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Can US house price falls happen here?

Roger Montgomery

We have all been reading and listening to the debate about Australian property prices and whether they are going to crash. It's hard to ignore when august journals like *The Sydney Morning Herald* report,

"The Australian real estate market is in the grip of the biggest housing bubble in the nation's history and Melbourne will be at the epicentre of an historic 'bloodbath' when it bursts, according to two housing economists."

More level heads suggest that for prices to crash either interest rates need to jump dramatically, or unemployment-inducing economic conditions need to transpire.

Hoping for a bargain

Perhaps because I love a bargain and I am an optimist (a value-investing optimist hopes for lower prices), I have until now been broadly in agreement with those expecting a correction of some magnitude. I was in Malaysia in the 1990's when the skyline was filled with cranes and I was in New York and Florida in 2007. In both cases, overbuilding was followed by a collapse.

Today, I am not sure whether we are due for a significant correction, despite the crane-filled skylines in Brisbane, Melbourne and Sydney.

The reason for my more sanguine view is the result of some simple calculations, using ABS data, into the demand and supply picture for Australian property. The weakness in my thesis is that I am looking at aggregate data rather than city-specific data. But aggregate data was all that was needed for some to predict housing price collapses elsewhere in the world.

Factors affecting house prices

Employment, inflation expectations, interest rates, debt-to-income ratios, house-prices-to-income, financial stress measures and the like all influence short-term property prices, but basic demand and supply seem to be the most important influences over the medium term. And given very few people buy property to 'flip' over the short term, it is the medium term we should focus on.

There is merit in looking at household formation as a proxy for demand and construction as our indicator of supply. With the exception of the circa 80% falls in property prices in mining towns in Australia, the most notable real estate price collapse that occurred recently was in the US.

Figure 1 illustrates one of the conditions that preceded the collapse; a sharp jump in the level of construction. According to the US Census Bureau, in the years prior to the GFC, the number of dwellings under construction had risen from 993,000 annually in 2000 to 1.1 million in 2003, 1.2 million in 2004, 1.4 million in 2005 and 1.2 million in 2006.

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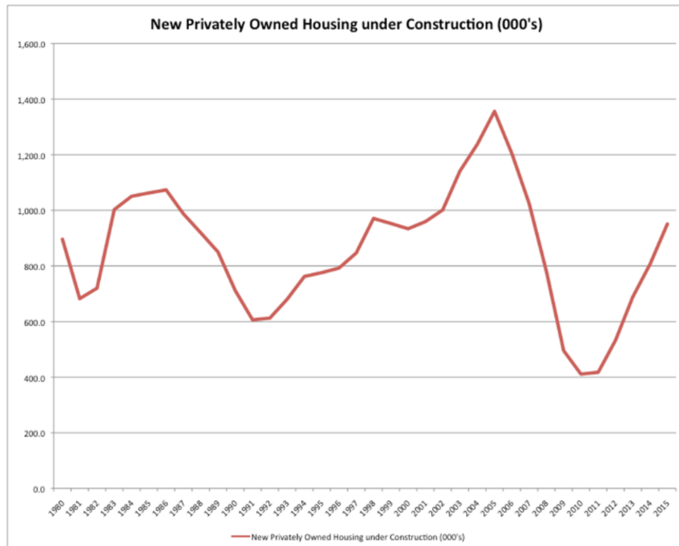
Figure 1. US private housing construction, 1980-2015



Source: US Census Bureau

Meanwhile, according to the US Census Bureau's Current Population Report entitled *Projections of the Number of Households and Families in the United States: 1995 to 2010,* household formation was increasing at about a million per year. In other words, the US was oversupplying dwellings for seven years, and by 2007, possibly a million excess dwellings needed to be soaked up.

Houses were simply being built faster than they could be occupied. In 2012, Warren Buffett observed as much when he said, *"In normal times, we need about one million or more homes to keep up with household formation."*

And we know what happened next.

How many residential dwellings are needed in Australia?

In Australia today, dwellings are being constructed at a rate faster than they can be occupied by newly-formed households.

According to the Australian Bureau of Statistics (ABS) March 2015 report *Household and Family Projections, Australia, 2011 to 2036*, *"The number of households in Australia is projected to increase from 8.4 million in 2011 to between 12.6 and 12.7 million in 2036."*

In other words, household formation is increasing at about 1.6% annually and in 2017 that equates to about 150,000 new dwellings required.

The ABS also reports dwelling units commenced and the construction industry is currently building about 56,000 dwellings per quarter. That's 228,000 per year, a lot more than seem to be needed. More importantly, this has been growing since 2011 when 35,000 dwellings were being constructed per quarter, which was about the same number as the number of new households being formed. It roughly balanced.

So if we assume an average of 47,000 dwellings were constructed per quarter in the years 2012 to the first quarter of 2016, and we add the 18,000 or 19,000 monthly approvals occurring now and project this number for eight months until the end of 2016, we arrive at a supply of 923,000 dwellings. During this period, the number of dwellings required, as estimated by household formation, is 716,249. That suggests an oversupply of about 200,000 dwellings.

At the current rate of household formation, that oversupply could be soaked up in about 18 months, provided construction of new dwellings ceased completely. But of course construction will continue and the oversupply will take longer to be absorbed.

It looks like Australia has a greater oversupply problem than the US did in 2007. The estimated 18 months is more than the twelve months oversupply the US had and after their property market collapse, it took five years before property prices began recovering.

What about sub-prime in the US?

But before we jump to the conclusion that we are due for a crash, keep in mind that our banks have not been extending $700,000 subprime mortgages to Mexican strawberry pickers earning $14,000 per year.

It's reasonable to expect property prices will not rise by much in the next few years and it is certainly possible they could fall. But the sort of falls experienced elsewhere in the world do seem unlikely, which means my hopes of a bargain in the next few years may be just that: hope.

However, I am reminded of the inflationary effect on global asset prices from quantitative easing. Cheap and plentiful money injected into the financial system triggered the purchase of assets by institutions migrating away from the safety of cash into (apparently) higher-yielding assets. But the easy money is over, particularly in the US, where the Fed ceased its third quantitative easing programme in October 2014. Since then the amount of money in the system – the US balance sheet – having reached about $US4 trillion (up from $800 billion in 2008), has stopped rising.

Unsurprisingly, the world economy is now slowing. If quantitative easing was responsible for inflating asset prices, the end of QE must surely have the opposite effect. And sure enough, it is.

Since 2014, commodity prices have collapsed; oil has fallen from $115 per barrel to $40 per barrel and commodities from wheat and corn to copper and cattle have collapsed. Other assets aren't doing too well either; the US, UK and Australian stock markets are about where they were in 2014.

So why are property prices persistently high? Because they aren't traded on an exchange. They're a clunky asset and re-pricing is less efficient as they can take weeks if not months to sell and even longer to settle.

And there's a generation of students, and twenty-something-year-old low to middle income earners with multi-million dollar mortgages over property investment portfolios that don't even know what an interest rate is. They aren't strawberry pickers on $14,000 but what will they do if and when rates rise?

Don't worry about rushing into residential property

One thing I'm confident about. The probability of a bargain is higher than the probability of prices running away from you. There's no need to rush and it may pay to have some cash around rather than a lot of debt.

Roger Montgomery is the Founder and Chief Investment Officer at The Montgomery Fund, and author of the bestseller 'Value.able'. This article is for general educational purposes and does not consider the specific needs of any individual.

Five lessons from the recent turbulence in share markets

Don Stammer

In the first ten weeks of 2016, share markets were often described as turbulent. Globally, shares shed 11% of their value between the start of the year and mid-February. Predictions of a global recession were frequent and shrill. Oil and iron prices tanked. Adding further to the gloom, a cleverly-marketed research report did its rounds, predicting a collapse in Australian house prices and bank shares.

Then, the widespread gloom dissipated. By mid-March, key share indexes in the US and Australia – and, surprisingly, those in emerging economies – had recovered most of their earlier losses. Bulk commodity prices shot upwards, with iron ore up by an impressive 66% from its low point. Bank shares were keenly sought.

Before drawing out the five lessons, what were some of the causes of these gyrations?

Markets often swing widely when big investors take or unwind similar positioning

In January and early February 2016, many large investors – hedge funds particularly - adopted similar investment decisions. This included selling, and in some cases shorting, assets that would likely plunge in price when China fell into a hard landing.

Fiduciary's Michael Mullaney described the January sell-off in shares as reflecting "an oversold condition with everyone on one side of the boat". Later, the rush to close out these short positions added intensity to the share market rebound, often at significant cost to investors still holding the short positions that were so popular among hedge funds previously.

Investors put too much emphasis on soft numbers on the Chinese and US economies

In January and early February, many investors interpreted data on China's external trade and manufacturing as confirming the 'contraction' of the Chinese economy. Subsequent information shows that continuation of useful gains in retail sales and the services sectors in China have partially offset the slowing growth in manufacturing and heavy industry. China faces many problems, but the hard landing predicted since 2011 has, so far at least, been avoided.

In the US, market sentiment in the early weeks of the year focussed too much on the risks of consumer spending remaining soft and on US banks being crippled by the write-downs on their energy loans. As it turned out, US job creation and consumer spending have continued to track at reasonable rates.

Lower oil prices hurt some … but benefit many

Recently, the key indexes of average share prices have often moved in lockstep with the oil price. It seemed as though the oil price was being taken as an indicator of global growth. As well, there were (exaggerated) concerns the lower oil price would create a banking crisis.

In reality, the fall in the price of oil – which results more from excess supply than from contracting demand – is bad news for most energy producers but will, over time, favourably affect many businesses (lower costs) and households (enhanced spending power).

Investors need to be wary of predictions of an imminent housing crash in Australia

Periodically, claims are made that Australian housing is in a bubble, house prices are about to crash and the prices of our bank shares will crumble because of bad debts.

A report marketed in January and early February by a local portfolio manager and a UK hedge fund argued our house prices and bank shares could soon lose half or more of their value. Their shrill conclusions were given front-page coverage in *The Australian Financial Review.* It carried no alternative expert views and gave little recognition to the low default rates that are a feature of housing finance in this country given that most loans are full-recourse to the borrower. Excesses in the Australian housing market are usually worked off by average house prices moving sideways for a few years; falling prices are rare.

The Australian Financial Review's Christopher Joye suggested investors who'd shorted bank shares would be scrambling to buy them back to close out their positions. Subsequently he commented,

"Bank stocks have bashed the 'johnny-come-lately' hedge fund barbarians that stormed the gates last week. The catalyst has been fact triumphing over the hedge funds' book-spruiking fiction."

What lessons have we learned?

I have distilled these five lessons from the last three months of turbulence:

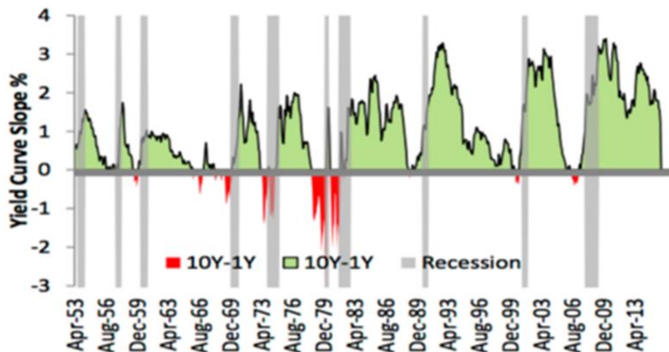
1. When sentiment on the global economy is fragile, the accumulation of even mildly negative news can drive share markets a lot lower. (Extreme things also happen when the prevailing view in share markets is ebullient. For example, a year ago, share markets rose on both good and disappointing news on economic activity: strong data because they suggested better profits; and weak data because they meant interest rates would be lower for longer).

2. When expectations in share markets build up in a largely uniform way, investor positioning – and the subsequent unwinding of those positions – can trigger big moves in share prices.

3. Sometimes (such as 2008), a sharp fall in share prices portends a lengthy period of difficult times for investors in shares. At other times (for example, 2011 and, it seems, early 2016), the crash in share prices soon corrects and may well be quickly forgotten. As Paul Samuelson famously quipped in 1966, the US share market had predicted nine of the previous five recessions.

4. The challenge for investors is to pick whether or not a share market sell-off will be followed by a lengthy slump in share prices. This requires giving fresh thought to the risk of an early recession. The traditional indicators of imminent recession include, but are not limited to: a sharp rise in unemployment; a sudden tightening in credit; and a flattening or inversion of the yield curve.

   In the US, the shape of the yield curve has a good record in predicting recessions, as the chart below shows. But much depends on investor confidence and sentiment, and that's hard to foretell.



5. Investors were too pessimistic early in the year on global growth prospects. Now, there's a more balanced outlook, with shades of grey in assessments on economic prospects in China and the US. But the key concerns of many investors – such as the sustainability of negative nominal interest rates in Europe and Japan and the stretched valuations on shares in companies with strong growth in earnings – have not been overcome. Further swings in investor sentiment should be expected in the months ahead.

Perhaps the most important lesson is that at times of stress, sensible diversification, including a good allocation to cash, makes sense.

Don Stammer chairs QV Equities, is a director of IPE, and is an adviser to the Third Link Growth Fund and Altius Asset Management. The views expressed are his alone and do not address the circumstances of any individual. This paper draws on material in a column by the author published in The Australian.

Superannuation's shift to digital communication

Emma Longmore and Richard Body

There's no doubt that superannuation funds are moving their member communication and education into the digital world and the pace is increasing. But compared to the broader rate of technological change and uptake in other industries, funds still have much ground to gain.

Willis Towers Watson has been monitoring funds' digital technology use since 2013. Last year, we went back to the industry to evaluate the overall trends and examine some key indicators, such as popular versus effective digital channels, potential roadblocks and what the future looks like.

Budget allocation to digital

All funds surveyed are increasing digital technology across a wide range of channels and, with it, their budgets. The current multi-channel take-up rate is 62% and funds are also using a wider spread of channels than previously.

In the past two years, 75% of funds have stepped up their spending on digital member communications by 10% or more. Around 35% of funds are spending $150,000 or more on digital communication (this excludes their fund website). Participants told us that the most significant investments to come will be made in improving mobile websites, their main website and webinars, as well as calculators.

Mobile websites are now rated as the most effective technology for communicating with members while more standard tools such as traditional websites and emails continue to be widely-used. Looking ahead, though, funds are expected to shift their focus to the use of apps.

Although apps, games and quizzes are not currently rated as effective as mobile websites, their use has increased at least five-fold. Our original survey in 2013 found less than one in 10 funds used these channels to engage members but, by 2020, funds believe apps will be their most-used tool for member communication.

Although ranked low in terms of overall effectiveness, participants who use social media (such as Facebook and Twitter) agree that as a liaison tool, it plays a crucial role. While a low touch tool for member communication, it is used by most funds to monitor the industry and the media and deal directly with member concerns. In 2013, participants acknowledged a small role for social media but it appears that funds are still feeling the need to have a presence there, mainly as a channel for listening and reacting to members.

Less than half of our 2015 survey participants use webinars, yet the same proportion rated them as highly-effective. The funds running them agree that they work extremely well.

Print still has a significant role to play in the overall strategy, but this is dropping, from 38% in 2013 to 32% in 2015. By 2020, this is expected to drop to 11%.

The benefits of digital

Funds told us a key benefit in using digital communication is that it is personal, targeted, immediate and interactive. Increasingly, members are only wanting information that is relevant to them. Funds say this trend will be a priority for them as they increasingly move towards using online benefit statements and other personalised communication.

A range of channels is in play and the mix is wider than ever before. Our 2013 report predicted the rate at which funds would take up a multi-channel approach would increase from 45% to 77% by 2017.

Perhaps this is no surprise. A study of 30 countries by *We Are Social* on how web traffic is shared across devices shows that although digital information is still largely accessed through laptops and desktops (approximately 60%), access via mobile devices already stands at 30% and growing fast. Ensuring fund information and tools can work across different platforms is therefore crucial.

Tools used to deliver education

Funds continue to pick and choose from a wide range of digital media. More traditional digital channels such as calculators, websites and email remain top tools (see Figure 01). Although not surveyed in 2013, around three quarters of funds surveyed are now using mobile websites as part of their member education package.

Survey respondents cited mobile websites to be the most effective technology, unsurprising given the statistics around increasing mobile use, followed by non-mobile websites (see Figure 02). At the time of our 2013 report, over half of the Australian population was using smartphones, but it has now grown to almost three-quarters. This raises the bar for how funds must evolve to match member preferences and continue to create more sophisticated mobile-compatible tools.

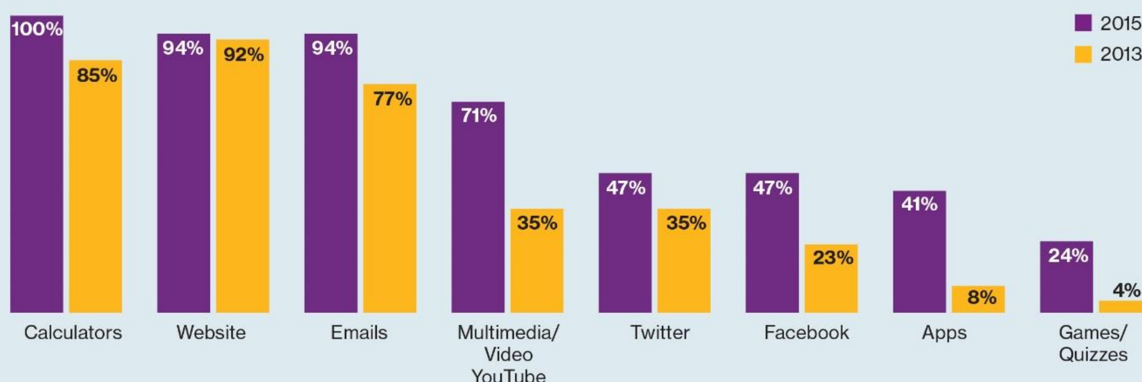
Figure 02: **How effective do you find these technologies in communicating with members?**

Most effective tools (% of "high" ratings received)

1. Mobile website (82%)
2. Website (75%)
3. Calculators (63%)
4. Emails (63%)
5. Multimedia/Video/YouTube (53%)
6. Apps (40%)
7. Webinars (40%)
8. Games/Quizzes (25%)
9. Facebook (20%)
10. Twitter (13%)

In 2013, almost all funds predicted that they would still be using standard tools such as websites and emails in 2017, and this has played out as expected. However, the future sees big drops in the predicted use of websites (down from 96% to 65%) and emails (from 96% to 53%) by 2020. It is possible

Figure 01: **Which online tools does your fund use to deliver financial education to your members?**



that in the case of websites, funds are switching their focus to mobile websites, however the reason for the expected drop in the use of email is less clear.

The use of calculators has increased, and was a feature in every fund surveyed in 2015, as compared to only 85% of funds in 2013. Looking ahead, four-fifths of funds intend to dedicate more resources to calculators.

The roadblocks

A key concern for funds continues to be around the security of member data, as well as practical issues such as resourcing and cost. Many participants felt that there was a skills and capabilities gap which might be restricting some funds from increasing the use of technology-based communication.

Since 2013, there has been little change to the perceived benefits of using technology to communicate with fund members. However, as members become used to regular updates, this breeds new challenges such as keeping up with continuous change.

Participants told us that learnings from the broader financial industry should drive much more sophisticated security and that superannuation needs to look at how banks have managed it.

Resourcing digital specialists who understand technology, digital and superannuation is incredibly difficult. Small to mid-sized organisations, in particular, would not find it viable to have one internal resource who has both the breadth and depth of skills needed in the digital space. As a result, super funds are partnering to help them grow their digital capabilities.

A full copy of our survey findings, with insights on current and future digital direction from UniSuper, Cbus, CareSuper, Kinetic Super, Maritime Super, HESTA and Australian Catholic Superannuation and Retirement Fund, can be found here.

Emma Longmore is the Communication Leader and Richard Body the Head of Digital Solutions for Willis Towers Watson Australia.

Estate planning: where there's a will, there's a way

Gemma Dale

Part 1 of this series on estate planning looked at the decision-making process that should be followed to prepare an effective plan. Parts 2 and 3 outline the documentation required to ensure that your strategy is effectively executed, starting with your will. Given you will not be around (or perhaps not have capacity) to ensure your wishes are met, an estate plan and a will must be carefully drafted by a qualified professional to ensure the outcome is implemented as intended.

Focus on the prime objective

In Part 1, we asked to whom, when and how you would like your assets distributed. Many people are advised to plan around tax minimisation or even prepare simple plans in order to save legal costs, without keeping their primary objectives in mind. Prioritising secondary objectives or trying to minimise costs can lead to adverse and even disastrous consequences for those left behind. Tax laws change and poorly-drafted documentation is more easily challenged (and overturned), and your beneficiaries may be left fighting for what was originally intended. It is critical to draft all your documentation around your original objectives.

Many people will go to a solicitor they know, but it may be better to choose an estate planning specialist if your circumstances are complex or your current solicitor is more of a generalist (if he or she looked after your conveyancing, for example). The Law Society in your state will have a list of qualified solicitors and information regarding specialisations, such as the Wills and Estates Law Specialist Accreditation.

What a will can and cannot address

Your will is the legal document that outlines how the assets that comprise your estate are to be distributed, but some primary assets are *not* included in your estate:

- any assets you jointly own with another person. Unlike assets that are held as tenants-in-common, these assets automatically revert to the surviving joint owner on your death.

- your superannuation. Superannuation death benefits can only be paid to specific individuals (see below) and the trustee of your super fund generally has discretion as to how these are distributed,

unless you instruct otherwise via a binding nomination.

- a reversionary income stream. If you have an income stream (such as a superannuation account-based pension or an annuity) with a reversionary beneficiary, it will not form part of your estate, but continue to be paid to that person.

- life insurance proceeds (including those held in superannuation). These will be paid to the nominated beneficiary on the policy, or according to the discretion of the superannuation trustee.

- assets held in a fixed or discretionary trust of which you are a trustee or beneficiary, or by a company in which you are a director or shareholder. Any shares or units you hold, however, generally will form part of your estate.

Your will deals with the remainder of your assets – cash, shares, property, personal effects and so on. Your solicitor will give guidance as to how your wishes regarding these assets should be documented. Some people are highly prescriptive about each asset, beneficiary and potential scenario (such as a specific bequest of each item to one person), while others avoid 'ruling from beyond the grave' and take a more principle-based approach (such as dividing the proceeds of the estate three ways if there are three primary beneficiaries).

Timing of beneficiary receipt

Timing of the receipt of your estate by young or otherwise vulnerable beneficiaries requires care. Some prefer their children to reach a mature age before accessing an inheritance, while others are comfortable with it being made available when they reach 18. Others provide for their children over time, for example, 10% at age 18, 40% at age 25 and so on, or providing for specific expenses such as university fees or a house deposit. A testamentary trust can assist with delivering to these objectives.

There are pros and cons to both the general and specific approaches. While the specific approach offers certainty, it can also create significant challenges if estate equalisation is an objective, as is common when leaving assets to adult children. How do you ensure each beneficiary receives a bequest of equal financial or emotional value? This is particularly difficult if asset valuations have changed dramatically since the will was drafted, or if other issues such as capital gains tax and sale costs have impacted the final value more than expected.

The downside of the general option is that it may require assets to be sold, with adverse tax and valuation consequences, if there are large assets that are not easily divisible. It may also create conflict if more than one beneficiary wishes to receive a particular asset. This is particularly common in rural families where the family farming property is the sole asset and only one beneficiary wishes to continue working on the land. Specialist succession planning assistance should be sought in this scenario.

Ultimately the decision to be highly specific or general in your will falls to you, however it helps to have a solicitor who is supportive of your strategy or who is willing to help you understand any limitations in your approach. A good solicitor will work through multiple scenarios, to check your wishes are met in different circumstances. These could include you pre-deceasing your spouse, you and your spouse dying simultaneously, your whole family dying simultaneously etc. While such scenarios are tough to contemplate, documenting your wishes in each event ensures that you have provided for those who are left behind.

Keep your will up-to-date

Your will should be checked and may require regular updating, either due to the passage of time, value of assets or a change in your circumstances. For example, a marriage or divorce will render your will invalid, but a marriage separation will not. If you do not update your will following a major relationship change, the entire estate may be awarded to a new spouse and children from the previous marriage may miss out. The period prior to a separation or divorce is crucial, because if you pass away unexpectedly, your previous spouse may inherit your estate against your wishes.

It's important to take control of your estate to ensure not only that your own wishes are met, but that problems are minimised for your beneficiaries at a difficult time.

In Part 3, we will look at other documentation, including powers of attorney, insurance and superannuation benefits.

Gemma Dale is the Head of SMSF Solutions at National Australia Bank. This information is general only and does not take into account the personal circumstances or financial objectives of any reader. Readers should consider consulting an estate planning professional before making any decision.

Unlisted managed funds fight back, even for SMSFs

Graham Hand

In recent years, the growth of Listed Investment Companies (LICs) and Exchange Traded Funds (ETFs) has captured the headlines, making unlisted managed funds appear old-fashioned and outdated. This is despite the fact that Australian retail managed funds hold about $750 billion (according to Plan for Life), compared with about $30 billion in LICs (according to the ASX, up from about $15 billion in 2012) and about $22 billion in ETFs (according to BetaShares, up from about $5 billion in 2012).

Clearly, LICs and ETFs are making inroads, boosted from 1 July 2013 by the banning of commissions paid to advisers by providers of managed funds on new allocations, and the increasing use of ASX-listed products. ETFs have been driven by low costs and interesting product niches, while LICs have benefited from high-profile managers moving into this space with attractive deals heavily promoted by brokers. But managed funds still dominate portfolios overall.

What is the evidence managed funds are recovering?

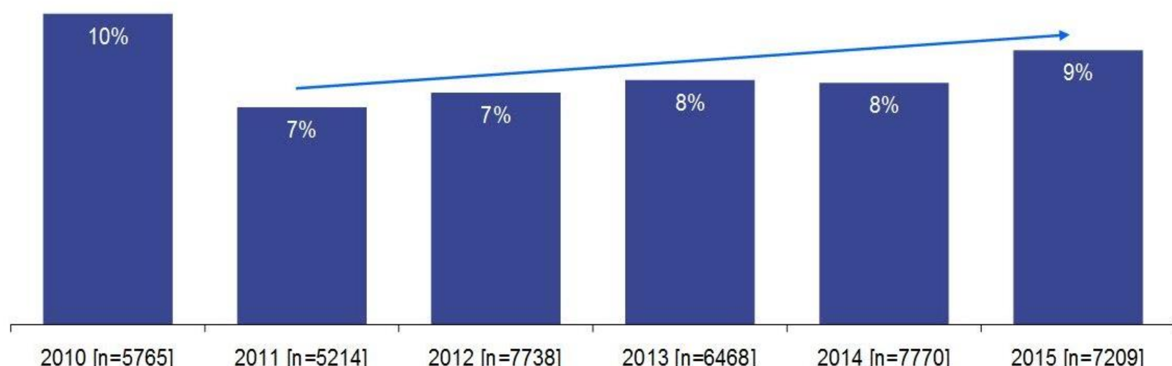
The Investment Trends *2015 Investor Product Needs Report* surveyed almost 10,000 investors in October 2015. It showed investors are finding it more difficult to identify investment opportunities in shares, but unlike previous times when they switched to cash and term deposit, now they are hunting elsewhere for income and capital growth. They are turning back to professional fund managers, with 15% of investors saying they intend to invest in unlisted managed funds, compared with 12% two years ago. The gradual recovery in investible assets in managed funds since 2011 is shown below.

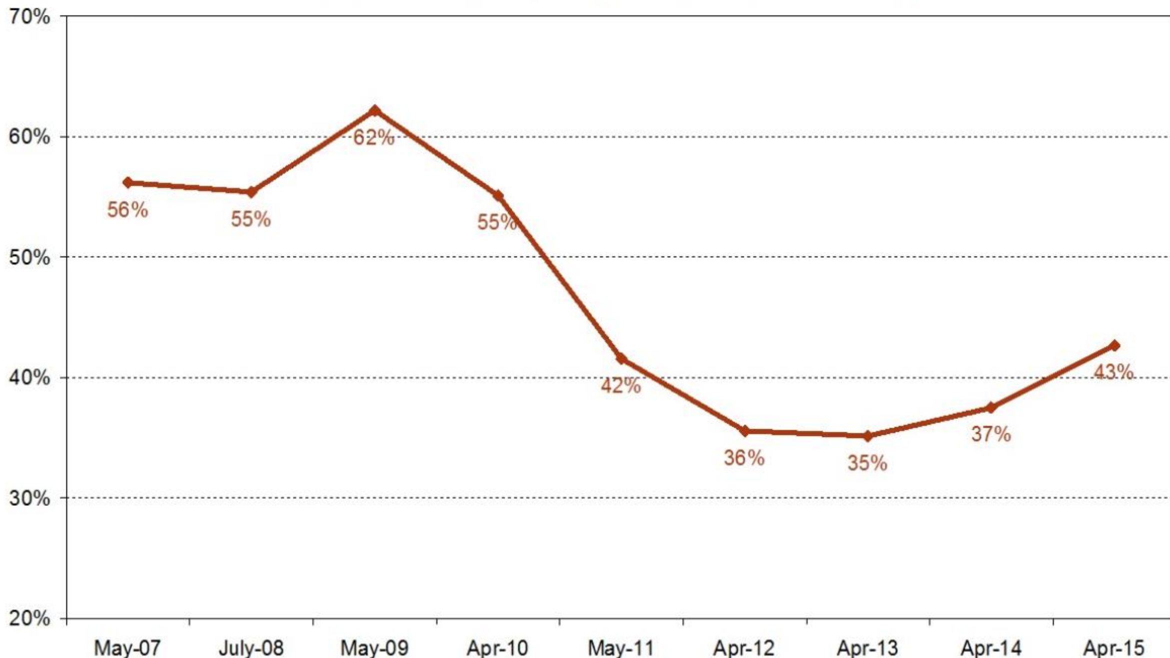
Investment Trends also reports an increase in self-directed activity, with 'word-of-mouth' and 'online channels' instigating investments into managed funds. This shows up in the increase in SMSFs using managed funds, shown next page. Surprisingly, the share of people first learning about managed funds through 'family and friends' has risen from 14% to 27% since 2012, with advisers falling from 42% to 27% over the same period.

According to Plan for Life, the leading five providers of managed fuds are BT (18.5% of total FUM), AMP (17.4%), CBA/CFS (15.8%), NAB/MLC (14.2%) and Macquarie (8.1%).

As further evidence, OneVue reported in its recently released SMSF asset allocation survey for December 2015 that, among its clients, investments in managed funds rose by 5.1% to 28.2% of total assets compared to March 2015, with listed shares falling by a similar amount. Investments in cash and term deposits also fell. OneVue noted that its SMSFs are advised by accountants and financial planners, and these portfolios differ from self-directed.

Allocation of investable assets to unlisted managed funds across all investors
Dollar weighted averages as a percentage of all investments
Source: Investment Trends October 2015 Investor Product Needs Report





What type of funds are being used?

The types of managed funds (as well as ETFs and LICs) attracting more attention are:

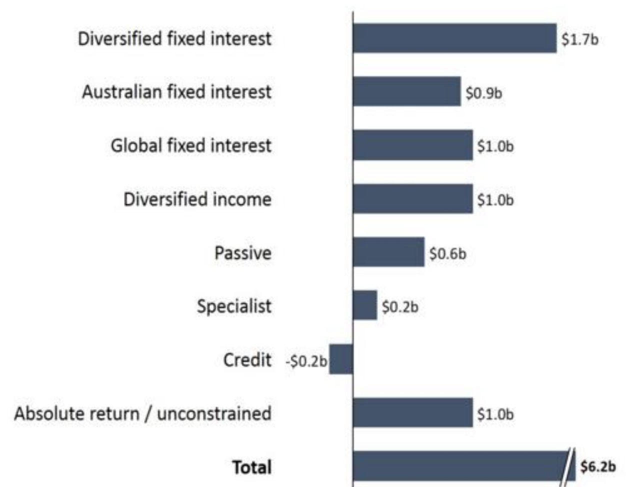
- international equities
- active Australian equities
- infrastructure
- property
- income funds, including bond funds and equity income.

Global funds have become more popular as investors realise the importance of diversifying beyond the ASX, which is dominated by a few banks, Telstra, BHP, Woolworths, Wesfarmers and Telstra. There was also a widespread expectation over 2015 that the Australian dollar would continue falling. While there remains a perception that active fees are too high, more SMSF trustees are turning to active managers because they are finding it difficult to pick stocks outside the ASX20.

Infrastructure, property and income funds are all benefitting from the low interest rates available on cash and term deposits, and the perception of their defensive characteristics.

This final category was probably the year's biggest surprise, especially in fixed interest. The global bond market is estimated at about USD100 trillion, far larger than the value of all listed companies on the world's stock markets. Yet traditionally, fixed interest plays a minor role in most self-directed allocations, including SMSFs. However, Tria Investment Partners reports all types of fixed interest did well in 2015, and "the data shows fixed income is continuing to receive healthy new flows, and more than any other single asset class."

This is an asset category where managed funds have a much better range of alternatives than LICs (where fixed interest is negligible), although there are several bond and cash ETFs available.



What role is mFunds playing in the managed fund recovery?

The ASX offers a 'settlement service' in managed funds, which allows an easier investment process than the painful, time-consuming process of filling out the offer document of a fund manager. Like ETFs and LICs, certain managed funds can be accessed on market in the same way as shares.

The mFunds service can best be described as a 'work-in-progress'. It has been boosted recently by the addition of new fund managers such as Fidelity and J.P. Morgan, and the first major bank online broker, nabtrade, and now offers a broad range of managers and fund styles. But it can only be accessed through a participating broker, and the two largest retail online brokers, CommSec and E*Trade, are not participating to protect their own businesses (and those of related companies). The total amount invested through mFunds, according to the ASX Funds Monthly Update February 2016, was only $102 million spread across 149 funds. About half that is in fixed income, a healthy percentage.

Nevertheless, mFunds is not yet material in the overall picture.

Each product type will have its place

It's difficult to see a future in wealth management without a strong role for all three structures: managed funds, LICs and ETFs. Both LICs and ETFs are on a rapid growth path, and ETFs in particular will be boosted by ongoing cost focus and the (albeit slow) trend towards roboadvice.

But those who have written off managed funds should recognise it is not only the reigning champion in terms of FUM, but with massive fund manager support, hundreds of millions of capital invested in major platforms, adviser and bank branch distribution and wide product range, it will not relinquish its crown anytime soon.

Graham Hand is Editor of Cuffelinks.

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