Firstlinks
a Morningstar company

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Editorial

Given the current rental crisis across many parts of the country, The Australian Housing and Urban Research Institute (AHURI) has released a timely new report that profiles residential property landlords: who they are, who buys rental properties and who sells them, and how long they hold onto their investments.

The study, *'Modelling landlord behaviour and its impact on rental affordability: Insights across two decades'* covers 2001-2021 and includes recommendations for government policy, which we'll get to later.

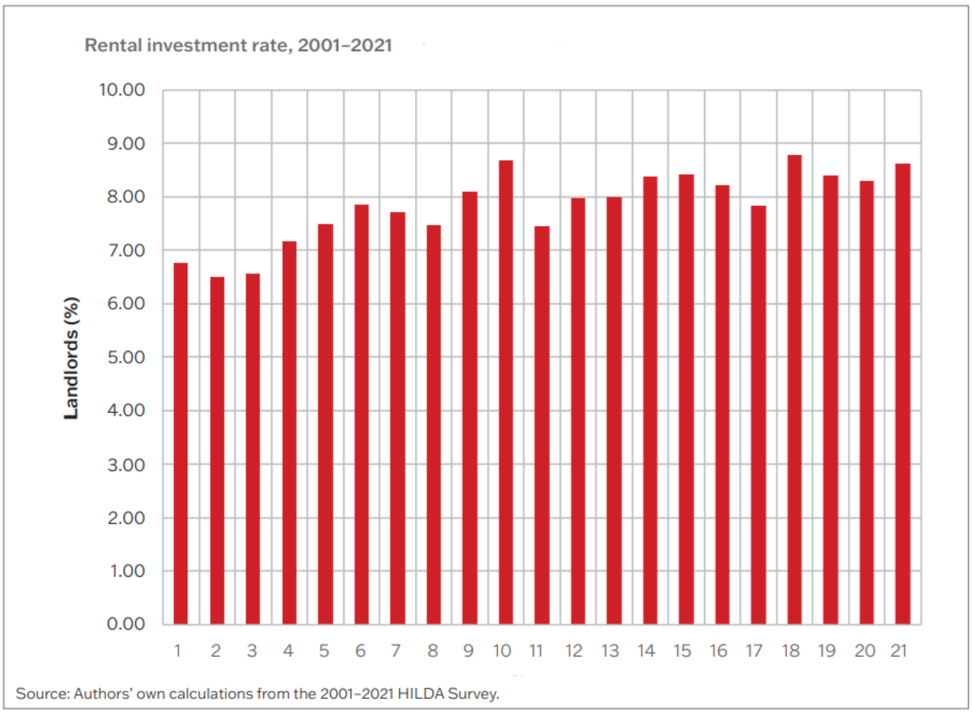
Here are they key findings of the report:

1. More people are residential property landlords than ever before.

In 2021, 2.2 million Australians were landlords, accounting for about 8.7% of the population. That's up from 6.8% two decades ago.

2. Most rental properties are sold within a short period of time.

50% of rental properties are sold within two years and the average holding period is four years. About 28% of rental properties are retained beyond 20 years.



3. Buyers of rental properties are generally younger.

Many buyers are aged between 25 and 34. The typically profile of a buyer is also that they're married, employed, have post-school education qualifications, higher incomes, and lower personal mortgage burdens, relative to outright owning.

Those who retain their rental properties for longer tend to be in stronger economic positions with full-time employment and higher incomes.

4. Landlords sell rental properties due to life transitions or financial difficulty.

The odds of selling a rental investment property in the short-term are raised among pre-retirement landlords aged 45-54 years, by marital separation, unemployment, the absence of post-school qualifications, lower incomes, and personal mortgage burdens.

Mean characteristics of buyers, sellers, and retainers of rental investment properties, per cent by column unless stated otherwise

Characteristics	Buyers[a]	Sellers[b]	Retainers[c]
Male	49%	48%	53%
Female	51%	52%	47%
Mean age (years)	45	49	50
Employed full-time	62%	53%	59%
Employed part-time	20%	21%	20%
Unemployed	2%	2%	1%
Not in the labour force	16%	24%	20%
Postgraduate degree	18%	18%	22%
Bachelor's degree	21%	19%	20%
Other post-school degree	32%	33%	33%
Year 12	11%	11%	9%
Year 11 and below	18%	19%	16%
Married	66%	69%	71%
Defacto	15%	12%	13%
Separated	2%	3%	2%
Divorced	5%	6%	4%
Widowed	2%	3%	3%
Single never married	10%	7%	7%
Has children	44%	43%	42%
Homeowner	77%	85%	85%
Renter	17%	11%	11%
Rent-free	6%	4%	4%
Low-income[d]	15%	21%	14%
Moderate-income[d]	43%	45%	42%
High-income[d]	42%	34%	45%
Sydney	17%	17%	18%
Melbourne	18%	18%	17%
Brisbane	10%	10%	9%
Perth	8%	8%	8%
Adelaide	5%	5%	5%
ACT	2%	2%	3%
Tasmania	2%	2%	2%
Northern Territory	1%	1%	1%

Source: Authors' own calculations from the 2001-2021 HILDA Survey.

Notes:
a. Buyers are those who shift from non-landlord to landlord status between t and t+1.
b. Sellers are those who shift from landlord to non-landlord status between t and t+1.
c. Retainers are those who retain landlord status between t and t+1.The characteristics are derived from wave t.
d. Disposable incomes were converted to real equivalised incomes, then classified into three categories: low, moderate, and high income. The thresholds for these categories were derived from a national distribution of real equivalised disposable incomes. The low-income threshold represents the lowest 40 per cent of this distribution and the highest 20 per cent represents the high-income threshold.

5. People living in well-off areas are more likely to buy a rental investment property, but they're also more likely to sell the property in the short-term.

6. Investment property purchases increase when economic conditions are strong.

(Unsurprising)

7. Negative gearing discourages the sale of rental investment properties and increases the average holding period for rental investments.

All things being equal, negative gearing provides significant incentives for landlords to hold onto properties. Being negatively geared reduces the odds of selling over time by nearly 20%.

If negative gearing was removed, it would increase the after-tax cost of holding a rental property and reduce the average hold period for rental investments. A one percentage point increase in the cost for holding rental properties raises the odds of selling over time by 8.9%.

8. Cutting the capital gains discount would reduce the supply of rental properties and push up rents.

The study did simulated models halving the CGT discount from 50% to 25% over the period 2001-2021, and found that landlord costs would increase, as would the chance that high income landlords sell their rental investment properties. It also found that average rents would have risen slightly, and rental cost burdens would have increased across all income groups.

Policy recommendations

While the report's findings are enlightening, its policy recommendations are less so. The three main recommendations are:

- Establishing programs that offer education on property investment retention. This is to support landlords' efforts to retain property and promote the supply of long-term rental housing to the rental property market.
- Any tax reforms such as reducing negative gearing should be done gradually to reduce the impact on rental markets. That's because negative gearing benefits encourage the retention of rental investment properties, and decreasing these benefits suddenly would lead to a jump in rental property sales and a drop of properties available to renters.
- Long-term freezes to rental increases aren't the answer. That's because it would discourage the buying and retaining of rental properties, thereby reducing the supply of housing into the private rental market.

While the report focuses on landlords and what can be done to encourage them to buy and hold onto properties, there are other things that are needed to increase the supply of housing into the rental market, including:

- **Incentivising new developments.**
  Governments can offer incentives such as reduced development costs and tax breaks to encourage builders to construct more rental properties.
- **Reducing planning red tape.**
  There needs to be faster approvals for developers to help speed up the building of more rental homes.
- **Increase institutional investment in the rental market.**
  Make it more attractive for institutional investors to enter the rental market by giving them tax incentives and promoting long-term leases.
- **Encourage older people to downsize.**
  Reduce stamp duty and other impediments to downsizing. This can increase the supply of larger properties for families.

The AHIRU study provides valuable insights into landlords and some clues about how to fix the rental property market. These issues have been neglected at this Federal Election, which has focused almost exclusively on home buyers over renters. As houses become ever more unaffordable, forcing more people into renting, I suspect the rental market will become a more visible issue in future elections.

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How much time have you spent reading about Trump and tariffs over the past two months? And how much of that time has been useful for your investing? If you're like me, the answers are: a lot, and zero. In my article this week, I urge investors to ignore Trump and instead focus on the time-tested investing principles for building real wealth.

Also in this week's edition...

Even experienced investors often fail to exploit the underlying potential of dividends. Why? Their focus typically diverts to high current yields. **Josh Veltman** and **Jen Nurick** suggest an alternative approach that can offer both a strategic edge and psychological anchor.

Labor has announced a $2.3 billion Cheaper Home Batteries Program, aimed at slashing the cost of home batteries. Open to all households, small businesses and community groups, the scheme aims to turbocharge battery uptake nationwide. **Noel Whittaker** says while good in theory, the scheme has several drawbacks.

Chinese electric vehicles have taken the world by storm. But with soaring tariffs, overcapacity, and rising scrutiny, they may face tougher times ahead, according to **Carolyn Cui**.

REITs have suffered in recent years from rising interest rates and trends such as work-from-home. Yet, since Trump's election, they started to quietly outperform. Can it continue? **Resolution Capital's Andrew Parsons** thinks REITs can offer a potential safe haven in a more volatile, Trumpian world.

European equities are surging ahead of the U.S this year, driven by strong earnings, undervaluation, and fiscal stimulus. With quality founder-led firms and a strengthening euro, **Garry Laurence** believes Europe may be the next global investment hotspot.

The Federal Treasurer, Jim Chalmers, has repeatedly trotted out the line that "there's been a $207 billion cumulative improvement to the budget bottom line" since Labor took office. **Tony Dillon** says it's a rubbery claim that warrants further scrutiny.

Traditionally, duration – a measure of a bond portfolio's sensitivity to interest rates – was the bedrock of defensive allocations in investor portfolios. However, in more recent times, this has changed - duration has been in the doghouse. Today, an important question is whether duration is still something to be feared. **Haran Karunakaran** of **Capital Group** suggests investors could benefit from adding a moderate amount of duration back into their portfolios.

In *Firstlinks*, we've written quite a bit about Australia's $5.4 trillion intergenerational wealth transfer, the largest in its history. This unprecedented shift is prompting many Australians to rethink the question of legacy: What do I truly want to leave behind? In response, many are turning to philanthropy. **Rachel Rofe** outlines how structured giving vehicles can maximise the impact of your legacy while making estate planning more tax efficient.

Lastly in this week's whitepaper, **Magellan** looks at the future of transport and the innovations that are transforming how we move.

An enlightened dividend path

Jen Nurick, Josh Veltman

What makes one business the envy of others? Every investor will have their answer but ours is a company's ability to sustainably pay and raise its dividend quickly over a long and healthful lifetime. If a company can achieve that – moreover, if an investor can identify that – this dividend trajectory will eventually be reflected in its share price, the former pulling the latter upwards like a magnet. This lockstep relationship, though historically proven, has seldom been seized as it demands patience, discernment and laser focus on the behaviour of the dividend above other enticements, or else investors risk becoming imperilled by distractions. For those who correctly identify a company of this profile, investors will gradually become attuned to the propulsive rhythm of a dividend grower, steeled by every increase, each a psychological keel. Our conviction in this approach is so absolute that, were we stranded on an island save for this annual information on our dividend-raising companies, that would be enough.

The hidden power of growing dividends

Even experienced investors often fail to exploit the underlying potential of dividends. Why? Their focus typically diverts to high current yields. However, underlying these yields are companies which the market expects will either pay out almost everything they earn, leaving little to reinvest for growth, or who do a poor job reinvesting their earnings. The dividends of these high-yielders typically stagnate or even shrink, providing minimal dividend growth propulsive power for the share price to follow suit, or worse, pulling their share price downwards if the dividend is cut. Conversely, companies which reinvest the bulk of their earnings at very high rates of return, and can do so for a very long time, tend to offer low initial dividend yields. However, over time, as their dividend grows rapidly, the dollars received, and yield on cost, will not only catch up to their high-yielding counterparts but eventually eclipse them, while simultaneously driving their share prices upwards at a much faster rate.

Consider companies ABC and XYZ. Both companies begin with $100 of capital on which each earns 20%, $20 this year. ABC is a typical high-yielder with little dividend growth. It pays out 75% of its earnings as dividends, with little to reinvest in growth, while XYZ only pays out 25% of its earnings, reinvesting the rest. Put otherwise, ABC compounds its capital at 5% per year (25% of 20%), while XYZ compounds its capital at 15% per year (75% of 20%). Assuming both companies rinse and repeat each year, which is the more compelling investment?

	Company ABC				Company XYZ			
Year	Capital	Earnings	Dividend	Reinvested	Capital	Earnings	Dividend	Reinvested
0	$100.0	$20.0	$15.0	$5.0	$100.0	$20.0	$5.0	$15.0
1	$105.0	$21.0	$15.8	$5.3	$115.0	$23.0	$5.8	$17.3
2	$110.3	$22.1	$16.5	$5.5	$132.3	$26.5	$6.6	$19.8
3	$115.8	$23.2	$17.4	$5.8	$152.1	$30.4	$7.6	$22.8
4	$121.6	$24.3	$18.2	$6.1	$174.9	$35.0	$8.7	$26.2
5	$127.6	$25.5	$19.1	$6.4	$201.1	$40.2	$10.1	$30.2
6	$134.0	$26.8	$20.1	$6.7	$231.3	$46.3	$11.6	$34.7
7	$140.7	$28.1	$21.1	$7.0	$266.0	$53.2	$13.3	$39.9
8	$147.7	$29.5	$22.2	$7.4	$305.9	$61.2	$15.3	$45.9
9	$155.1	$31.0	$23.3	$7.8	$351.8	$70.4	$17.6	$52.8
10	$162.9	$32.6	$24.4	$8.1	$404.6	$80.9	$20.2	$60.7
28	$392.0	$78.4	$58.8	$19.6	$5,006.6	$1,001.3	$250.3	$751.0
29	$411.6	$82.3	$61.7	$20.6	$5,757.5	$1,151.5	$287.9	$863.6
30	$432.2	$86.4	$64.8	$21.6	$6,621.2	$1,324.2	$331.1	$993.2

Source: DivGro

Data shows that companies able to sustainably grow their dividends quickly (albeit from smaller initial bases), ultimately prove superior propositions. Yet most investors overlook the inherent value of such companies. Chasing initially higher dividend yields and immediate income, ABC investors ultimately settle for lower total returns, punctuated by slower dividend growth and its attendant psychological repercussions. Conversely, XYZ investors, who sacrificed the 'allure' of an initially higher dividend yield and delayed 'immediate' gratification, experienced a multiplicative effect. Their dividend continued to ascend quickly, ultimately surpassing the yield of the supposed high-yielder, while their share price ascended at a correspondingly faster clip. ABC investors did not exploit the open secret of sustained high rates of dividend growth: where the dividend goes, the share price follows.

Gordon Growth Model

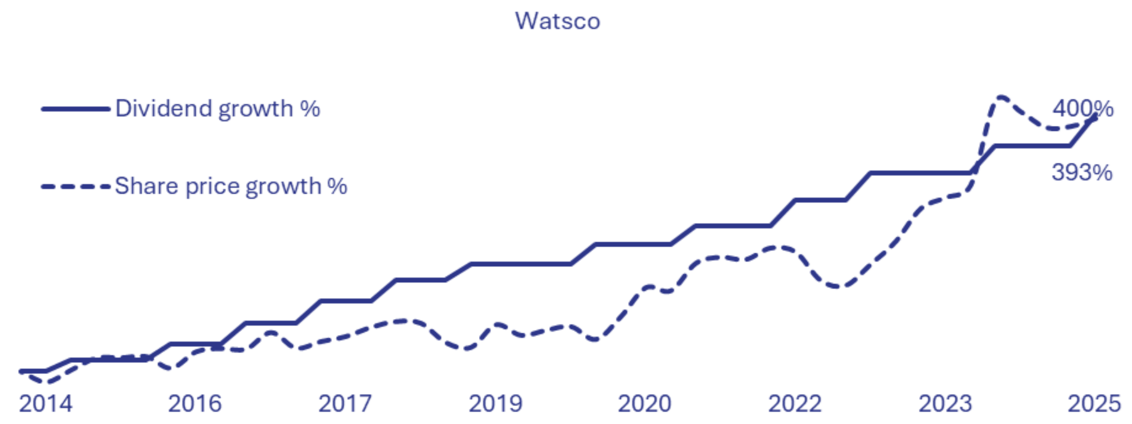
Our roadmap for excellent dividend growth began at MIT. There, the Gordon Growth Model, developed in the 1950s, laid the groundwork for what we do. Three key findings were established: 1) dividend behaviour is the most reliable predictor of future company performance; 2) dividend-paying companies, especially those who can consistently raise their dividends at faster rates, outperform; and 3) the expected total annual rate of return equals the sum of a company's current dividend yield plus the expected sustained rate of growth of that dividend.

This model has been rigorously tested over many decades. Within our own methodology, we have unspooled a significant psychological unlock that makes a singular focus on dividend growers much more effective than traditional approaches. Picture that remote island again, where the only information we receive is our dividend receipts, rising each year at double-digit percentage increases compared to the same payment in the year prior. This single number, more so than any other, illuminates the trajectory of our company, showcasing that its business, and our investment, are on track. This easeful trackability of dividend growth – and the concomitant positive reinforcement it engenders – provides a superior anchor to buoy investors in a volatile environment. It is our opinion that the magic of dividend growth is underused because its effect on investor psychology is too readily dismissed. The success of this approach rests on the investor's capacity to remain permanently focused on the dividend behaviour, rather than becoming sidetracked.

The makings of superb dividend growers

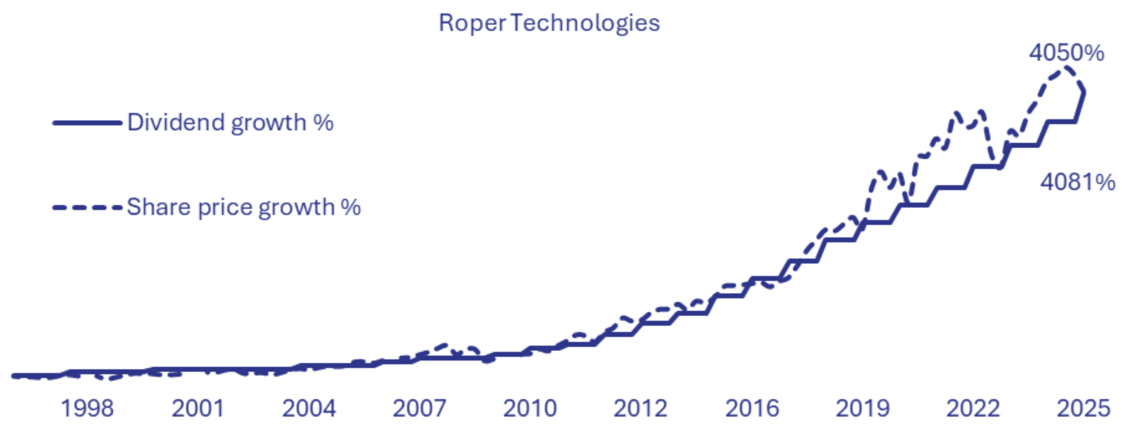
Rapid dividend growers are shielded by special features, and those detailed here should be treated as appetisers – with a caveat. These features are non-exhaustive and should be considered alongside the emotional armament of collecting growing dividend receipts. They may include but are not limited to: a proven dividend growth track record; an unequal playing field; low to moderate payout ratios; a privileged business model; little or no debt; high returns on capital; and a long, sheltered reinvestment runway. (Certainly, companies who can grow their dividends at high rates over the short-term but reach a reinvestment ceiling or are subject to significant cyclical forces beyond their control, exist but don't make the cut).

What does? Take Watsco (NYSE: WSO) – whose dividend has grown more than 100x since 2000, catalysing a similarly remarkable magnification of its share price. As North America's dominant HVAC distributor, Watsco benefits from its vital role in a time-sensitive supply chain: OEMs supply distributors, who accordingly supply technicians servicing urgent needs, especially in humid markets like Florida. With the broadest inventory, lowest prices, and fastest fulfilment, Watsco is the go-to partner for technicians for whom winning the job heavily depends on the speed and product availability of their distributor. With 120+ million HVAC systems in the North America's installed base requiring frequent and urgent repair, and with significant share still to capture, Watsco's dividend growth future is extremely promising.



Source: DivGro, company filings

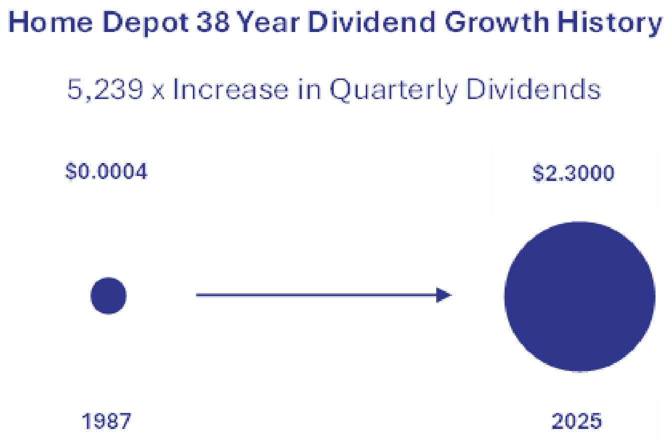
Roper Technologies (NASDAQ: ROP) has always understood that dominating a niche could be more valuable than the absolute size or growth rate of that niche. Roper pivoted from industrial machinery to medical equipment, then software and most recently, high-margin software networks.



Source: DivGro, company filings

Each shift boosted its EBITDA margins from ~30% to over 50%. Its playbook? Roper acquires the leader in a narrow but critical niche, improves that business and acquires complementary capabilities, and over time upscales its margins and profitability. Since 1993, Roper's dividend has grown more than 15% per annum compounded, with its share price escalating accordingly.

Finally, consider home repairs behemoth Home Depot (NYSE: HD). Together with Lowe's (NYSE: LOW), it operates a powerful duopoly that commands more than 30% of the one trillion dollars spent annually on US home repairs and maintenance. Their size provides all the attendant scale advantages, principally the ability to price products well below fragmented competitors, taking market share in every environment. As the average age of North American homes exceeds 40 years (a critical inflection point for repair and maintenance), Home Depot and Lowe's are poised to continue benefitting from price leadership, market growth, and market share gains.



Source: DivGro, company filings

The ability to identify and focus on long-term rapid dividend growth is both a strategic edge and psychological anchor. For those disciplined enough to execute effectively, the potential rewards – compounding returns, rising income, and enduring peace of mind – can be profound.

Josh Veltman and Jen Nurick work across Investor Relations and Communications at DivGro.

Don't let Trump derail your wealth creation plans

James Gruber

How much time have you spent reading about tariffs over the past two months? If you're like me, it's been hundreds of hours. And how many of these hours have been useful to your investing? If you're like me, the honest answer would be zero.

In a recent interview, Emma Fisher of Airlie Funds Management alluded to this, saying that we'd all become economists:

> *"There's a great saying: In bull markets, everyone becomes a long-term investor; in bear markets, everyone becomes a macro economist."*

And specifically on tariffs, she said:

> *"We saw it in COVID. A lot of people focused on 'hey, I'm going to figure out where the virus is going next and become an expert in virology.'"*

What Fisher suggested was that we spend so much time worrying about what's in the news, and what's happening with the economy, politics, geopolitics, and so on, that we forget what's important to investing and building wealth. For her, it's bottom up stock picking. For us, it's a little different, as we'll detail later.

But an obvious question is: why do we spend these thousands of hours on things that don't really matter?

The answer is simple: we're trying to beat the market and get rich quick.

That leads us to do all sorts of silly things. Buying stocks like lottery tickets, hoping they'll be the next Nvidia. Buying the latest hot trend – gold as an example right now. Buying the latest hot fund manager without studying whether their outperformance is sustainable.

What should we be focusing on, then?

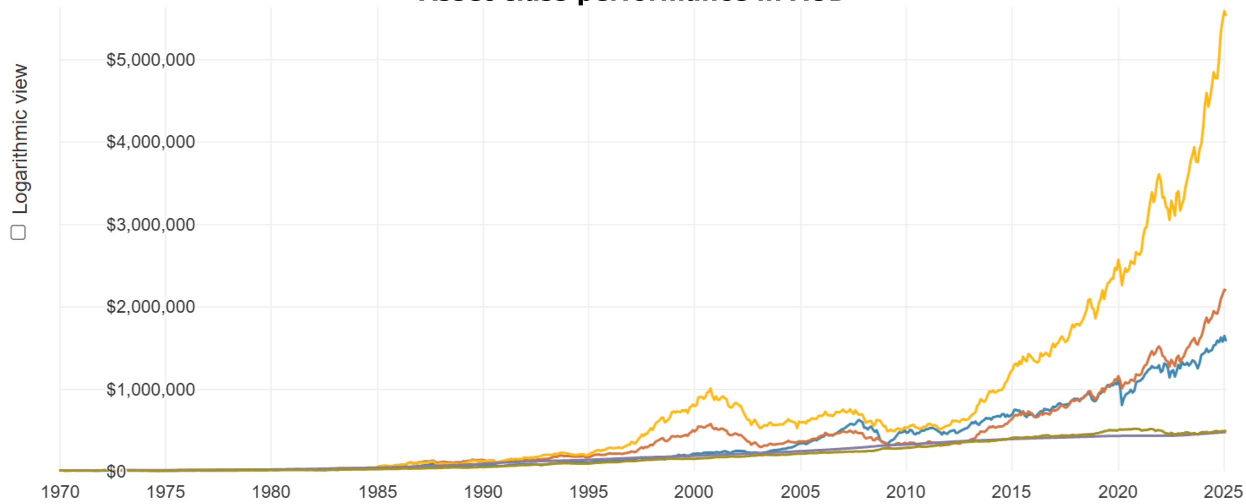
Zooming out on what really works

Investing isn't a science, though more investors should treat it as such. That's because there are a few 'laws' that are as iron clad to investing as gravity is to science.

1. Stocks are the best asset class over the long-term.

In the long-term, stocks thrash every other asset class, whether it's cash, bonds, gold, or anything else.

Asset class performance in AUD



Asset classes	Value at 28 Feb 2025	Return since 1 Jan 1970
Australian Shares	$1,579,263	9.6% p.a.
International Shares	$2,198,763	10.3% p.a.
US Shares	$5,536,553	12.1% p.a.
Australian Bonds	$493,472	7.3% p.a.
Cash	$477,483	7.3% p.a.

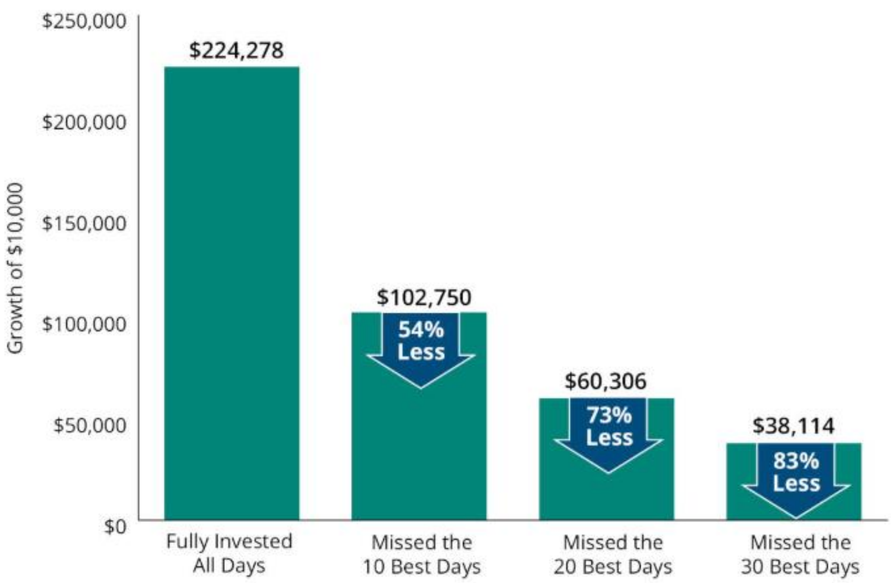
Portfolios	Value at 28 Feb 2025	Return since 1 Jan 1970

Source: Vanguard

2. Staying in the market matters.

To reap the benefits of stock's long term returns, it's essential to stay invested. If you don't stay invested, then you risk missing out on the best days in markets, which can have a huge impact on your returns. That's why trying to time markets is a waste of time, and detrimental to building wealth.

S&P 500 Index Average Annual Total Returns: 1995-2024



Source: Hartford Funds

3. Compounding is magic

If you invest in stocks and hold onto them, then you let compounding work its magic.

The compound interest table below is one of the most important tables in investing, and one that should be taught to every adult and child.

Compound interest table (future value of $1)

Period	5%	7%	10%	16%	20%
1	1.05	1.07	1.1	1.16	1.2
2	1.1	1.14	1.21	1.35	1.44
3	1.16	1.23	1.33	1.56	1.73
4	1.22	1.31	1.46	1.81	2.07
5	1.28	1.4	1.61	2.1	2.49
6	1.34	1.5	1.77	2.44	2.99
7	1.41	1.61	1.95	2.83	3.58
8	1.48	1.72	2.14	3.28	4.3
9	1.55	1.84	2.36	3.8	5.16
10	1.63	1.97	2.59	4.41	6.19
11	1.71	2.1	2.85	5.12	7.43
12	1.8	2.25	3.14	5.94	8.92
13	1.89	2.41	3.45	6.89	10.7
14	1.98	2.58	3.8	7.99	12.84
15	2.08	2.76	4.18	9.27	15.41
20	2.65	3.87	6.73	19.46	38.34
25	3.39	5.43	10.83	40.87	95.4
30	4.32	7.61	17.45	85.85	237.38
35	5.52	10.68	28.1	180.31	590.67
40	7.04	14.97	45.26	378.72	1469.77

Source: Young research

The table shows the snowball effect of compounding returns.

Historically, the Australian share market has returned about 10% per annum (p.a.), including franking credits. At that rate of return, $10,000 turns into $67, 300 in 20 years and $452,600 in 40 years. And it gets even better if you can invest further savings along the way.

Boiling it down to an equation

If I had to boil wealth down to a simple equation, it would be this:

Saving + investment + time = wealth

The problem is that most investors don't save enough, don't invest enough, and don't allow enough time.

Why? Because most have a goal of getting rich, but they don't have a system for reaching their goal. Goals without systems are worthless.

Let's say that you want to invest $10,000 in the Australian stock market and achieve the goal above of turning that money into close to $450k in 40 years' time, by compounding the money at 10% p.a. What's the best way of achieving this goal? There are three main options:

1. Investing in a low-cost ASX 200 ETF.
2. Investing in a managed fund.
3. Investing in ASX shares directly.

The first option has a high probability of working. The latter two options require greater research, use of your time, and willpower, and consequently have less probability of working.

The power of automating your finances

I've been involved in investing for a long time, and I've become a big fan of automated investing - using apps and platforms to invest an initial amount of money in ETFs/managed funds, and then regularly top that up with savings.

There are many apps that investors can use to do this now. The mix of technology and convenience is luring younger investors into these apps, and I view this as a good thing.

Why automate? Because it provides a system for investing, like the one I mentioned above.

Why don't more investors do this? Because it's boring and requires discipline and sacrifice.

But it can be worth it.

Going back to the compound interest table, though with a twist this time. If we initially invest $10,000 in an ASX 200 ETF and add $1,500 per month over 40 years, and the ETF has compound returns of 10% p.a., then you'd end up with a little of $10 million.

That's the power of saving, investing, and time. And it's the sure-fire way to building wealth.

James Gruber is Editor at Morningstar.

Pros and cons of Labor's home batteries scheme

Noel Whittaker

Labor has announced a $2.3 billion *Cheaper Home Batteries Program*, aimed at slashing the cost of home batteries by around one-third. Open to all households, small businesses and community groups, the scheme aims to turbocharge battery uptake nationwide.

The rebate is based on a battery's usable storage capacity and excludes installation costs. It offers roughly $370 per kilowatt-hour (kWh), equating to about 30% off the battery's base price. For example, a 13.5 kWh Tesla Powerwall 2, priced at around $11,900 (plus installation), would attract a rebate of nearly $5,000.

The rebate is not means-tested but is limited to one battery per household. Installation must be carried out by accredited providers, and further details on eligibility, start dates and application processes will be released state-by-state, pending jurisdictional agreements.

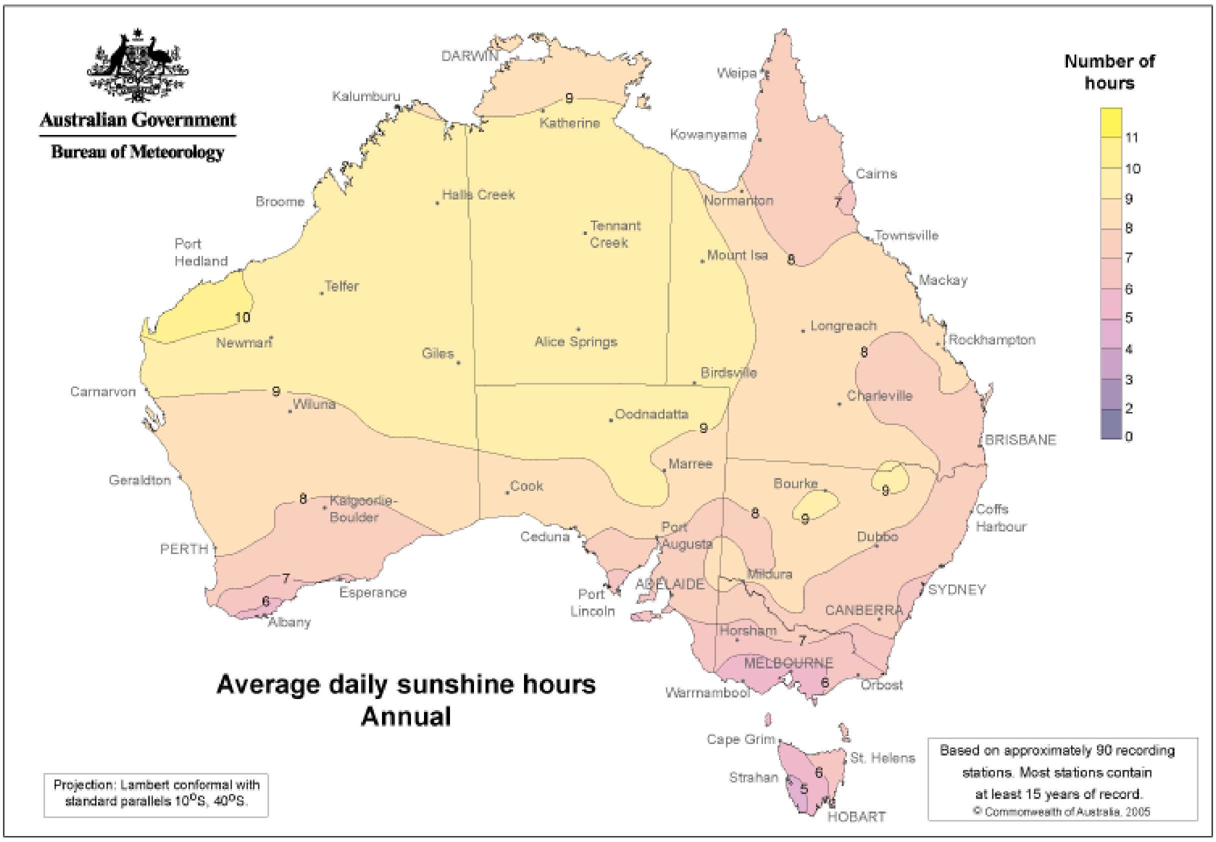
Is it good policy?

The proposal might be good in theory, but it's a different thing in practice.

When COVID struck, we found ourselves with a cash surplus thanks to refunds from cancelled trips and decided to install a Tesla Powerwall. It's been a trouble-free appliance and can even think for itself. Recently, when a cyclone was approaching, it sent me a text advising it was charging from the grid so it would be full in case of a blackout. The days before the cyclone were cloudy, so no electricity was coming from solar.

It's impressive technology — but that doesn't mean it adds up.

Consider a typical day in a household with solar panels and a battery. The day usually starts with the battery down to its minimum and no solar power being generated. At this stage, all electricity is coming into the house from the grid. As the sun—if it appears—rises, solar begins to offset grid use. If conditions are favourable, solar output eventually exceeds household consumption, and the battery begins to charge. But as the afternoon wears on, solar generation drops. The moment it can't meet demand, the house draws from both the battery and the grid. It's common to end the day with a near empty battery — especially in winter when the sun sets early.



All a battery can do is store excess energy when your solar system is producing more than you're using. Once the battery is full, the surplus goes to the grid — and as we all know, there's not much money in that.

Let's pretend it's been a perfect day to see how the numbers work. The sun is shining brightly, and by sunset your battery is full — charged entirely from your own solar panels at zero cost. Keep in mind this is also the time most people return from work, just as power generation fades and demand surges. We're currently paying around 30 cents per kilowatt-hour, which means a fully charged battery holds just $3.60 worth of electricity. It's great to be using free power from your battery, but in reality, that full battery is only saving $3.60.

And solar generation varies greatly depending on where you live, how many panels you have, and even the direction of your roof. Still, let's assume you manage to fully charge and use your battery on 200 days of the year. That means the total annual saving amounts to just $720 — not nothing, but hardly the game-changer it's claimed to be.

Given Labor's proposal offers a $5,000 discount on a battery like a Tesla Powerwall, the homeowner is still left with the balance — around $12,000 — once installation is included and the total cost climbs to about $17,000. At annual savings of just $720, it would take 16 years to recover the cost — which, by coincidence, is also the estimated lifespan of the Tesla Powerwall battery. In other words, just as you've broken even, the battery may be ready for replacement.

Another major drawback is its basic unfairness. The people most likely to be cash-strapped are renters, and they cannot install solar and batteries on a rental property because they'll never get their money back. There's an argument that savvy landlords might install the wiring, solar panels and battery to increase rents, but we're heading for an unholy alliance of Labor and the Greens. It is Greens policy to freeze all rents — so what landlord would go to the expense of installing a solar system when there's every chance their rents would be frozen?

The nonsensical part

Here's a real head-scratcher from the latest battery rebate announcement: if you install a battery before July 1, you qualify for the subsidy — but you're not allowed to switch it on until that date. Seriously?

You can pay for it, install it, wire it up, and connect it to the grid — but then it must sit idle for months. That's not just bureaucratic nonsense — it's policy gone mad.

The whole point of the scheme is to ease pressure on the grid and help households save money. Forcing people to wait defeats the purpose. It's process over purpose — and a reminder that common sense is too often missing in Canberra.

Noel Whittaker is the author of Making Money Made Simple and numerous other books on personal finance. His advice is general in nature and readers should seek their own professional advice before making any financial decisions. Email: noel@noelwhittaker.com.au.

Will China's EV boom end in tears?

Carolyn Cui

In the shadow of China's towering automotive achievements lies a complex tale of innovation, ambition, and market forces run amok.

From the historic rollout of the first 'Liberation' truck in 1956 to the present, where Chinese electric vehicles (EVs) dominate the global stage, the journey has been nothing short of remarkable. Yet, this success story is tinged with all sorts of challenges.

With President Trump returning to the White House, the term 'tariff', which he famously lauded as "the most beautiful word," is once again taking centre stage in matters of global trade and politics. Earlier this year, President Trump announced a 25% tariff on imports from Canada and Mexico, as well as an additional 20% tariff on Chinese imports, citing the countries' inadequate actions to curb fentanyl flows.

Then, as part of President Trump's 'Liberation Day' announcement on 2 April 2025, he imposed an additional 34% tariff on Chinese imports, with the new tariff going into effect on 9 April 2025. As a result, Chinese EV makers, who have experienced a surge in exports in recent years, are subject to a whopping total of 154% tariff.

Despite the dual challenges of internal economic strains and rising trade obstacles, Chinese automakers are actively transforming the global automotive landscape. This period of change not only spotlights the companies but also prompts a deeper examination of the sustainability and competitiveness of their rapid growth, as well as the broader implications for the future of transportation.

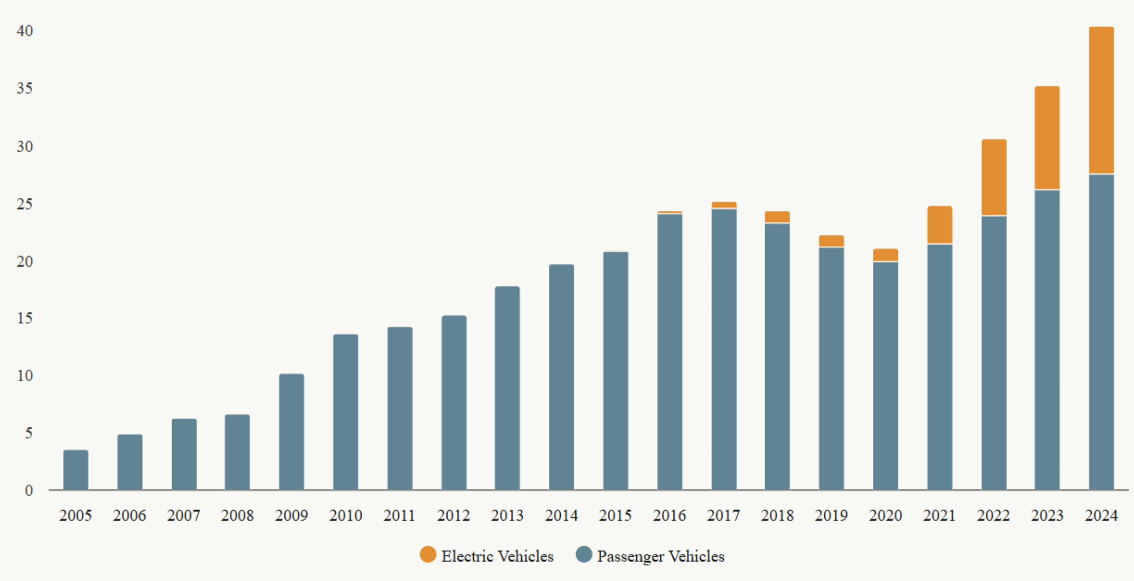
A sudden success

China's automotive odyssey commenced in 1956 with the first 'Liberation' brand truck coming off the production line at the First Automobile Works in Changchun, Jilin Province.[1] This pivotal moment signified the close of a chapter in which China lacked the capability to produce its own automobiles.

However, it was not until Deng Xiaoping's open-door policy in the late 1970s that the industry's engine truly started. Foreign joint ventures injected much-needed technology and expertise into China's auto industry, steering it onto the fast track.

The subsequent decades marked a period of explosive growth. Admission to the World Trade Organization in 2001 kick-started an era of unparalleled expansion, with the country's economic rise fueling a burgeoning demand for passenger cars. This shift culminated in 2009 as China dethroned the US as the world's top auto market, a position it has not relinquished since.

Rise of Electric Vehicle Production (in millions)



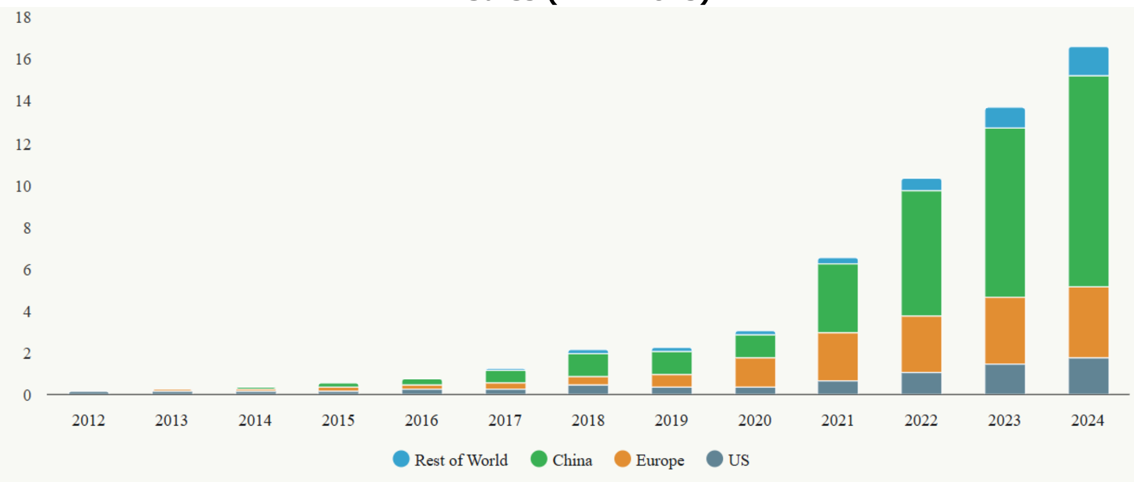
Source: China Association of Automotive Manufacturers. Data as of December 2024.

The surge in vehicle production and sales has contributed to urban pollution and traffic congestion in China, prompting Beijing to steer toward electric vehicles as a remedy in recent years. Backed by government support and their robust manufacturing capabilities, Chinese automakers shot to dominate the global EV market, claiming about 70% of total new registrations last year.[2]

An inevitable glut

However, the sector has become overcrowded quickly. At present, there are over 60 passenger car manufacturers in China, far exceeding the 20 to 30 companies typically found in other more established markets. The oversupply in EVs is further exacerbated by government incentives and access to cheap financing. By the end of 2023, Chinese EV capacity had surpassed what was needed to meet global demand, reaching a level equivalent to 116% of worldwide needs, according to a Goldman Sachs analysis.[3]

EV Sales (in millions)



Source: IEA. Data as of December 2024.

The excess capacity reflects China's distinct market dynamics. Unlike the cyclical fluctuations seen in other markets, demand in China often starts from an extremely low baseline and then expands dramatically in both scale and speed. This pattern poses challenges for accurately forecasting market size, particularly at the onset of a growth cycle.

On the participants' side, certain companies have managed to ride the wave of transient undersupply, reaping significant profits and capturing the attention of capital markets. This profitability often sparks a frenzied reaction from market followers, eager to invest in the burgeoning sector. When this unpredictable demand surge is met with a swift supply-side reaction, the likelihood of imbalances naturally increases.

Government policies, while aimed at promoting industry development, can exacerbate such imbalances. In January 2024, the Chinese government updated its EV objectives, mandating that EVs represent 45% of all new car sales by 2027.[4] Although national EV purchase incentives were phased out in 2023, local subsidies remain, fostering sector expansion. Additionally, China's "dual-credit system" has simplified the process for consumers to acquire license plates for EVs, further bolstering the industry.

In our view, the industry mirrors the initial success of China's solar and steel sectors. But the long-term effects are questionable, as this pattern of state-driven growth could lead to a repeat of past challenges. In those industries, subsidies triggered rapid expansion and market dominance, only for overcapacity to flood the market, driving down prices and profitability as global demand lagged.[5] Without sustained innovation or strong export markets, the industry may face a familiar downfall: a policy-fueled boom giving way to a bust as subsidies fade and excess supply overwhelms weaker firms.

China Fuels EV Surge with Subsidies and Tax Breaks

Type of Support	2009 - 2017	2018	2019	2020	2021	2022	2023	Total
Rebate	37.8	4.3	3.3	3.5	7.4	9.2	0.0	**65.7**
Sales Tax Exemption	10.8	7.7	6.4	6.6	16.4	30.3	39.6	**117.7**
Infrastructure Subsidies	2.3	0.2	0.2	0.3	0.3	0.6	0.6	**4.5**
Research & Development	2.0	3.6	3.4	3.5	4.3	3.9	4.3	**25.0**
Government Procurement	7.8	1.6	1.4	2.9	1.7	1.8	0.8	**18.0**
Total	**60.7**	**17.4**	**14.8**	**16.8**	**30.1**	**45.8**	**45.3**	**230.9**
Spending as Share of Total Sales	42.4%	22.7%	23.3%	25.4%	18.3%	15.1%	11.4%	**18.8%**
Subsidy per Vehicle	-	13,860	12,311	12,294	8,538	6,656	4,764	-

Source: Center for Strategic and International Studies. Data as of December 2023.

Tesla, Inc. experienced these dynamics firsthand. The American automaker was able to construct a gigafactory in Shanghai within a year. To finance the plant, Tesla received US$521 million in loans from Chinese banks at favorable interest rates, and US$82 million in grant funding. The local Shanghai government also granted Tesla a corporate income tax rate of 15% for 2019 through 2023, compared to the typical 25% rate in China.[6]

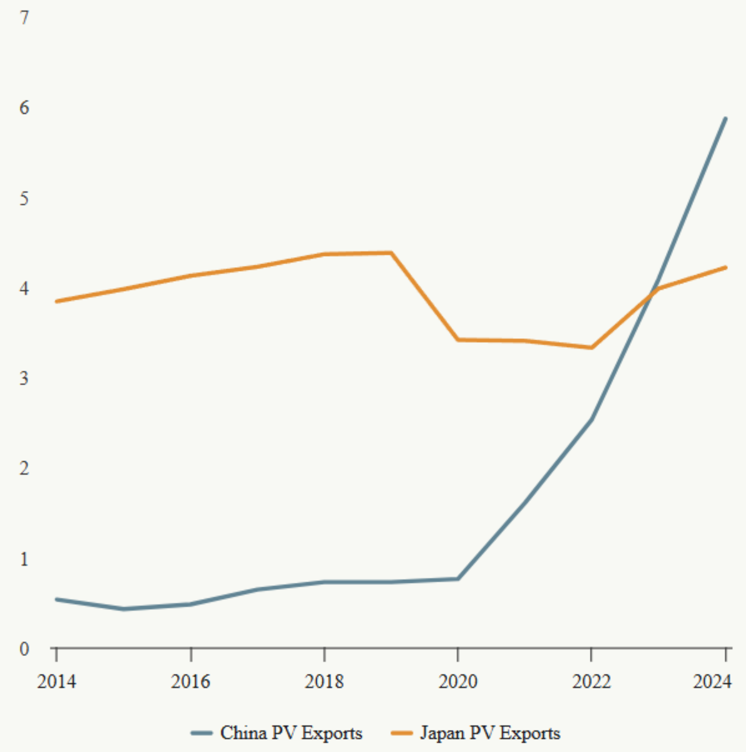
On the other hand, the completion of Tesla's manufacturing facility in Berlin took about two years. Productions at the factory have faced numerous delays due to concerns about its environmental impact, as well as Red Sea shipping attacks. During a 2023 visit to the Shanghai gigafactory, Tesla's CEO Elon Musk praised the facility, stating, "I tell people throughout the world, the cars we produce here are not just the most efficient production, but also the highest quality."[7]

For now, the surplus seems unabated, with most managements across the Chinese auto industry still maintaining a positive outlook. According to Goldman Sachs, companies were expected to expand their EV capacity by 18% in 2024 to 17 million units—three million more than what the world needs.[3]

Cost control created cost advantages

Chinese EV manufacturers set themselves apart from the competition mainly through their cost controlling measures. A study by Goldman Sachs showed that Chinese automakers' costs are 47% lower than those of their global peers.[3] Economies of scale are crucial in the capital-intensive sector, with high production facility utilization rates being crucial for spreading out fixed costs and optimizing variable cost management.

China is Outpacing Japan in Passenger Vehicle Exports (In Millions)

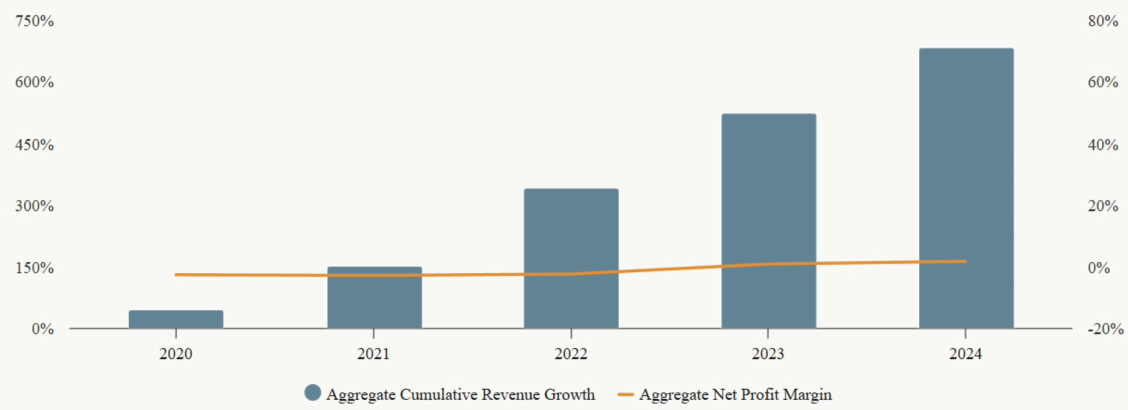


Source: China Association of Automotive Manufacturers. Data as of December 2024.

BYD Company Ltd., a leading EV player in China, has harnessed vertical integration as a strategic lever to achieve a significant cost controlling advantage. By managing the entire production chain, from securing raw materials to manufacturing core components like batteries and electronic control systems in-house, BYD effectively reduces reliance on external suppliers, minimizes production costs, and mitigates supply chain risks.

Within China, growing popularity of EVs took a toll on the country's conventional internal combustion engine (ICE) cars, whose sales contracted by 17.4% in 2024.[8] Overall, its automotive market is experiencing saturation, evidenced by a capacity utilization drop to 56% in 2024. This saturation is driving Chinese automakers to pursue international markets. From 2020 to 2024, China's auto exports surged by nearly 500%, as reported by the China Association of Automobile Manufacturers. In 2024, China exported a historic 5.86 million vehicles, including 1.3 million EVs, surpassing Japan as the world's leading car exporter.[8]

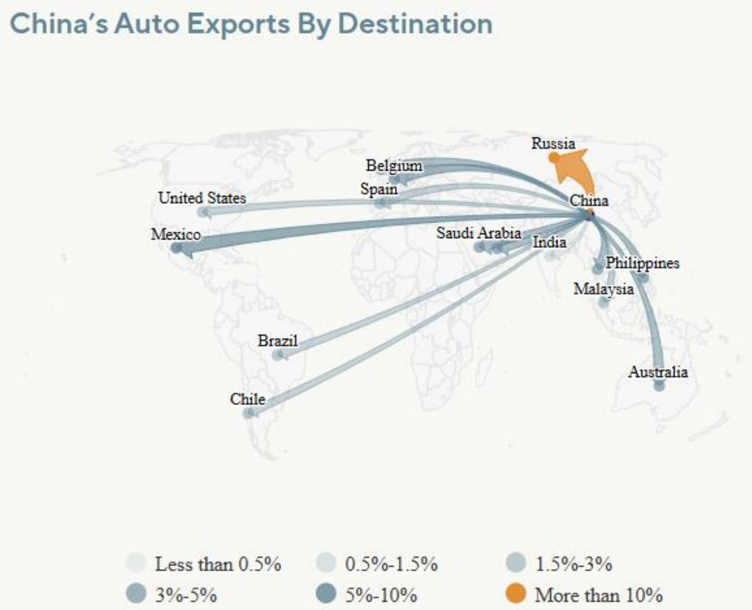
Thin margins among Chinese EV producers have become a growing concern as fierce competition and overcapacity take their toll. Companies like BYD, Xpeng, and Li Auto are locked in a price war to capture market share, driving down vehicle prices while production costs remain high due to reliance on expensive batteries and advanced tech.[9] Government subsidies have softened the blow for some, but as these incentives taper off and domestic demand slows, many firms are struggling to turn a profit. This race to the bottom threatens the sustainability of the industry over the long run.



Source: Bloomberg. Data as of 25 March 2025.

Global tensions

However, the surging export activity of Chinese automakers has triggered a global response. Critics argue that Chinese cars, often coming with deflated price tags, have undercut producers abroad and sparked a price war that few can sustain. Nations, feeling the pinch of cheap imports, resort to protective tariffs and other barriers in a bid to shield their industries, sometimes igniting trade disputes with Beijing.



Source: China Association of Automobile Manufacturers, China Ministry of Commerce, GQG Research. Data as of 2023.

In the US, the Biden administration doubled tariffs on EV imports from China to 100% beginning in August 2024, posing significant challenges for Chinese firms targeting the American market. Europe, while showing a divided stance, voted in October 2024 to impose tariffs up to 45% on Chinese automakers, while over 40% of China's EV exports are absorbed by this crucial market.[10]

Contrastingly, Brazil's rising demand for Chinese EVs has led to gradual tariff increases and local manufacturing by companies like BYD, as Mexico also sees Chinese firms establishing production to circumvent US tariffs and serve the North American region, with Thailand in Asia-Pacific rolling out incentives for zero-emission vehicles, attracting Chinese EV manufacturers.

China's auto exports by destination

The trend of establishing overseas production facilities is not without its financial challenges, as the costs associated with setting up factories and navigating different regulatory environments may weigh on the profits of Chinese EV makers.

"In theory, there's nothing wrong [with affordable Chinese EVs outside of China], but in practice, there's a lot wrong," former US ambassador to China Nicholas Burns said in an interview last year. "The government of China and the provincial governments are subsidizing the Chinese EV manufacturers so there's no level playing field, and they take the cars, they sell them below the cost of production into Europe or Brazil or the US."[11]

Hidden challenges come to light

But the issue isn't merely external. Overcapacity signifies a deeper inefficiency within China's own resource allocation and its industrial sectors. EV overproduction squanders raw materials, energy, and labor, while intensifying environmental woes. Over the long run, the misallocation of capital may hamper China's long-term growth prospects by diverting resources from potentially more productive sectors. For Chinese companies, the burden of excess capacity also increases financial stress, with potential loan defaults posing a threat to the stability of China's banking system.

For example, as Nio Inc., a Chinese EV maker, was on the brink of exhausting its funds in 2020, a provincial government swiftly stepped in with a $1 billion investment for a 24% stake in the company. Concurrently, a state-controlled bank led a group of other lenders and pumped in another $1.6 billion. These state investors are probably facing buyer's remorse now, as Nio's share price had tumbled as much as 90% from its highs.[12]

Environmental issues remain, even with zero-emission commitments. As China's leading EV manufacturer, BYD has made significant strides in advancing sustainability, staying in line with Beijing's strategic ambitions to cap carbon emissions. However, in 2023, BYD found itself embroiled in controversy with competitor Great Wall Motors.

Great Wall alleged to three regulatory bodies that BYD's hybrid models were equipped with atmospheric pressure fuel tanks instead of the required high-pressure ones, potentially causing non-compliance with emission standards and gaining a cost advantage by simplifying vehicle configurations.

In a hastily composed response, BYD vehemently rebutted the accusations but failed to address the heart of Great Wall Motors' core claims. Instead, BYD challenged the completeness of the emissions test report and shifted the discussion toward themes of national interest, focusing on the "new energy business" and the promotion of "Chinese brands."[13]

Still, it remains to be seen whether BYD has indeed skirted regulations.

China's pole position in the global automotive race

In the global automotive race, China's position is both enviable and precarious. Following a period of rapid growth, Chinese automakers, especially those emerging in the EV sector, are now grappling with an economic slowdown domestically and starting to dump low-priced cars overseas. This has led to a significant market imbalance with the potential to unleash a series of aftershocks.

The state of China's auto industry acts as a pulse-check for the vitality of the world's second-largest economy, with its trends being closely monitored as an indicator of either burgeoning prosperity or looming challenges.

At GQG, we closely track these industrial and geopolitical developments, integrating them into our in-depth company research. Our investment decisions are made within a multifaceted, complex global context.

We believe China's automotive sector stands as a critical indictor of the economic strategies that will shape President Trump's second term in office. President Trump's emphasis on encouraging domestic manufacturing foreshadowed his latest move to increase the 100% tariffs imposed by the Biden administration on Chinese-made EVs. Concurrently, President Trump's tight-knit relationship with Tesla's Elon Musk, whose company has considerable investments in China, is likely to introduce a layer of intricacy to the development of these trade policies.

Stay buckled up.

Carolyn Cui is a senior investment analyst at [GQG Partners](). This article contains general information only, does not contain any personal advice and does not consider any prospective investor's objectives, financial situation or needs. Before making any investment decision, you should seek expert, professional advice.

End notes

[1]"The First Liberation Brand Truck." People's Daily Online.
[2]"China's EV Sales Account for 70% of Global Total." Sina Finance.
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REITs: a haven in a Trumpian world?

Andrew Parsons

The dramatic changes to U.S. tariffs settings challenges the financial market's Trump pro-growth market narrative which heralded the start of 2025. Instead, investors now face conditions which look likely to invoke a global economic slowdown, if not recession, with significant pressure on corporate earnings from higher costs together with unsettled consumer demand and production patterns.

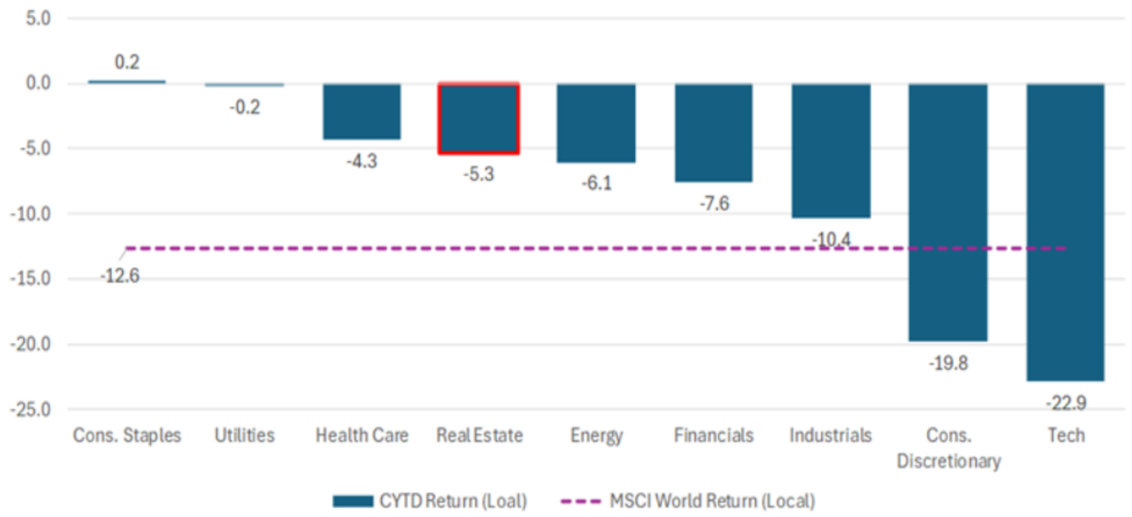
Regardless of where Trump's tariffs settle, the market is coming to terms with higher risk hurdles when assessing investments. Whilst we cannot be sure about absolute outcomes, in this environment we believe REITs are relatively well placed to produce competitive risk adjusted returns. As we will explain, income security generated by select real estate combined with the operating and capital strength of REITs underpin our belief.

The fundamentals underlying our optimism

We see the biggest threat to our constructive thesis on REITs relate to a scenario involving the onset of stagflation and acknowledge that a deep and extended period of economic contraction will increasingly weigh on real estate returns. We also can not dismiss the possibility of additional imposts on real estate as Trump seeks to find alternate sources of income to provide tax relief for businesses and ordinary citizens. Given Trump's background, this latter risk would be somewhat surprising.

Our reasons for optimism are starting to play out. Whilst Global REITs have not been spared in the broad sell down of publicly market investments, as investors seek less economically sensitive areas of the market they have outperformed broad equities thus far in 2025. Thanks to underlying strong fundamentals, we believe there is scope for this trend to continue.

Figure 1: Global Equity Performance CYTD



Source: MSCI World Index (Local Currency). 07 April 2025

Importantly, to date, bond yields have been relatively stable and there is room for central banks to reduce interest rates should there be clear evidence of a rapidly deteriorating economy and/or reduced consumer price inflation. That said, core inflation dynamics remain challenging, and central banks will be loath to repeat the mistakes of past stock market corrections such as that which occurred post the 1987 crash when emergency rate cuts fuelled higher inflation. Whilst REITs will not be totally immune, their earnings are less sensitive to slowing economic activity and increasing costs pressures.

Critically, real estate and REIT earnings are not directly affected by changes to tariffs.

From an operating expense perspective, REIT outgoings largely relate to property taxes, repairs and maintenance, property management and insurance. Hence, by and large, these are unaffected by tariffs.

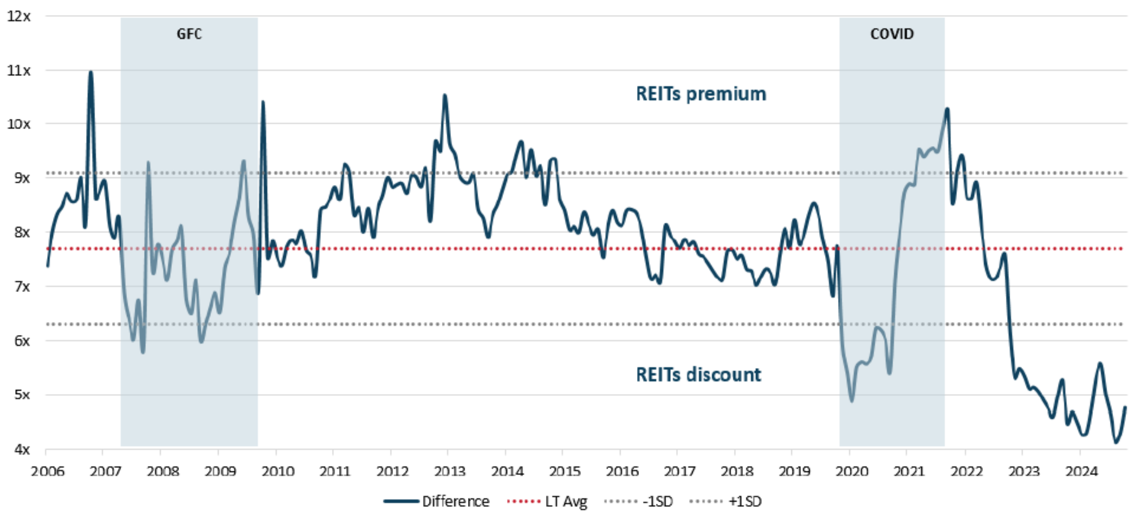
In many underlying real estate categories, REIT revenue (rental) streams are relatively secure thanks to medium to long-term lease contracts, often three to 10 years in duration, which provide cashflow security. Where these lease structures are common, industrial and office property are perhaps the most vulnerable to a prolonged economic slowdown thanks to diminished tenant demand. We are significantly underweight REITs with office and warehouse exposures, in total representing less than 15% of the portfolio, with the U.S. being less than half this figure.

In other segments such as residential, self-storage, and hotels, income is often derived from short term lettings. In some of these instances, occupier demand is needs-based and hence income tends to be relatively resilient. Clearly hotels are the most economically sensitive to which we have minimal exposure. Of course, this income profile is subject to tenant credit. We would note that the largest single tenant underlying our REIT property portfolios generates less than 2% of total portfolio income [Astria Senior Living].

Furthermore, increased tariffs will put further upward pressure on building material replacement costs, making real estate development economics even more challenging unless rents rise meaningfully. Of course, tenant demand is critical but weaker demand will not be compounded by a growing supply overhang and in an environment where real estate vacancy rates are historically low.

For broader equities investors, we believe the picture is more challenging. Trump's policies are likely to put pressure on corporate profits and margins as businesses will find it difficult to pass on the full cost of higher import prices to their customers. De-globalisation will create other challenges including sources of production, re shaping of supply chains and capital needs for businesses. We expect in this environment greater investor scrutiny on fundamental value and real cashflows from business models that have been over hyped and overpriced.

Figure 2: Relative EV/EBITDA spreads



Source: Resolution Capital. Spreads calculated as EV/EBITDA difference between FTSE EPRA Nareit Developed Index and MSCI World Index. 28 February 2025

Crucially, we do not believe current REIT earnings multiples takes into account the key replacement cost dynamic. Based on this fundamental tangible quality, by our estimates, commercial real estate is currently trading at/below replacement costs with low new construction. Consequently, REITs multiples appear on the surface to be very undemanding versus broader equities. Hence, the sector could benefit from investors continuing to rotate from more economically sensitive sectors into more defensive cashflows. It is reasonable that investors will view real estate as being a relatively secure investment and generating meaningful income distributions (REIT legislation requires a substantial payout of after depreciation earnings).

From a capital perspective, the REIT sector is in a strong financial position. By and large, the sector doesn't require meaningful additional debt or equity to meet any additional capital commitments, dividends are covered by operating cashflows and refi needs are manageable. Indeed, REIT capital structures are arguably stronger today than in any period entering an economic slowdown over the past 30 years. Most debt is structured with fixed interest rates generally for more than three years, cushioning earnings from short term market rate volatility.

Whilst an outcome of bottom-up analysis, towards late 2024 and into early 2025 we reduced our exposure to the U.S. REITs and are now meaningfully underweight the U.S. market for the first time since 2015. We have positioned the portfolio away from the more economically sensitive sectors and little development exposure. REIT capital structures are robust and at this stage we see no need to meaningfully increase cash levels. In addition, we will continue to focus on those REITs best placed to withstand more challenging tenant demand conditions.

Andrew Parsons is a Co-Founder and Chief Investment Officer at Resolution Capital, an affiliate manager of Pinnacle Investment Management. Pinnacle is a sponsor of Firstlinks. Resolution has launched the only active GREIT Fund in Australia (ASX:RCAP). This article is for general information purposes only and does not consider any person's objectives, financial situation or needs, and because of that, reliance should not be placed on this information as the basis for making an investment, financial or other decision. For more articles and papers from Pinnacle Investment Management and affiliate managers, click here.

Why Europe is back on the global investor map

Garry Laurence

So far this year, the DAX index is up 7% while the S&P 500 is down 12%. This illustrates Europe's biggest outperformance relative to the US in over two decades. Currently, the STOXX Europe 600 is trading at just 14.6x 2025 earnings, significantly lower than the S&P 500 trading at 19.4x.

Global investors are starting to diversify away from the US equity markets and the US dollar. The uncertainty surrounding Trump Tariffs has led to increased international diversification in asset allocation.

European equities offer a rare combination of quality and value. Robust European businesses (often founder-led with durable earnings streams) are trading at meaningful discounted valuations compared to those in the US. These companies are also exposed to unique opportunities only viable in the European market. The Euro is also appreciating, up 11%, against the USD this year.

Germany's fiscal shift: An economy boost amid market volatility

Amid the noise of global macro volatility, Germany has quietly staged a policy pivot. Its new fiscal policy, declared on March 4, aims to boost borrowings to renew economic growth.

Germany's major fiscal boost includes a new €500 billion infrastructure investment fund, an exemption from the 'debt brake' for defence spending above 1% of GDP, and a rise in the net borrowing cap for federal states from 0% to 0.35% of GDP.

This movement presents Germany's most aggressive fiscal stimulus in decades, positioning Europe as the next investment hotspot in the global macro landscape.

Europe's expansion of monetary and fiscal policy provides a drastic contrast against the US tariffs, which primarily attack US domestic consumers. The US is effectively tightening fiscal policy and heightening the risk of stagflation, which will make it hard for the Federal Reserve to loosen monetary policy. This divergence could be the catalyst for European equity outperformance from 2025 onward.

Our European investments

At Profeta Global Investment Funds, we invest in quality (and mostly founder-based) companies in the European market. We currently have over 30% of our portfolio invested in Europe in high-quality companies including Nomad Foods and Euronext. Our collection of European companies has delivered and is expected to deliver strong earnings results, despite market downturns and volatility, as we invest in their resilient cash flows and long-term growth potential. Our current positioning is governed predominantly by defensive businesses with stable and growing earnings streams.

Nomad Foods

Nomad Foods delivered a strong set of results with organic revenue growth of 3.1% in 4Q24, driven by 4.7% volume growth. EBITDA grew 17.6% and their earnings per share were up 31%. This is a very strong result for a consumer staples company.

Nomad Foods has seen an inflection in volume growth, driven by winning back market share from private labels as well as new product initiatives, particularly in the frozen chicken categories in Germany and Italy. The stock has been appreciating nicely in the past month, and we expect this to continue with positive earnings momentum.

Profeta met with Stefan Descheemaeker, Nomad Food's Chief Executive Officer, in London. Stefan founded Nomad Foods with Martin Franklin and Noam Gottesman, building the company into a leading frozen foods business in Europe.

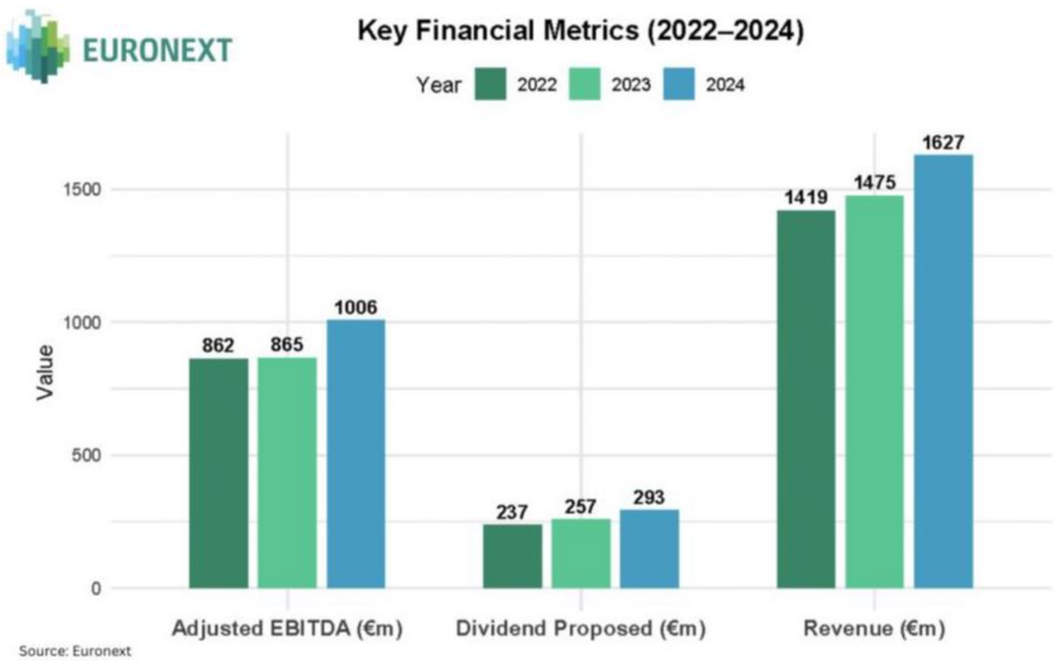
Over the past decade, Stefan has transformed Nomad Foods into a market leader in frozen fish, vegetables and poultry. The business has doubled earnings over the past decade and is expected to grow continuously earnings per share at a double-digit rate.

The United Kingdom is their biggest market with about 1 billion in sales, led by the Birds Eye brand. Nomad Foods also owns Ledo, the leading ice cream brand in Croatia, with a 70% market share. They have started selling Ledo ice cream in Austria, where the brand has strong recognition amongst consumers.

Since it was listed in 2014, we have been following Nomad Foods and have been impressed by Stefan and the team's execution in the food industry over this time. We have also been impressed with the capital management steered by the other two founders, Martin Franklin and Noam Gottlesman.

We like to invest long-term in owner-managed businesses with management being aligned with shareholders. In this case, we have this benefit as the founders still own 17% of the company, but we also have highly experienced billionaire financiers in Noam and Martin making the capital decisions.

Euronext



Euronext delivered a strong set of results for 4Q24 and the full year 2024. For FY24, revenue grew 10.3%, EBITDA was up 16.4% and adjusted earnings per share grew 19.6%.

All divisions drove strong earnings growth with trading revenue up 14% and clearing revenue up 19%. 58% of their revenue is from non-volume related businesses, making this equities-and-derivatives exchange a defensive business during weak economic cycles. Custody and settlement revenue grew 9% and advanced data services revenue grew 8%.

Profeta recently met with Georgio Modica, Euronext's Chief Financial Officer (CFO), in Paris. Georgio has been the CFO at Euronext for the past eight years, over which time earnings per share have more than doubled.

Alongside Stéphane Boujnah (CEO), the management team and the board, Georgio has done a tremendous job consolidating the European exchanges industry and building up the business both organically and through acquisitions.

Euronext's recent acquisition of Bolsa Italiana has been a success with most of the cost synergies delivered and all the clearing from London Clearing House migrated to their own platform. This has given them more flexibility to launch new derivatives products. Georgio is excited about the outlook for organic growth.

Their commodities derivatives are seeing strong growth with a large increase in the number of professional trading members. They are also set to launch power derivatives in the Nordics. In 2024, FX trading and power trading had a greater than 30% growth and Georgio expects continued strong growth out of fixed income and power trading.

Garry Laurence is the Chief Investment Officer at Profeta Investments. This article contains general information only and is not intended to provide you with financial advice or consider your objectives, financial situation or needs.

Chalmers' disingenuous budget claims

Tony Dillon

Jim Chalmers said in his recent pre-election Treasurer's debate with Angus Taylor that "there's been a $207 billion cumulative improvement to the budget bottom line. The debt this year is $177 billion less than what we inherited."

It's a line he trots out often, but in reality, gross debt has risen $45 billion under the Albanese government and is expected to hit $1 trillion in 2025-26. So what does he mean?

Chalmers is referring to a statement in the March Budget papers: "The underlying cash balance has improved by a cumulative $207 billion over the seven years to 2028–29, compared to the 2022 Pre-election Economic and Fiscal Outlook (PEFO)", and this "means that gross debt is $177 billion lower in 2024–25 than forecast at the PEFO".

So his statement that debt is 'less' is disingenuous. Something only falls when an ***actual*** number at a point in time is less than an ***actual*** number at a prior point in time. Not when it is less than a ***forecast*** number. Deviating from a guess is not the same as actual movement.

If we unpack the numbers here, $34.9 billion of the $207 billion is a restatement in the budget of the PEFO forecast underlying cash balances over the five years to 2028-29. The rest is actual deviation from the PEFO forecasts for the 2022-23 and 2023-24 financial years. The PEFO projected a combined deficit of $134.4 billion for the two years to 2023-24, but instead there were back-to-back surpluses totalling $37.9 billion.

When actual differs from forecast, it is usually due to government policy decisions and/or external impacts where key forecast parameters vary from reality. In the case of the two surplus years, the windfalls were almost all due to higher-than-expected commodity prices and therefore stronger company tax receipts. And, to a lesser extent, a robust labour market and a higher individual tax take, including some bracket creep.

Note that budget papers and the PEFO forecasts tend to be conservative with commodity price assumptions. They will normally revert to long-term averages quickly rather than persist with, or at least taper, prevailing higher market prices.

The 2022 PEFO was probably even more conservative with key assumptions, at a time when we were just emerging from the volatile Covid period. It surely is outdated for comparison purposes. In any case, had commodity price assumptions been more aligned with the market in the first two PEFO forecast years, the so-called budget windfall would not be as pronounced and would give politicians less to crow about.

How worthwhile is a comparison of actual to forecast budget measures, then? It can be useful but with limitations. In isolation, comparing forecast underlying cash balances to actual is not a good measure of fiscal prudence. But it can have some value if variations can be separated into policy versus external impacts. Are there factors outside of government control? Is there an element of luck?

A comparison can be worthwhile to the extent that forecast assumptions are realistic. If assumptions are too conservative, an apparent windfall might create the illusion of good government and tempt structural spending. Too aggressive, and worthwhile spending programs might be curbed. Forecasts should be as realistic as possible to foster policy and spending discipline, with actual outcomes used to assess policy decisions.

And as to whether a budget is really better off due to an actual versus expected windfall, that will depend on the nature of the gain and how it is used. If temporary, say as a result of a commodity boom, and the windfall is baked into permanent spending, then the budget has not improved. If temporary and used to pay down debt, then yes that translates into improvement. And if the windfall is structural as a result of good policy, then that improves the long-term budget position.

Budget numbers revealed a tax revenue windfall under the Albanese government of nearly $400 billion that contributed to the two surpluses. However, the bulk of that has been locked into spending, leaving just $95 billion to go towards budget repair. Spending as a percentage of GDP is forecast to reach 27.2% in 2025-26, up from 24.4% in 2022-23.

It would seem, then, that the government did not heed the advice of economist Chris Richardson. After the second surplus was revealed, Richardson said that "while it's very tempting whenever there's a surplus, we can't pretend that the good news is forever and make permanent decisions off the back of temporary luck."

Tony Dillon is a freelance writer and former actuary.

Duration: Friend or foe in a defensive allocation?

Haran Karunakaran

Before the 2008 Global Financial Crisis (GFC), duration – a measure of a bond portfolio's sensitivity to interest rates – was the bedrock of defensive allocations in investor portfolios.

However, in more recent times, this has changed - duration has been in the doghouse with Australian investors. And for good reason.

Low bond yields meant traditional fixed rate bonds paid very little income.

Low bond yields also weakened the defensive qualities of duration; the negative stock-bond correlation became less reliable. 2022 encapsulated these concerns, with bonds selling off in tandem with equities. Bonds failed to deliver on their defensive promise exactly when it was needed the most.

But one thing we know for sure is that markets are always evolving. And today, an important question investors should be asking is whether duration is still something to be feared.

A new era for duration: Learning from 2022

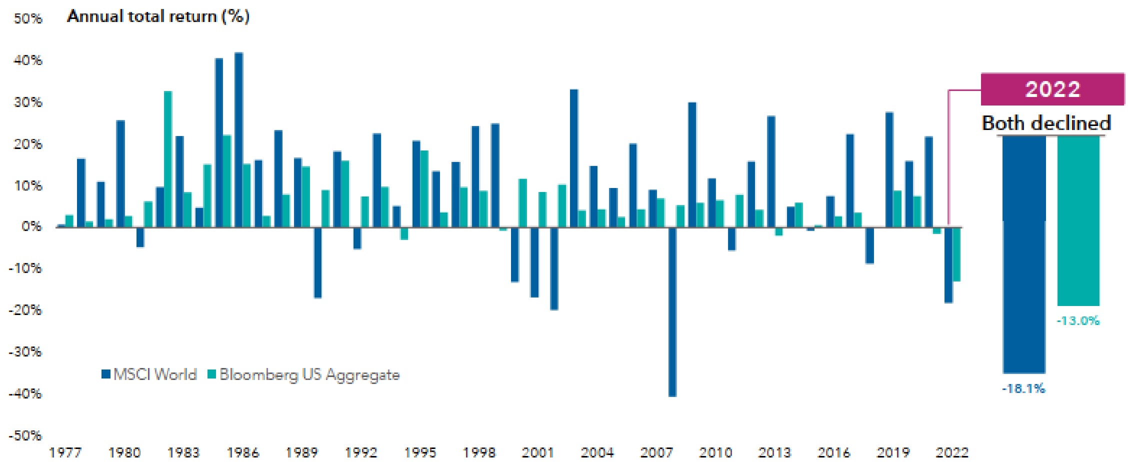
Many investors were understandably scarred by 2022. US equities declined by 18% and, while bonds did better, they too saw a decline of 13%.

It is important to put this in historical context – this was the first time in almost 50 years that both equities and bonds declined in the same year. And going back to 1977, there have only been 5 years in which bonds delivered negative returns. 2022 was unusual!

What drove negative returns for bonds that year? One of the most aggressive interest rate hike cycles we've seen in modern history. The Federal Reserve hiked the US cash rate by 4.25% (equivalent of 17 standard hikes!); the RBA was not far behind raising the cash rate by 3%.

Though this experience remains fresh in our minds, it is important to understand that a repeat of 2022 is very unlikely today. Our starting point is a much higher cash rate. Though a little above central bank targets, US inflation also sits in a comfortable range. The Federal Reserve sees rates as overly restrictive and expects to cut down to a 3% cash rate over the coming years. This would be positive for bond returns – a far cry from what we saw in 2022.

2022 was the first time in nearly 50 years that stocks and bonds both delivered negative returns



Past results are not a guarantee of future results. As at 31 December 2022 in USD terms. Returns above reflect annual total returns for all years. Stocks represented by the MSCI World Index. Bonds represented by the Bloomberg US Aggregate Bond Index. Sources: Capital Group, Bloomberg Index Services Ltd., MSCI.

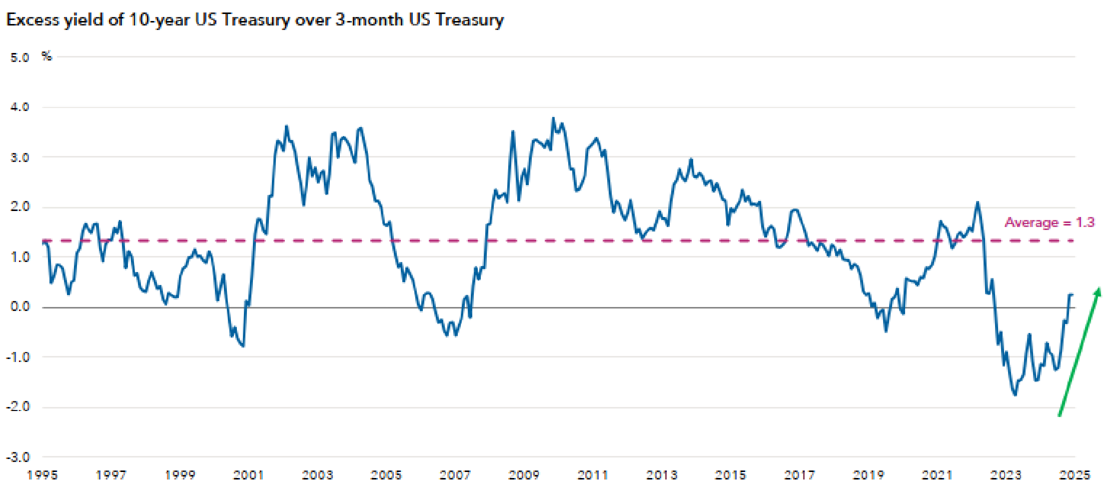
The often-overlooked benefits of duration

We believe that in stable market environments duration can be valuable in investor portfolios.

Firstly, duration has historically provided investors additional yield (or income) in portfolios. This benefit can be proxied by looking at the difference in yield between longer-duration bonds (e.g. 10 Year US Treasuries) and equivalent quality short-duration bonds (e.g. 3 Month Treasuries). As shown in the chart below, over the last 30 years this gap has averaged at 1.3%. In other words, an investor would have earned an additional 1.3% p.a. by allocating to fixed rate, duration exposed bonds.

The last two years have been quite unusual in that yield curves have been flat or even inverted. This has been normalising in recent quarters, and we expect to see term premia gradually return to levels closer to historical ranges.

Duration has provided additional income in most environments

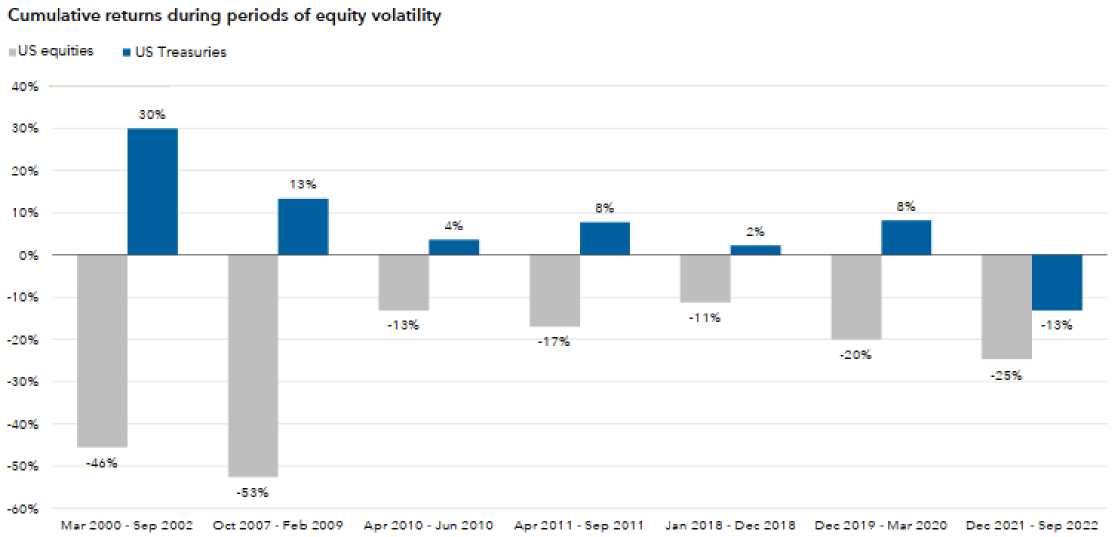


Past results are not a guarantee of future results. As at 31 January 2025 in USD terms. Source: Bloomberg.

Secondly – and potentially more importantly today - duration has historically been a good diversifier of equity risk (don't forget this key role of fixed income in a portfolio context).

In every significant equity drawdown over the last 25 years except for 2022, "hard duration" (proxied by US Treasuries) has provided positive returns, as shown in the chart below. In the uncertain times we now find ourselves in, this diversification benefit is critical. It allows investors to lean into their growth assets (e.g. equities, private credit etc.) with confidence, knowing that there is a strong defensive ballast there to provide potential protection in an unexpected downturn.

Historically, duration has been a good diversifier of equity risk



Past results are not a guarantee of future results. Data from January 2000 to December 2024, in USD terms. Source: Bloomberg. US equities represented by the S&P 500 Index. US Treasuries represented by the Bloomberg US Treasury Index. Analysis looks at equity market drawdowns greater than +10% since 2000.

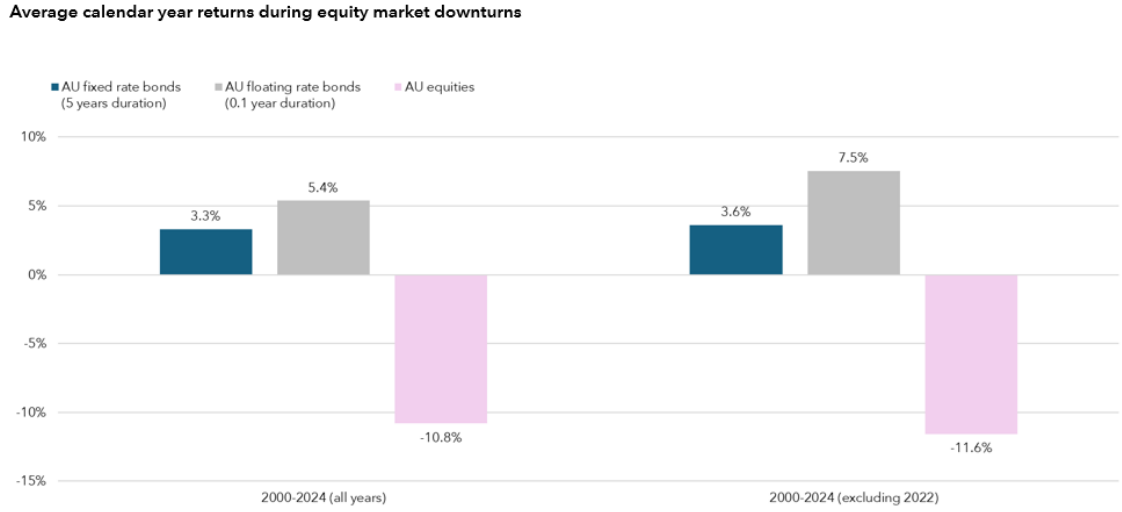
When thinking about the diversification benefits of bonds, it is worthwhile considering floating rate credit – now a 'go-to' fixed interest allocation for Australian investors.

Stating the obvious, floating rate bonds have negligible duration exposure. This means that their price is not impacted by interest rate moves. For example, if a central bank cuts rates in response to an economic downturn, floating rate bonds would *not* benefit from capital appreciation. This means the diversification benefit of floating rate bonds is limited.

This is illustrated clearly in the chart below, comparing the return of fixed vs. floating rate bonds during equity market downturns. Fixed rate bonds (with approx. 5 years of duration) have generated much stronger returns during equity market downturns compared to floating rate. If we exclude 2022 – an unusual 'one-in-fifty-year' occurrence – the diversification benefit of fixed rate bonds is even more pronounced.

While floating rate credit can add value in a portfolio, its role as a defensive ballast is not necessarily a strength.

Fixed rate bonds have provided stronger diversification benefits compared to floating rate



Past results are not a guarantee of future results. Data from December 2000 to December 2024, in AUD terms. Source: Bloomberg. AU fixed rate bonds represented by the Bloomberg AusBond Composite Index. AU floating rate bonds represented by the Bloomberg AusBond Composite Index. AU equities represented by the ASX200 Index.

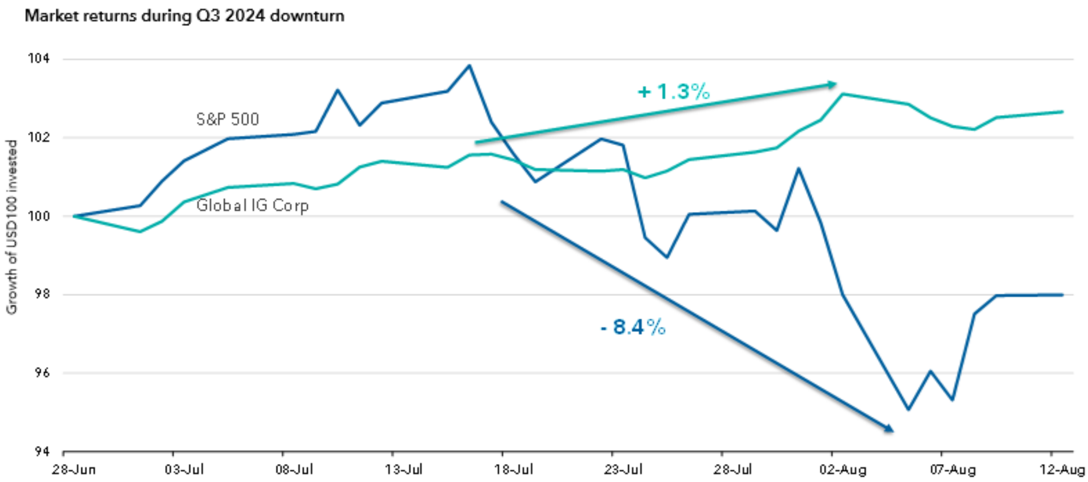
Duration's diversification benefits are more reliable today

More so than the last few years, fixed rate bonds today are well placed to provide this diversification within an equity dominated portfolio. Higher cash rates mean there is more room for bond yields to fall, which can provide greater capital appreciation during risk-off events.

Moreover, central banks now have both the ability and the willingness to cut rates when economic conditions worsen. This was less feasible in 2022 when cash rates were near zero and fighting inflation was the main priority.

This shift in the Fed's reaction function (and the market's anticipation of what the Fed might do) was clearly illustrated in early August 2024. At that time, a weaker-than-expected labour report in the US and lower market liquidity led to a correction in equity markets and increased expectations for Fed rate cuts. As equity markets sold off, higher quality bonds partially offset this with positive returns. With inflation now under better control, the Fed's dual mandate of managing inflation and employment has enabled it to shift its focus towards supporting the labour market.

Diversification in action



Past results are not a guarantee of future results. Data from 30 June 2024 to 12 August 2024, in USD terms. The investment results shown here are for S&P 500 Index (net dividends reinvested) and Bloomberg Global Aggregate Corporate Total Return USD Hedged Index. Source: Bloomberg. Fed: Federal Reserve. IG: Investment grade.

A time to be on friendlier terms with duration

Two years on from 2022 and investors remain cautious about duration.

However, we think now is the time to reconsider your biases. With heightened geopolitical uncertainty, having a strong ballast is crucial in a portfolio. And duration can play a key role in delivering that.

A combination of higher bond yields and a change in the macroeconomic environment means duration can now bring several potential benefits back to bond portfolios.

- **Additional yield compensation**: Comparable to pre-GFC levels
- **Returning diversification benefits**: Providing stability during market downturns
- **Lower risk of a 2022-style intervention from central banks**: Reduced likelihood of aggressive rate hikes

As a result, we think investors could benefit from adding a moderate amount of duration back into portfolios.

Doing this within a wrapper of a high-quality global credit strategy could be particularly attractive given the potential to earn additional income and take advantage of mispricing across this very broad universe.

Haran Karunakaran is an Investment Director at Capital Group (Australia), a sponsor of Firstlinks. This article contains general information only and does not consider the circumstances of any investor. Please seek financial advice before acting on any investment as market circumstances can change.

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$5.4 trillion wealth transfer poses deep questions on legacy

Rachael Rofe

Australia is in the midst of a $5.4 trillion intergenerational wealth transfer, the largest in its history. Fuelled by decades of rising property prices and investment gains, this unprecedented shift is prompting many Australians to rethink the question of legacy: *What do I truly want to leave behind?*

As James Gruber explored in his 12 March editorial, this transfer has the potential to entrench inequality, concentrate privilege, and distort economic incentives – what he termed a "generational tragedy." But the impact isn't only economic. When wealth arrives without context or purpose, it can disorient the next generation, dulling ambition, blurring identity, and eroding a sense of value. Warren Buffett's widely quoted maxim captures a growing sentiment: *"I want to give my kids just enough so that they feel they can do anything, but not so much that they feel they can do nothing."*

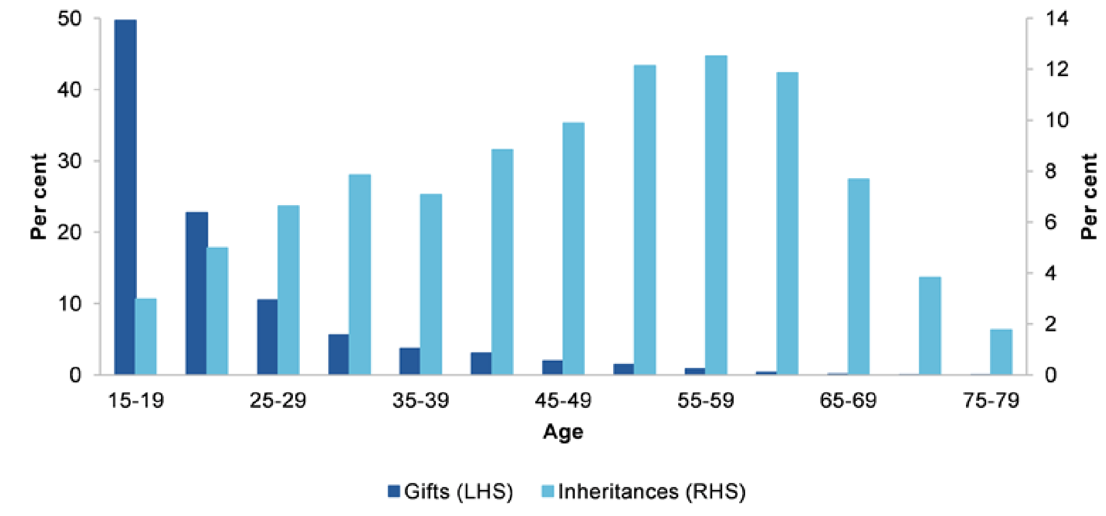
In response, Australians are turning to philanthropy. Not only to share wealth but to pass on values, engage their families meaningfully, and ensure their legacy enriches more than just their descendants. Structured giving vehicles offer a rare combination of emotional resonance and strategic advantage, enabling donors to model generosity across generations while accessing tax benefits, both during life and through their estate.

The new face of inheritance

Unlike previous generations, modern heirs are more likely to receive wealth at a time when they are less likely to need it. The average recipient is in their 50s, typically at or near peak earning years, and is often already established in regards to their career and property ownership. While the median inheritance across the population remains modest, the figures grow significantly in affluent households.

At the same time, financial dynamics within families have shifted. Adult children are increasingly supported earlier in life through home deposits, school fees for grandchildren, or gifts during their lifetime from the 'Bank of Mum and Dad'. By the time a formal inheritance arrives, many recipients are already financially independent.

Figure 1: Gift recipients are younger than inheritance recipients



Source: The Productivity Commission's [Wealth Transfers and their Economic Effects](#) report, December 2021.

If the kids are alright, what kind of legacy matters now?

A practical response: Giving structures

For families who want to pass on more than just money, philanthropy is a meaningful alternative. Structured giving through sub-funds (also known as giving funds) in Public Ancillary Funds or Private Ancillary Funds is gaining popularity as a way to model generosity, reduce tax, and involve future generations in purposeful giving.

Donations into these structures are fully tax-deductible in the year they are made or can be spread over up to five years. This has made them a popular tool for managing large tax events during life – such as business exits, asset sales, or bonuses – allowing donors to receive a larger tax deduction when they need it most, while retaining flexibility to thoughtfully distribute the funds to charities over time.

Chris Cuffe, Portfolio Manager and trustee Director of the Australian Philanthropic Services Foundation, notes that structured giving is increasingly common among pre-retirees looking to front-load their giving during their income earning years.

"Just as many people pre-fund their retirement through superannuation, structured giving allows you to pre-fund your giving, claim the tax deduction while you're earning, then support the causes you care about over time during your retirement alongside your children and grandchildren."

Once established, the capital is irrevocably committed to the community. A minimum of 4% (for public ancillary funds) or 5% (for private ancillary funds) must be distributed to charity each year, while the remaining balance is invested for long-term growth. Investment returns are tax-free, enabling the fund's giving capacity to grow and compound over time.

Structured giving can also play a strategic role in estate planning. Where an ancillary fund is already in existence at the time of death, assets bequeathed to it are eligible for capital gains tax rollover relief. This allows families to direct assets with significant unrealised gains into philanthropy, which maximises the impact of the gift while enabling a more tax-effective distribution of the estate.

More than money: A tool for connection

One of the most powerful aspects of structured giving is its ability to unify families around shared values. This alignment between purpose and planning is what makes philanthropy such a compelling legacy tool.

Parents are increasingly involving the next generations in conversations about charitable priorities, community needs, and family values.

For Simon and Susan Power, establishing a giving fund in the APS Foundation following a liquidity event opened a meaningful conversation with their children about wealth, responsibility, and impact. *"It's helped our kids understand the privilege we have and the responsibility that comes with it,"* Simon says. *"Giving has become part of our family's story."*

From the outset, the fund was designed to be collaborative. *"The key reason we set it up was to involve the kids in giving,"* he explains. *"They decide together who we support each year."* In the first year, their children chose a grassroots charity helping kids play local sport – something close to their hearts. *"We went to a presentation where supported kids spoke. It was incredibly powerful,"* Susan recalls.

Rather than a transactional handover of assets, philanthropy provides a platform for families to reflect on what they stand for. It is increasingly common to see a founder establish a giving fund during their lifetime, involve their children in decision-making, and use the fund as a long-term vessel for charitable capital – one that can continue well beyond their own lifetime.

"It's become something we do together as a family," Simon adds. *"We talk about what matters to us, and decide where to give. It's one of the most meaningful conversations we have."*

For some, this is about reimagining what they see as an outdated model of inheritance. For others, it's about anchoring their wealth in purpose and passing on a legacy of generosity.

A quiet shift is underway

Australians are generous – more than 80% give in some form – but what is changing is the structure, scale, and sophistication of that giving. There are now more than 3,000 ancillary funds in Australia, managing billions in capital committed to the community. "Contributions to these vehicles in the last financial year (FY24) are anticipated to have reached a record high, building on the exponential growth in contributions over the past decade.

Structured philanthropy is moving from the margins to the mainstream of wealth and estate planning. It's being embraced not only by ultra-high-net-worth individuals, but also by retirees with appreciated assets and professionals seeking to create lasting impact. While once considered the domain of the very wealthy, structured giving is now far more accessible, with meaningful benefits beginning to accrue from donations of around $40,000.

A legacy that lasts

The traditional model of inheritance is changing. For a growing number of Australians, legacy is no longer defined solely by the transfer of wealth but by the opportunity to pass on values, purpose, and a vision for the future. As we navigate the largest intergenerational wealth transfer in history, philanthropy is emerging not just as a way to give back, but as a way to look forward.

Rachael Rofe is Head of the [APS Foundation](), a Public Ancillary Fund offered by Australian Philanthropic Services.