Firstlinks
a Morningstar company

Edition 489, 23 December 2022

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Editorial

I was talking with a work colleague this week and we were consoling each other about the performance of our personal investment portfolios this year. He mentioned that he regretted not partially selling stocks he held at the start of the year. He knew the stocks were overvalued but he liked them and put off selling anything. The market went down and by then it was too late.

My colleague's dilemma is common. It's often the investment decisions that we don't make which we come to regret the most. Why do we hold off making decisions, sometimes forever?

Let's first explore the science behind botulinum toxin, otherwise known as Botox, for some clues.

Botox and emotions

Originally developed to help people suffering from facial spasms, Botox has become one of the world's most popular cosmetic treatments. It works by paralyzing the nerves that cause the muscles in the face to contract.

In the early 1990s, researchers found that injecting the chemical into the frown lines between the eyes caused partial paralysis of the forehead - it reduced wrinkling. A scientist at Barnard College in New York, Joshua Ian Davis, wondered whether Botox could change a person's behaviour. If you immobilize part of the face, could that reduce the emotional experiences that you have?

The theory harkens back to the 19th century American philosopher and scientist, William James, who believed that thought and emotion didn't precede action, but followed it. James surmised that you didn't think and then act, but you acted and then formed a thought about that action. The same went for emotion.

Davis tested the theory on two groups of women. One group had just undergone Botox treatment, while the other group went for an alternative treatment that involved injecting a filler into the forehead. Both treatments sought to give a more youthful appearance, but only the Botox paralysed the facial muscles.

Davis asked the women to watch several video snippets: a serious documentary on Jackson Pollack, a humorous clip from America's funniest videos, and a stomach-churning video of a man eating live worms. After seeing the videos, Davis asked the women to rate how they felt. The women who'd undergone Botox reported less of an emotional reaction to the clips compared with the group who'd had filler treatment.

The conclusion? Immobility causes a loss in emotional experience.

The Zeigarnik effect

If actions can precede emotions, what about thoughts? In the 1920s, a young Russian psychology graduate, Bluma Zeigarnik, sought an answer.

One day, she was having tea with her university supervisor in a café in Vienna. The pair was watching how the waiters and customers behaved and noticed an interesting pattern. When a customer asked for the bill, the waiter could easily recall the food that the customer had ordered. But when a customer paid the bill, and then disputed the bill, the waiter struggled to remember anything about the order. It appeared that once a customer paid for the meal, it finalized the matter in the minds of the waiter and the details of the order were erased from their memory.

Zeigarnik went back to the laboratory to test the idea. She asked people to do a set of simple tasks, such as putting toys into a box and stacking wooden boxes. On occasion though, she stopped the participants before they had finished the task. As she'd observed with the waiters, Zeigarnik found that the unfinished tasks stuck in people's minds and were easier for them to remember.

Zeigarnik concluded that starting an activity causes a type of mental anxiety. Once you finish a task, your mind has a sense of relief and the task is quickly forgotten. But if you don't complete an activity, for whatever reason, then your mind nags at you until you finish what you've started.

Fixing procrastination

What has Zeigarnik's experiments got to do with procrastination? Procrastination often happens because you become overwhelmed by the size of a task. Zeigarnik's research suggests that if you just start an activity, your mind will be anxious to complete that activity.

Going back to my work colleague's regrets about his investment portfolio, he would've been better off starting the sale of his stocks, even in small increments. That way, he'd have been more likely to complete the sales, rather than putting them off.

This technique to overcome procrastination can apply to other investment decisions:

- Do you want to take advantage of the higher deposit rates now offered by smaller banks compared with larger banks? Then start an application for a deposit account with one of these smaller banks.
- Do you want to take advantage of the market downturn to buy a blue-chip company? Start by buying a small portion of what you intend to buy.
- Do you want to buy a market ETF but you're afraid that a market downturn may be around the corner? Then, buy a small position in the ETF, or buy equal portions each month over a 6 or 12-month period. The latter is known as dollar-cost averaging and it's a smart way to overcome procrastination and the fears and anxieties which often come with it.

In this week's edition ...

After a 2022 to forget, what will 2023 bring? **Bill Evans** thinks inflation will prove sticky in Australia and interest rates will rise in the first half of the year before plateauing in the second half. He sees rate cuts beginning in 2024 as the economy stalls and unemployment rises.

Robert Almeida predicts inflation will fall sooner than what Bill does, and that's good news for fixed income. It won't be as good for stocks though as it'll bring a long overdue profit margin reset.

Australian Ethical's **John Woods** agrees with Robert's views on inflation as all the key indicators he looks at suggest it's going to fall. He's also a bull on defensive assets such as bonds and infrastructure. These assets should help the portfolios of conservative investors such as retirees.

And in this week's white paper, **Fidelity International** offers its 2023 outlook for everything from the macroeconomic backdrop to all the key asset classes.

Meanwhile, **Meg Heffron** is back, and she has a bone to pick. She says that while the Labor government left SMSFs alone in the October budget, it might be a different story come next May's budget. Meg suspects there might be something designed to break up large SMSFs.

Shared equity mortgages have been talked about for years, but it's been left to governments to develop initiatives in this area. **John Kavanagh** reports that things changed this year.

Alex Pollak of Loftus Peak says streaming is disrupting the way TV is consumed and it's likely that all TV will be streamed within ten years. Alex believes Netflix, irrespective of the naysayers, remains the only game in town when it comes to profitably running a streaming service.

Finally, in the spirit of reflection at this time of year, we reprise Graham Hand's 2021 article on collectibles. Recently, the collector featured in the story, John Quick, had this to say:

> *"Dear reader, I still cannot believe the generosity of Graham and often go back and follow the stories of other collectors. I have been very fortunate that I have had quite a few collections gifted to me since this article was printed. Collecting offers so many positives including meeting like mind people who share the passion.*
>
> *Not everything is about money. I still get a buzz from finding that elusive card or two which has been sent to me by people who are down sizing or have simply lost the interest and passion of collecting.*
>
> *Of course, there are many who are no longer with us but there are still people out there who go to the trouble to seek out collectors and move collections on. Better to move things on than to see them go into land fill.*
>
> *Happy collecting to all you collectors out there Cheers......John"*

Merry Christmas everyone and thank you for supporting *Firstlinks*.

James Gruber

2023: a tale of two halves

Bill Evans

The Reserve Bank Board lifted the cash rate by 0.25% at its December meeting.

Markets were convinced that the Governor would soften his guidance with a weaker tightening bias. In the event he maintained the guidance used in the last two meetings, that "the Board expects to increase rates further in the period ahead" although adding "but is not on a pre-set course." That term has been used in previous communications and does not detract from the interpretation that the statement carries a strong tightening bias.

Central banks to remain resolute on inflation fight in 2023

Despite market pricing now only anticipating around a 50% chance that the cash rate will reach our target of 3.85% from the current 3.1% by May, we confirm that forecast.

Forces we expect will require that higher rate by May include evidence of very high inflation prints for both the December and March quarters. Our current forecasts are: 7.5% for the December quarter (6.7% underlying) and 6.6% for the March quarter (6.5% underlying).

While these numbers indicate that inflation is slowing, mainly because of easing supply side pressures, the Board will be cautious given that wage increases will be intensifying in the first half of 2023 and some components of inflation – particularly services – will remain a challenge while the need to anchor inflationary expectations in the face of such high inflation prints will be ongoing.

Convincing evidence that wages are lifting quickly will also be apparent by the May meeting with wages growth on the way to a 4.5% peak by the June quarter. Only the December quarter Wage Price Index report will be available by the May meeting – and is expected to show a forecast 3.6%yr gain up from 3.1%yr in September – but this will be enough to unnerve authorities given anecdotal evidence of ongoing pressures and still historically low unemployment.

Meanwhile the Australian economy is likely to be showing only a modest slowing. There will be some initial resilience for consumers – spending growth is expected to run at a 2% annualised pace in the first half of the year, down from 4% annualised in the second half of 2022 but still running at a reasonable pace. The unemployment rate is forecast to still be holding near 50-year lows by March. We have also been surprised by the strong recent recovery in population growth and the surge in jobs growth in October and November which will provide some added growth support.

So the May Board meeting will see the Board confronted with inflation in the 6–7% range; an unemployment rate near 50-year lows; clear evidence of rising wage pressures and a degree of uncertainty about how long restrictive policy will be required in the US and other major developed markets.

The situation will turn more decisively from mid-year. Consumer spending is expected to stagnate in the second half of 2023; the unemployment rate will edge higher; and inflation pressures will continue to ease, providing RBA with some comfort that the inflation rate can eventually return to the target band.

This scenario is consistent with the RBA going on hold through the second half while making it clear that rates are unlikely to be eased in 2023. Markets are currently flirting with around a 50% chance of a further rate hike in the second half of 2023 to be followed by a rate cut later in 2023 – in our view both prospects, which imply a very skittish approach to policy, appear to be unlikely.

Sustained policy easing in 2024

As we move into 2024, ongoing evidence of a stalling economy and rising unemployment, coupled with a slowdown in wage pressures and the inflation rate edging back towards 3%, will allow the RBA to begin to cut the cash rate back towards the 'neutral zone' which we believe is 2.5–3.0%. We anticipate around 100bps of cuts in 2024 from the March quarter pushing the cash rate to 2.85% by year's end.

Central banks will be tentative in running policy on the basis of forecasts given their recent disappointing forecasting records. But we believe that by 2024 even the RBA will feel sufficiently confident to move away from the clear contractionary stance of policy. It will still be dealing with inflation rates running above the 2–3% band (3.9% headline; 3.6% underlying by end 2023) but a move into the band will be more clearly within sight, particularly with unemployment rising and wages growth easing.

The policy objective will shift from fighting inflation towards providing relief for a stagnating economy in the context of existing restrictive policy.

That profile for the RBA will be close to that of the FOMC – we expect the fed funds to be lifted in January and March 2023, before going on hold for the remainder of 2023 despite nearly two years of an economy that is near stall speed.

That policy will be seen to be needed to ensure that the decline in inflation is sustained into 2024. With this achieved, the Fed is expected to also pivot to responding to the stalled economy, providing extensive rate cuts in 2024. Note that the latest FOMC forecast 'dots' show 100bp of rate cuts in 2024 despite the inflation target (PCE inflation) only slowing to 3.1% by end 2023.

We are anticipating an even lower inflation rate by end 2023 and lower outcomes in 2024 that allow for more extensive rate cuts during that year – in the order of 200bps.

Key risk is inflation stickiness around wages and services

But there may be some stickiness in inflation in both economies initially, presenting a clear risk to market pricing, which is currently anticipating FOMC and RBA rate cuts in the second half of 2023.

If inflation is slower to fall the FOMC, in particular with a more ambitious inflation target, will need to signal its strong commitment to lowering inflation permanently, delaying rate relief – the task of bringing inflation below 3% might prove much tougher than moving it from 8% to 4%.

That task will be closely aligned with the progress in slowing wages growth. While there is evidence of slowing inflation for goods prices and even shelter costs, it is apparent that stubbornly high wages growth is holding up inflation in the core services sector. The risks are that the challenge of reining in wage-driven service sector inflation may be much more difficult than we are anticipating.

In our view the issue for both RBA and FOMC in this inflation fight is around wages and the direct link to services inflation. Goods inflation pressures are easing as supply chains are being restored and demand is slowing. But wages growth is increasing in Australia and remains elevated in the US due to record labour shortages. Even though Australia does not have a labour participation problem like the US, COVID disruptions and restricted immigration are affecting labour supply in both countries.

Greater momentum in wages growth than we currently envisage that would stem from rising inflationary expectations represents the dominant risk to our central cases.

Markets again pre-empting shifts

The key theme which we promoted through most of 2022 was that 2023 was going to be the year when bond rates would fall and the appetite for the USD would wane. We had thought US 10-year Treasuries would fall towards 3.2% by end 2023 from the 4% starting point by end 2022, while the AUD would lift from USD0.65 to USD0.72 in 2023.

We did not sufficiently count on the propensity for markets to be pre-emptive. Once the headline inflation rate in the US appeared to peak markets factored in a lower terminal federal funds rate – a rational response to the sustained expected weakness in the US economy – and this move spread to Australia.

Those anticipated falls in bond rates and increased aversion to the USD, including support for the AUD, were partially brought forward to the final quarter of 2022.

We have only made a slight reduction in the end 2023 target rate for US 10-year bonds, from 3.2% to 3.1%, with the fall from 4% + occurring more in late 2022 than 2023.

With the AUD now expected to finish the year at USD0.68 rather than USD0.65 we have revised up our end 2023 forecast from USD0.72 to USD0.74.

Conclusion

The risks to these scenarios are evenly balanced. The supply side drag on inflation could overwhelm the lingering demand side, mainly represented by rising wages and bold pricing policies from businesses, to yield a much faster slowdown in inflation in both the US and Australia than we are factoring in. That would open up the possibility of earlier rate cuts in both markets than we currently envisage.

On the other hand, the supply side drag may prove to be unsustained while demand pressures build and inflationary expectations become entrenched. That would raise the unsavoury prospect of an extended round of rate hikes in both economies during the stagnation in the second half of 2023.

That fear of stagflation should motivate both the FOMC and the RBA to err on the side of higher rates in the near term and to remain resolute in keeping rates on hold in 2023.

In summary, we see 2023 as a year when inflation falls; economies stall; central banks continue to tighten decisively in the first half; are on hold by mid-year; and remain resolute through the remainder of the year.

That will lay the platform for an extension of the falling inflation in 2024 and the conditions for sustained policy easing.

Compared to our central scenario, markets are too dovish on the RBA in the first half of 2023; too ambitious around the timing of rate cuts both by the RBA and FOMC later in 2023; and too cautious around the extent of rate cuts in 2024.

Bill Evans is the Chief Economist at Westpac. This material contains general commentary only and is not intended to constitute or be relied upon as personal financial advice. This information has been prepared without taking account of your objectives, financial situation or needs. The forecasts given above are predictive in character and whilst every effort has been taken to ensure that the assumptions on which the forecasts are based are reasonable, the forecasts may be affected by incorrect assumptions or by known or unknown risks and uncertainties. The results ultimately achieved may differ substantially from these forecasts.

Download the full report 'Market themes for 2023 and 2024' (PDF 47KB)

Meg on SMSFs: Would a limit on fund or balance sizes make sense?

Meg Heffron

In a monthly column to assist trustees, specialist Meg Heffron explores major issues relating to managing your SMSF.

Nothing bad happened to super in the October 2022 Federal Budget despite many predictions about possible changes to tax laws, limiting funds to $5 million and the like.

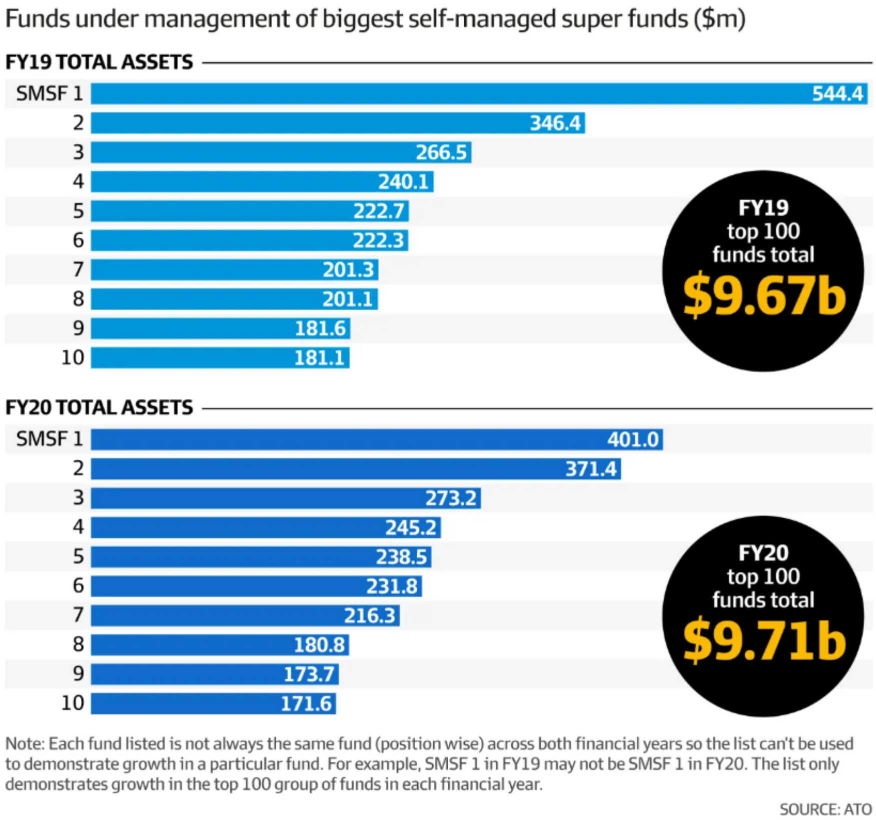
But the fact that those things didn't change in October doesn't mean they won't be on the agenda in May 2023. It seems to me that most new governments treat their first budget as an opportunity to exclaim with horror that the cupboard is bare so "tough decisions will need to be made" and lock in some funding for their top election commitments. Everything else gets left for the next budget so they can enjoy their honeymoon period.

That means we should be thinking ahead to May 2023 – what's likely then?

Might that be the time when we see something designed to break up very large SMSFs gain some traction? What could that look like?

Who would be impacted?

There are certainly some enormous SMSFs. For example, in August 2022, the AFR quoted values for Australia's three largest SMSFs as $401 million, $371.4 million and $273.2 million. And 32 SMSFs had more than $100 million. That's some very large funds.



Using the latest ATO statistics (which are based on returns for the 2019-20 financial year), there are very roughly 600 funds that have more than $20 million. Since most SMSFs have two members, that's $10 million each. Again, a lot of money.

And all the investment income earned by those funds is being taxed at 15% (at most). Presumably the people who belong to these very large funds would pay much more tax if they had to take their money out of super. So not surprisingly, there are loud calls for us (as a community) to spend less money on providing generous tax concessions to people in this position.

But is the answer a hard limit on size? I'm not sure that's a great plan.

For a start, if there is a limit at all it should be at a member level – not a fund level. So a fund with twice as many people should be allowed to be twice as large. And obviously it should apply to all super funds, not just SMSFs. Even with those adjustments, is a hard limit on member balances the way to go?

There are a couple of reasons I favour an alternative – and I'll explain one shortly.

Eventual demise of extremely large funds

Let's remember that this isn't necessarily a long-term problem in any case. A few factors will drive these very large funds to dissolve of their own accord in time.

The one thing that forces all of us to take money out of super eventually is death. For the majority of people who die, the only amount of their super that can stay in their fund is whatever their spouse is able to take as a pension. If he / she can't take it all as a pension it has to come out of the fund as a lump sum. And this is where the $1.7 million transfer balance cap plays a role – it limits the amount that can be taken as a pension, indirectly forcing money out of super whenever someone with a large balance dies.

These days, there is a limit on virtually every type of super contribution that can be made (personal injury settlements are the one exception – and I expect no-one would begrudge someone creating a $10 million SMSF if they received $10 million in a compensation payment for a terrible injury). In short, these days it's virtually impossible to put enough money into super to grow a balance to the current dizzying heights of these very large funds. That means most of these very large funds have probably been around for a long time and perhaps have members who are getting older.

So here's my first hypothesis – I bet a lot of these large funds have two members and both are in their 70s – 80s. As soon as one of them dies, the fund value will fall dramatically. And that's without any change in the law.

And my second hypothesis – the rest of us stand no chance of getting there because we won't be able to put enough into super to make it happen. I wouldn't be at all surprised if we see the number of funds with balances in excess of $20 million fall dramatically in the next 10 years but the number with $1 million - $5 million increase as those in their 40s and 50s approach retirement. We've had the benefit of compulsory super for most of our working lifetimes but by the time we were able to really focus on our retirement savings, contributions were very tightly controlled.

Is change really needed?

So, is this a problem worth compromising the current simplicity for or will it go away on its own?

If your view is still firmly in the 'reign in tax concessions for the wealthy', I wonder if there are better alternatives than a hard balance cap.

There was a time (before 2007) when it was compulsory to start taking money out of super at a certain age – for most people it was 65 (a little later for people who were still working but let's work with 65). At that point it was compulsory to turn all of one's super balance into a pension or take it out of the fund entirely. Funnily enough, removing this rule (called "compulsory cashing") back in 2007 is probably one of the things that has allowed these mega funds to stick around for so long – there's simply no requirement to take the money out before death anymore.

What if we went back to some form of compulsory cashing and it became compulsory for everyone to start drawing down on super at some point?

The challenge these days would be that there's only so much anyone can move into a pension (the transfer balance cap strikes again). And I'm not an advocate of forcing everyone with more than $1.7 million to take every other dollar of their super out as a lump sum immediately. Imagine the potential for investment chaos, fire sales of assets etc.

Rather, what if we had a second class of pension that didn't get all the same great tax perks as a modern day "retirement phase pension" but with no limit on size? Perhaps the investment earnings on the money in these pensions could still be taxed as if the money was in accumulation phase – whereas no tax is paid when money is in a retirement phase pension? In fact, we already have a pension that works this way – transition to retirement pensions for people who are under 65 and haven't yet retired.

Or perhaps the earnings on money in these pensions could be taxed at an even higher rate than 15%? Or perhaps the drawdown rates could be higher, so the balance is forced out of super faster than a traditional pension. I'm sure we could be imaginative here.

The key is that something along these lines would force all who hit the magic age to start drawing down on their super in some way. But they could do so steadily over time rather than all at once.

It would also mean we're not imposing arbitrary limits on balance sizes – any government that does this can expect immediate challenges. There will be calls for leniency in times when markets are volatile (… all the time), protests of unfairness for those who cashed out large super balances only to see their assets plummet in falling markets. There would no doubt be calls for the change to be phased in over time or for some members to be specifically excluded from it (known as 'grandfathering'). And these requests would be reasonable – those with large super funds have grown them legally, they've made long-term decisions about investments and tax. It would be unreasonable for them to be told to change everything 'tomorrow'.

There will be (perhaps rightfully) cries that the ASX and our property markets will be decimated by large SMSFs offloading millions of dollars as they cash out their members' benefits. Over the long term, will there be an incentive to invest more conservatively? And there are no doubt many others I haven't thought of.

None of that sounds like a great result even in the interests of spending less on tax concessions for people who clearly don't need them.

One final point – both this government and the previous one have wittered about formally documenting a purpose for superannuation. In all my thinking about what our future state should look like, I've assumed that when someone eventually does that, the purpose will be in line with my particular paradigm (super is for saving for retirement but should result in money coming back out again during the member's lifetime). No matter what the purpose ends up being, our next steps should be guided by it rather than just a knee jerk desire to take something from wealthy people.

Meg Heffron is the Managing Director of Heffron SMSF Solutions, a sponsor of Firstlinks. This is general information only and it does not constitute any recommendation or advice. It does not consider any personal circumstances and is based on an understanding of relevant rules and legislation at the time of writing.

To view Heffron's latest SMSF Trustee webinar, 'Super contributions unpacked', click here (requires name and email address to view). For more articles and papers from Heffron, please click here.

The impact of inflation on retirement incomes

John Woods, Maria Loyez

This is an edited transcript of an interview that Australian Ethical's Head of Asset Allocation, John Woods, did with colleague, Maria Loyez.

Maria Loyez: Tell us a little bit about the market and the economic backdrop.

John Woods: Look, 2022 has been a volatile market. I'd describe the world at the moment as fragile. Markets are beginning to be positioned more constructively after the shocks we experienced in the first half. If you look at the market pricing of key indicators like inflation, it implies that it will become more under control, that central bank policy will be effective in bringing it down to within expected ranges. And that's echoed when we look more broadly as well in areas like agriculture prices and commodity prices. So, if you take wheat futures or something like that, it will also show a downward sloping price for the future as well.

Loyez: Inflation has been one of the biggest talking points of 2022. Do you want to talk about what your view is on that and what the implications are for investors?

Woods: Inflation should be a central theme in investment through time. It's the most important variable in retirees achieving the standard of living that they're anticipating. And 2022 has really seen the regime that we were in pre-pandemic change. That regime that we were in was catalyzed by a period of QE, of disinflation coming from China, and the market was always worried that after a period of such unorthodox monetary policy that inflation could emerge. And as we saw the supply shock to energy prices and broader commodities at the start of the year, inflation accelerated rapidly. And now, we're in a period of high, volatile inflation. But if we look at indicators from the market that try and look forward from today, such as the TIPS and agriculture prices, both are sloping downwards and suggest that the action that central banks have been taking over the last six months to raise rates rapidly almost at an unprecedented level are beginning to have an impact.

Loyez: Potentially some good news for the future.

Woods: The market is positioned constructively for 2023. There are a number of risks to that. If we look back at history, the Fed - only one time in the last 11 have they been successful in engineering a soft landing. But [Jerome] Powell has all the lessons of his predecessors in the past to look back on. So, he will be cognizant of the mistakes they made.

Loyez: That sounds like good news generally. Is that changing your long-term view of assets and how they might perform over time?

Woods: It is. I mean, inflation is the single most important variable in understanding your retirement outcome. Our multi-asset funds are designed to exceed inflation. And the tools that we can use to deliver inflation-plus returns in moderate inflation environments, like some of the defensive assets - bonds, infrastructure - they're becoming more important part of our allocation from here.

Loyez: You talked about multi-asset funds. Along with asset allocation you look after multi-asset funds as well, because they go hand-in-hand.

Woods: That's right.

Loyez: Can you talk to us a bit about the performance of the multi-asset funds this year?

Woods: The managed funds we have on offer – the Balanced Fund, the High Growth Fund – the first half of the year was really impacted by the energy crisis, the panicked moments we had as parts of Europe and the rest of the world focused really on prioritizing energy security over energy transition. We saw oil up over $100, nearly $120, through that period. And we don't invest in fossil fuel companies. So, that was a significant headwind to our performance.

Source: Trading Economics

In the second half of the year, we start to see longer-term trends emerge. So, there's still headwinds from rising rates, but that commodity shock has abated, and our performance has started to catch up a little bit and start to exceed benchmarks again through the second half of the year.

We have a very long-term focus but it's pleasing to see that some of the trends we were invested in prior are coming back to the fore through the later part of the year.

Loyez: Well, that sounds promising. So, those funds also include unlisted assets.

Woods: Yeah.

Loyez: They're probably some of the most interesting stories. Do you have any favorites that you're looking at?

Woods: Unlisted assets have a really important role in multi-asset portfolios, particularly for an ethical investor. That's how we get a lot of our diversification is focusing on assets that we can't obtain in public markets because we can go deeper into the broader range of private assets.

Favorites at the moment – look, we're invested in a fund that's affiliated with the CSIRO. They've been doing some really good work with early-stage capital, so venture capital. And I'm excited by a number of their projects. One that comes to mind is the investments they've been making in plastic recycling - breaking plastics down back to their original polymers so we can recycle them as much as possible.

And that's exciting for a number of reasons. One, the returns have been fantastic. And two, if you think about the impact that has - plastics are hard to abate use of fossil fuels because to-date they haven't been infinitely recyclable. But this is changing that narrative, so I'm really excited for what that could bring.

Loyez: Does that mean I'll no longer be stockpiling my soft plastics in the cupboard?

Woods: Hopefully.

Loyez: Are there any other unlisted assets that you are interested in?

Woods: This year we saw one of our first investments in way to abate carbon through natural capital. I think that was an exciting milestone for us, and there's a significant future in those assets, particularly as we begin to discern different types of ways to abate carbon.

Loyez: Just thinking about John Woods, your personal portfolio, how are you thinking about that at the moment and with the knowledge that you've got of the markets?

Woods: I think with a personal portfolio, it's important to identify a core strategy and stay committed to that, particularly for the bulk of your retirement savings.

I have a long-term investment horizon. One year doesn't change my view. I've identified my risk appetite through the volatility we've had over the last 10, 15 years. And I'm confident that the asset allocation I have in place will serve me well into the future. In an environment like this, it's tempting to respond to the news, but it's important to stay committed to your long-term strategy.

Loyez: And what are you most optimistic about for 2023 and beyond?

Woods: Beyond 2023, I am very optimistic about this energy transition. If I look back at some of the long-term metrics, looking at something like barrel of oil per GDP – it's been on a continual decline. The cost of energy for the world's population has been on a continual decline. And if I look at some of the trends in renewable energy in particular, it's possible that we could actually see an acceleration in that decline of energy costs. And what we can do with that is really exciting.

Maria Loyez is Chief Customer Officer and John Woods is Head of Asset Allocation at Australian Ethical, a sponsor of Firstlinks. This information is of a general nature and is not intended to provide you with financial advice or take into account your personal objectives, financial situation or needs.

This is an edited transcript of Maria and John's interview published 19 December 2022. View the original interview here.

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The return of shared equity mortgages

John Kavanagh

Shared equity mortgages, as a solution to Australia's housing affordability problem, have been talked about for years, but apart from a few failed commercial attempts it has been left to governments to develop initiatives in this area.

But this year things changed, with several financial institutions partnering with investment managers and fintechs to launch shared equity products. Product rollout is still in the early stages, so we are yet to see whether it will work this time.

Products launched or in-train

Groups launching or planning to launch shared equity products include:

- AMP Bank working with investment company Bricklet;
- Home Owners' Partnering Equity (HOPE) working with Police Bank and possibly other lenders;
- mortgage insurer Genworth and shared equity deposit bond developer OSQO;
- FrontYa; and
- OwnHome

AMP's shared equity partner Bricklet was founded three years ago and has been working with property developers Mirvac and Stockland to develop a shared equity service for property investors. Its partnership with AMP is its first move into the owner occupier market.

It has funding from two private funds owned by high-net-worth investors. Under the arrangement with AMP, the funds will acquire 20-30% of the equity in the property, allowing the bank to lend at a loan-to-valuation ratio of 80% or less and not charge lenders mortgage insurance.

Bricklet chief executive Darren Younger said the investors would expect to hold their equity for five to 10 years, at which time the borrower would be expected to refinance and pay them out (the homeowner can buy out the equity investor at any time).

Investors will receive an annual fee of 6% of the value of their investment in the property and any capital gain on sale of their equity.

Younger said Bricklet would pre-approve home buyers with as little as A$20,000 of savings.

AMP Bank group executive Sean O'Malley said the bank was targeting borrowers with appropriate income to service the loan but who don't have a deposit. The product is not designed for social housing purposes.

HOPE launched a shared equity scheme this year, announcing that it had raised A$30 million of investor funds. The HOPE scheme will co-invest up to 50% of a mortgage and is designed for essential workers such as teachers, police and nurses.

In November, its initial partner Police Bank settled its first loans under the scheme.

Mortgage insurer Genworth has invested in OSQO, a start-up that hopes to fill home buyers' deposit gaps. OSQO is developing a platform that raises funds from a range of sources, including private investors, to provide home buyers with a 'shared equity deposit bond' to fund a deposit.

OSQO will pay investors quarterly interest at prevailing mortgage rates, which is passed through from the home buyers, and advise home buyers on the best time to refinance and pay out their OSQO finance.

It claims its fees will be cheaper than the cost of lenders mortgage insurance would be if the borrowers took out a loan with a loan-to-valuation ratio over 80%.

Genworth chief executive Pauline Blight-Johnson said she hopes to have an OSQO product in the market next year.

FrontYa, which was launched last year, offers to double a home buyer's deposit with a contribution of up to $250,000 for approved properties. The funding is for six years and FrontYa will take 25% of the property's capital appreciation over that time.

If there is no increase in value, the property owner is only required to repay the deposit funding. The company is yet to provide any details of partnerships with enders of its business activity.

OwnHome, which was launched last year, offers a variation on the shared equity theme. It will buy the property for customers, who enter a lease agreement and an option agreement.

The option to buy the property from OwnHome can be exercised any time from year three to year seven. The price will be the OwnHome purchase cost plus an increase of 3.8% a year. Each year, 2.5% of the monthly lease payments go to "purchase credits".

OwnHome does a serviceability assessment of the customer to determine what the price of the property will be and then allows the customer to choose a property in that price range. OwnHome will be the title holder until the option is exercised.

And in another variation, BankFirst has a Shared Equity Agreement that supports parents or other family members who contribute money towards a deposit. The formal agreement protects the contributor's interest if circumstances change and they need the money back.

John Kavanagh is Associate Editor of Banking Day. This article is republished with permission.

Beware the hit to earnings in 2023

Robert M. Almeida

Volatility in financial markets happens when participants are faced with new information that runs counter to prior assumptions. This year, the mistaken assumption was inflation, which has proved far more problematic than central bankers and investors expected.

The gyrations across equity and fixed income asset classes in 2022 can be almost entirely traced back to inflation, interest rate levels, and expectations for each. This year, whether it was stocks or bonds, the longer the duration an asset had, the worse it performed. This is important to consider as we set return expectations looking ahead to 2023.

Peak inflation? Probably

In recent weeks, after markets were presented with data that pointed to a potential inflation peak, risk assets rallied, led by longer duration stocks and bonds. While only time will tell if we've hit the inflation high-water mark or not, the combination of base effects, the tightening pace of financial conditions, and rising recession odds will likely decelerate inflationary pressures in 2023.

However, not unlike how investors underestimated inflation, I believe they may be underestimating its impact on corporate profits. While falling inflation may prove beneficial for bonds, it could still prove problematic for profits and consequently stock prices.

Fading wealth effect, rising costs

As economies re-opened in 2021 and consumers were brimming with spending power due to government transfer payments, economic growth and corporate revenues skyrocketed, achieving double-digit growth rates.

Corporate revenues can be broken down into units and price. The number of units sold and at what price combine to produce revenues. Not only was unit growth strong, but more notable were prices paid, as evidenced by four-decade high inflation. While corporate input costs were rising, they were matched (or exceeded) by higher prices of goods and services sold, protecting profit margins.

During inflation booms, companies generally raise prices on the back of a positive wealth effect. Rising values for financial assets, used cars, homes, etc., combined in this episode with very high savings and rising wages, to generate significant pricing power for corporations. This cycle was typical for a high inflation period. However, what is also typical is what happens when inflation recedes.

Pricing power during inflationary booms, like the one we just experienced, tend to be ephemeral. For pricing power to be sustained, it must be accompanied by value-add. And that hasn't occurred over the past year.

As the wealth effect fades due to falling financial asset prices and increasing investor anxiety, consumer behavior changes. And we have already seen signs of it. This earnings season, operating results from some US retailers show that consumers have begun trading down and prioritizing necessities, such as food, over non-essentials. Inflation usually peaks when consumers' capacity to spend cannot meet the price at the checkout counter.

Falling inflation may potentially lead to higher equity multiples because long-term interest rates may have peaked (and that is good for long duration bonds). Though in my view, investors are underappreciating the drag on profits from falling prices.

Will history repeat?

Profits are a function of revenues and costs. While revenues are likely to decelerate with the economy and inflation, costs typically don't recede as quickly and the earnings cycle ends. We believe history will repeat, and here's why:

- While some companies have announced job cuts, most notably in the technology sector where customer demand is softening, there remains an overall labor shortage combined with a skills mismatch between available workers and the high-skilled jobs that remain unfilled. This should result in sustained elevated labor costs.

- The second cost input is capital. Following the global financial crisis, central banks made sure capital was both abundant and cheap. While inflation may recede some, it's not likely to fall to pre-covid levels due to structural dynamics at play such as an aging population with more consumers and fewer producers and significant increased capital investment by businesses seeking to decarbonize.

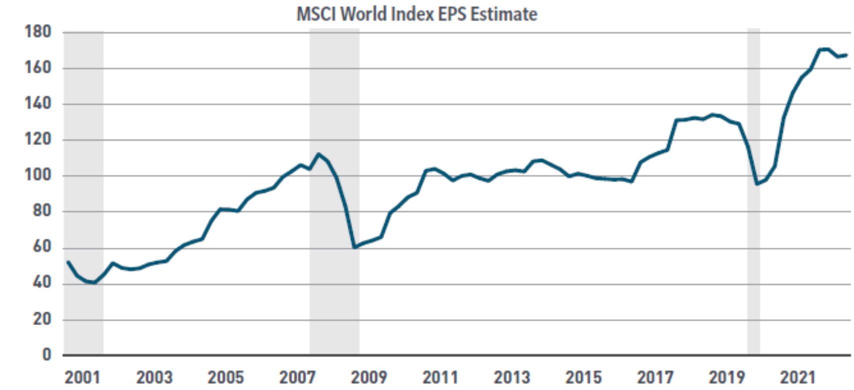
- While inflation and revenues are likely to recede in 2023, they will do so at speeds much faster than input costs. The result will be a lower profit margin regime than the all-time highs observed over the past several years and I don't think this is yet reflected in asset prices.

Unrealistic expectations

Exhibit 1 shows analysts' global earnings expectations over the past several decades. Historically, in recessionary periods, profit margins plummet. But as the data show, analysts' earnings estimates have slipped, but not by much.

The reasons, I suspect, are simple. Analysts tend to follow corporate guidance. And while companies are increasingly recognizing weakening end-demand, they're also telling investors that they can reduce costs while sustaining historically high margins. But we have our doubts.

Exhibit 1: Earnings estimates remain elevated



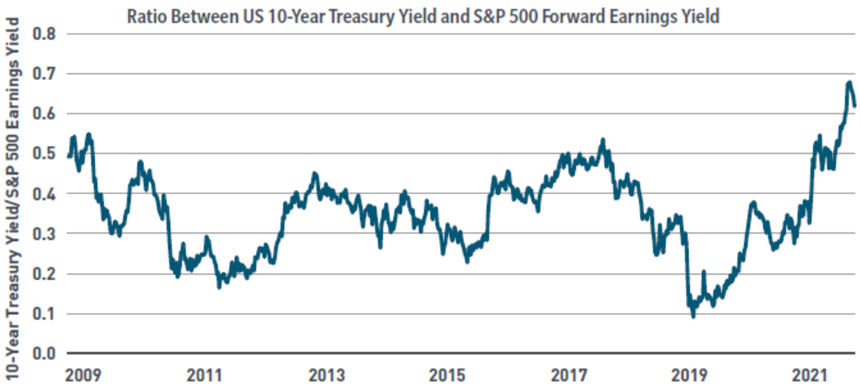
Source: Bloomberg, as of 25 November 2022. Areas in gray = recessions.

However, some companies will be able to sustain higher margins because they sell a good or service that's highly valued by their customers. But the reality is that the majority will not. And those most at risk are companies with high and/or inflexible fixed costs and needing to increase capital expenditures to decarbonize amid a higher interest rate, falling inflation, weakening demand, environment.

What we expect for 2023

- While inflation should decelerate but remain elevated relative to the pre-pandemic period, the slowdown should prove a tailwind for select bonds, particularly high-quality sovereigns, municipalities and investment-grade issues. And relative to equities, bonds haven't been this cheap in over a decade. The chart below illustrates the ratio between the yield offered by the US 10-year Treasury and the 12-month forward earnings yield on the S&P 500.

Exhibit 2: Relative to stocks, bonds look cheap



Source: FactSet. Weekly data from 4 December 2009 to 2 December 2022. S&P 500 Forward Earnings Yield is calculated as 1 divided by next-twelve-months price to earnings ratio.

- Decelerating inflation is good for fixed income but will likely halt this earnings cycle and bring a long overdue profit margin reset. But not for all.

- Companies with uncompetitive products or services facing elevated capital costs and mandatory capital investments will be most at risk. Softer, but still relatively higher inflation compared with the post-GFC period will likely preclude financial bailouts and a return to unnaturally low interest rate regimes. These assets will become stranded.

- Conversely, while investors may find that even well-run companies have some, albeit small, level of margin reset, the opportunity to grow market share and take greater ownerships of profit pools will lead to even better operating performance over the long-term. The coming inflation slowdown and margin recession will create a new and positive earnings cycle for enterprises with a demonstrable value proposition and an ability to out-earn their natural cost of capital. And I am wildly excited about that.

Robert M. Almeida is a Global Investment Strategist and Portfolio Manager at [MFS Investment Management](). This article is for general informational purposes only and should not be considered investment advice or a recommendation to invest in any security or to adopt any investment strategy. Comments, opinions and analysis are rendered as of the date given and may change without notice due to market conditions and other factors. This article is issued in Australia by MFS International Australia Pty Ltd (ABN 68 607 579 537, AFSL 485343), a sponsor of Firstlinks.

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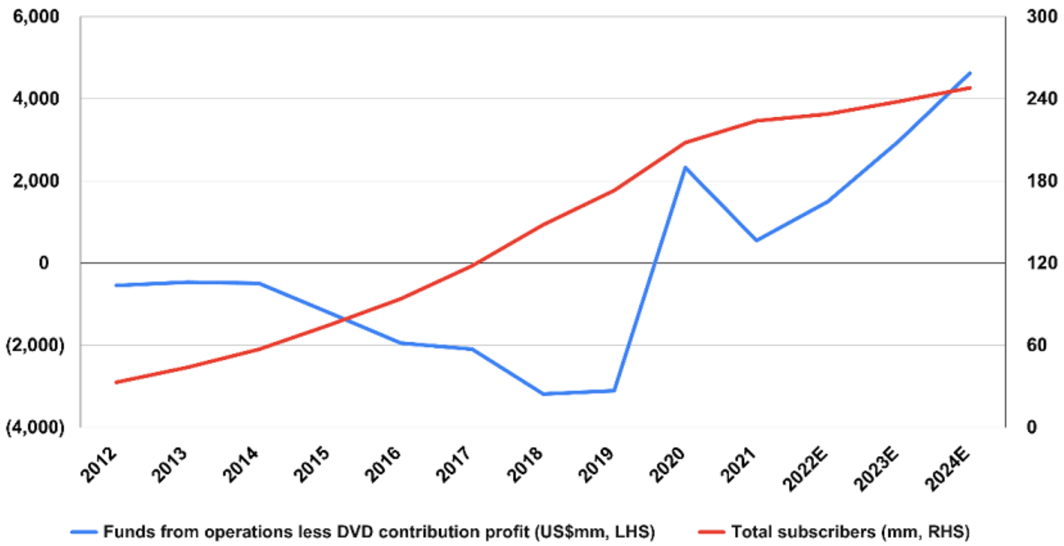
Why Netflix is winning the streaming wars

Alex Pollak

"The mechanisms for the monetization of content are in disarray." - US Cable-TV veteran James Dolan

Streaming is disrupting the way TV is consumed and further changes are imminent - it is likely that all TV will be streamed within ten years. The chart below shows how Netflix only succeeded when total subscribers exceeded 175 million across the world, generating a US$5 billion turnaround to record funds from operations (excluding DVD profit) of over US$2 billion in 2020.

Netflix subscribers vs profitability



Source: Company Reports, Morgan Stanley

Netflix, irrespective of the naysayers, remains the only game in town when it comes to profitably running a streaming service. The company is not in losses, either cash or accounting, and will generate around US$11 of earnings per share this year. This is after expensing US$14 billion on movies and TV, likely the same next year. This content spending and library represent a moat which will be hard to breach. Its decision to move into advertising looks set to further underwrite profit growth.

Why Murdoch got out of movies and TV, and why Disney is struggling

Having seen Netflix succeed, permanently disrupting the business model, traditional media companies such as Disney, Paramount and Warner Bros Discovery followed. All are facing crises.

Entertainment is a scale business, so when no less an operator than Rupert Murdoch realised his film and TV business was sub-scale, he abruptly sold the company, 20th Century Fox. Murdoch had seen this film before: while attempting to build his News Corporation into a company worth US$50 billion, Google and Facebook managed to create businesses that were 10 times more valuable in a fraction of the time - at the direct expense of Murdoch's News Corp/Fox.

Murdoch made the smartest business decision of his life and sold. Disney bought.

The merged Disney Fox last month filed a US$1.5 billion quarterly loss in its streaming service despite being over the magic 175 million subscribers, implying that something is very wrong with its cost structure. The reported results were so bad that the company fired its chief executive Bob Chapek and brought back the previous CEO Bob Iger.

As we noted of Disney's move into its own streaming service in 2019, to generate meaningful subscriber additions and hit scale the company would first have to remove its own content from rival cable and streaming platforms. This removal would hit hard the 41% of total revenues (US$24.5 billion in 2018 out of US$59.4 billion) and 42% of total operating income (US$6.6 billion of US$15.7 billion) the company generated from these businesses at the time.

In our 2019 article we said:

> *"Streaming will ultimately disrupt and supplant traditional free-to-air channel viewing globally, with the emergence of four or five players, like Disney+ and HBO, along with Netflix and maybe Apple, as the new majors. But [the] buyers who pushed the Disney stock price up 30% in the three-month lead-up to the announcement won't be the same as those who will be around to stomach the five years of grinding and significant losses the company will have to absorb, all with little clarity on the final success of the venture. For Disney, this may be a fairy tale ending, but the plot calls for some very dark times first."*

This cable-streaming balancing act is being attempted by many other large legacy players, mostly without real success. Warner Bros Discovery (owner of HBO/CNN/Time Warner and maker of Game of Thrones) which last year changed hands for the second time in two years, is also struggling to get its streaming service into the black. So is Paramount, Peacock and even AMC, a cable TV major in the US which has been around for over 50 years (and is the maker of Breaking Bad and Mad Men, among many achievements).

Below is an extract from a memo to AMC employees by its chairman explaining the problem:

> *"Our industry has been under pressure from growing subscriber losses primarily due to cord cutting. At the same time we have seen the rise of direct to consumer streaming apps including our own AMC+. It was our belief that cord cutting losses would be offset by gains in streaming. This has not been the case."*
>
> *And then this stunning admission: "The mechanisms for the monetization of content are in disarray."*

Legacy players are racking up significant streaming losses

Selected Streaming Service EBITDA*	3Q22	2Q22	3Q21	TTM**	Subscribers (mm)
Netflix	1,770	1,812	1,921	6,543	223
Paramount	-343	-445	-198	-1,746	67
Peacock	-614	-467	-520	-2,096	15
Warner Bros. Discovery	-634	-558	-309	-2,574	92
Disney	-1,381	-972	-532	-3,649	236

*EBITDA = Earnings Before Interest, Tax, Depreciation and Amortisation, **TTM = Trailing Twelve Month
US$mm unless otherwise stated, data as at Calendar Year Q3 2022
Note: Disney DTC EBITDA losses assume ~$365M FY22 D&A

Source: Company Reports, LightShed Partners

Disruption, incentives and cost structures

Incentives and optimised cost structures are crucial in any business, and they help explain much of the success Netflix has had in streaming to date. The company does not have to decide whether or not content goes to cable, movie theatres or streaming (or in what order). It also doesn't have to make that choice while being held hostage by its capital structure - legacy players have *a lot* of debt and require linear network profits to service it.

Netflix will continue to benefit from the shift to streaming, especially as cord-cutting accelerates, and from other growth drivers like its password sharing and advertising initiatives. This will be revenue growth on top of its already profitable streaming model.

Meanwhile its competitors are still searching for a cost structure that works in streaming at the same time they experience structural declines in some of their largest and most profitable business segments (linear TV).

We don't believe the dark times are over for these legacy media players just yet.

Alex Pollak is Chief Investment Officer and Co-Founder of Loftus Peak. This article is for general information only and does not consider the circumstances of any individual. Loftus Peak Global Disruption Fund (ASX:LPGD) is available to investors on the ASX as an active Exchange Traded Managed Fund.

What to do when your collectibles become collapsibles

Graham Hand

The media loves the little-guy-made-good stories, where the comic book bought by a kid for a few cents is now worth thousands of dollars. If you had the foresight to buy and hold a 1950 VW Kombi with the prized 23 windows, you have not only enjoyed 70 years of driving (and repairing) but it may now fetch half a million dollars. A pair of Michael Jordan game-worn Nike sneakers recently sold for a sneaker record of US$615,000, while Star Wars action figures produced before 1985 can fetch up to $10,000.

These examples of how a few made a lot create an impression that almost anything old and 'collectible' will be bought by someone if the holder waits long enough.

But for every sought-after basketball card, there is a 'collector' Olympic pin nobody wants. For every vintage Super Mario video game, there is a 'collectible' photo of Shane Warne taking his 300th test wicket sitting idly on eBay. And don't think your collection of old first-day covers in a stamp album in the attic is a part of your retirement income strategy. With a few exceptions, there is little demand for most ordinary stamp collections as a check on eBay or Gumtree will confirm.

And then there is my once-valuable and loved mint collection of phonecards which only one person in Australia really wants, and that's not me. More on that later.

Yes, there are many success stories

In all bubbles and manias, popularity initially creates its own momentum. Buyers beget buyers, especially in an age of social media where minor celebrities can have a million followers. But they quickly move on, and so do their fans.

The reason stamp collecting has lost its lustre is that few people send stamped letters. Where once a letter covered in exotic stamps from an uncle or auntie living overseas drove enthusiasm for the hobby, now an email or text is received to celebrate a birthday. Most schools had stamp-collecting clubs which created a buzz, but it's now more likely to be a video game.

Collecting items goes in and out of fashion, and the secret to making money is to stay ahead of the wide adoption and not get caught when the excitement dies down. Two examples of products that have experienced a renaissance are Pokémon cards and Lego.

Pokémon cards from the late 1990s and early 2000s were originally exchanged in schools based on the successful Nintendo video game. It then died, but interest has been revived by leading YouTube influencers taking part in 'unboxings' of sealed cards. During COVID, people have more time to follow these celebrities and jump on the bandwagon. There is also a rumour that Pikachu, a Pokémon character, will be a mascot at the 2021 Tokyo Olympics.

In 2003, the Danish company, Lego, was struggling with massive debts and declining markets when it made a strategic change away from simple bricks for buildings into 'toys-to-life', where action figures relating to movies or games were issued in Lego sets. The most collectible sets are the early Star Wars editions, and an unopened Millennium Falcon from 2007, part of the Ultimate Collector's Series, can now fetch thousands of dollars. Many other Lego classics have also appreciated as part of the overall Lego revival, helped by the television programme, Lego Masters, which is a global hit and a big success in Australia.

Perhaps the most famous of all collectibles, at the point where significance and scarcity meet, is the 1938 Action Comic No. 1, featuring Superman's debut. There are only about 100 surviving copies, and in mint condition, it can fetch over US$3 million. As a sign of its appreciation, sales have been recorded for $US82,000 in 1992, $US150,000 in 1997 and US$2.2 million in 2011.

The rise and fall of the phonecard frenzy

Not all these stories end well financially, but most can end happily.

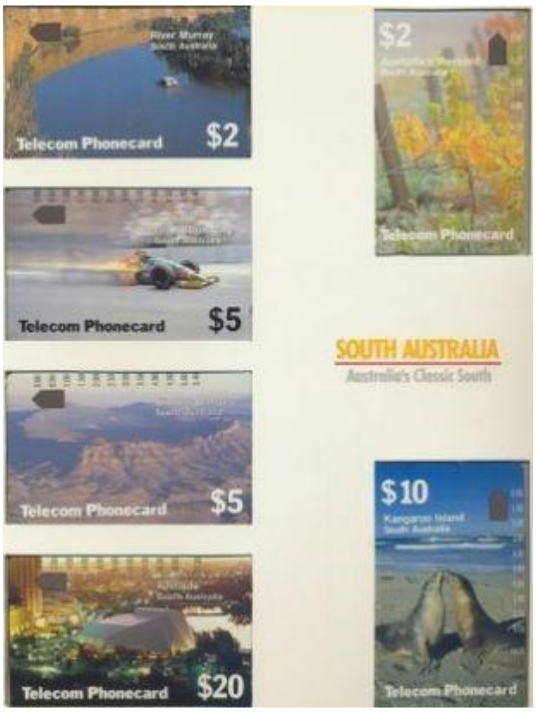
Telecom (now Telstra) began issuing phonecards to operate their public pay phones in 1989. This was pre mobile phones and while most people with homes had a landline, pay phones on the street were still popular. Some people could not afford their own phone, while renters did not bother with a connection, and it was common to see queues at pay phones as people waited impatiently for others to finish.

Telecom issued standard, plain phonecards with their simple logo and prepaid values up to $50, but soon realised collectors would be far more interested in editions and series with different themes. Thousands of people started collecting phonecards, used or mint, and it became a lucrative service offered by stamp and coin dealers.

Cards issued in mint packs included sporting heroes, events such as Australia Day and the Grand Prix, state series, and cards issued by companies and organisations – the list was endless. Serious amateur collectors and professional dealers published catalogues of cards and prices, and for a few years, it developed into a serious hobby to rival stamps and coins.

The most prized card of all, as shown below in a price list from 1992, was the South Australia mint pack in the state series. I remember buying it for $90 after walking from dealer to dealer looking for a pack. Most had sold out, and the market went crazy, peaking at over $1,250.

Serious money was being made. Here are the cards in the South Australia pack, with a face value of $44.



I rarely bought in the secondary market, preferring to acquire almost everything that Telecom issued, sometimes in multiple packs, convinced their value would rise as scarce editions sold out quickly. I did not go into the international phonecard game where the range, demand and supply were infinite. Japan in particular had a massive phonecard bubble.

I arranged my cards into neat folders and categories. Now when I think back, I realise I was in my mid-thirties and it's embarrassing to consider how much time the hobby consumed. I was hooked on the thrill of collecting, of obtaining everything, and the future investment potential. My recollection is that I spent about $3,000 on cards (don't tell my wife) which at one stage had at least doubled in value.

I had a lot of fun and I became an expert in Australian phonecards for a few years. A serious collector issued a monthly newsletter which became compulsory reading.

The technology changed by 1998 and pay phones no longer accepted phonecards. The first 1G mobile phone was introduced by Telecom in 1987 (and retailed for $4,250) although the iPhone was not released until 2007. During the 1990s, mobile phones gradually made their way into more hands, reducing demand for pay phones.

The serious collector market for phonecards collapsed from about 1994, and it never came back. Long before then, I had lost interest, and my collection went into the attic. I'd like to say it was a strategic decision to park them until they increased in value, but with my children showing no interest, the cards went the same way as old mobile phones, dated pairs of glasses or souvenirs from an overseas trip. They sit in a bottom drawer, and for some reason, we cannot bring ourselves to throw them out, and they gather dust as the years roll by.

Discovering my phonecard collection again

In my case, for at least 25 years until a few months ago, and I was not even sure where I had stored them. Then we sold our home of 30 years and started clearing out all the storage spaces. And there was my prized collection, neatly wrapped in plastic bags, as good as the day they were minted.

There was no point moving them to our new place, so what was the best way to deal with them? Sell them, of course.

Telstra (ex Telecom) had stopped buying them back 10 years ago. As I looked through them again, I was reminded how much I had spent. Noting that 1993 dollars were worth twice what they are now, many pristine cards held $50 of stored value. I found some of my favourite cards, once treasured with their beautiful presentation boxes and packages. And there was South Australia, itself once worth $3,000 in today's money.

So I hopped onto eBay and Gumtree to check my riches. I knew they had fallen in value, but I did not realise most were almost worthless. South Australia pack for sale at $20, no bids. Mint cards for $2 and $5. Bags of used cards, the lot for $20. No buyers.

And I had hundreds of cards. There was no way I could be bothered listing them and waiting for a bid, or responding to questions, and then posting them to a buyer (if one existed).

I rang a few stamp dealers who once dealt in phonecards. Each said the same. With few exceptions, there was little demand, they were not worth bothering with, the market has collapsed. So much for my precious.

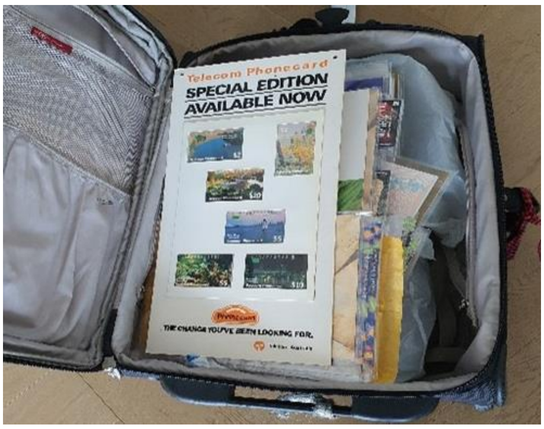
And then along came John Quick, and the solution was right before my eyes.

Forget the money, make someone happy

I could not simply throw them out, and I did not want to take them to our new place and store them for another 30 years.

I Googled 'Phonecard collecting' and the name of the President of the Australian Phonecard Collectors Club (APCC) came up. I emailed John, and he promptly replied, saying that while there are still a few motivated people adding to their collections, prices are very low. He already had an extensive collection but would be willing to pay for cards he was missing. He did not know anybody in Sydney or NSW who was looking for the more common mint packs, and he lived in Adelaide. It would hardly be worth mailing my cards to him in the hope he would buy a few.

Then an idea came to me. Later in the year, I would be attending a wedding in Adelaide. How about I take all my phonecards with me and just give them to him. Gratis. John was happy to meet, indeed, pick me up at the airport, and I would show him my cards over dinner at his place.



Come the appointed day, I packed all my cards into the biggest suitcase I could find. I was amazed at the quantity and weight. It came in at 22kg, a smidgen under the weight allowance for the flight.

At Adelaide Airport, John arrived in his little blue Suzuki to pick me up. He saw my suitcase and carry-on baggage, and pointing to the case, he said:

"Is that what I think it is?"

"Yes," I replied. "Full of phonecards."

"Oh dear. My wife will kill me."

The case filled his car boot and we drove to his house while we had my first chat about phonecards for a quarter of a century. At his home, his wife greeted me at the door with a friendly smile, until she saw the suitcase.

"Is that what I think it is?" she asked.

I soon learned she had tolerated her husband's collecting for decades while taking little interest in it herself. But they were both mad Port Adelaide AFL supporters, so I pretended I knew what that meant and the ice thawed.

Still, taking out all the phonecards was a shock. I had forgotten how much I had accumulated. We spread them over the dining table, and John was thrilled to see them, as shown below. Like a kid in a lolly shop, I had found the most passionate collector of Australian phonecards in the world.

But then a worrying pattern unfolded. He already owned nearly everything I had brought, and in some cases, I had multiple copies of the same item. He started to pick out a few cards, the ones he wanted, such as hard-to-find cards from a Bowral Tulip Festival. Those he absolutely loved, but had he misunderstood the reason for my trip?

"John, you do realise that I'm giving you all this, don't you? I didn't lug 22kg of phonecards from Sydney to Adelaide just so you could pick out a couple."

His wife looked skeptical. Was she wondering if this was a setup of some type? Did he even want them? I reassured them there was no catch, they could keep the cards with a face value of thousands of dollars for free, to give me the satisfaction of knowing they had gone to a good home.

And so we enjoyed dinner, talked cards and football and he explained how once the APCC served over 300 members doing a thriving trade and holding regular meetings and auctions. Now there were maybe a dozen people seriously involved, including a few with massive collections. Websites are maintained with extensive historical records but it's not enough to generate new interest.

Satisfaction all round, I left everything behind and headed for my hotel.

Over the next few days, John emailed me each day on how much he was enjoying going through my cards. He wrote:

"Sorted through your cards and have put them into order of issue. Am still wrapped to have filled the gap with the Bowral Tulip Festival cards. Have sold a few of your cards to a collector friend of mine. Am sussing out some of the APCC members to see if anybody might be interested in me auctioning off some of your packs early next year. Could you please send me your banking details and any monies I am able to raise. I will happily send you the funds. I'm just so happy that you were prepared to go to so much trouble for me to be given first look at what you had available. As I have said previously, it was a real pleasure meeting you."

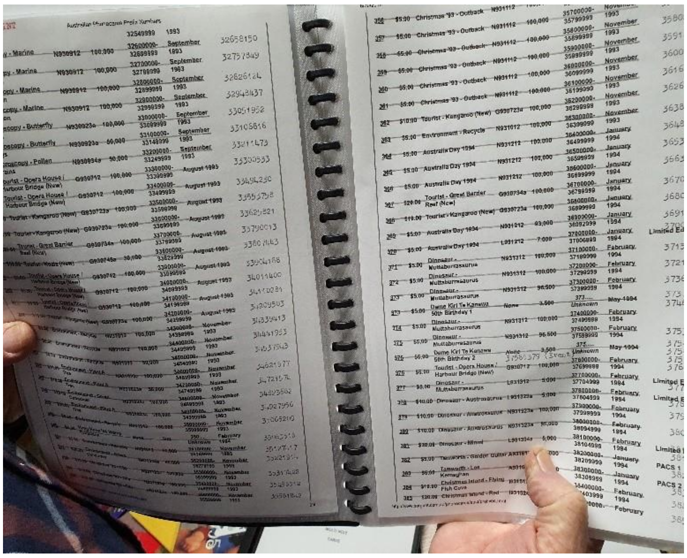
I don't want the money, it was a great result as is.

Are there any lessons about collecting?

Financially, I lost a few thousand dollars, but I enjoyed the thrill of the chase in keeping my collection complete and studying the market. So the first lesson must be that you need to enjoy the actual collecting and not consider it solely as an investment.

Second, however, if it is an investment, watch for signs of interest waning and be prepared to sell, even if you miss the peak. There's a good chance that collectors will move on to another exciting trend, especially when there is little rationale for follow-up demand. Phonecards died because the technology was replaced and people stopped using them. The ability to generate new demand comes with the ongoing Star Wars franchise, the nostalgia for old cars like the Kombi, or the legendary status of Michael Jordan. Stamps are facing the same ignominy as phonecards, although they have 200 years of history to support the hobby.

I ask myself if I collected simply for the pleasure itself or if there was always a money incentive. If I'm honest, there was a financial motivation, and part of my enjoyment was the rapidly-rising value. I made the mistake of assuming the hobby would continue to grow. John is different. He loves the cards and collecting for what they are, and his forensic attention to cataloguing his cards has become a major part of his retirement. He showed me his database and spreadsheets, part of which is shown here, and he clearly lives by a higher calling than my motivations.



And the final lesson is that there is always someone out there who will love your collection more than you do, even if they do not need to pay for it. Find them and make them happy, before Pokémon Go becomes Pokémon Gone.