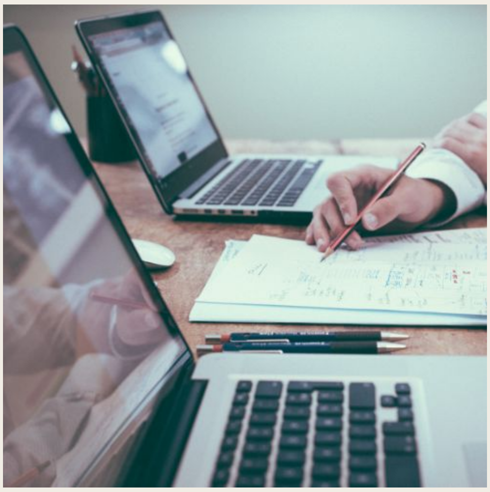
PATTINSON F.S

Your dreams, our passion, the future together.

November 2019 Newsletter

With the help of this newsletter we hope to keep you updated on what is happening in the financial world today. Welcome to our News Bulletin.

Is the Market 'Due' for a Downturn?



The U.S. stock market has been growing for more than a decade. Is it due for a prolonged downturn? I won't speculate on that, but I will say that a lot of people seem to be falling prey to the Gambler's Fallacy when discussing the market today.

Fallacy: A false or mistaken idea (Merriam Webster)

The Gambler's Fallacy is what we call that gut feeling that tells you it's just time for a trend to reverse, even when there is no fundamental evidence to support it. One clear way to illustrate the Gambler's Fallacy is using a roulette wheel.

Each time you spin the wheel, the ball has the same chance of landing on red as it does on black. The previous spin has no bearing on the one that comes after--and you know this. Still, in spite of that knowledge, if you were to spin the wheel 10 times and the first nine came up red, you'd probably feel like black was more likely to show up next just because it's "due." It's a natural reaction to the knowledge that the odds are even, but that law of probability only applies to a very large number of spins, not strings of five, 10, or even 20. It is perfectly within the bounds of chance that the ball could land on red 100 times in a row, but that just feels wrong to us because we expect the colors to even out quickly.

Lottery players fall prey to the same error. For example, which of the following bets would you guess has the higher probability of winning in a pick-five draw with numbers 1 to 50?

Bet A: 2, 13, 25, 31, 43

Bet B: 4, 4, 4, 4, 4

You know it's a trick question. You know they have the same odds. The mathematical reasoning goes like this: The first draw is one of the numbers 1 to 50. Each time a number is drawn it is put back in, and the next draw can also be any one of the 50 numbers. Therefore, any combination of the numbers has the same odds of winning as any other.

Still, to most people Bet A seems more likely because it feels more representative of a random draw. In fact, one study of the Maryland Lottery showed that once a number was drawn, players chose that number less frequently in the following weeks.

Predicting Market Behavior

Right now, after an 11-year period of expansion in the U.S. market, with the Dow at record highs, many economists and market pundits are predicting a downturn. It's not uncommon to hear phrases like, "The market is due for a correction," and that statement may be correct. The important thing to ask, though is, "Why do you think that?" If the reason they give is that the market "usually" doesn't continue to rise for longer than a certain number of years, then the prediction is unfounded. Australia is in its 28th year without a recession, for example.

As Project Syndicate points out, "Expansions don't die of old age." Expansions end because of fundamental changes in economic conditions and in the underlying value of stocks and industries. "We've never seen a run this long," is not a real reason why a market would turn. Maybe a downturn is due, but if you are going to put your money on that bet, make sure you have a better reason than, "It just feels like it's time."

Avoiding the Booby Trap

The gambler's fallacy is a tough one to tackle because it's powered by desire and fear (two very powerful emotions) disguised as logic. It is a classic shortcut of intuition, and it can be very hard to stop, check yourself, and really examine whether you're actually following sound logic, or just falling for emotional "mathiness."

To be frank, I think the best way to avoid the booby trap is to get out of the gambling mindset altogether. Research on investor behavior shows that people who "tweak" their holdings to respond to new market information usually end up costing themselves in the long run. The trading costs and fees associated with moving your money around--not to mention miscalculations and mispredictions--usually cost investors more than they gain by making a change. It's boring, but the buy-and-hold strategy really does mean that you shouldn't be thinking about moving your money around in the middle of the investment time period.

"But playing the market is fun," you say? "Besides, I'm better at it than you think." I know. It can be really fun, and there's a way to do it without losing your shirt.

To gift or not to gift? What about your pension?

With Australia's age pension being subject to an assets and income test, a simple way for part-pensioners to increase their pension payments is to give away some assets.

Not surprisingly the government is on to such an obvious strategy. It's called gifting, and while it is perfectly legal for you to give away whatever you want whenever you want, if you exceed the relevant limits, Centrelink will continue to assess, what it calls "deprived assets", for five years.

The limits

Gifting is defined as giving away assets or transferring them for less than their market value. Limits are the same for both singles and couples.
If you give away less than $10,000 within a single financial year and no more than $30,000 over five consecutive financial years, Centrelink will disregard these gifts.

Any gifts in excess of the allowable amount will be assessed as an asset (and, where applicable, subject to the income test) for a period of five years from when the gift was made.

Planning ahead

These rules don't just apply to existing pensioners. They also concern anyone who is applying for the age pension, as recent retiree Frank discovered.

Frank has reached age pension age and based on his current assets and income he should be eligible for a part pension. However:

- Four years ago he gave his daughter one of his cars, valued at $25,000.
- At the same time he gave his son $25,000 in cash, to match the value of the car.
- Two years ago Frank sold a beach house on the open market for $210,000. This was $40,000 less than the initial valuation from the estate agent.
- In the past year he spent $35,000 on home renovations and $15,000 on an overseas trip.

What does this mean for his pension assessment?

The money spent on renovations and holidays count as normal living expenses, not a gift. Likewise, with $210,000 being the best offer Frank received for his holiday home after it had been on the market for a couple of months, the property would not be considered to have been disposed of for less than its market value.

Whilst he understands that the money he gave to his son is clearly a gift, Frank's biggest surprise is the treatment of the car. Four years after he gave it to his daughter it's about to be treated by Centrelink as an asset Frank still owns.

That means Frank gave away $50,000 in one year. The annual 'Gifting Free Area' is $10,000, so the difference, $40,000, will be counted as an asset for the next year. This will reduce his pension by more than $100 per fortnight.

If Frank had thought about his pension five years before he was eligible to apply for it, he could have achieved a better outcome.

Seek advice

To gift or not to gift? It's an intricate question. The right answer depends very much on personal circumstances, talk to us today!

Source: Financial Writers Australia, April 2019

Should you have any queries in relation to this newsletter, please feel free to contact our office.

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Economic Update - November 2019

Within this month's update, we share with you a snapshot of economic occurrences both nationally and from around the globe.

US data shows strength

- US reporting season stronger than most expected
- US Fed cuts rate in another split decision
- RBA cuts rate to 0.75%

We hope you find this month's Economic Update as informative as always. If you have any feedback or would like to discuss any aspect of this report, please contact our team.

The Big Picture

The month of October was expected by many commentators to disappoint on a number of fronts: the US reporting season was expected to show weakness; the Brexit deadline of October 31st might produce a bad 'no deal' outcome; and the Australian economy was expected to deteriorate.

As it turned out, October witnessed a number of positive outcomes. Broker estimates of company earnings had been pared back but Q3 reporting season produced many strong upside surprises. As a result, the S&P 500 performed strongly over October making a new all-time high.

Market activity was justified not by earnings simply beating lower expectations but the outlook for future earnings also improved. A few big tech companies' stock prices fell sharply. The gloss has come off the so-called' unicorns – companies that recently listed and rapidly became massive. Such a more considered view of such companies with little or no track record of profitability might help the future stability of the market.

US GDP growth also exceeded expectations for Q3. The initial estimate for the year to Q3 was 1.9% compared to the expected 1.6%. The Q2 result of 2.0% was only a fraction higher.

The start of October's US labour force survey produced some mixed results. The unemployment rate fell to an almost 50-year low of 3.5% from 3.7% but wages growth was a little lower than expected at 2.9%. Only 136,000 new jobs were created but that number may have been tainted by strike activity. The 46,000 GM people on strike also makes it more difficult to interpret the November 1st data release.
The US Federal Reserve ("the Fed") met at the end of October to consider its interest rate policy. A few weeks ago, there was an estimated probability of keeping rates on hold at about 25% (using the CME Fedwatch tool that constructs such probabilities from futures contracts). The day before the October 30th statement, that probability had fallen sharply to around 2.5% - which then fell to 0% just hours before the statement.

To continue reading please visit: www.infocus.com.au/news/economic-update-november-2019

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