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Editorial

I've been reflecting on the debate within the comments section around the tax policy announced by the government. Firstlinks is not a political publication and instead seeks to inform investors about topics related to markets and building wealth.

This is where politics and markets intersect. Various government policies impact markets and strategies to build wealth. The tax proposals are an obvious example. Firstlinks will continue to cover those topics.

However, I'm going to be stricter about what I let through in the comments section. There are legitimate concerns about the tax proposals. I personally share those concerns and I have several misgivings about the impact on the country.

Significant changes to the tax code should be debated. But – at least on this publication – the debate needs to be productive. Name calling may be edifying but it doesn't help to inform readers so I won't publish those comments going forward. I hope this helps to keep the comments section focused on the relative merits of various proposals.

Firstlinks will also continue to publish content on both sides of a debate. Public discourse isn't helped by Australians retreating into echo chambers.

If your comment doesn't get published feel free to email me at mark.lamonica1@morningstar.com with any questions. Please feel free to leave comments on Firstlinks' editorial policy.

Should investors be a little more worried?

Recently I've been speaking to members of the Morningstar Investment Management team. I haven't come away from these conversations overly confident.

Markets are forward-looking and represent investors' collective view of the future. Those expectations are priced into markets. Understanding what investors are anticipating there is no context for valuation levels.

A seemingly reasonable valuation can look optimistic in retrospect if the bottom falls out of the economy. High valuations are deceiving if there is enough growth.

Investors are exceedingly positive. And maybe the market is right to be optimistic, and everything will turn out ok.

The Strait of Hormuz may open and energy prices may drop leading to lower inflation. AI might be all it is cracked up to be with infrastructure investments paying off. We might be at the precipice of an AI enabled surge in productivity.

Is everyone optimistic?

A closer look at what is happening shows not every investor is quite so optimistic.

Bond yields are surging and at their highest level since 1997. This may indicate bond investors are not as confident inflation will be transitory. The equity risk premium narrows when yields are high as bond become more attractive.

It is also worth looking under the hood of the share market's narrow rally. The S&P 500 increased in value by $9.19 trillion in market cap from March 30 to the record close on May 11. The 10 largest companies by market cap accounted for 62% of that gain and the semiconductor sector made up 43.80%.

Perhaps the AI boom will continue and momentum will win out. Perhaps the shares being left behind represent the best opportunity.

In the midst of the boom leading up the global financial crisis Citigroup CEO Chuck Price infamously said "when the music is playing you gotta get up and dance." Investors are dancing – the question is, will the music will keep playing.

Final thoughts

The rosy scenario priced into the market may not eventuate. And that is what investors should ponder. This is not a universal call to action or a warning. All long-term investors deal with volatility and predictions about the future are rarely worth the paper they are written on.

Instead, it is a call to assess your own situation and how different market scenarios will impact your life. It is the investor that matters and not the investments.

Mark LaMonica.

In this week's edition **Nick Maggiulli** argues the more wealth you have the less risk you should take. Something to consider as this bull run continues.

Simonelle Mody extols the benefits of simplicity. She makes a compelling case.

John Abernathy warns against complacency given US fiscal pressure, China's shifting growth model and Australia's structural constraints. In his view the global investment landscape is becoming less forgiving - yet markets have yet to fully adjust.

A sustained disruption through the Strait of Hormuz is forcing a rapid drawdown of global inventories. **Paul Gooden** writes that without a resolution, the arithmetic points to a supply shock by early August and a sharp surge in the oil price.

In the face of inflation and potential interest rate increases infrastructure remains a safe haven. According to **Magellan** looks at different infrastructure plays and how they might be impacted by the current environment.

Several programs and policies are in place to help first time homebuyers. Little attention is paid to the needs of renters. **Jason Teh** looks at the historical drivers of rent levels and what policies could ease the recent rent increases.

As super balances grow, SMSFs are becoming central to retirement outcomes. **Michael Hamilton** says without proper planning for "Armageddon" scenarios, even well-structured funds can unravel when it matters most.

Curated by Mark LaMonica and Leisa Bell

Markets without a margin for error

John Abernethy

The world economy is not yet sliding into recession, but the outlook has become more difficult. Growth through 2026 will be challenged by the Iran war, the associated oil shock, rising inflation, and weakening confidence in the USD and US bond market. A rebound in 2027 remains plausible, but only if the energy shock resolves in the coming months.

This matters because asset markets are still priced as though the post-GFC world of suppressed real yields remains intact. The 'risk-free' rate has been redefined by investors over the past decade, and that redefinition has supported a major expansion in equity valuations. The key question is whether that reset is sustainable.

After the GFC, and again through COVID, central banks drove bond yields toward zero. In Europe and Japan, negative real yields became normal. In the US and Australia, the use of QE (quantitative easing) compressed yields and encouraged investors to move further out the risk curve. That supported higher PERs (price-to-earnings ratios) and lower earnings yields.

Although real bond yields had begun to normalise before the current oil shock, equity valuations did not adjust in the way history might have suggested. US PERs have remained elevated even as bond yields rose. More recently, as the Iran war pushed energy prices higher, bond markets barely moved. Real yields declined, and the US equity market recovered to record highs.

This is the defining issue for investors. If the US 10-year Treasury yield is higher than the earnings yield on the S&P 500, investors are accepting a lower implied return from equities than from government bonds. That can persist for a time, particularly where earnings growth is strong, but it is not a comfortable long-term foundation.

The US market's valuation has been supported by the extraordinary profitability of the major technology companies. The so-called Magnificent Seven now account for around one-third of the S&P 500's market capitalisation. Their operating margins, ROEs (returns on equity) and investment capacity are unlike anything available in Australia. The four major hyperscalers alone are expected to spend hundreds of billions of dollars on capex in 2026, much of it directed toward AI infrastructure.

This is not simply a market concentration issue. It is an economic power issue. Only the Chinese state can plausibly match that scale of investment. That is why trade policy, IP protection and technology restrictions will remain central to the global outlook.

Australia sits in a more difficult position. The average ROE across the Australian share market is materially below the US. Outside a small number of high-quality companies, many Australian large caps generate returns that are only modestly above, or in some cases below, a reasonable cost of equity. The causes are structural: weak productivity, high energy costs, elevated labour costs, regulation, tax complexity, and an index dominated by banks and miners. Banks sell largely undifferentiated products, and miners are price-takers in global commodity markets. Neither sector has the same earnings power as the dominant US technology platforms.

The 2025 calendar year highlighted how unstable asset-class leadership can become in this environment. Precious metals performed strongly, the USD weakened, and Australian equities lagged most major markets. The weakness in the USD should not be dismissed as a short-term move. It reflects growing concern about US fiscal sustainability and the long-term role of the dollar in global settlement.

The US remains the world's financial anchor, but its fiscal position is deteriorating. Net interest on federal debt is now a major expenditure item, and the deficit remains large despite reasonably strong nominal GDP. Public debt is moving toward levels last seen after WWII. This has been manageable because global trade and reserves still rely heavily on the USD. Any credible challenge to that position — whether through BRICS trade settlement, digital currencies or reduced foreign Treasury demand — would have major consequences for bond markets and global liquidity.

The tariff war adds another complication. The US objective is to pressure China, but China has shown considerable resilience. Exports to the US have fallen, yet China has redirected trade toward ASEAN (Association of Southeast Asian Nations), Africa, Latin America and Europe. Its trade surplus remains substantial. Tariffs may therefore do less to weaken China than to accelerate the development of a more independent trading bloc outside US influence.

For Australia, China's economic evolution is critical. The old model of steel-intensive growth has matured. Recycled steel is rising, and demand for iron ore is likely to be capped over time. Australia's resource base must therefore pivot toward the next phase of Asian industrialisation: India, Indonesia, copper, lithium, rare earths and energy security. Relying indefinitely on iron ore royalties and company tax is not a strategy.

Domestically, Australia faces a stagflationary risk. Growth is below trend, productivity is weak, real wages remain pressured, housing affordability is unresolved, and energy policy remains incoherent. Inflation, which had appeared to stabilise near 3%, is vulnerable to a renewed push above 4% as fuel, freight and food costs rise. Unlike the US, where debt risk sits primarily with the government, Australia's debt burden sits with households. That makes further rate increases more painful.

The implication for investors is straightforward. Equity indices are priced for a favourable outcome, while the macro environment has become less forgiving. Sustaining current valuations will require strong earnings growth, stable bond markets, contained inflation and ongoing liquidity support. That is a demanding combination.

Investors should focus less on chasing index momentum and more on quality, cashflow and sustainable yield. In equities, that means businesses with pricing power, sensible balance sheets and credible returns on capital. In credit, it means transparent structures, secured exposures and lenders with clear governance. Yield without visibility is not yield; it is speculation.

The coming period is unlikely to reward complacency. Slower growth, persistent inflation, geopolitical disruption and inflated asset prices are a difficult mix. Portfolios should be built around assets that can withstand that environment rather than assets that depend on the risk-free rate remaining permanently suppressed.

Download the full version of the Letter to Investors here.

John Abernethy is Founder and Chairman of Clime Investment Management Limited, a sponsor of Firstlinks. The information contained in this article is of a general nature only. The author has not taken into account the goals, objectives, or personal circumstances of any person (and is current as at the date of publishing).

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The investment mistake killing your returns

Simonelle Mody

"Design a portfolio you are not likely to trade… akin to premarital counselling advice; try to build a portfolio that you can live with for a long, long time." ***Robert Arnott, Research Affiliates***

The financial industry has long projected an image of delivering superior returns through complex strategies. And this certainly might be the case for a small portion of institutions on a short-term basis. But there is a struggle to consistently deliver alpha. Notably, professional money managers operate in a very different environment to retail investors.

Despite this, I find the portrayal of superiority has worked quite well and forms part of why some retail investors are drawn to sophisticated investment options.

How we got here

Sophistication has long been a status symbol.

It has developed well beyond the social markers of luxury goods and prestigious education to now deeply embed itself in the investment industry.

Retail bias for complexity stems from the assumption that intricate structures are inherently superior to simpler ones. We can fall into this trap by layering portfolios with additional products, strategies or structures, convinced that it will lead to better outcomes. This pertains not only to overly layered portfolios, but also an uptick in interest for complex products, once reserved for the likes of institutions.

The intellectual foundation of the 60/40 portfolio can be traced back to Modern Portfolio Theory (MPT), developed by Harry Markowitz in the 1950s. Thus, the birth of 'the efficient frontier' - the concept of optimising returns for a given level of risk through diversification.

For decades, the 60/40 model was a gold standard for a balanced allocation, however in recent decades, the landscape has shifted. Inspired by the success of David Swensen and the Yale Endowment Fund, the industry has shifted to embrace a more complex construction approach, while questioning the adequacy of the traditional 60/40 mix. Many retail investors have followed suit.

The democratisation of access to alternative investments have seen allocations shift toward hedge funds, private equity, infrastructure and private credit to increase returns and reduce correlation with public markets. Consequently, the average investor's toolkit is much broader now and contains a wider array of asset classes.

But this hasn't been without trade-offs, and it raises a few important questions that inevitably complicate things for retail investors. Chief among them is our ability to assess liquidity risk and valuation transparency in markets. Perhaps more importantly, does added complexity actually translate to better outcomes?

The confounding bias for investment complexity

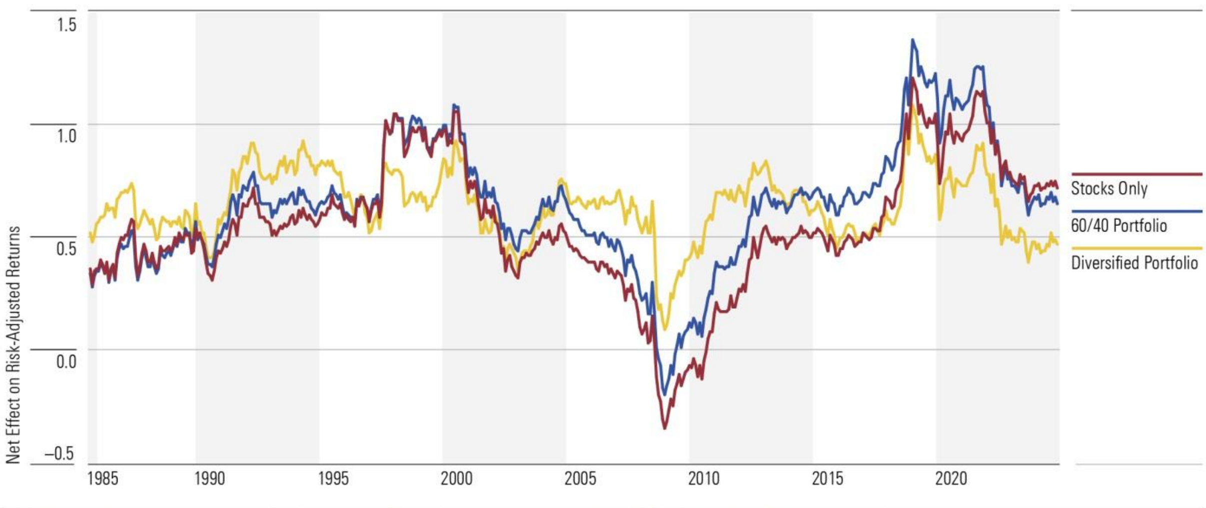
Simplicity can be hard to appreciate and even harder to achieve in an industry focused on the proliferation of new products.

Research Affiliates released an article almost a decade ago on this issue. The authors asserted that investors have a profound bias toward complexity. They attribute this to two drivers: the incentive for asset managers to justify higher fees by leaning into complex strategies, and investor perceptions of intricate market dynamics demanding investment complexity. The paper raises a crucial point that this behaviour encourages performance chasing that manifests in a whipsaw pattern of buying and selling at the wrong times.

The industry earns higher fees through selling sophistication. But not all of these promises materialise in the long term. The most recent Morningstar analysis from the US found that active fund strategies struggled mightily from July 2024 through June 2025, with just 33% of strategies surviving and beating their asset-weighted average passive counterparts. This marks a 14% drop from a year earlier but also reflects a wider pattern of long term active underperformance amongst the higher fee funds.

Another US-based study was conducted to test the value of diversification. This compared a portfolio comprised of 11 different asset classes, a plain-vanilla 60/40 portfolio and an all-stock portfolio over the long-term. The below graph demonstrates the findings of this exercise.

Exhibit 4 Risk-Adjusted Returns (Sharpe Ratio)



Source: Morningstar Direct. Data as of Dec. 31, 2024. The rolling 10-year Sharpe ratios are for stocks only, a 60/40 portfolio, and a fully diversified portfolio. Both portfolios assume annual rebalancing.

The diversified portfolio improved risk-adjusted returns (as measured by the Sharpe ratio) versus an all-stock portfolio during most rolling 10-year periods between January 1976 and August 2017. However, its relative performance has diminished in more recent years.

In contrast, the classic 60/40 has shown remarkable consistency. Since 1976, it has outperformed a stock-only approach about 83% of the time and since early 2005, it has come out ahead of the diversified portfolio in every rolling 10-year period.

We can all draw our own conclusions from this data, but it does make the case that simplicity has often been just as effective (if not more) than attempting to invest in every asset class under the sun.

Ultimately investing is a game of trade-offs. There will always be a portfolio that outperforms yours retrospectively. But that doesn't mean it forms the gold standard approach for the future or for your specific goals. Staying grounded to your objectives and strategy is essential to avoid the temptation of overcomplicating your portfolio in pursuit of elusive outperformance.

A case in point

The allure of alternative asset classes has drawn investors into intricate products that some may struggle to fully grasp the mechanics of. This lack of understanding can have serious consequences.

A good example (albeit, before my time) is the 2008 collapse of Basis Capital, an Australian hedge fund whose strategy hinged on investing in complex instruments known as collateralised debt obligations (CDOs). At the time, these products were well rated, but critics have argued that the risks were largely misunderstood by the wider community.

When the market turned in the wake of the global subprime mortgage crisis, margins calls were made and Basis Capital was forced to sell off in a plummeting market. The fund was unable to recover and that consequently resulted in combined losses of $350 million.

One could argue the issue here wasn't just the product itself, rather the broader ecosystem that failed to scrutinise products for their complexity and lacked an understanding of whether they were suitable for retail investors. Category ratings and performance metrics only go so far. Not every well-rated product belongs in a retail portfolio.

Managing complex financial products and overly layered holdings requires more time, effort and resources. This can create inefficiencies and result in a directionless portfolio with lower overall returns. On top of this, there are significant cost implications. Investing in complex products or even choosing to hold a large number of them result in higher fees and expenses. These naturally eat into your ability to compound returns over time.

Some sage advice

To conclude, I'd like to point you towards one of my favourite snips from Buffett's 2016 Letter to Shareholders.

> *"Over the years, I've often been asked for investment advice, and in the process of answering I've learned a good deal about human behaviour. My regular recommendation has been a low-cost S&P 500 index fund. To their credit, my friends who possess only modest means have usually followed my suggestion.*
>
> *I believe, however, that none of the mega-rich individuals, institutions or pension funds has followed that same advice when I've given it to them. Instead, these investors politely thank me for my thoughts and depart to listen to the siren song of a high-fee manager.*
>
> *That professional, however, faces a problem. Can you imagine an investment manager telling clients, year after year, to keep adding to an index fund replicating the S&P 500? That would be career suicide. Large fees flow to these managers, however, if they recommend small managerial shifts every year or so. That advice is often delivered in esoteric gibberish that explains why fashionable investment "styles" or current economic trends make the shift appropriate.*
>
> *The wealthy are accustomed to feeling that it is their lot in life to get the best food, schooling, entertainment, housing, plastic surgery, sports ticket, you name it. Their money, they feel, should buy them something superior compared to what the masses receive.*
>
> *In many aspects of life, indeed, wealth does command top-grade products or services. For that reason, the financial "elites" – wealthy individuals, pension funds, college endowments and the like – have great trouble meekly signing up for a financial product or service that is available as well to people investing only a few thousand dollars. This reluctance of the rich normally prevails even though the product at issue is –on an expectancy basis – clearly the best choice. My calculation, admittedly very rough, is that the search by the elite for superior investment advice has caused it, in aggregate, to waste more than $100 billion over the past decade.*
>
> *Human behaviour won't change. Wealthy individuals, pension funds, endowments and the like will continue to feel they deserve something "extra" in investment advice. Those advisors who cleverly play to this expectation will get very rich. This year the magic potion may be hedge funds, next year something else. The likely result from this parade of promises is predicted in an adage: "When a person with money meets a person with experience, the one with experience ends up with the money and the one with money leaves with experience."*

A new era of product democratisation is truly upon us. Challenges have shifted from a lack of access to a lack of complete understanding. It’s important to acknowledge that the temptation to emulate institutional strategies should be grounded by a clear view of our role as retail investors and what we are trying to achieve in our lives.

Simonelle Mody is an Investment Specialist at Morningstar Australia. She writes for retail investors and financial advisers on topics spanning portfolio construction, market trends, ETFs and investor behaviour.

The ticking clock on oil reserves

Paul Gooden

There is a point, somewhere around early August, when the global oil market runs out of road if current conditions persist. That is not scaremongering. It is arithmetic, and it is worth understanding the working.

The trigger is the double blockade of the Strait of Hormuz, the narrow waterway through which roughly 20 million barrels of oil per day would ordinarily flow. With that corridor constrained, the world is drawing down its reserves at an unsustainable pace. The clock is ticking, and the market, in my view, has not fully reckoned with what that means.

The numbers that matter

The global oil market consumes around 100 million barrels a day. Of the roughly 20 million barrels a day normally transiting through Hormuz, perhaps 5 million are being rerouted and 3 million are getting through. That leaves a shortfall of around 12 million barrels a day. Factor in approximately 2 million barrels a day of demand destruction caused by already-elevated prices, and you are still left with a 10-million-barrel-a-day hole, being plugged for now by inventory drawdowns at roughly 300 million barrels per month.

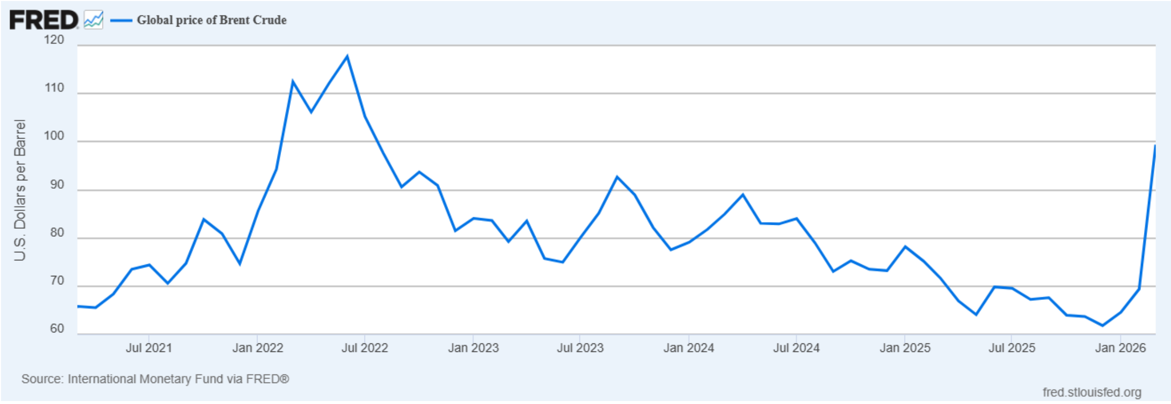
We began the year with approximately 8.5 billion barrels in storage across all definitions: crude, products, strategic reserves, pipeline fill, and refinery stocks. We have already committed to losing around a billion barrels. That brings the floor into view. Operational tank bottoms, the minimum inventory the system needs to keep functioning, sit at around 6.5 billion barrels.

If we continue drawing at this rate over May, June and July, we hit tank bottoms globally in early August. And before that, certain countries and geographies will feel the pinch sooner. Regional shortages are likely to emerge over June and July, ahead of any global reckoning.

The price needed to balance the books

Once you hit tank bottom, the calculus changes entirely. You can no longer borrow from storage. Supply must equal demand. And to close a 12-million-barrel-a-day shortfall through price alone, you need an oil price that forces significant demand destruction, particularly in emerging markets where consumers have the least capacity to absorb the blow.

My estimate is somewhere between $130 and $150 a barrel. Brent crude is currently hovering around $107.



That is not a forecast of inevitability. A diplomatic or military resolution to the Hormuz blockade would change the picture considerably. But a solution is needed, and the longer it does not arrive, the more severe the eventual adjustment is likely to be.

Why equity investors are more cautious than you might expect

One might reasonably expect energy equities to have surged in this environment. They have not, and the reason is worth understanding.

Equity investors are wary of what I would call day-one headline risk. The moment a credible diplomatic breakthrough is announced, an estimated 120 million barrels of oil sitting in tankers behind the Strait of Hormuz could hit global markets relatively quickly. That initial price shock would weigh on energy equities, and investors are understandably reluctant to be caught on the wrong side of it.

There is also the sheer noise of the current environment to contend with. News flow is fast, contradictory, and heavily politicised. It is worth noting that when we look at the Brent oil price on screen, we are looking at the prompt month of a financial futures curve, not a physical barrel. The financial flows in these contracts run at roughly 100 times the volume of the physical market. That makes the price highly sensitive to tweets, headlines, and political messaging, some of which may well be deliberate.

The typical futures contract is also only four to six weeks out, and the market's working assumption seems to be that this will be resolved in that timeframe. In my view, the full impact of the disruption has not yet been properly priced in.

Where we are, and what comes next

Energy equities are currently pricing in something closer to $70 a barrel. I believe the mid-cycle oil price needed to balance global supply and demand over the next three to five years is closer to $80. That gap is meaningful, and for investors willing to look through the near-term uncertainty, it may ultimately represent an opportunity.

But the more immediate point is this: the oil market is not broken yet. Inventories are still providing a buffer. There is still time for a diplomatic solution to change the trajectory. What there is not, however, is an unlimited runway. The buffer is finite, the drawdown rate is high, and the mathematics of the situation are unambiguous.

The market may be used to living with geopolitical noise. What it is less accustomed to is a situation where the noise has a hard deadline attached to it.

Paul Gooden is Head of Natural Resources and a co-portfolio manager for the Global Natural Resources strategy at Ninety One.

Managing the impact of the Middle East conflict on listed infrastructure

Magellan Infrastructure Investment Team

Oil at ~US$90-$100/bbl (barrel) represents a ~60% hike in prices from pre-conflict levels, with risks of higher prices omnipresent. Since the commencement of conflict, the ensuing closure of the Strait of Hormuz, damage to energy infrastructure in the region and resurgence in global geopolitical uncertainty are conditions to truly test the mettle of any asset class, including infrastructure.

And yet, our scenario analysis (at the end of this article) suggests that while there will undoubtedly be a short-term impact, likely concentrated in airports and toll roads (along with rails and communications), resolution for infrastructure assets should take place over a matter of months. The overall outcome is one of resilience, with infrastructure relatively well-positioned to absorb a supply-driven energy market shock.

Impact

The direct impacts of the energy market shock are felt unevenly across infrastructure sub-sectors.

Some sub-sectors are most exposed to an energy price shock: Airports are top of this list given flight cancellations, higher ticket prices, passengers avoiding Middle Eastern airports (and air travel more broadly) as well as increasing risks of jet fuel shortages. Some airport businesses are better protected (such as Aena, which operates the Spanish airport system and is better insulated from traffic flows with the Middle East), while others have direct exposure to the conflict through ownership of assets in the Middle East, and significant traffic flows to and from the region (such as ADP). We also expect transport infrastructure (such as Transurban, ALX) could be affected, as higher petrol prices and outright shortages of fuel have an impact on travel patterns on toll roads in the near term. However, it should be noted that historically, toll road traffic has shown little impact from fuel price increases and while we have seen a sticker-shock effect, we expect this will normalise quickly in the absence of fuel shortages.

Rail infrastructure is also more exposed. For rail (for example, CSX), the short-term impact can actually be positive, whereby higher oil prices can support a modal shift from trucks to rail. However, as a supply-side shock feeds through to weaker economic activity, there is a negative cyclical impact on freight rail volumes.

For communications, particularly US tower companies that have largely fixed-price escalators, higher energy prices are a headwind as they push through to higher inflation that affects the value of real earnings.

Other subsectors are resilient in the face of a supply-side energy shock: Regulated utilities are in this group. This set includes transmission and distribution companies such as National Grid, gas utilities such as Italgas, US integrated power companies such as CMS Energy and water companies such as United Utilities. These businesses are regulated, earning an agreed rate of return on their capital invested. They also experience dependable demand throughout economic cycles; for example, with residential demand for electricity typically holding firm even as energy, economic and other shocks occur.

Right now, this group – particularly US regulated electricity utilities – has a structural tailwind. Large-scale capex to build generation capacity to meet the demands of data centres, along with investment in renewables, is underway and is not expected to slow.

Resolution

Infrastructure businesses are characterised by demand consistency, and, in our definition, by consistent cash flows. By design, these businesses largely have pass-through mechanisms to recoup inflation and to generate reliable earnings. As a result, we would expect listed infrastructure to recover effectively from surging energy prices. The timing of this recovery is the key, as is the risk of rising interest rates, which complicates the outlook.

Inflation pass-through mechanisms determine the speed of resolution: In a supply-side shock, inflation rises swiftly, which can drive cost pressures for infrastructure companies as input prices jump. Infrastructure assets typically have some degree of inflation pass-through built into their concession or regulatory framework. While there is considerable variability across agreements, there are three broad groups to keep in mind when estimating the recovery profile for an infrastructure company.

The first wave comprises those companies where inflation pass-through is the timeliest. This includes those companies operating in regulatory systems that provide return allowances in real terms, escalating revenues with inflation and indexing debt costs to market yields. Systems in the UK and Australia provide this inflation coverage. The UK water sector (including Severn Trent and United Utilities) has this explicit protection. Rail infrastructure (such as Norfolk Southern and CSX) is also in this wave, reflecting the sector's discretion to charge rates to customers that support their "revenue adequacy". These companies can therefore pass through inflation under this standard. Their pricing power is also key.

The second wave includes those companies where inflation is recovered with a modest lag. For utilities, we mean those companies operating in regulatory structures where return and cost allowances are set in nominal terms. This system provides coverage for inflation with a lag. US utilities are in this group as are toll roads. Most toll roads' pricing mechanisms (such as for Transurban) include quarterly or at most annual toll price reviews. Toll roads generally have low price elasticity, thus the earnings impact is mitigated or in some cases such as where debt costs are largely fixed, can actually benefit in the short term as prices rise faster than debt costs.

Airports (such as Aena and ADP) are somewhere between the first and second waves, with the regulated component of their earnings set on a multi-year basis, with some inbuilt (but not dynamic) protection for inflation. For example, Aena can cover inflation with a two-year lag as adjustments are made in the following financial year. The unregulated businesses typically have revenue-sharing arrangements (for example, for concessions on site), which benefit from retail pricing that quickly adjusts for inflation.

The third wave includes communications infrastructure companies (such as American Tower). US tower companies typically operate under long-term contracts that work largely on fixed-price escalators. Rising inflation can therefore erode real earnings. We note that outside the US, however, some tower companies have more inflation relief and are more akin to airports in terms of cover. For example, European tower company Cellnex has ~65% inflation linked and ~35% fixed-price escalators.

As a result, there is a lag of as little as a few weeks to as much as 6-12 months for an asset's pass-through mechanism to catch up to rising inflation and then pass on these costs to end users. This is unique to the asset class and is important to charting the sector's path out of an energy supply shock.

However, we note that this outlook assumes the energy shock is predominantly one of price, not availability. Outright supply disruptions for jet fuel, supply disruptions or fuel rationing for road transport are risks to airports and toll roads. Even if there is a CPI reset on tolling, for example, significantly lower volumes on the roads due to fuel rationing would lead to lower revenues. Such a scenario would mean the recovery takes longer, as activity normalises at the same time as pricing settings are updated.

We are watching for higher real interest rates: Higher interest rates are the second-order effect of higher inflation and have impacts on listed infrastructure companies. The long duration of infrastructure assets means that higher real rates have a negative impact on valuation. A rate-led downturn in economic activity has historically had a larger impact on infrastructure, as compared to an average downturn.

Right now, real rates look contained, and central banks are taking a measured approach to assessing growth and inflation risks stemming from the Middle East conflict. Should we see central banks commencing aggressive hiking cycles, that would have a significant influence on discount rates and asset valuations. Equally, market concerns on fiscal sustainability for major governments (such as big fiscal support packages or defence spending) are a risk to longer-term benchmark rates, should yields start to rise.

If higher rates materialise in the coming months, it is important to distinguish between share price performance and business fundamentals. Companies that are seen as 'defensive' are often out of favour when interest rates rise as investors prefer higher-growth sectors. However, this is often a reflection of strong demand environment, not a reflection on the quality of underlying earnings. Over time, businesses that have solid fundamentals should see this reflected in their stock prices.

Outcome

Longer term, infrastructure has sound shock absorption capacity.

This is not an easy period for markets. While uncertainty abounds, one thing we do know is that infrastructure assets have the consistency in demand and cash flows to support their recovery from an energy supply shock.

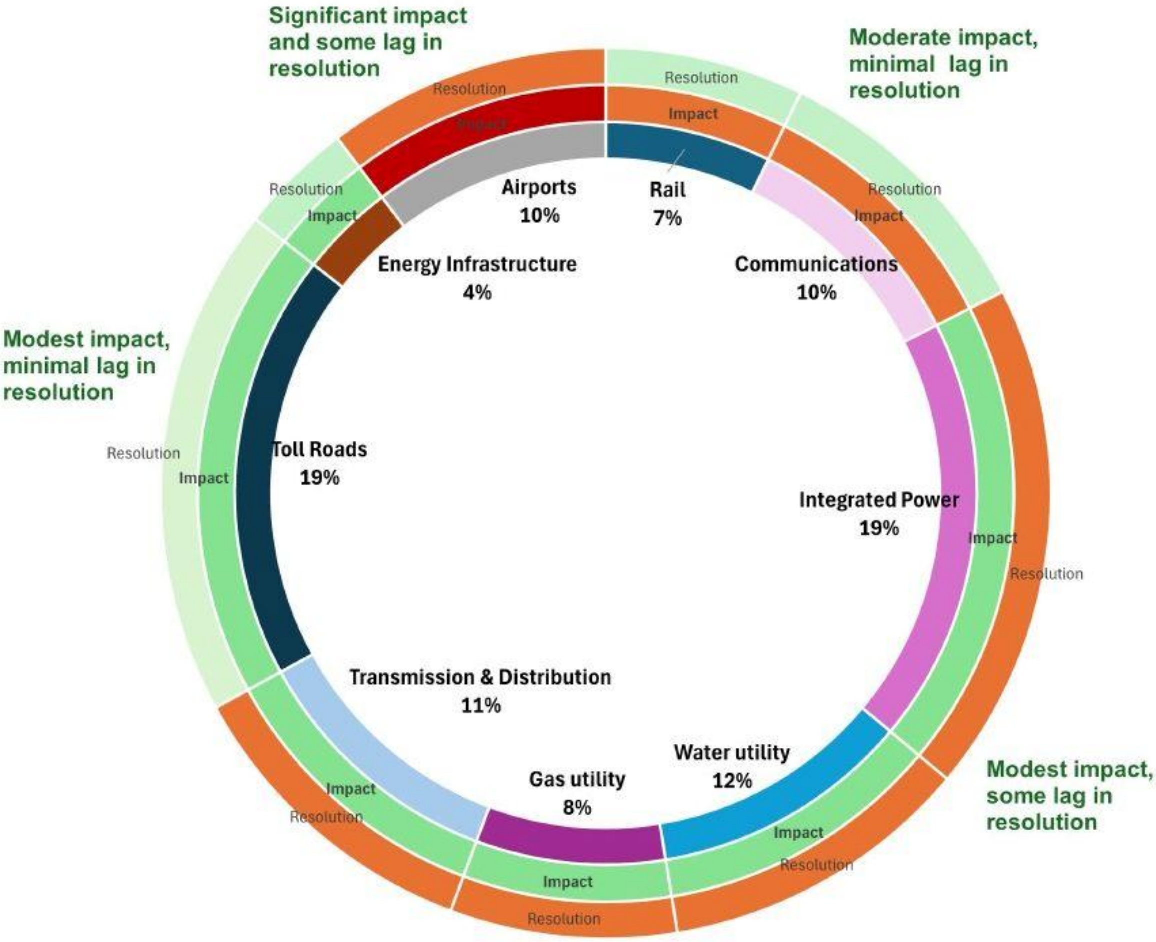
In the case of roads and airports, the near-term outlook is affected by the current conflict in the Middle East. However, once conditions normalise, we would expect to see a swift return in demand, given solid momentum in population growth and air travel demand that was in place prior to the conflict.

For communications infrastructure, the prevalence of mobile device use suggests that this sector will continue to power through near-term disruptions, with these assets hard to substitute, and demand continuing to grow.

For regulated utilities, their regulated earnings model and consistent demand support sustained cash flows and return on equity through market cycles. There is also a structural growth story in play for this sector, with large capex pipelines (owing to data centre demand and renewables build out) also supporting the outlook for earnings growth.

For our strategies, we note that we do not invest in companies with direct exposure to commodity prices, and consequently, we do not benefit from rising oil and gas prices (for example, through allocation to midstream services companies). However, the run-up in these commodity-price exposed companies is typically short-lived and is followed by a downshift in stock prices as energy markets normalise.

Navigating the impact of energy supply shock on listed infrastructure



Source: Analysis undertaken on the Magellan Infrastructure Fund March 2026

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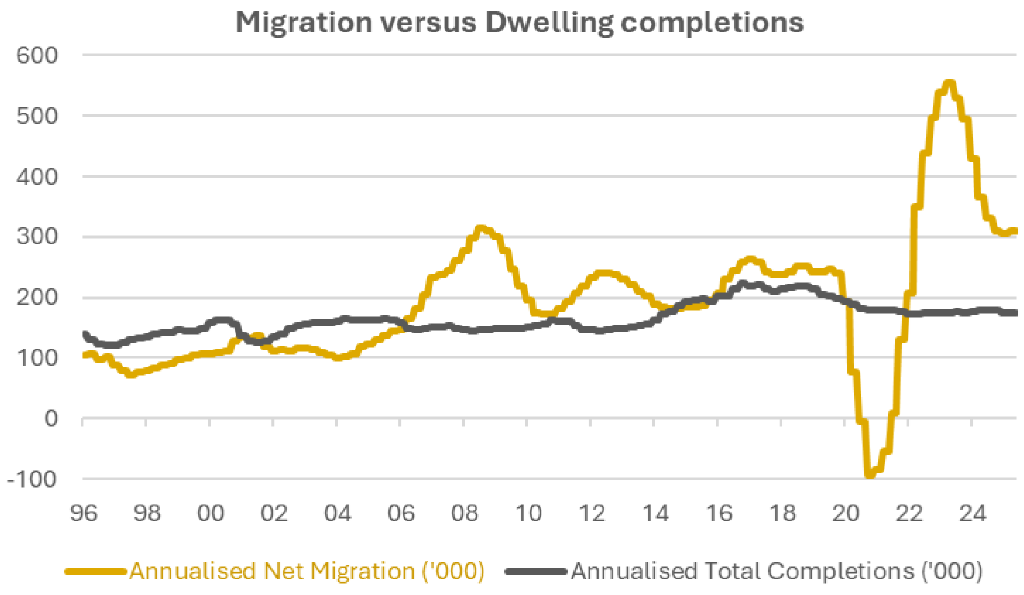
Rent inflation and the missing policy

Jason Teh

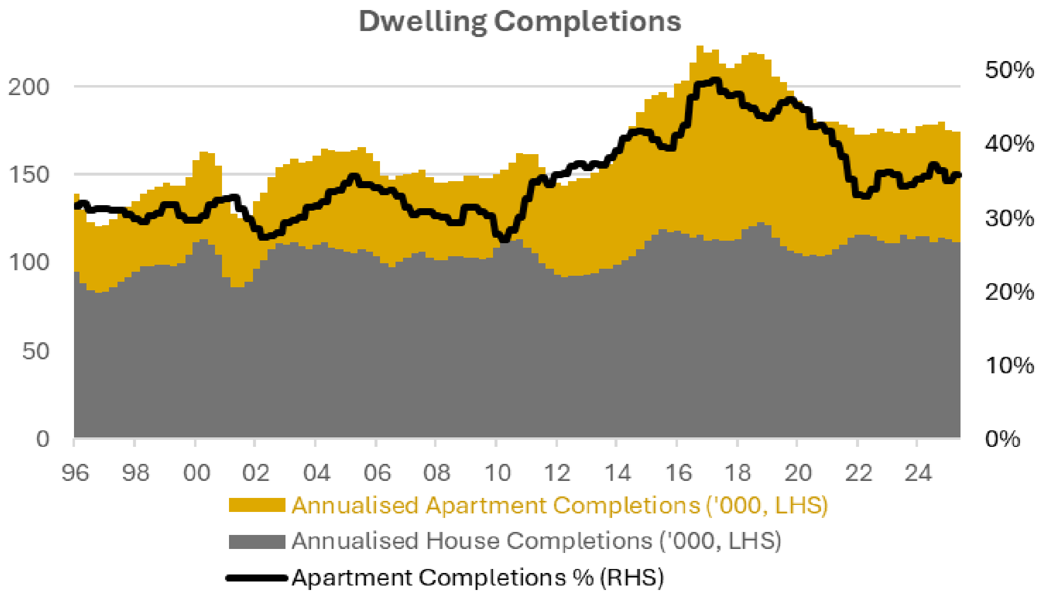
Rent is the defining issue of Australia's cost of living crisis. It has risen nearly 40% since 2020 and is consuming a record share of household income. The root cause of the rental crisis is the gap between the number of people who need housing and the number of dwellings being built to house them. The chart below shows an uncomfortable truth: annualised net overseas migration against total dwelling completions from 1996 to the present.



Source: FactSet, Vertium

Despite net migration coming off its record breaking 2022-23 peak, it is still running at an elevated level around 311,000 per year. Total dwelling completions are running at approximately 175,000, slightly below pre-COVID levels. The gap between demand and supply represents the structural shortfall that is driving rental inflation. Net migration and dwelling completions capture the core drivers of rental supply and demand. Adjusting for other factors such as household formation rates, the proportion of completions available for rent, or changes in existing rental stock would refine the analysis but not change the broad conclusion.

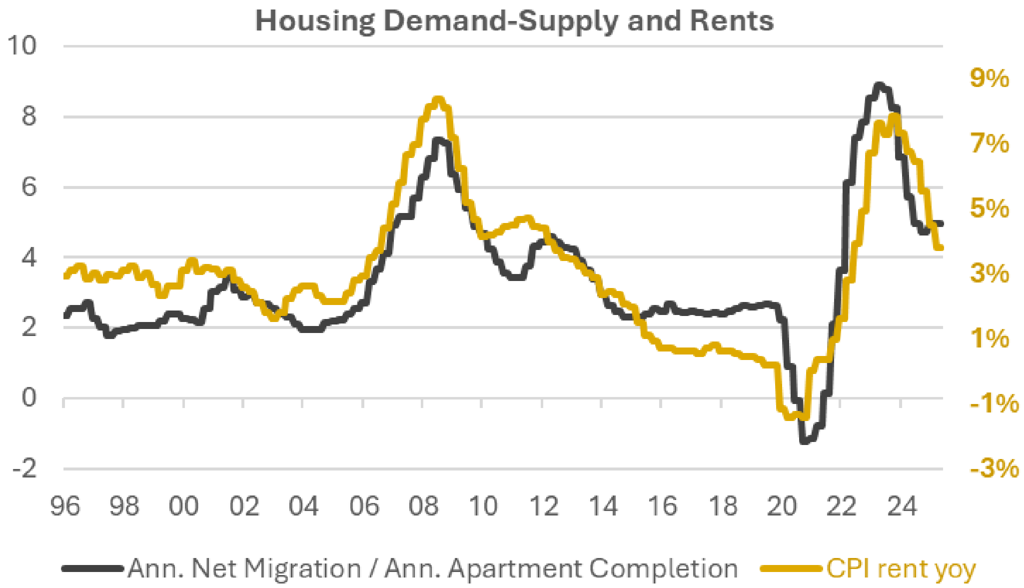
Over three decades, total dwelling completions have moved within a relatively narrow band, averaging about 165,000 per year. This stability is driven by house completions, which have been anchored at around 105,000 throughout. Apartment completions are more volatile — surging from around 30% of total completions prior to 2010 to nearly 50% at the 2017 peak before settling back to around 35%. But because they represent the smaller share of total completions, their volatility is dampened at the aggregate level.



Source: FactSet, Vertium

The simple economics of rent

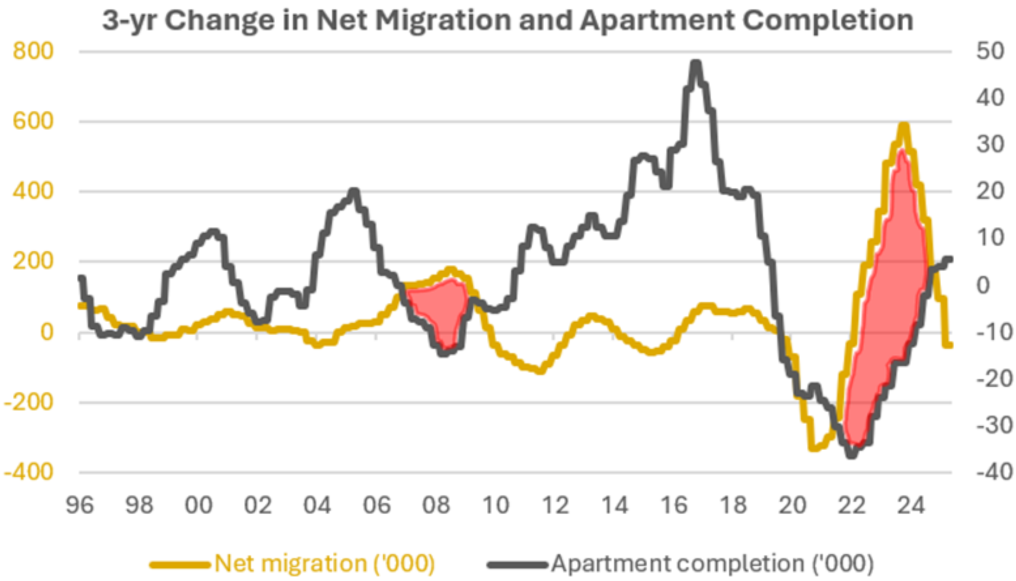
While apartments represent the smaller share of completions, they matter because they deliver supply at a volume detached housing cannot match. A single high-rise approval can yield hundreds of dwellings on a hectare of land where detached housing yields around fifteen. When the apartment pipeline runs at capacity, rental supply grows fast enough to absorb population growth and rents ease. When it stalls, nothing else compensates for the volume lost. Apartments are the release valve — and investor presale demand is the mechanism that opens it. The chart below plots the ratio of net overseas migration to apartment completions against CPI rent growth from 1997 to the present. The relationship between the two is unmistakable.



Source: FactSet, Vertium

Two rent booms

Australia has experienced two distinct episodes of severe rental inflation, one before the 2008 Global Financial Crisis (GFC) and one after the 2020 COVID pandemic. The underlying drivers were virtually identical: strong net overseas migration landing in a market where dwelling completions could not keep pace. The following chart shows the 3-year change in annual net migration and apartment completions to highlight the gap between demand and supply.



Source: FactSet, Vertium

In the pre-GFC episode, Australia's resources boom led to net overseas migration accelerating sharply, lifting net migration from 2006, while multi-dwelling completions experienced a decline. The migration-to-completions ratio rose sharply, and CPI rents surged. Rents eventually stabilised as migration fell in the aftermath of the resources bust. Lower rates used to stimulate the economy during the GFC also encouraged housing supply, which gradually rebalanced the housing market and further eased rent growth.

The post-COVID episode followed the same script, only more severely. Net overseas migration surged, eclipsing the migration dip during the lockdowns. This demand landed in a rental market where the supply pipeline had been hollowing out for years, compounded by post-COVID supply chain problems that extended construction timelines.

Despite comparable peak CPI rent growth of around 8% for both episodes, the post-COVID episode has felt far worse for renters. In the mid-2000s, the resources boom delivered strong economic growth and wages broadly kept pace with rising rents. After COVID, the picture reversed. Lacklustre economic growth and weak productivity left wages struggling, while inflation pushed workers into higher tax brackets. Bracket creep is eroding after-tax purchasing power. Full-time workers are now paying an average of 20% of their income in tax, the highest in over two decades. The result is that renters facing a 40% surge in rents since 2020 have done so with after-tax incomes that have barely moved in real terms. Australian households are now dedicating a record 33% of household income to rent, nearly double the 18% recorded in 2007-08. The rental crisis is not just a housing problem — it is the cost-of-living crisis.

Rent relief period

It was not always this way. Between these two rent booms sits an episode of genuine rental relief. Falling interest rates from 2012 fuelled strong capital gains expectations for housing, which in turn produced a boom in investor lending. The major banks — Commonwealth Bank, National Australia Bank, Westpac and ANZ Group — were the engine of this boom, growing their investor mortgage books aggressively as demand surged. By early 2017, interest-only loans represented 64% of all new investor lending. This capital funded a record apartment construction pipeline. Critically, this supply boom occurred despite the restrictive planning rules commentators today cite as the primary impediment to new supply. When investor lending economics were favourable, the market found a way.

The surge in apartment supply produced a prolonged period of subdued rent growth from 2016 to 2020. Completions surged while net migration was subdued and the ratio fell. CPI rent growth approached zero. For renters, it was genuine relief delivered entirely by private investor capital responding to market incentives.

While renters benefited from the excess supply, APRA grew concerned about the housing boom. Worried about systemic risk from concentrated interest-only lending, APRA imposed a cap in March 2017 limiting interest-only loans to no more than 30% of new residential mortgages. The major banks were forced to reprice interest-only loans higher and restrict approvals, directly curtailing the investor lending that had been driving apartment supply. Investor loan growth collapsed. The apartment presale market, which depends on investor buyers to unlock construction finance, dried up. The supply pipeline that had been delivering rental relief collapsed almost overnight. Fortunately, net migration remained stable and rents held steady.

The missing policy

The lesson from 30 years of data is clear: reducing rent inflation requires pulling two levers.

Lever one: reduce population growth

Immigration is one of Australia's great economic strengths. It brings skills, diversity and long-run productivity benefits. But like any good policy taken to an extreme, the costs eventually outweigh the benefits. Annual net migration running at 311,000 into a market completing 175,000 annual dwellings is not an immigration policy — it is a housing and cost of living crisis. Moderating migration to levels the housing stock can absorb reduces rental demand pressure directly and immediately. The international evidence is unambiguous. New Zealand, Canada and the United States all cut immigration materially in 2024-25, and in each case rental inflation decelerated sharply within months. Migration is the demand lever governments can pull immediately.

Lever two: incentivise investor lending for new builds

Investor credit conditions drove the 2013-2017 apartment supply boom. Unless the government plans to subsidise every dwelling itself, it needs to unleash the private sector. The new build negative gearing exemption creates the right incentive. For listed residential developers like Mirvac and Stockland, the exemption is a potential demand tailwind, but making it work requires credit conditions that allow investors to act on it. Today, those credit conditions are more restrictive than at any point during the 2013-2017 boom.

APRA should consider reducing the 3% serviceability buffer that was set for emergency interest rates in 2021. Now that the cash rate has normalised, the serviceability buffer is suppressing the investor borrowing capacity that drives apartment supply. More importantly, the single most effective policy lever to recreate the apartment supply boom is lower interest rates. But the RBA cannot cut rates in an environment where government spending is stoking demand. Every dollar of government spending that adds to inflation delays the rate cuts that would unlock investor lending for new builds and ease the rental crisis.

Yet the government's supply response largely bypasses the private sector. The National Housing Accord, announced in October 2022, targets 1.2 million new homes over five years, or 240,000 completions per year. The problem is that the absolute peak of the greatest investor lending boom in Australian history delivered only 223,000 completions in the year to March 2017. The reason the target will likely be missed is simple: the Accord offers very little incentive to the private market that drives apartment supply. Its spending is overwhelmingly directed at social and affordable housing. The Accord contains no mechanism that replicates the credit conditions which produced the only episode of genuine rental relief.

Conclusion

The supply-demand framework is not complicated. Rents rise when migration outpaces housing supply and fall when supply catches up. History has demonstrated this in Australia and the international evidence confirms it is not unique to this country.

What is complicated is the political will to pull the levers that work. Moderating migration, recreating the credit conditions that built the last apartment boom, and resisting fiscal spending that keeps inflation elevated and delays rate cuts that would unlock private sector construction — these are the levers that move rents. Until those levers are pulled, the negative gearing reform will have little impact and Australia's cost of living crisis will remain unresolved for the third of Australians who rent.

Jason Teh is the founder and Chief Investment Officer of [Vertium Asset Management](); and a Portfolio Manager at [Clime Investment Management Limited](), a sponsor of Firstlinks. This article is general in nature and does not constitute or convey personal financial advice. It has been prepared without consideration of anyone's financial situation, needs, or financial objectives. Before acting on the areas discussed and contained herein, you should consider whether it is appropriate for you and whether you need to seek professional advice.

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The Risk-Wealth Paradox: Why more money means you should take less risk

Nick Maggiulli

There's a common belief that as your wealth increases, your capacity to take risk increases as well. After all, when you have more, you can afford to lose more, right?

This might be correct in the extremes, but this argument doesn't hold in more typical wealth ranges. Why?

Because a dollar isn't always a dollar. And once you understand this, you'll never look at risk-taking the same again.

A dollar is not a dollar

In the real world, people don't treat every dollar the same. As I discussed in *The Wealth Ladder*, your first $10,000 is more impactful than your next $10,000. It's also true that your first million dollars is more impactful than your next million dollars. And so forth.

The reasoning for this is two-fold. First, every step up *The Wealth Ladder* creates a sort of lifestyle floor that people don't want to go below. For example, once you know what it's like to not worry about grocery prices, you don't want to go back to a world where you do.

Second, the more wealth you have, the more wealth you require for a *large* lifestyle change. Going from taking a bus/train to taking a plane might cost 1.5x-2x more depending on where you're traveling. But going from flying first class to flying private will cost 10x more. It's these *exponential* increases in cost for marginal increases in convenience that creates this step-like structure for wealth.

As a result, it becomes optimal to de-risk as your net worth increases. So while you *can* take more risk as you get richer, it doesn't mean that you *should*.

Of course, the risks you take will always be *relative* to your desires. If you won't be satisfied until you're flying private in Level 5 ($10 million -$100 million), then you have to keep taking big risks. But, if you're content flying commercial in Level 4 ($1 million -$10 million), you can dial it back much sooner.

As your wealth changes relative to your desires, your capacity to take risk will change with it. The closer you are to being fully content, the less risk you should want to take. I call this the Risk-Wealth Paradox.

The Risk-Wealth Paradox

The Risk-Wealth Paradox goes against the economic theory on risk appetites. Standard economic theory suggests that as our wealth grows, our *absolute* capacity for risk increases. As we build wealth, we can lose more and still survive.

But the Risk-Wealth Paradox suggests that the *rational* choice is the opposite—as wealth grows, risk-taking behavior should collapse. This is true because while the financial cost of a loss goes down with more wealth, the psychological cost goes up.

I've previously discussed how your appetite for risk *should decline* in middle age as your liabilities increase (e.g., children, aging parents, etc.). I would apply the same line of thinking to those who have built some wealth. As your net worth increases, preservation becomes more important than chasing increasingly expensive luxuries.

Why is this the case? Because once you've won the game, the value of gaining a dollar plummets while the pain of losing a dollar soars. This is the fundamental principle behind prospect theory. Prospect theory states that people react to gains and losses asymmetrically. In other words, the pain of losing $100 is larger than the pleasure of winning $100, at least for most people.

And when you're wealthier, it's like prospect theory *on steroids*. If you had a $2 million net worth, the pain of losing $1 million is significantly larger than the pleasure of gaining an additional $1 million. It might even be larger than the pleasure of gaining $4 million. While these amounts are arbitrary (and will vary from person to person), they exemplify the impact that wealth can have on risk-taking.

The other reason for the risk-wealth paradox is the amount of time it takes to recover from a significant loss. If someone with $1,000 in a brokerage account lost it all, they could likely earn it back relatively quickly. But if someone lost $100,000 in their retirement account, it could take years to save that amount of money.

Unless your income can keep up with your wealth over time, you'll have to decrease how much risk you take. Why? Because as your portfolio grows it becomes harder to replace future losses with future earnings. If you can save $50,000 a year, you can replace a 20% loss on a $1 million portfolio in under 4 years (assuming a 5% return on your money). However, to replace a 20% loss on a $5 million portfolio it would take over 14 years!

This divergence is what contributes to what I call the risk squeeze.

The risk squeeze

Your ability to take risks throughout your financial life will be influenced by three primary factors—your age, your liabilities, and your level of wealth. As each increases, you should naturally want to take *less* risk. Unfortunately, these tend to all move up in middle-age. Does this mean we should be holding 100% Treasury bills when we are in our 40s?

Of course not, but you have to consider how your risk taking should change over time. When I started invested I had 15% in U.S. bonds. Then I was 0% U.S. bonds for a few years. And now I'm 20% U.S. bonds with a growing amount of Treasury bills and tax-free municipal bonds on the side (for an eventual home purchase).

Is this right? I have no clue. But it allows me to sleep at night. I've been fortunate to build some wealth and I also now have a family I'll need to support in the future.

The risk squeeze is upon me and I've already taken steps to reduce my risk accordingly. I'm no longer playing to win. I'm playing to not lose.

What about you? Where are you in your financial journey? Is the risk squeeze upon you?

It's easy to critique someone else's risk-taking, but far harder to be honest about your own. I can't tell you how much risk to take. But if you've won the game, stop playing.

Nick Maggiulli is the creator of personal finance blog Of Dollars And Data and the Chief Operating Officer at Ritholtz Wealth Management. For disclosure information please see here. This article was originally published on the Of Dollars and Data blog and is reproduced with permission. If you liked this article, consider signing up for Nick's newsletter.

SMSF estate planning: Eight things to consider

Michael Hallinan

Increasingly, super is the next major asset after the family home (sometimes it *is* the client's most significant asset, as demonstrated in McIntosh v Mcintosh [2014] QSC 99. It is therefore imperative that any estate planning for your client must also involve planning for their SMSF.

Here are eight things that SMSF trustees could consider:

1. Consider what 'Armageddon' is for every SMSF

What is each fund's 'Armageddon', or worst-case scenario?

This will be subjective for each SMSF.

For example, in a 'husband and wife' fund where the wife always left the running of the fund to her husband, what if the husband suddenly died or lost mental capacity? Could the wife continue with the fund, or would it all be too hard for her?

2. Check the trust deed and (for a corporate trustee) the trustee constitution

It is essential for the constituent documents of the fund to authorise any 'Armageddon' strategies to be implemented.

For instance, making a binding death benefit nomination (BDBN) can achieve certainty regarding payment of a super death benefit, and can prevent disputes. However, does the fund trust deed authorise a BDBN to be made? If so, would the BDBN lapse after three years or can it be non-lapsing?

What about the trustee constitution? In a two-member fund with a corporate trustee, if one member dies the survivor can usually carry on as the sole director/shareholder. However, the trustee constitution must authorise this.

3. Amend trust deed and/or constitution if unsatisfactory

If the fund trust deed and/or trustee constitution do not authorise the relevant 'Armageddon' strategies, they will require amendment.

Consider also whether the trust deed should be completely updated (a common strategy) or should the amendment be more bespoke (especially where necessary to "grandfather" previous provisions).

4. Discuss 'Armageddon' with your clients

If the worst case scenario happened, what are the options? For instance:

- Could the surviving member continue to operate the fund, perhaps as a sole director of a corporate trustee?
- Or would it be better to simply wind up the fund and rollover to an APRA-regulated or small APRA fund?

5. Consider using the same trust deed for all SMSFs

If you have clients who came to you with an existing SMSF trust deed, these conversations may be quite different for each of them depending on what their trust deed says.

It may make sense (and ultimately save your clients angst and expense) to have the trust deeds for all clients fully updated to a modern trust deed, well before their 'Armageddon' arrives.

6. Ensure all members have valid EPOAs

If all fund members have an up-to-date enduring power of attorney (EPOA), it makes things much easier in the event that:

• A member loses capacity - their attorney can become the trustee or director of the trustee in their place under s.17A of the SIS Act;

• A member departs overseas indefinitely - their attorney can become the trustee or director of the trustee in their place to avoid fund residency issues.

However, you need to ensure (on an ongoing basis) that the person nominated as attorney is not a disqualified person (e.g. someone convicted of an offence involving dishonesty), otherwise they will not be able to act as trustee or director of the trustee in place of the member.

7. Ensure BDBNs are up to date and non-lapsing

The last thing your clients need is for a situation like *Katz v Grossman* or *McIntosh v McIntosh* to happen to them.

SMSFD 2008/3 confirms that, with a correctly structured trust deed, a well-written BDBN can provide both certainty and an appropriate and tax-effective succession of your clients' superannuation death benefits.

Whilst being non-lapsing means not having to remember to renew a BDBN, another issue is that some SMSFs don't authorise a BDBN to be made by a member's enduring attorney, so if it lapses and the member has since lost capacity the BDBN cannot be renewed.

8. Change from individual trustees to corporate trustee

For many reasons it is prudent to change from having individual trustees to a single corporate trustee, such as:

- Ease of administration on the death, bankruptcy or incapacity of a member;
- Ease of administration if a member departs overseas; and
- Minimise the risk of incurring multiple 'speeding ticket' fines from the ATO.

Michael Hallinan is Special Counsel – Superannuation, for SUPERCentral, an independent online platform provider of SMSFs, advice, legal documentation and wealth management services to accounting and financial planning firms throughout Australia. Please note that these comments are for your consideration only and are provided to assist you in deciding whether to proceed to obtain a formal opinion on the issue. These comments cannot be relied upon by either you or any of your clients until and unless we issue that formal opinion.

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