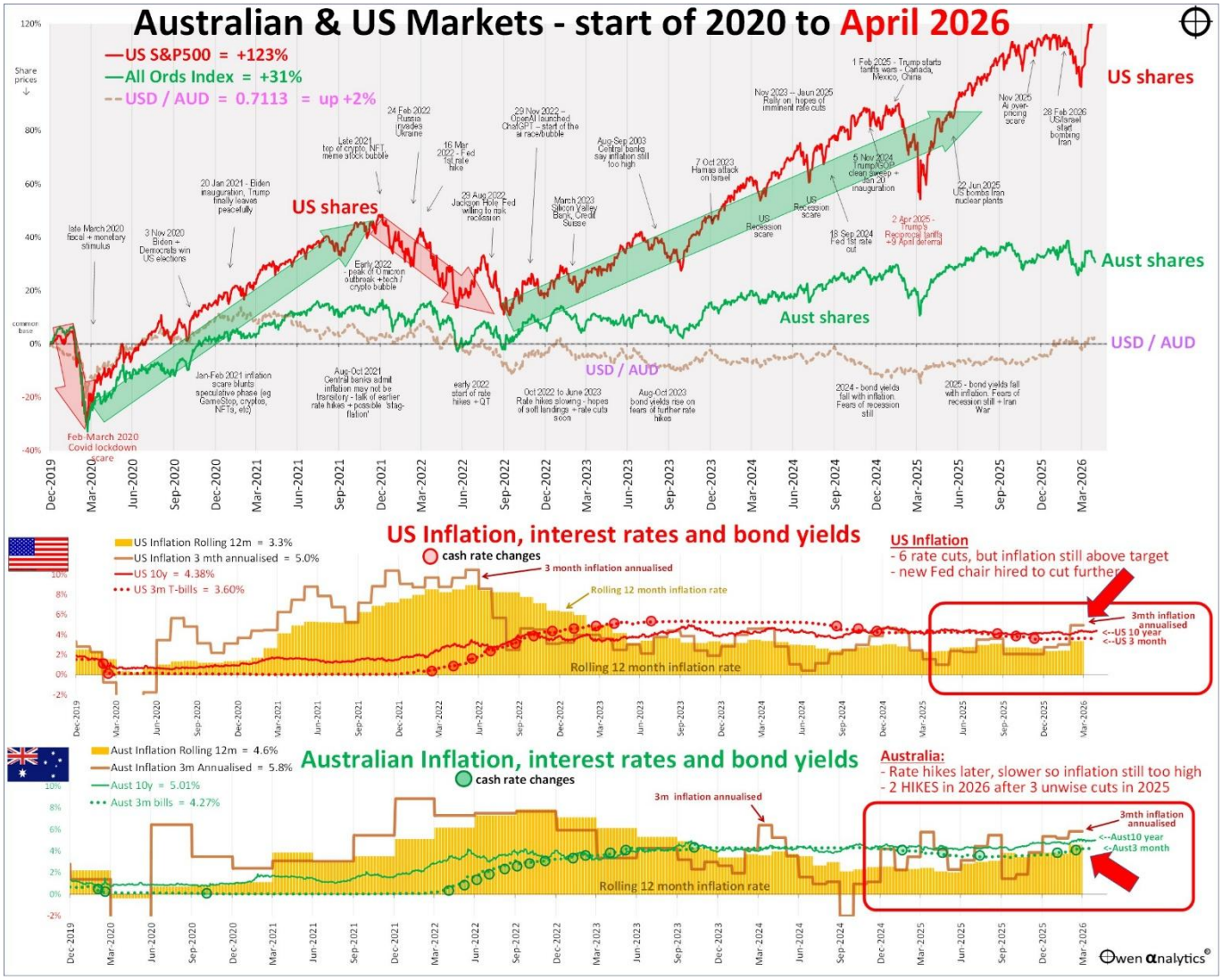
- Share markets around the world rebounded in April after a very brief war / inflation scare in March, but the ASX remains a global laggard.
- Investors have two positives to support their bullishness. The first is hope that Trump retreats (dressed up as an epic 'win' of course) because his most urgent goal is to get fuel prices down in order to retain MAGA voters in the November mid-term elections.
- The second positive is strong US profits, thanks to tech / ai, and the bonanza for fossil fuel producers like the US.
- The war continues, but is increasingly looking like a stalemate, probably with higher energy prices and inflation for a while yet. Rate cuts or rate hikes?
- Share markets everywhere (not just US tech) are still vastly over-priced on numerous measures – including and especially in Australia. A major global correction is due.
- Bond markets posted more losses again as yields kept rising in expectation of higher inflation and interest rates ahead.
- The AUD rose and US dollar fell with the share rebound, as per the usual pattern in global panics / rebounds.
- Commodities prices mostly rebounded in April, benefiting ASX resource stocks.

But first - my essential 1-page snapshot chart [next page] - covering Australian and US share markets, short and long-term interest rates, inflation, and the AUD/USD exchange rate. It is my go-to chart that tells me what happened when and why, whenever answering queries from advisers, investors, doing webinars, market updates, etc.

Not only does this have all the detail I need to answer investor questions from advisers, but even from the back of the room you can easily see the big picture on where we are for share markets, currency, inflation, long & short interest rates.

I will get into shares in a moment, but from the back of the room you can see that share markets had a minor hiccup in March (top right corner of the chart – red for US, green for ASX), but are back on track in April.

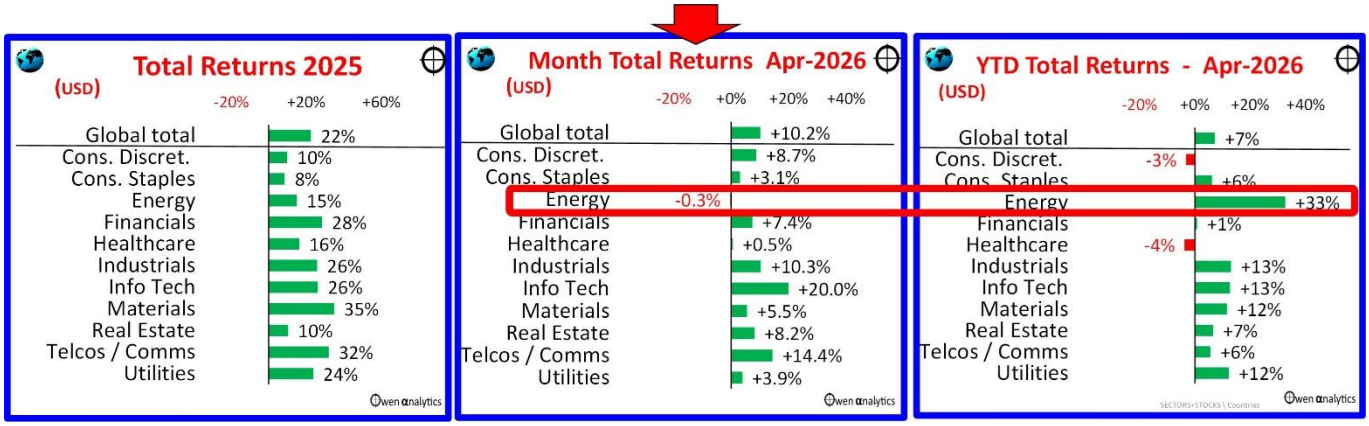
Bottom line – if you were rattled by the volatility and price falls in March then you ain't seen nothin' yet! (or you are too young to remember what a decent sell-off looks and feels like!)



Share markets

Global share markets rebounded in April after the brief sell-off in March when panicking investors sold down just about everything except for oil/gas stocks profiting from higher prices with the Strait of Hormuz closed.

The next charts show total returns from global industry sectors for April 2026 (middle chart), calendar year to date (right), compared to 2025 (left chart):



The stand-out sector up is fossil fuels ('energy') – with across-the-board double-digit rises in the major stocks as they profit most from the global supply squeeze.

Major country share markets

Share markets almost everywhere had a great month in April. Here are the main markets:

Best of the major markets has been Japan, led by Softbank (big Facebook holding plus other US tech bets), Keyence (robotics), and Shin-Etsu Chemical (plus assisted by weaker yen). Next best was the US (tech/ai giants).

So far in 2026 global share markets are ahead by 6% (in local currency terms). This may make it a fourth good year in a row in the current boom, following three very strong years averaging +20% per year in 2023, 2024 and 2025.

Share markets everywhere (not just US tech/ai stocks) are still vastly over-priced on a variety of measures – including and especially in Australia, and we are well and truly due for a global correction. Refer to the above reports on share market pricing.

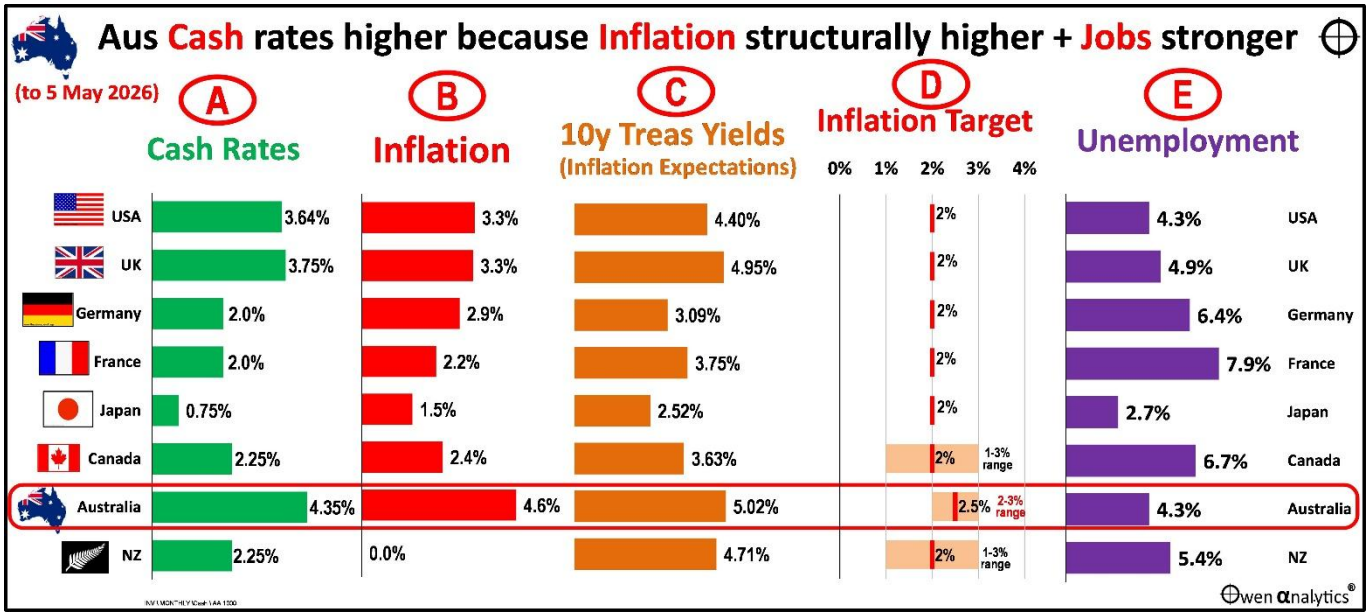
Inflation & interest rates

A stalemate in the US/Iran looking like a reasonably likely outcome would mean above-target inflation lasting longer (after short-term rises).

Despite inflation remaining sticky around the world, central banks have mainly held cash rates flat this year – taking a middle road between further rate HIKES to reduce spending and inflation, versus rate CUTS to stimulate slowing economies due to higher prices. In the US, Jerome Powell had his final meeting as Chair of the US Fed rate-setting board, which voted to keep rates flat.

Australia is the exception of course. The RBA has been the only central bank in the world to switch from rate cuts after the 2021-23 inflation surge, back to rate HIKES – with three hikes so far this year (February, March and May).

Even before the latest war on Iran, Australia already had the HIGHEST cash rate amongst its peers – because we have the highest inflation, the highest inflation expectations (treasury yields), the loosest/highest inflation target, and the lowest unemployment rate among our peers.



It now remains to be seen how expansionary / inflationary the upcoming May Federal Budget actually is. (The budget will range somewhere between 'highly expansionary / inflationary' and 'ridiculously expansionary / inflationary'). Apologies once again to my kids and future grandkids who will be paying for this chronic fiscal diarrhoea through higher interest rates and taxes for the rest of their lives.

Either way, more rate hikes are on the way if inflation is to be returned to target range.

Trump's agenda?

The following is what I said in my end of March report:

The most important factor for the direction of short-term investment markets prices will be Trump's twists and turns on the war front (or tariff front, or any of his other hobby horses du jour). Not even Trump knows what he will say or do one minute to the next, so it is pointless trying to guess.

However, I have two fairly sound reasons for being relatively positive for share markets in the coming months.

First - Trump probably has one central aim in the short term: to retain MAGA votes in the November mid-term elections. To do that he must (1) get oil prices down, and (2) minimise the number of Americans coming back in body bags.

This points to a relatively quick end to the war. Or at least an end to disruptions in oil/gas supplies, which means opening the Strait of Hormuz to restore normal shipping.

Second – in the event of a sharp economic recession, governments of all flavours in the US, Australia and just about everywhere else no longer have any notion of fiscal discipline. They have shown in the GFC and Covid that they will literally throw 'free' money at anything and everything in order to retain populist votes. Politicians no longer have the stomach nor the intellectual framework for 'tough medicine', 'business cases', trade-offs, or discipline.

The longer-term consequences and downsides will be even higher debts and widening intergenerational inequity, but it supports asset prices in the short-medium term. The current global tech/everything boom is being held up by hopes of endless monetary and fiscal profligacy.

This theory remains my Base Case scenario. Trump is desperate to get out but it must be with him 'winning'. The problem is finding something to call a 'win'. He is now reduced to a rather tiresome tirade of threats, then backdowns, then mysterious alleged 'negotiations' with nameless parties on behalf of Iran about a so-called 'deal', then more threats, and more back-downs.

The most likely outcome is probably yet another humiliating US withdrawal dressed up as a 'win', but leaving a festering mess behind.

Ashley Owen, CFA is Founder and Principal of OwenAnalytics. Ashley is a well-known Australian market commentator with over 40 years' experience. This article is for general information purposes only and does not consider the circumstances of any individual. You can subscribe to OwenAnalytics Newsletter here.

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