Transcript

The Ideas Exchange

Episode 18: How clear goals help you find the investment that is right for you

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[00:00:03] **Rory Cunningham** Welcome to the Ideas Exchange by ASX connecting you with market experts, investment updates and ideas. I'm Rory Cunningham, Senior Manager of Investment Products at ASX and this is our monthly podcast covering everything from investment trends through to different ways to invest using a variety of products.

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[00:00:56] **Rory Cunningham** Thank you for listening to the Ideas Exchange podcast. We're joined today by Shani Jayamanne from Morningstar. Shani, thank you very much for coming on the show.

[00:01:05] **Shani Jayamanne** Thanks so much for having me, Rory.

[00:01:06] **Rory Cunningham** Shani, before we get into our discussion, can you tell the audience a little bit about yourself? What do you do at Morningstar and how did you get into the industry?

[00:01:14] **Shani Jayamanne** Yeah, for sure. So I work as a Senior Investment Specialist at Morningstar Australia, and I'm a co-host of the Investing Compass podcast. What I do there is I work in the individual investor team and I try and make the information about equities and capital markets accessible for all. So, it can be a really complex area and I try and distil this down into really simplified concepts through the podcast, as I mentioned, webinars and also guides and written content.

[00:01:43] **Rory Cunningham** So today we're going to be talking a little bit about goals based investing. Shani you've recently published a paper that I had the pleasure of reading, and the paper is really targeted at trying to help investors find the right vehicles to achieve their investment goals. The guide is called 'Selecting Investments That Are Right for You', and it's taking a look at how investors can take a goals based approach to investing. So my first question for you, Shani, is how is goals based investing different from any other type of approach to investing?

[00:02:14] **Shani Jayamanne** Yeah, that's a really great question, Rory. Essentially what a goals based approach is, is that your portfolio is constructed around achieving a particular financial goal instead of just making as much money as possible. So the key to goals based investing is that we focus on the investor and not the investment.

So we've seen a lot of retail investors flow into the market recently where they've been able to throw a dart a dartboard blindfolded and get good returns. And that's been without any consideration for the risks that they're taking on and the goals that they're trying to achieve. Their objective is simply wealth maximisation, so they're just trying to make as much money as possible. And of course, that works great when the markets are going up. But we've seen in the last few years, sorry, in the last few months, that it's caused a lot of nervousness for many investors as markets have tumbled. And we saw a lot of volatility and we are still seeing volatility in the market today. So what goals based investing means is that you're just taking in the amount of risk that you need to achieve your goals and nothing more. And it also means that you've selected investments that you know are aligned with what you're trying to achieve. So you have more confidence in the investments that you've chosen and there's less chance of you buying and selling, switching out of investments every now and again just because of the volatility in the market is making you nervous. And that will be to the detriment of your portfolio returns.

[00:03:22] **Rory Cunningham** Yeah, I think the growth in the amount of retail investors entering the market is something that we've definitely observed from an ASX perspective. In my day job I look after the ETF market and there was an incredible jump in the number of investors buying ETFs back in March of 2020. It's now estimated that there's probably about 2 million investors in Australia that are using ETFs. And I suppose what you're saying there is, instead of buying an ETF or a fund or even a stock first, take a step back, think about what is the goal that you're looking to achieve. Is that right?

[00:03:57] **Shani Jayamanne** Yeah, exactly.

[00:03:58] **Rory Cunningham** Great. So for someone that's looking to invest based on their goals, how do they approach portfolio construction?

[00:04:04] **Shani Jayamanne** Yeah. So I'll give a really brief overview of this because we want to focus more on how to select investments. But there is a full walk through of constructing a portfolio in an episode of Investing Compass, which is a podcast that I co-host with Mark LaMonica as part of Morningstar Australia's podcast. So the first thing that you really want to do is you need to define your goals and whether that's buying a house or a three month holiday or a comfortable retirement, whatever it is, you need to know how much it's going to cost, how much you've already saved towards the goal, and how long you have until you achieve it. And once you've done that, you need to work out what you need in terms of a rate of return from your investments. And you can do this with any financial calculator. It's basically a rearrangement of the time value of money formula. So you can search for one on Google or we have one on Morningstar Investor, which is our subscription product that you find the percentage annual return that you need to get to your goal. So that's your required rate of return. And of course you need to account for inflation to make sure that you maintain your purchasing power. So a dollar today isn't worth a dollar tomorrow. So you just need to make sure that you're accounting for that. And this process does seem quite complex when you explain it like this, but again, it's detailed exactly how to do it in the portfolio construction episode that we have.

[00:05:11] **Rory Cunningham** Yeah, inflation is a really important factor to keep in mind, particularly in the current environment where we're seeing a rapid rise in inflation around the world. So how does your rate of return feed into selecting your actual investments then?

[00:05:25] **Shani Jayamanne** Yeah, great question. So as we spoke about, we want to make sure that your investments and investing is centred around the investor. So why do you actually invest? You invest to reach financial goals. You're not investing just for the sake of it. And so you need to be able to define this rate of return. And that means that you understand firstly whether your goals are achievable. So if you end up with a required rate of return of 25%, it's more than likely that you're just not going to be able to sustain that type of return over the long term. So you're able to adjust your expectations or adjust the other variables so you can save more or give yourself more time to reach your goal. So it's really about having a plan and adjusting that plan as you move on. And so this rate of return informs the type of asset allocation you have. So Roger Ibbotson, he was an extremely well regarded professor and he was a founder of Ibbotson Associates, which is now actually a Morningstar Company. He says that on average, 90% of the variability of returns and 100% of the absolute level of return is explained by asset allocation. So asset allocation is pretty important and it's a huge determinant of your total return outcome. So what you're actually going to have at the end of the day in your brokerage account or your portfolio.

[00:06:32] **Rory Cunningham** Okay. So if we take it in different steps, step one, what's the goal that I want to achieve? It could be buying a house, saving up for a car, saving up for a holiday. Step two, think about the rate of return that I need in order to achieve that financial outcome. And then once you've decided on that, then you need to think about what asset allocation I need in order to achieve that type of return. So what is asset allocation?

[00:06:56] **Shani Jayamanne** Yeah. So asset allocation is simply how much you're allocating to each asset class. So an asset class could be Australian equities, it could be international equities, it could be a fixed income. So you purposefully allocate based on the prospective risk in return for that asset class. So at Morningstar we have asset allocation guides based on how much risk you need to take to achieve your goal. We're definitely not the only ones who do this, they're all over the internet, so you can go and find one. But I can give you an example of ours, so our aggressive asset allocation looks at a return of CPI plus 4. So 4% above inflation to ensure we also maintain that purchasing power that we were talking about. So it has a 35% allocation to Aussie equities, it has a 45% allocation to international equities, with half of that in hedged and a smattering of allocations to Aussie and international listed property, infrastructure, fixed interest and cash with the remaining 20% there.

[00:07:47] **Rory Cunningham** Yes. So I'm not going to lie. This seems like a pretty involved process.

[00:07:51] **Shani Jayamanne** Yeah, it is.

[00:07:54] **Rory Cunningham** Can you talk us through, practically as an investor, how I start to go about implementing that?

[00:07:58] **Shani Jayamanne** Yeah, for sure. There's a difference between what we're talking about now, which is a very structured approach as opposed to just investing in a couple of ETFs on the ASX, because that's really worked well for investors, especially those who started investing in the last ten years. We've had a really good market where it's just been this extended bull run and investors have been able to profit. But that is definitely an anomaly. If we look at the past hundred years, on average, we've had a bear market every three years and the market is just not this hockey stick to the sky that keeps going up and up, over the very long term it is, but

there's lots of volatility in between that and you really have to look at your goals in terms of when you need to achieve them because they're usually a shorter time frame than that. And you can definitely do that. You can invest in a few ETFs and just hope that you reach your goal, but it's definitely better than not being in the market. But it's important to remember that a large part of investing and your outcomes is determined by your behaviour. At Morningstar we do do a study called 'Mind the Gap' and it looks at the behavioural gap. The behavioural gap is how much our irrationality really costs us as investors. And the way that we study this is that we look at the return achieved by a fund and then we look at the return received by an investor. And these are different. So the fund return is based on the underlying assets in the fund. The investor return is based on the inflows and outflows of actual investors deciding to buy into a fund or sell out of a fund. And those inflows and outflows have no direct impact on the performance of the fund. But the timing of your investments have a huge impact on the return that you get. So we found that that gap is huge between the investor and the investment. So we did a really comprehensive study back in 2013 where we looked at ten year returns and we compared the average return of funds and the average return of investors. And looking at global share funds in the survey, we found the average return over ten years was 8.77%, which is pretty good over ten years. And then we looked at the average return that investors got and it was 5.76%, which is not as good. So that difference of almost 3% a year is a gap that occurred because we make poor decisions as investors. We just decide to switch in and out of investments depending on what's going up and what's going down. And that's called the behavioural gap. And so when we look at how to prevent this, you prevent it by having confidence in your investments and having a plan which shows why you're invested in certain assets. So, have a plan that's written down and quantified. So this is the plan structure that we recommend at Morningstar. And, you know, this podcast was supposed to be about selecting investments and it will be, but we deliberately do this as the last step because we believe that each investment you hold in your portfolio should be deliberate. It should be linked to your financial goals, and it should have a purpose. And that way you're much less likely to switch in and out of investments and penalise yourself for doing so. Because when you look at 3% per annum, it is a huge difference, especially over a long time frame and compounding of returns, especially if you're reinvesting your dividends. So it is really important to just make sure you have a long term horizon, you have the confidence in your investments and you stick to your plan.

[00:10:53] **Rory Cunningham** Yeah, I think the point that you made around investors that have been investing over the last ten years is a really good one. I recorded a podcast with Gemma Dale last month and we talked about the rising interest rate environment, and for anyone that has been investing or started investing in the last ten years, they have not invested into a rising interest rate environment. So these things that we're talking about are extremely important, I think, for experienced investors, but arguably even more important for investors that have come to the market in the last 5 to 10 years. Okay. So we've built a plan, starting with a financial goal, finding out your required rate of return, then the asset allocation mix that you need in order to get to that return. So how do we actually then start to select the investments? Keeping in mind that there's a lot of choice out there.

[00:11:42] **Shani Jayamanne** So, first you need to understand how long you have until your goal. So generally, short term goals will require assets with liquidity and little to no volatility. So most likely a cash product. Your medium and long term goals will require a mix of assets and that ratio depends on how much risk you need to take to achieve your goals. So the types of investments that you have in each bucket will

vary. So the process of selecting investments does need to be repeated for each bucket.

[00:12:05] **Rory Cunningham** And by bucket you're referring to the different asset classes?

[00:12:08] **Shani Jayamanne** Yeah, exactly. So in the guide that I've written, it goes through a decision tree. And the questions you have to ask yourself when you're selecting investments are, are you going to invest in individual securities, so stocks, or are you going to invest in collective investment vehicles? And collective investment vehicles are simply ETFs, managed funds, LICS, etc. Then if you decide on a collective investment vehicle, you have to decide whether you're going to go active or passive. So active is when you have a professional picking the assets for you, and passive is when it follows an index or basket of securities that have the same characteristics. Either way, there's no one picking the assets for you in passive investments. And then the third question is whether you're going to focus on exchange traded or non exchange traded products. So that's simply whether you buy something that's on the ASX or whether you buy something unlisted like a traditional managed fund. And I think it's important to mention here that you've got to ask these questions for each asset class that you are investing in. So it might be easier to invest in international securities through an ETF. I recently read a study that had statistics on SMSFs and how they're actually accessing international securities, and by far it was through ETFs. So you might want to focus on ETFs for international securities, but then for domestic securities, you might want to go to individual stocks.

[00:13:19] **Rory Cunningham** So just to kind of separate the two, so we've got asset classes that we're going to use to achieve a desired rate of return. And those asset classes from conservative through to risky go cash, fixed income, property or property securities and then equities and equities can be broken down by domestic equities. Those are those stocks that are listed on the ASX and then there's international equities that are listed on overseas markets like the New York Stock Exchange, Nasdaq, London Stock Exchange, etc.. And then what you're saying is in order to get access to those asset classes, you can either invest directly. A lot of investors will be familiar with investing in Australian stocks directly. There are companies like CBA and BHP that are listed on the ASX or you might use a collective investment vehicle such as an ETF or a managed fund in order to get access to those particular asset classes.

[00:14:18] **Shani Jayamanne** Yeah, exactly.

[00:14:18] **Rory Cunningham** So when deciding if you're going to invest in individual securities or use those collective investment vehicles, how do you make that decision?

[00:14:27] **Shani Jayamanne** So investors all have circumstances and goals that are individual to them, one size does not fit all. So equities, as you mentioned, Rory, they vary in region, they vary in sector, size, there's like small, mid, large cap stocks. And they have a multiple of variables regarding financial positions as well. And that means that equities are able to offer range and choice for investors. And they don't also have fees of professional management that you have with collective investment vehicles. Then apart from variety, you should really consider whether you have an investing edge that will offer you an advantage over professionally managed products.

[00:15:01] **Rory Cunningham** Investing edge, I love that. What is an investing edge?

[00:15:04] **Shani Jayamanne** Yeah, so investing edge are advantages that investors have that make it more likely that they'll be successful with equity investments. So you just want to make sure that you're thinking about whether you have any of these edges. And that might mean that investing in stocks directly is what's right for you.

[00:15:18] **Rory Cunningham** Okay, so what are the different types of edges that an investor can have?

[00:15:23] **Shani Jayamanne** Yeah. So there's four main advantages that we believe investors can have and those are informational advantage, analytical advantage, structural advantage and behavioural advantage. So we can start with informational advantage and that means you know something about a company or an investment that others don't and that means that it's not priced into the equity. So traditionally this meant insider information, but we don't consider that because it's illegal. But this edge was a lot more common when the investing community was exclusive and it wasn't democratised like it is now. Like any investor now can go and invest on the ASX, but before it wasn't really like that. So almost everyone has access to the same information as each other. Like if you go onto the ASX website, it has all of the financial data that you could ask for. It has a lot of information on ASX stock. So it's extremely hard to find an informational edge because there's so much information out there that everyone can access because of the Internet. And you know, there's pretty crazy stories about how hedge funds would hire satellites to count cars in shopping centre parking lots to anticipate future returns. But obviously as individual investors, this isn't something that we can do. So, you do need to consider whether informational advantage is really something that you have because it doesn't really exist in a traditional sense. So there's analytical edge and it refers to the ability to interpret widely available information in an insightful way. So, analytical edge, it can manifest itself in many ways. So it might take the form of a quantitative model, and that's able to look at security or economic metrics a little bit better. Or it may simply be that an individual has a deep knowledge of an industry and can better predict the impact of a company strategy or if there were any legal or regulatory changes or even a business trend. So this is what we try to do at Morningstar. So that's our analysts. So they do analyst research reports and they have very in-depth knowledge of the industry, the market conditions, the company. And so we try and use Analytical Edge to provide our subscribers with more information. And then there's a structural edge. And this is where we at Morningstar believe individual investors can really find an advantage against professionals and professional investors. They do have competing priorities. They're trying to do things that support the company that they work for and maximise their own compensation. Obviously, we all go to work to do a job and we do it to earn a paycheque. So they're all trying to do the same thing as us. And you know, your only focus as an investor is to achieve your goals.

[00:17:44] **Rory Cunningham** So let's talk a little bit about structural edge. You mentioned that there's competing priorities. So how does competing priorities impact the return outcomes that investors get compared to if they were just investing themselves?

[00:17:58] **Shani Jayamanne** Yeah, so it's easier for individuals to have a focus on long term investing. Lots of professionals say they are long term investors, but the environment that they operate in just doesn't encourage this. So many professionals are under pressure to outpace or at least match that his peers over one year periods, because if they fail, that investor money walks, like you see all of these sort of graphs

that you see on the AFR every year where it's like these are the top funds that have outperformed and you normally see in the next year or so that a lot of the funds do flow into these funds. So, we do see that professionals do compete in this way. And what it usually does is it causes something called closet indexing, and that's when active managers build portfolios that don't really differ that much from underlying indexes. And it also leads to performance chasing, where professionals are really just focussed on hot stocks and sectors. And what that leads to is that many professional investors really just lack the patience to wait for stocks trading at meaningful discounts, to fair value, or their patience to hold cheap and unloved shares long enough for them to approach fair value. So that's really just saying that they're not able to invest for the long term. They really just have to keep switching in and out, have to keep making these decisions based on how the public are perceiving their performance. So we conducted a study at Morningstar of U.S. domestic equity funds, and it found that turnover rate was 63%. And turnover rate is simply the average holding period for stocks and how much they actually switched in and out. So the average holding period for stocks was 19 months, and we just don't consider that long term at all. And, you know, you have to consider the transaction costs that come with trading that often, not to mention the capital gains that you get from that constant turnover. So it's not like professional investors aren't aware of how important it is to invest for the long term. They probably know better than most. But the issue is that they're in this high pressure environment where they have a few things competing, obviously returns, but also are competing against their peers and being compared against their peers, their job security and obviously their remuneration, because most of the time, I've worked at fund managers, their bonuses are usually tied to the performance of their funds. So there's all these things to consider. And yeah, obviously individual investors don't have to consider that.

[00:20:04] **Rory Cunningham** And so I can hear your argument building here. Individual investors obviously aren't in the same situation.

[00:20:11] **Shani Jayamanne** No, they're not. And it does make it easier without all this pressure to invest for the long term and not to say that this is easy. Long term investing isn't easy by any means. And, you know, that's why we see that behavioural gap that I spoke about before and that's why behavioural edge is really important to consider. It means you're able to hold steady and hold your investments when markets are faltering and that's a really good skill to have as an investor. And we've obviously done studies for this as well at Morningstar that show this, and it shows that the time in the market can be more important than the actual investments that you choose. And one other advantage that investors have, which I'll mention quickly, is the ability to buy low and sell high. We all know that this is how to successfully invest, but the way that professional investors are structured in their job prohibits this in all kinds of ways, mainly in the fact that they don't have to look at what's going on. They don't have to just look at what's going to make a good investment. But they also have to look at the flows that are coming in and out of the funds. That adds a level of difficulty and complexity to their decisions that we just don't need to account for as individual investors. So, for example, if they have an influx of withdrawal requests, they need to take that into account because they need to make sure there's enough liquidity in the fund to actually fulfil these withdrawal requests or they need to sell down on assets. So it's a really tricky situation where sometimes they're just forced to sell assets they really don't want to.

[00:21:30] **Rory Cunningham** Okay. So I suppose if you had one of these edges, you'd consider investing in equities, perhaps. But let's say you're someone like me that

doesn't have any of these edges that you've talked about. Does that mean that I should use ETFs or professionally managed investments?

[00:21:45] **Shani Jayamanne** Yeah. Look, I think that's a question for yourself, what you feel comfortable and confident in as an investor, because at the end of the day, if that's going to encourage good behaviour on your end and that's long term investing where you know your investments and you've invested with confidence in your investments, that's what you're looking for. But in theory you'd be better off investing in a collective investment vehicle instead. So when I say collective investment vehicles, I mean obviously investments where you're pulling your cash with other investment like ETFs, LICs, which you find on the ASX and managed funds which are unlisted, but you can also find through mFund, if I'm not mistaken.

[00:22:18] **Rory Cunningham** Yeah, that's right.

[00:22:20] **Shani Jayamanne** Yeah. Okay. And obviously this can be active or passive so we can get into this, but it doesn't necessarily mean that you're assigning a stock picker to pick on your behalf, but you're accessing a vehicle that diversifies your portfolio over multiple holdings, not just one.

[00:22:34] **Rory Cunningham** Yeah, active and passive or what we call index tracking has been a huge debate, well, really over the last number of years. And we've definitely seen probably in the last 5 to 10 years, a lot of investors voting with their funds and moving towards that passive or index investing approach, especially as it's become easier to invest via things such as exchange traded funds. So how do you propose that investors choose between active or passive?

[00:23:02] **Shani Jayamanne** Yeah, we've definitely seen that, Rory. I think now in the US when we look at where funds are invested, over half of funds invested in US equities is through passive vehicles. But, maybe we can start by going through a couple of definitions. So, an active strategy is when you outsource your funds to a professional manager who will invest the funds based on a particular strategy or an investment style. And what they're looking to do is beat a benchmark set for the fund. And a passive strategy is when a fund, which can be exchange traded or unlisted, tracks an index or a portfolio. So in other words, no stock picking is occurring. It's just based on a theme, a trend or an index. And you know, as you mentioned, throughout the industry there's this debate between the merits of both. But I think it's really important to stress that you don't need to be aligned to either church. You're able to have both active and passive in your portfolio.

[00:23:50] **Rory Cunningham** Yeah. Can you just give us some examples of typical indices that a passive fund might seek to track?

[00:23:56] **Shani Jayamanne** Yeah. So the S&P 500 is the largest, which is the 500 largest stocks by market capitalisation in the U.S. But you could also invest in the ASX 200, which is the same. It's the top 200 stocks in Australia by market capitalisation. So that means the largest companies.

[00:24:12] **Rory Cunningham** And so when trying to consider between using an active fund or using a passive fund, what are your thoughts for investors there?

[00:24:20] **Shani Jayamanne** Definitely. So the first couple of things that you have to consider is how efficient the underlying market is and how much does it cost. So how much it costs is easy. So let's speak a little bit about efficiencies and the degree of

efficiency, and that really looks at how prices in that market of a stock reflect the underlying value of those businesses or companies that are in the stock market. Now, this is something that nobody really knows how to measure. But what we can look at is how often does an active manager actually outperform their designated index? And this is normally a lot harder in markets where there is intense competition or widespread investor interest. So for example, large cap stocks like the ASX 200 that we mentioned, you're going to find it really difficult to achieve return that over performs the benchmark and that's because these companies are heavily researched by institutions like Morningstar or fund managers and brokers alike. So they're really well understood. But when you go lower down in the market where there aren't eyes on the companies and traditional brokers don't cover them, there are opportunities for these companies to be overlooked. So we can see this in the small cap markets and emerging markets. So, this is somewhere where active managers may be able to provide value. So, another research report that we've done and we publish this one half yearly, it's called the 'Active Passive Barometer', and it's US focussed, but it's pretty relevant to the Aussie market as well because the characteristics of the Aussie market are very similar to the US. What the results show is that in general active funds have failed to beat their benchmarks, especially over the long term. So only 24% of active funds topped their passive rivals over a ten year period. But when we look at where they succeeded, it was really high with international funds, real estate funds, bond funds. So, inefficient markets where there's not as much interest there. And the data confirmed that the lowest success rate was large cap U.S. shares. So exactly we're saying, a really well researched area where there's a lot of eyes on it, not just in the U.S. but around the world, but just keep that second component in mind, which is fees. If the fees are too high, it might just be worth going passive.

[00:26:17] **Rory Cunningham** What do you consider to be a high fee?

[00:26:19] **Shani Jayamanne** Yeah. So tying into the efficiency of underlying markets, it's really important to understand how much you're paying to access these markets and whether effecient markets are worth consigning to active managers. So it's not uncommon for active managers in Australia to charge between 0.8% to 1.5% as a management fee, and many of them have failed to beat their designated benchmarks. We're seeing in the US that there is a lot of competition for funds, fund flows and they're able to make their funds a little bit more efficient as well. So we've seen the price of funds going down quite a lot in the US, so it is quite efficient to access these markets in the U.S., but we haven't really seen that in Australia yet. So I would say anything above that sort of 1% mark, you're probably paying a bit too much.

[00:27:02] **Rory Cunningham** Okay. That's good guidance. So that sort of rounds out that conversation around active and then also passive. How do you know whether to choose an investment that's traded on an exchange like the ASX or whether to access an unlisted managed fund?

[00:27:18] **Shani Jayamanne** Yeah. So this is kind of the meaty bit in the guide and the guide sort of set out that decision tree which I'll quickly go over again as a refresher. So, investing in direct equities or collective investment vehicles, direct equities, okay, great. You go and do that. Collective investment vehicles. Okay. Are you going to do active management or passive? And for either of those choices, we're now going on to listed, or unlisted. So when we get to this point, we're really looking at situational differences and how you invest as an investor and also personal circumstances. So in many cases with popular funds, you can find unlisted and listed versions. So for example, Magellan Global, it's on the ASX and it's unlisted.

[00:27:56] **Rory Cunningham** Yeah. That's been a trend over the last sort of 3 to 5 years. The number of managers now that have both listed versions of their funds and unlisted, there's over 240 exchange traded funds. Now there's over 240 mFunds or unlisted managed funds and also listed investment companies and trusts, as well. So a number of those managers have both versions, which is great, just giving investors more choice. But in considering those situational factors, what are they?

[00:28:26] **Shani Jayamanne** Yeah, and I won't go through all of them because there's quite a lot, but I can go through a couple of the main ones. The first is transaction costs. So we're really looking at barriers, and this has been lowered for retail investors, trading is getting cheaper and cheaper, but they're not managed. If they're not managed, they can eat into your investment returns. And with listed vehicles, so ETFs, LICs, equities for direct investment. They do incur brokerage every time you buy or sell, in most cases. There are some brokers now that offer $0 brokerage, but in most cases, if you're with one of the larger brokers, you will be paying a transaction cost. So this does have to be something you consider if you're an investor that's investing frequently or if you're drawing down on your investment. So if you are in retirement and you're drawing down and investing frequently is what the majority of us do, right? Like there's not a lot of us walking around with large lump sums. So I invest with every paycheque or two. I would consider that pretty frequent investing. A managed fund doesn't have brokerage costs. I don't know any managed fund that charges a fee for trading, but you do need to keep in mind that one of the great things about listed vehicles is that they're not hard to access. And, you know, Rory did talk about this trend where we'd seen a lot of funds listing in the last five years or so. And that's because retail investors are becoming a larger part of the market. And these fund managers, they traditionally just went through financial advisors. So financial advisors would be the way that a lot of retail investors would access these managed funds. But because as more self-directed investors, a lot more DIY investors, fund managers really want to accommodate for this. And listing a particular fund makes it a lot easier and a lot more accessible for them. And, you know, managed funds, they have a lot of paperwork and more importantly, they have really high minimum investments compared to ETFs and LICs. So if you are investing frequently, whether that be with every paycheque or you are breaking it into a lump sum, you do need to consider transaction costs with your investments.

[00:30:17] **Rory Cunningham** What about trading? So you obviously can't trade in the traditional sense with managed funds. They don't have a market to trade on because as it says by their name, they're unlisted.

[00:30:27] **Shani Jayamanne** Yeah. There are some investors who find trading flexibility really, really important. They want the option of buying or selling assets, you know, between ten and four. And that's something they value a lot. But managed funds are unlisted and they trade based on a unit price. So the unit price is struck each day. And what this means is that you're not able to trade intraday as you are with ETFs, LICs, direct equities, all of which are listed. Ultimately though, personally I think trading flexibility really shouldn't be a significant consideration if you're a long term investor. Having flexibility to do trade intraday is not really a priority over a long term horizon. I mean, if you're holding onto something and you're looking to sell it in five, ten years, does it really matter that you're able to access it every single day?

[00:31:09] **Rory Cunningham** Yeah, right. I think the other thing there worth considering is where you want to hold managed investments. For example, if you're

accessing the range of products that's available on the ASX, you can hold them on a holder ID number. Likewise, if you want to access manage investments directly, well then you're setting up accounts with each different fund manager, but obviously you avoid having to pay brokerage fees. So it's more of a list of pros and cons I suppose.

[00:31:35] **Shani Jayamanne** Yeah, for sure.

[00:31:36] **Rory Cunningham** So we've covered a lot. I'm going to give you the task of trying to summarise this in that, can you give our listeners some key takeaways for them to consider?

[00:31:46] **Shani Jayamanne** Yeah, for sure. So the main point is that it's so important, especially in times like now, where there's a lot of market volatility to have a plan, a plan that you can keep going back to. So a plan that shows why you're invested in what you're invested in because it's so easy for people to obviously falter at times like this when the markets are volatile. And if you have an investment that you don't really know why you're invested in that, it's likely that you will either going to buy or sell and you know, that is detrimental to your outcomes in the long term. And I think it's really important as well to understand that investing isn't just for the sake of investing. We invest so that we can reach a goal and investments are really just a vehicle for this and nothing more. And a lot of people get enjoyment out of investing, which is really great. I think that's great. But I think regardless of this, you need to acknowledge that for many of us, investing is a pathway to financial independence or self-sufficiency for reaching financial goals. We're humans, we've got a lot of things that we want to achieve. It's not just about watching the number tick up in your brokerage account, it's just not what investing is for. So we should always start with us. We should always start with what we're trying to achieve and basing our investments on that by understanding how much risk we need to take on and understanding which assets will achieve that and in what portions as well. And it's only then that we have to look at investment. So I think that when we hear these conversations and I get it all the time because of what I do for work, where you go to a barbecue and someone asks me what the next hot tip is, the next hot stock tip, and that way of investing is just not sustainable in the long term. So if I told you the next hot tip was BHP, which it isn't, so don't go and invest in that just because I said that. You'd go invest in it and then what? It goes down 20% the next day and you have no idea why. You have no idea what the merits of the company is. And you also have taken on risk that might have been unnecessary for what you're trying to achieve. So always think about yourself first and what you're trying to do before investing, and it'll help you become a more successful and confident investor, which is what we're all trying to do.

[00:33:36] **Rory Cunningham** That's great. Shani, thank you very much for joining us on the Ideas Exchange podcast.

[00:33:40] **Shani Jayamanne** Thanks so much, Rory. It was great to be on the podcast.

[00:33:43] **Rory Cunningham** Thank you all for listening to us today and listening to Shani. The three things I suppose I got from this conversation was one, we should always start with our goals before making an investment decision. Also to think about how we want to access different asset classes. Are we going to access asset classes directly or are we going to use a professional investment manager? And lastly, how do we want to do that? Do we want to do it directly with a professional investment manager or do we want to do it on an exchange via a broker? And again, as Shani

elaborated on during the podcast, there's always different pros and cons in consideration for investors. I'm Rory Cunningham. You've been listening to The Ideas Exchange, and we look forward to talking to you next month.