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Investing in the new world

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In the business world, the rearview mirror is clearer than the windshield.
Warren Buffett

The whole history of the world is summed up by the fact that, when nations are strong, they are not always just, and when they wish to be just, they are no longer strong.
Winston Churchill

Focus on the long game

Unsurprisingly the media is dominated by Covid-19 related matters almost above all else. The people that are most impacted by these are:

1. Those medically impacted, especially the elderly
2. Those who lost their job
3. Those who lost their business or are struggling still to keep it afloat
4. Landlords who borrowed too much
5. Those mentally impacted by the current stresses of the above points or just simply fearful of the disease

Whilst the events are significant, especially for those directly impacted, when it comes to prudent investing it is important to look through the very current events and determine what are the major forces that will impact over the longer term.

Some of the impacts are directly related to Covid-19 however there will be both indirect and completely unrelated changes in the landscape that will materially impact markets and client portfolios over the medium to longer term.

Changes in consumer behaviour

It will not take a rocket scientist to deduce that demand for commercial property is likely to face structural headwinds as corporates adjust the working arrangements for their employees, especially around working from home. Just one day a week could see property demand fall, but this is just the start. Then there's the coffee shop, the lunch shop, the bar after work which are all likely to see a knock-on impact.

Consumers are likely to either spend less as they are home more often or spend differently with online shopping. Either way the changes will likely be profound, and some prudent analysis and strategy is required to successfully navigate these changes.

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Paying for it all

Twelve months ago, I wrote "Lack of Interest" regarding falling interest rates. Little did I know then the forces of Covid would further crush already low rates. For example, if you buy a 10 year Australian Federal Government Bond it will yield you 0.89%, this is a meagre $890 per annum for every $100,000 you lend the government. On top of this, your get NO COMPENSATION for inflation. This year inflation to the March quarter was 2.2%, if this rate was consistent for 10 years when the government gave you back your money it would only be worth $80,444 in today's dollars. This is diabolically damaging to any portfolio if all that you owned were term deposits, bonds or cash.

As I said last year, we are almost certainly "lower for longer" when it comes to interest rates so banking on them going up is more than likely going to lead to disappointment.

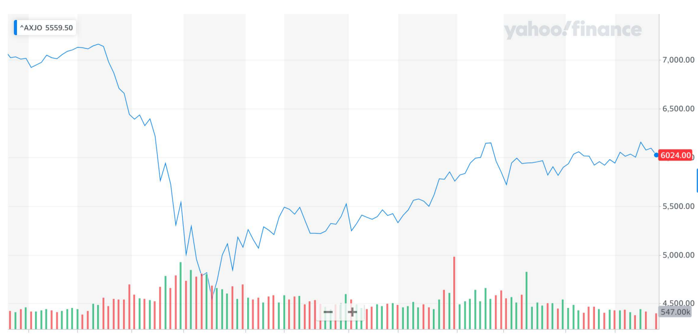
With the explosion in government debt due to Covid financing we are not holding our breath, which is why we must maintain asset diversification, even if it is hard to do so.

Equity disconnect?

With equities ramping 25-35% from their lows in March most people are wondering what's going on. Firstly, shares got very cheap before they rallied strongly off these lows, especially once the first-wave curves of Covid started to flatten. Equity markets are forward looking and behave accordingly. Secondly international shares now have income higher than term deposits. This has never happened before in my lifetime! Further Australian shares yield about double international shares. On a relative trade compared to interest rates, those looking for income have been hunting here.

As I always say never ignore the "grandmother rules", one being '*you can't have your cake and eat it too*'. Share investing comes with material capital risks.

This is where a portfolio approach to investing makes sense, you diversify your risk, '*don't put all your eggs in one basket'* and ignore an easy or sure thing, '*if it sounds too good to be true it probably is'.* Understand that there will always be a cost (both financial and non-financial) in finding the right solution, '*there's no such thing as a free lunch'.*



Source: Yahoo.com

Thank you Grandma for your wisdom.

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Geopolitical dangers

With China getting belligerent in their dealings with many other countries, not just Australia, the great power struggle between China and the United States runs the risk not only of increasing the risks of a 'hot war', i.e. one with bullets and missiles, but also by stoking the risks of higher inflation. Again by example, if inflation averages just 1% higher than previously stated (3.2%) your $100,000 drops to less than $73,000 in 10 years if left to rot in a government bond or term deposit and, on current rates you'll receive less than $75 a month from the bond!!

Whether it is geopolitical tensions or other sources of inflation risk investors have become very complacent about the impact of inflation as it's been benign for so long. For anyone investing in the 80's they will tell you this is a risk that cannot be ignored. As a result, we have started to increase inflation protection inside portfolios.

What is ESG?

Most people know about 'ethical investing', or a process of determining where your investment dollar goes based on a philosophy of trying to do good, or at least not do bad. Formally it is known as Environmental, Social and Governance principles, or ESG. Essentially you want to look after the environment, not hurt people and make sure that companies are managed by ethical and responsible community minded leaders. There is also a slightly different approach called sustainable investing.

This is something we are working hard on at the moment, however there are many challenges. Firstly, almost every individual investor has a different personal definition of 'ethical investing'. Whilst most people would not wish to be involved in the manufacture of land mines or pollute rivers through gross negligence, there are some finer subtleties whereby investors will differ. Gambling, alcohol and liquor will split a few opinions and whilst mining and logging is not loved by most, good luck with your next house without wood and nails. So for some environmentally minded miners and loggers are OK, but others have a different view.

Therefore, finding the right mix for an investor's preferences that picks up the positive screens, e.g. developer of wind energy, and has the right mix of negative screens, no child labour or nuclear energy, is very challenging.

Secondly whilst the investment managers are definitely taking more notice, the current investment structures and ratings systems, upon which we rely to find the right solution for individual clients, is still in its early stages of development.

Nevertheless, we are working hard at the moment to build a portfolio of possible solutions that will be valued by an increasing number of our clients and many other investors. We'll have more on this issue in the future.

Where to next?

Whilst the current medical crisis dominates the headlines there are many longer term issues that we think will impact our clients and we are strongly focused on navigating these choppy waters ahead to ensure that we protect capital, preserve lifestyle and provide our clients with the kind of life they have always wanted and that they deserve.

Longer term success cannot be knowing exactly what the future holds as this is not realistic nor practical.

Longer term success however is being aware of the opportunities, as well as the risks and seeking to ensure the correct balance is maintained and to ensure that discipline, rigour and care are maintained in the stewardship of your investment capital.

Please contact as at the office if you have any questions.

If you would like to discuss this paper or any other matter, please do not hesitate to contact us at support@lifestylewealth.com.au or (02) 9984 7774.

Kind Regards

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