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Editorial

The biggest policy issue facing the Government over the next few months is how to phase out JobKeeper and reduce JobSeeker. Stock markets continue to ride a mood of optimism, but a September withdrawal of support would create a rapid rise in unemployment with consequences for business loans, mortgages and home prices. Prime Minister **Scott Morrison** said this week:

"We cannot say to Australians that government or anyone else, ultimately, will be in a position to ensure that every job can be saved, and every business can be saved. That is unrealistic ... I'm not going to make false promises to the Australian people. We have cushioned the blow but we cannot prevent the blow." He said keeping JobKeeper and JobSeeker, "*would dull the dynamism of the economy and slow the recovery*".

Businesses and individuals exposed to lower economic activity need to plan how to survive for the long term, including recommencing loan payments. The **Australian Bankers Association** releases data on loan deferrals, now totalling almost $240 billion from 800,000 borrowers. This is not interest forgiveness, it is deferral. Payments may hit exactly as welfare support is removed and let's hope deferrals do not become impairments.

One of the other stimulus measures, the relaxation of access to super, has now seen two million people apply for $15 billion of what was supposed to be retirement savings. A new official rhetoric tells people it is their money to spend however they wish. Previously, its sole purpose was to finance retirement. **Senator Jane Hume**, the Assistant Minister for Superannuation, Financial Services and Financial Technology, said this week:

"The Government isn't in the business of telling people how to spend their own money. We don't do that. In the same way we still pay a JobSeeker to a person who might spend it on cigarettes and beer. If people choose to take their own money and spend it on something that isn't particularly helpful, that's their business."

Whoever thought the money in our cherished retirement system, tied up in more rules and regulations than operating a nuclear power plant, would be blown on ciggies and beer.

Meanwhile, the market is totally confused by US Fed Chairman, **Jerome Powell**. He threw a brick through the recovery window when asked how many Americans would never return to their old jobs. Powell said, "*Well, into the millions.*" Wall Street fell 6.5%.

Then a few days later, he announced that the Fed would go into the market and buy corporate bonds. Not Treasury bonds but corporate bonds rated as low as one notch above junk on 22 March. In the US, an estimated 20% of companies are 'zombies', where debt serving costs exceed profits, and they survive by borrowing more. Poor companies with compromised business models should be allowed to fail. Famous US brands such as **JC Penny, Hertz, Victoria's Secret, Diesel, Antler** and **Nieman Marcus** are no longer viable, just as **Amazon** destroyed **Blockbuster** and **Borders**, and **Apple** and **Samsung** undermined **Blackberry** and **Nokia**. It's sad for the victims but it's not the Fed's job to bail out weak companies.

So Australia has made it into Wall Street lexicon, as we now have bull markets, bear markets and kangaroo markets, jumping all over the place. Fame at last!

And in a sign of the times in Australia, the rebalancing of the local indexes by **Standard & Poor's** sees a local fallen icon, **AMP**, replaced by a milk company in the ASX50. We used to complain that our indexes were dominated by financial stocks, and at least the **CSL**s and **A2Milk**s are diversifying the index.

S&P/ASX 50 Index – Effective at the Open on June 22, 2020		
Action	**Code**	**Company**
Addition	A2M	The A2 Milk Company Limited
Removal	AMP	AMP Limited

In this week's edition ...

We look inside a remarkable change in the market that is influencing price behaviour. The so-called corona generation, or in the US, **Robinhood** traders, may be at the margin, but new retail investors are having a growing impact as their numbers increase rapidly. Will it be sustained?

We turn to **Warren Buffett**'s advice during the tech wreck of 2000 when people were saying he was out-of-touch and did not understand these amazing innovative companies. Twenty years later, people are asking if Buffett's methods are outdated, especially his ability to reposition his portfolio quickly.

Then **Marcus Padley** give 10 hints not only on how to look for capital losses to reduce your FY20 tax bill, but the best ways to clean up your portfolio rather than hanging on to the bugs that make a mess of your spreadsheet.

When markets are so uncertain, **Kate Howitt** falls back on three baseline factors to decide her next step, but there's one overriding influence for the coming storm.

If there is one part of retirement planning where advice is essential, it must be aged care planning. **Jemma Briscoe** explains a change coming on 1 July 2020 which advisers and their clients should understand despite the complexity.

Brendan Coates makes the case for the vital role of owning a home in retirement and policy solutions for renters. Any analysis of retirement needs to allow for home ownership in the planning.

Population growth has driven economic activity for centuries, but it has also come with a downside of environmental impacts. **Michael Collins** shows that for the first time, the world is experiencing population declines with profound implications.

This week's sponsor White Paper delves into the investment strategies of **Dr Allan Gray**, who set up his epynomious asset management business in 1973 and a sister company, **Orbis**, in 1989. He died at the age of 81 in November 2019 and his former colleagues describe his investing legacy.

Footnote. If you missed a fantastic 4 Corners programme on AI on ABCTV this week, take a look on iview. Scary stuff, far more advanced than I expected.

Easy money: download Robinhood, buy stonks, bro down

Graham Hand

"But a pin lies in wait for every bubble. And when the two eventually meet, a new wave of investors learns some very old lessons: First, many in Wall Street - a community in which quality control is not prized - will sell investors anything they will buy. Second, speculation is most dangerous when it looks easiest."

Warren Buffett, Letter to Berkshire Hathaway Shareholders, 2000. For a longer version of this extract, see the following article.

There are many coronavirus variations on 'This Time It's Different', but something is happening in stock markets on a scale never seen before. Call it Robinhood traders, the corona generation, YOLO (You Only Live Once), TINA (There is No Alternative) or simply retail investors, but trading by individuals has hit global equity markets in massive numbers. Some daily moves are called a battle between the smart professional sellers and the dumb retail buyers, but since the 23 March bottom, the dumb money has been right. So far.

Professional versus amateur

Most macro articles coming into the Firstlinks' mailbox recently from professional investors carry warnings about the disconnect between an economy in recession and a booming stock market. We have published many such as here, here and here.

Experienced market experts who have been through numerous investment cycles consider the market's recovery seriously overdone. It's called 'the most-hated rally' because many people have underestimated it. Magellan's CIO, Hamish Douglass, was quoted in *The Weekend Australian* on 13 June 2020:

"Those who know are scratching their heads wondering what is happening while the uneducated are grading on guesses ... Uneducated investors are getting excited. The optimism is based on no fundamental facts ... I don't think a V-shaped recovery is likely, or a depression, and we are likely just to muddle through."

Douglass has increased his cash holding from 6% to 17% during the pandemic, and his former partner and now Portfolio Manager of MFF Capital Investment (MFF), Chris Mackay, was holding cash at 46% of his portfolio at the end of May.

A leading US financial industry newsletter, *SA Macro View Daily,* in which articles are written by fund managers and other experts, led its Friday edition last week with these three warnings:

S&P 500: The Next Stock Market Crash May Have Just Started
By Victor Dergunov • 318 comments

The Fed Just Issued A Dire Warning For The Stock Market
By Mott Capital Management • 244 comments

We Ended Up In A 'Bubble Of Greed' Which Can't Be Explained By The Fed
By Robbe Delaet • 139 comments

In a Firstlinks survey in late April 2020, two-thirds of responses said a new low is coming. Our audience is older and wealthier than at other newsletters, implying SMSF trustees, retirees and advisers were not in a buying mood.

All of which suggests that the rapid rise in the market was at least influenced by another player and perhaps less-experienced retail investors were not the bunnies this time. It's newbies versus fundies.

Evidence of increased participation by retail

Bestselling author and Barefoot Investor, Scott Pape, has a large retail following, and he recently started his newsletter by saying:

"Something weird was happening at Barefoot. While the headlines were full of people hoarding toilet paper, we were seeing a huge spike in people asking me how they could buy … shares?"

Australian stock brokers are reporting increasing retail activity and a large increase in new accounts. In May 2020, the Australian Securities & Investments Commission (ASIC) took the unusual step of issuing a report on retail investor trading during COVID-19. It includes:

*"The average daily securities market turnover by retail brokers increased from $1.6 billion in the benchmark period (*Ed. 22 August 2019 to 21 February 2020*) to $3.3 billion in the focus period* (Ed. 24 February 2020 to 3 April 2020*). Retail trading as a proportion of total trading increased marginally, from 10.62% to 11.88% … Retail brokers were net buyers of securities over the focus period, buying $53.4 billion and selling $48.4 billion.*

***The rate of creation of new accounts (as indicated by their identifiers) is roughly 3.4 times higher** during the focus period (compared to the benchmark period). In the focus period, new accounts represented 21.36% of all active accounts."* (my bolding).

In the US, financial market commentary hotly debates the new impact of retail investors. One estimate is that since the coronavirus hit, 10 million new accounts have been opened at fee-free brokers, many by millennials and younger people who are bored at home during the lockup and unable to watch their usual sports and bet on the outcomes. As the market has recovered quickly, social media sites are filled with stories of people making large amounts of money and FOMO has struck.

The question is … are there now enough of them to drive the market?

What are Robinhood, Reddit and TikTok?

For most retirees and professional fund managers following traditional media, this new phenomenon of 'uneducated' investors punting around looks like a misguided mistake. What do these newbies think they are doing in our sophisticated market? What do they know about intrinsic value? The answer is, they don't know much, and they don't care.

These new Robinhood traders are having a 'bro down' party in the rising market, as satirised in the following variation from an episode of *South Park*.

South Park's 'Go Fund Yourself' episode satirised Silicon Valley's boy's club. Now memes are doing the same for day traders in the current rally. SOUTH PARK/COMEDY CENTRAL

In case the meaning of this 4 Point Plan written in 'bro speak' is vague, here goes:

1. 'Download Robin Hood' refers to the US stock market trading app (should be Robinhood) which has experienced incredible growth since the virus hit. It is free to trade and while in theory all users must be over 18, social media suggests older people are giving access to their friends and children.
2. 'Deposit stimulus' means the special payments made to unemployed people to support them during the crisis, suggesting the 'found money' is used to day-trade the market. In Australia, there is anecdotal evidence that the same is happening with JobKeeper and early access to super. While there is no data to support this claim, some people have more 'found money' than ever before.
3. 'Buy stonks' is a deliberate misspelling of stocks, but it's more than that. It captures what is happening on social media and chat sites such as Reddit where thousands of people read a tip which might sound ridiculous, but the consensus and numbers give it meaning. For example, someone makes a case for buying airlines when none of them are flying, based on the argument that Trump will save them, then followers jump aboard and airline shares rise rapidly. The fact that Warren Buffett just sold out gives the story even more gleeful momentum.
4. 'Bro down' is a meeting of people, usually males, with some common bond, in this case, ramping up stories on social media of which stocks to buy and then boasting about it.

The result is a bunch of new players making money day-trading and laughing at the world of fund managers and experts. Sure, they are inexperienced, but they work on the theory that stocks only go up, and if it's a terrible stock that just fell 50%, then that's even better. It has so much potential.

It sounds crazy to anyone taught to value a company based on the net present value of its expected future cash flows, but in this world, none of that matters. The new traders drove up the price of Hertz after it declared bankruptcy with massive debts and no revenue, and the share price rose so rapidly that Hertz planned a new capital raising.

Where are these communities hanging out?

TikTok is a massive global success story with a billion members who post short dance moves, lip sync routines, cooking sessions or whatever. It's also dominated by young people and millennials, and Robinhood advertises heavily to this market. The chat function on TikTok includes stories of quick daily market gains with videos on 'How to Trade' and 'Financial Advice', some of which are agonisingly naive.

Reddit is a large collection of online public forums where people share information and comment on posts by other people. It has become a global feedback site on almost any subject and the Robinhood site on Reddit has 300,000 members. A popular Reddit Australian site is ASX_bets with about 8,300 members. Reddit claims to be the number one resource for traders under 30, who can legitimately collude with extreme comradery.

And what of **Robinhood**? This is now a serious business. It has increased its user base by millions each month since March and embarked on a new share issue valuing the company at US$8 billion. It is privately held, and the app is not available in Australia. Robinhood makes money by selling data to high-frequency traders, which may translate into other activity by large players.

What do the online conversations look Like?

It's a virtuous circle while the music plays. Unless you follow the right people on Robinhood, Reddit, Twitter and TikTok, it's hard to know what's happening. Let's screenshot some of the conversations to give a flavour, but take these as anecdotes rather than facts.

A former Goldman Sachs Partner, Joseph Mauro, reported that his 10-year-old son can no longer play the hit game Fortnite during the day because his friends are on Robinhood:

> My son just told me that he can only play @FortniteGame in the evening... because half of his squad started trading. He is 10. @RobinhoodApp #TrueStory
>
> 2:00 PM · Jun 9, 2020 from ETRADE Financial · Twitter for iPhone

Hedge fund manager and writer of the well-known Felder Report, Jesse Felder, tweeted:

> **Jesse Felder** @jessefelder · Jun 10
> My 20yo son, stationed on an airbase in Turkey, just called to tell me about all the guys on the base going around bragging about how much money they've made buying "one-dollar stocks" on **Robinhood**.

Here are some extracts from the Robinhood user pages on Reddit as new players reach out to others for advice, such as:

> Pretty new to trading so I get that I'm not understanding everything. But unless you've put money that you need to pay bills, why is it that people freak out over losses? If you have a diverse portfolio, isn't the market eventually going to go back up (even if it might take a little bit)? Especially because it's already so low because of the pandemic, once this eases and we get a vaccine (give or take a year or two), we're going to see the rise again, no?

> Shitpost - Firehose is open! **Can someone explain options to me I'm making pretty good profit without them but everyone says there the way to make better profit quicker. I understand you buy a call if you think it's gonna go up and a put if it goes down but I don't understand other than that**

Hey everyone. Was looking for some feedback on my portfolio so far! I'm 24, and started with a couple thousand. My investment goal is for long-term growth, but also the potential for some short term gains. Open to other stocks/etfs I should look into, too. Thank you!

Shitpost I am a noob at investing and know nothing

Hey guys,

Just created an account and I don't know anything about what I'm doing. Any tips?

11 Comments Share Save ...

Even when there is a market sell-off, we see claims that Robinhood traders caused it (although this comment is probably ironic):

Michael Olenick @michael_olenick · 15h
Reason: the Robinhood traders thought things are going south so they all started to sell then the algos kicked in and started selling too. There's probably a post on reddit that kicked it off.

Their spiritual leader, Dave Portnoy

Dave Portnoy is the founder of a successful sports betting business called Barstool Sports. At the time when the pandemic hit, he had only bought one share in his life. Following the cancellation of most sports events, he turned to day-trading, doing live broadcasts about his portfolio to his 1.5 million Twitter followers as *Davey Day Trader Global (#DDTG)*. He's a big-time influencer. His handle is @stoolpresidente but watch the foul language. He tells how he is "*just printing money*", and "*With the volatility, it is kind of like watching a sports game."*

Portnoy's techniques feed directly into the needs of his audience for instant success, big ideas and brashness, with strategies that make professionals wince. At a time when few fund managers wanted to touch airlines and cruise companies, he saw the selloff as an opportunity, and thousands followed him into these stocks.

Dave Portnoy @stoolpresidente · Jun 8
A lot of people are asking me if Airlines and Cruises will go up tomoroew. My answer is see tenet #1 of the #DDTG playbook

1. Stocks only go up
2. When in doubt whether to buy or sell see Rule #1

189 752 6.4K

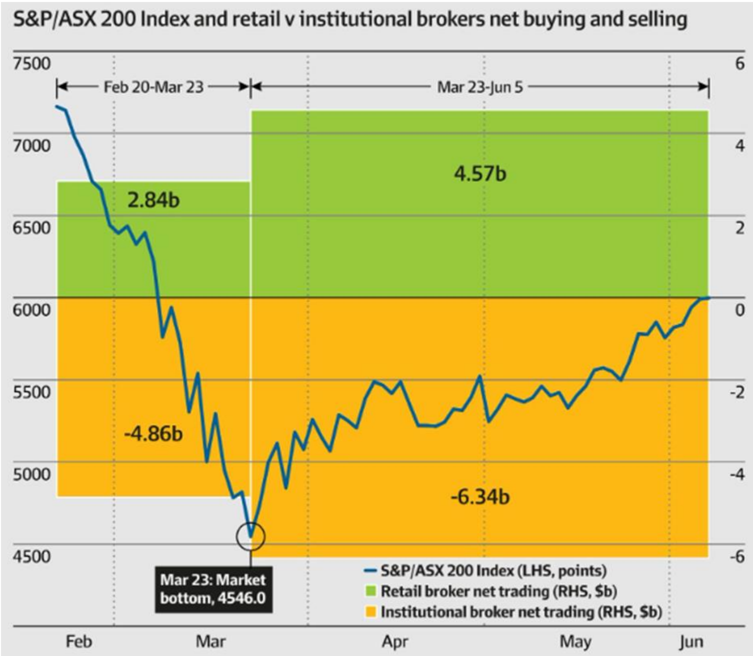
Here is a video of Portnoy at "*the most successful trading desk in the world*".

On 26 May 2020, Portnoy posted a video about the JETS fund which gives exposure to industrial stocks such as airlines. Daily turnover increased for US$50 million to about US$200 million and the price increased 18% in the next two weeks.

In Australia, brokers claim the Buy Now Pay Later stocks such as Afterpay and Zip have benefited from new traders adding to demand, knowing from their own use that these businesses are serious disrupters. Strong retail interest is reported in travel stocks such as Webjet and Flight Centre. During the heavy market fall for most of March, while professionals sought out traditional strong balance sheets, new players ran with beaten up stocks such as Kogan and The Reject Shop which have since rallied strongly.

Can this retail activity really have an impact?

Australia's largest retail broker, CommSec, manages only about 5% of market turnover, despite holding well over one million accounts. Overall, ASIC estimates that about 90% of trading is done by institutional brokers. However, other reports such as by broker Bell Potter suggest retail influence is higher. Its Coppo Report recently showed retail brokers as net buyers of $4.6 billion from 23 March to 5 June while institutional brokers were net sellers of $6.3 billion.

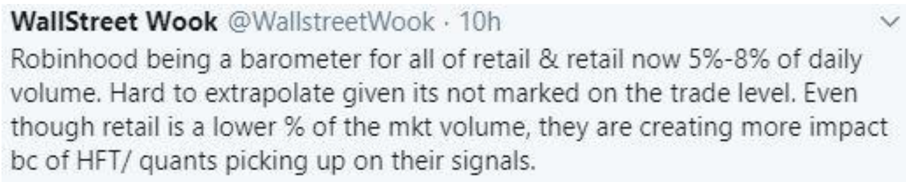


Source: Bell Potter, Blomberg, The Australian Financial Review

Two factors suggest retail influence is larger than their market share implies:

1. Share prices are set by the marginal traders. For most stocks, the amount of turnover each day is a small fraction of the total market capitalisation. Prices can move on modest volumes, especially in small-cap stocks with poor liquidity. A collection of retail buyers or sellers following the recommendation of an influencer could move the prices of some stocks significantly. Millions of small amounts add up, especially when supported by a vocal social media presence.

2. High Frequency Traders (HFT) are watching the sentiment in places like Reddit, Robinhood and TikTok and either trading ahead of retail or taking it as a guide. Then algorithms and quants that follow market momentum may kick in added support. Robinhood sells its data to HFTs. CNBC commentator Jim Crater recently suggested Wall Street veterans have started buying popular Robinhood stocks early in the day, as the online broker publishes the quantities held by its clients.


WallStreet Wook @WallstreetWook · 10h

Robinhood being a barometer for all of retail & retail now 5%-8% of daily volume. Hard to extrapolate given its not marked on the trade level. Even though retail is a lower % of the mkt volume, they are creating more impact bc of HFT/ quants picking up on their signals.

Several studies have tried to calculate whether this new group is making money, but the conclusions are complicated. Barclays reported no relationship between the aggregate holdings of stocks by Robinhood traders and the returns on those stocks. Soc Gen said these traders tend to hold both the best-quality stocks (familiar names such as Amazon, Facebook and Google) as well as the poor-quality names they are better known for. It's more likely the new traders are simply following a rising trend and doing well from it.

How will it end?

Anyone who has spent more than five minutes in stock markets thinks this will end badly, especially when leverage is involved. Although it's possible to make money in a falling market (say, using bear ETFs or put options) most new players are using a few thousand dollars and going long favoured stocks. In the next severe fall, a valuable lesson will be learned. Dave Portnoy's estimated worth is over US$100 million after selling his sports betting business, so it won't worry him to drop the odd million.

We also know there is a major FOMO at play here, where friends on social media boast of their gains and others hate to miss out, although they have little idea what they are doing. This will evaporate when losses become the norm.

The old adage was to sell when the taxi driver starts talking about his favourite stocks. Now the contrarian indicator is millions of overconfident and inexperienced gamblers who have only seen a rising market.

Also consider what has inspired this new generation of market speculators. The US Federal Reserve will do 'whatever it takes' to hold up the market. It is even taking the crazy step of buying corporate bonds. The money-printing machine knows no limits to supporting asset prices.

And going into the November presidential election, one of the candidates will set his campaign on making sure the stock market does not fall.

Regardless of what you think of Donald Trump (and there is much to dislike), tens of millions of Americans support him and his Make America Great Again rhetoric. He will do all he can to ramp up the economy for at least the rest of the year. Anyone ruling him out for another term hasn't seen Joe Biden without a teleprompter.

Eventually, most of the bros will move on when the stonks fall. Given Mr Portnoy is a gambler, let's finish with the words from the Kenny Rogers song:

You've got to know when to hold 'em
Know when to fold 'em
Know when to walk away
And know when to run
You never count your money
When you're sittin' at the table
There'll be time enough for countin'
When the dealin's done

Graham Hand is Managing Editor of Firstlinks. This article is general information and does not consider the circumstances of any individual.

Warren Buffett's letter on new investors and speculation

Introduction: Stock markets are facing a new paradigm with millions of inexperienced investors participating for the first time, facilitated by free trading apps and social media making it look like a fun game. Since the low of 23 March, many have made a lot of money and it looks easy.

So let's take a look at what Warren Buffett said in his annual letter to the Berkshire Hathaway shareholders in 2000 near the height of what became the 'tech wreck'. It was another time of massive speculation ignoring company fundamentals. This extract comes from his collection of letters here.

Now, speculation - in which the focus is not on what an asset will produce but rather on what the next fellow will pay for it - is neither illegal, immoral nor un-American. But it is not a game in which Charlie and I wish to play. We bring nothing to the party, so why should we expect to take anything home?

The line separating investment and speculation, which is never bright and clear, becomes blurred still further when most market participants have recently enjoyed triumphs. Nothing sedates rationality like large doses of effortless money. After a heady experience of that kind, normally sensible people drift into behavior akin to that of Cinderella at the ball. They know that overstaying the festivities - that is, continuing to speculate in companies that have gigantic valuations relative to the cash they are likely to generate in the future - will eventually bring on pumpkins and mice. But they nevertheless hate to miss a single minute of what is one helluva party. Therefore, the giddy participants all plan to leave just seconds before midnight. There's a problem, though: They are dancing in a room in which the clocks have no hands.

Last year, we commented on the exuberance - and, yes, it was irrational - that prevailed, noting that investor expectations had grown to be several multiples of probable returns. One piece of evidence came from a Paine Webber-Gallup survey of investors conducted in December 1999, in which the participants were asked their opinion about the annual returns investors could expect to realise over the decade ahead. Their answers averaged 19%. That, for sure, was an irrational expectation: For American business as a whole, there couldn't possibly be enough birds in the 2009 bush to deliver such a return.

Far more irrational still were the huge valuations that market participants were then putting on businesses almost certain to end up being of modest or no value. Yet investors, mesmerised by soaring stock prices and ignoring all else, piled into these enterprises. It was as if some virus, racing wildly among investment professionals as well as amateurs, induced hallucinations in which the values of stocks in certain sectors became decoupled from the values of the businesses that underlay them.

This surreal scene was accompanied by much loose talk about 'value creation'. We readily acknowledge that there has been a huge amount of true value created in the past decade by new or young businesses, and that there is much more to come. But value is destroyed, not created, by any business that loses money over its lifetime, no matter how high its interim valuation may get.

What actually occurs in these cases is wealth *transfer*, often on a massive scale. By shamelessly merchandising birdless bushes, promoters have in recent years moved billions of dollars from the pockets of the public to their own purses (and to those of their friends and associates). The fact is that a bubble market has allowed the creation of bubble companies, entities designed more with an eye to making money *off* investors rather than *for* them. Too often, an IPO, not profits, was the primary goal of a company's promoters. At bottom, the 'business model' for these companies has been the old-fashioned chain letter, for which many fee-hungry investment bankers acted as eager postmen.

But a pin lies in wait for every bubble. And when the two eventually meet, a new wave of investors learns some very old lessons: First, many in Wall Street - a community in which quality control is not prized - will sell investors anything they will buy. Second, speculation is most dangerous when it looks easiest.

10 reasons to sell your dud stocks for EOFY

Marcus Padley

The end of the financial year is a good time to assess your capital gains and work out if you have a net capital gain from stocks sold. If so, you should also be looking through the portfolio for stocks with losses that you could sell to offset paying tax on the gains.

You know the stocks, those duds you didn't sell when it was obvious you should sell. Those stocks that you shut your eyes to and hoped against hope they would rebound miraculously … but they kept falling. Those stocks. Those small illiquid stuff-ups that you regretted buying but let linger in your 'portfolio'. All those short-term trades that became long-term 'investments'.

Now is the time to think about selling them, especially the illiquid ones because by the time everyone else wakes up to their capital gains tax loss in the last two weeks of June, these stocks will have been dumped, making your emotional turmoil even harder to squeeze a trade out of. So better you assess and sell now before the bloodbath starts, which it does every year, in every small trading stock that has gone down.

Selection is personal

I have had an email asking which stocks are likely to be most affected by tax-loss selling. From your point of view, it is simply which stocks are in your portfolio, have not performed well this year and are small and illiquid and likely to get sold off by tax loss sellers. There are no 'good' stocks to take a loss on generally … just your own stocks. The stocks to sell are staring you in the face.

I could print you a list of the worst performers this year but it wouldn't help. It's personal. What do you hold that you could sell and what do you hold that other people will sell?

The only 'game' to play here is as a trader buying stocks that are small illiquid bad performers if they have been pummelled running into the last week of June. Stocks that are trading favourites always have a lot of stale holders. They are killed in June and often resurrect in July.

Hints for taking a loss and cleaning out the duds

It is one of the hardest things to convince a broker, let alone a novice trader, to take a loss. So to help with the process, we have developed arguments to persuade you (they don't seem to work on ourselves). If you are having trouble taking a loss, not enjoying your trading, are getting emotional and the stock is still in your possession … read my 10 reasons for why you should think about letting go of the dogs. You will put the sell order on before you get to the end:

1. If a stock is going down it is far more likely to continue going down than it is to turn on a sixpence to suit you.

2. The further a stock falls the more intense the selling becomes as higher losses cause more selling decisions, so sell early – an early loss is the smallest loss.

3. If you sell 10 falling stocks, it will be the right thing to do in nine cases, but you will only remember the other one.

4. If you sell now, you are no longer exposed, and all you have to do is come to terms with the loss.

5. If you sell now you can always buy it back – you might even buy it back lower than you sold it. Be aware of the ATO's 'wash-sales' rules explained later.

6. If you sell now, you enter the eye of the storm and all becomes calm. You have a moment to think and you can watch from a distance. You can always choose to enter the storm again and you will be thinking more clearly and be armed with a plan.

7. If you are making a loss on a stock, think to yourself … "if I had cash would I buy this stock now at this price?" If the answer is 'No', then why are you holding it? Sell it. Most people begin to 'hate' the stocks they lose money in … so this argument always works.

8. Your state of mind has a value. What would your spouse pay (or you pay) to have you carefree at the weekend instead of ripping the heads off the kids. Look after yourself. There are not that many weekends in the year or your life. Don't ruin too many of them by keeping risky loss-making positions until Monday because you didn't have the guts to sell them on Friday. There is no logic in being emotional about losses. If it's gone it's gone.

9. Averaging down is a mug's game. If you have money to invest you should be putting it in the best investment in the whole world. Do you really think that will be the very same stock you have already bought at a higher price and that is falling at the moment? Very unlikely. You already have an exposure … why do you need more of something that has already proved itself to be a dog.

10. If in doubt, sell it. It crystallises a capital loss for this tax year. Why wait until the end of the year to take your losses? Taking losses today could set you up for making and taking gains this year. You can always buy it back once you've made the sale.

ATO wash-sales provisions

If you do decide to take a loss before 30 June but plan to re-adopt one or more of your dogs in the new financial year, be mindful of the ATO's position on wash-sales. If you repurchase the shares you sold very shortly after at a similar price, the ATO will look at that transaction unfavourably and you may be subject to anti-avoidance rules.

Hopefully you hold good long-term stocks and won't have to take a loss, but when you do, read this again and see if you can get to the bottom of the list before you have put on the order to sell.

Marcus Padley is the author of the daily stock market newsletter Marcus Today. See marcustoday.com.au for a free trial. This article is for general education purposes only and does not address the personal circumstances of any individual, nor does it cover all possible events. Professional advice should be sought before taking any action, including taxation and financial advice.

The three main factors when the storm hits

Kate Howitt

Markets such as the one we're experiencing now show that we can't be agnostic about what's happening in the wider world. So, when I think about macro conditions and where markets might go, I always use a really simple way to break it down into three factors: 1. Fundamentals; 2. Valuations; 3. Liquidity.

If we've got good earnings growth, reasonable valuations, and abundant liquidity, then markets are more likely to go up. And vice versa. So, let's break it down.

1. Fundamentals

As we all know, we're in the midst of a pandemic which is bringing economic conditions that we haven't seen for a hundred years. If we look at the US, Gross Domestic Product (GDP) is probably going to be down 35% quarter on quarter for the second quarter.

Take the example of the energy sector. It is facing a triple whammy of excess supply, absent demand, and no access to capital markets to cushion the blow.

So, what we saw in March and April was the first half of the storm, the human cost, but soon we’ll begin to see the economic toll. One of the research providers that we talk to uses an analogy of dynamite fishing - where you blow up some dynamite beneath the water and then the fish start to rise to the surface. The first ones to rise are the little ones and then over time the bigger and bigger ones begin to rise.

This is the kind of process that will happen now. It takes a while for companies to experience financial distress and then actually go through to insolvency or bankruptcy. There's a lot of companies doing it tough now and we'll only see the ultimate impact as time goes by. So, we know the news will get worse from here but we don't know how bad it will be relative to our expectations.

2. Valuations

Valuations are not cheap. When you have periods of big volatility, predicting what earnings will look like becomes challenging and particularly hard because more than half of the companies on the Australian stock market have withdrawn guidance. Any kind of interim earnings estimate is really just a guess. But if you make some kind of a guess and then look at the price, we're actually back up to mid-term highs on PEs, although more so in the US market than here.

Australia’s price to book value is a better measure because it's more stable, but still moving around because there will be some write downs that will have to come out of this.

What’s impacting valuations on the other side though, is that we moved from a lower-for-longer expectation for interest rates to a lower-for-forever or lower-for-the-vast-foreseeable-future. And that is also putting a floor under valuations.

I think Australia and the US will have different fundamental outcomes but I think our valuation parameters are likely to be set by what happens in the US market. Lower rates or high valuation metrics in the US will boost us. If the US has challenging outcomes and their valuation parameters go back down, that will likely drag us back down too.

So that leads us to a really interesting question. What timeframe is the market currently discounting? Because we know that for maybe the next six months at least, economic outcomes will be very negative. So, either markets are looking through that and discounting all the way out - saying, “Well, I know this is going to be bad, but there's also the stimulus. And so, okay, I'll look through that.” And that's why share prices have bounced back up. Or markets are just not discounting at all.

How would that be?

We know markets are supposed to be discounting machines. They're supposed to look ahead and price every factor in to the value of stocks. We've had an unprecedented shift towards algorithmic and quantitative trading. I’ve been talking about this for a while and the shift of market participants from those that are trying to arbitrage price to fair value versus those in their trading on other proxies of outperformance.

It's possible now that the marginal buyer of markets is a bot or an algorithm that doesn't actually hear rumours, only published data. That old function - "I'll buy the rumour and sell the fact" or vice versa is not actually working anymore. Markets are not discounting the negative picture of the next six months. So, they've either lost a lot of the discounting capability and are just looking at the benign conditions that are currently on paper, or markets are looking all the way through to the end of this, even though we really don't even know how far in the future that is.

3. Liquidity

In March, we had a massive dislocation with very leveraged players, highly exposed to equity markets. As they exited positions, it created an enormously painful and rapid downdraft in share prices.

We've had enormous multi-trillion dollar Fed flows to the rescue and that put a floor under the panic and closed a lot of the arbitrage gaps that had opened up. But positioning in equity markets is now more fearful rather than risk-taking, so there's more money on the sidelines.

On the Australian side of the equation, the really interesting part now is superannuation. Super is an enormously-wonderful factor in the Australian economy, but right now we're asking a lot of it. We're asking for super to be the corporate re-capper. We've had a tonne of recapitalisations and they keep coming every single day. So we want superannuation money there to front up and buy these new issues.

And we now have a new role for super. We want it to be the household piggy bank. If a person has a cashflow problem now, they go to the ATO website and withdraw $10,000, and then again in July.

We now also want superannuation to abstain from dividends if companies cut or halve or restrict their dividends. And this is new for them because these superannuation funds have relied on very high dividend flows from their equity holdings. The Government is also asking super providers to step up and fund infrastructure and contribute to nation-building projects.

That's all a big ask on superannuation and it's definitely a change from 2008 when super just stood there as a re-capping vehicle.

Putting it all together

So, what does that all mean? We know that the fundamentals will get worse from here, but there's excess liquidity and the lower-forever impact of interest rates is currently putting a floor under valuations. Over the next few months, as we move from the eye of the storm to the economically-devastating bit, we'll see if low rates and high liquidity are still enough to support markets.

We'll find out if markets were looking way out ahead or actually not even as far as their noses.

Kate Howitt is a Portfolio Manager for the Fidelity Australian Opportunities Fund. Fidelity International is a sponsor of Firstlinks.

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Why the poor will pay more for aged care next year

Jemma Briscoe

From a financial advice and user perspective, it's crucial to understand the impact of the coming drop in the 'aged care interest rate' or Maximum Permissible Interest Rate (MPIR). Advisers should look at a client's personal circumstances, consider alternative scenarios and model not just the cost today but what it is likely to be in the future.

The MPIR is expected to drop to an all-time low of 4.10% from 1 July 2020. As with any change to government rates and thresholds, this change will create winners and losers. Unfortunately, the 'losers' are the low-means residents, people who are financially disadvantaged and receive government assistance with their accommodation cost whose lump sum could increase substantially. Ironically those who are not financially disadvantaged, known as 'market price' residents could be substantially better off if they pay by daily payment.

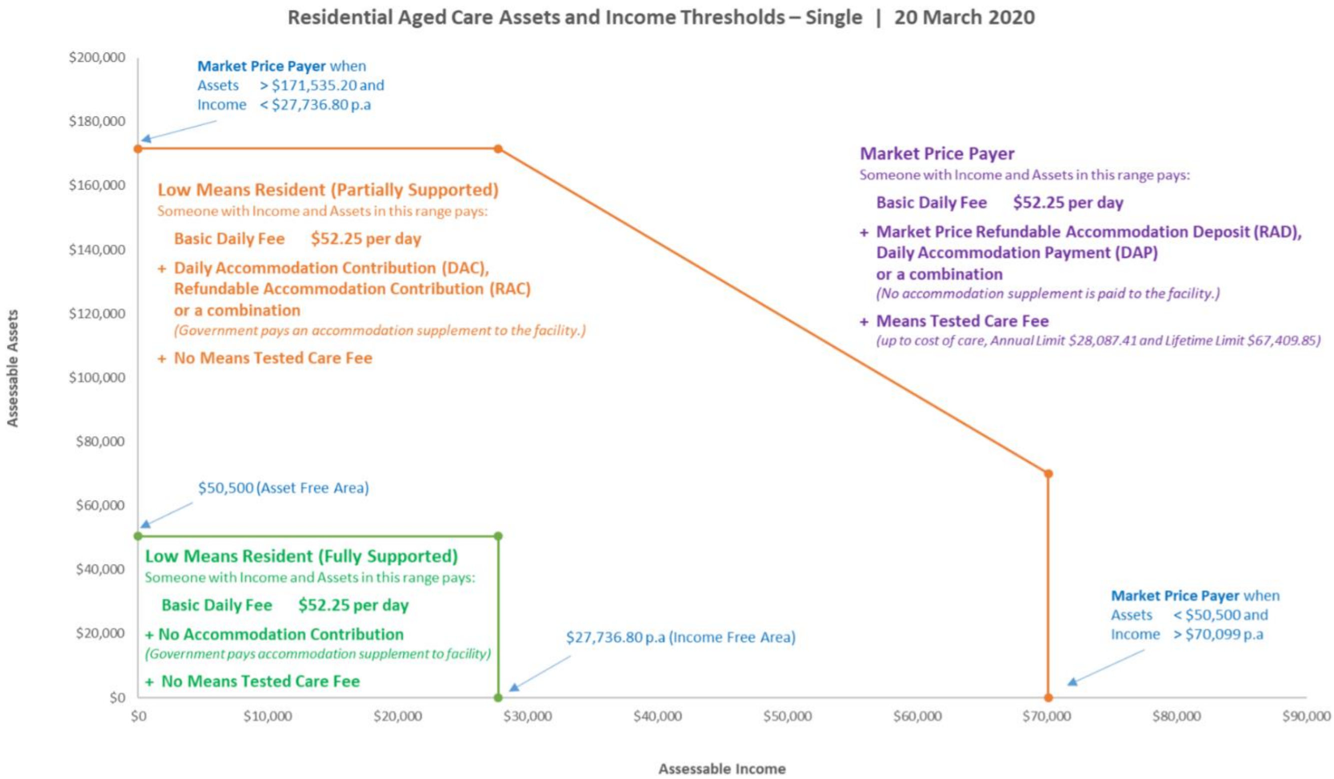
Let's look at the impact the reduced MPIR will have on new and existing residents, explore what this means for an aged operator's financial position and how advisers can deliver great advice to their clients.

1. Impact on new residents

When someone moves into residential aged care, they are assessed based on their assets and income to determine whether they are classified as a 'low means' resident or a 'market price' resident. It should be noted that this means assessment is not compulsory, those who choose not to submit an assessment will be considered a market price resident. The diagram below shows how the combination of assets and income determine the resident's classification.

2. Impact on low-means residents

Where the person's assets and income are below the orange line their accommodation contribution is calculated at 17.5% of assets above $50,500 plus 50c per dollar in excess of $27,736.80/year. The income threshold for a member of a couple is slightly lower at $27,216.80/year. The result is divided by 364 to calculate the person's DAC (Daily Accommodation Contribution). For people with assets and income below both the asset and income thresholds (inside the green line) their Daily Accommodation Contribution (DAC) is $0.



Source: Learn, Build, Deliver pro.agedcaregurus.com.au ACG Advice builder.

Low-means residents have the option of paying their accommodation contribution by daily payment, lump sum or a combination. The lump sum, known as the Refundable Accommodation Contribution or RAC, is calculated by dividing the daily accommodation contribution (annual) by the MPIR. In effect the daily accommodation contribution is the interest payable on that equivalent lump sum.

By nature of the formula the lump sum accommodation price for low means residents has an inverse relation to movements in MPIR, similar to bond pricing and yields. A decreasing interest rate (MPIR) will result in the equivalent lump sum increasing. Since the introduction of the Living Longer, Living Better (LLLB) reforms in 2014 the MPIR has reduced from 6.69% to 4.10% from July 2020. Changes to the MPIR don't affect existing residents, the rate is set on the date of entry to the aged care home and doesn't change while the resident lives there.

Changes to the resident's financial position will cause their accommodation contribution to be recalculated, if their assets and/or income reduce then their contribution reduces. Likewise, if their assets and/or income increase (which is far more common) then their accommodation contribution increases (they can also be subject to a means tested care fee). But they are always classified as a low means resident while they live in that aged care home and the accommodation contribution they can pay is capped at the Government funding the facility can receive (known as the accommodation supplement).

The amount of accommodation supplement the aged care home can receive is based on the standard of the accommodation and the ratio of low means residents to market price residents.

The table below shows the maximum funding an aged care home can receive based on their building standard and low means ratio.

Eligibility	Amount of Supplement	Equivalent RAC
If facility is significantly refurbished or newly built		
More than 40% low means, supported residents	$58.19	$518,032.93
40% or fewer low means, supported, concessional and assisted residents	$43.64	$388,502.44
If the facility meets building requirements *Aged Care (Transitional Provisions) Principles 2014*		
More than 40% low means, supported, concessional and assisted residents	$37.93	$337,669.51
40% or fewer low means, supported, concessional and assisted residents	$28.45	$253,274.39

Source: https://pro.agedcaregurus.com.au/ Resource library

3. Impact on market price payers

For market price payers who enter care after 1 July the reduction in MPIR won't change their lump sum amount but their daily accommodation payment (DAP) will be less. For example, a market price Refundable Accommodation Deposit (RAD) of $400,000 today has an equivalent DAP of $53.59, after 1 July the DAP will be $44.93 a saving of $3,161/year.

Historical context and need for advice

When the LLLB reforms were introduced in July 2014 a RAD of $400,000 had an equivalent DAP of $73.32 per day in 2014 this has subsequently decreased to $44.93 per day from 1 July 2020, a huge saving of 63% to the resident and a substantial drop in income to the aged care home.

In contrast, low means residents in 2014 could pay a maximum DAC of $52.49/day and their equivalent lump sum was $286,380. From 1 July, while the maximum DAC has only increased to $58.19/day the equivalent lump sum will be a staggering $518,033.

Like all great advice, the advice needs to take into consideration the client's personal financial needs and objectives.

There are many clients who may be on the borderline, while it may seem illogical, increasing their assessable assets to push them over the threshold to become a market price payer may be a good idea.

If the client is going to be a low means resident and they want to pay by lump sum, moving in now rather than after 1 July could mean the difference between paying $434,343 versus $518,033. Of course, the RAC is an exempt asset so paying more could actually be of benefit to their pension, paying the higher RAC could equate to an extra $6,500/year in age pension.

For other clients strategies to reduce their assessable assets could save them a great deal. Reducing the assessable assets by $20,000 could reduce the DAC by $9.62/day or $3,500/year – the reduction to the equivalent lump sum is $85,366.

The change to the MPIR could change the ratio of low means residents an aged care home chooses to keep. If the home meets the new (or refurbished) building standards but has a ratio less than 40% low means residents, the most they can receive is $43.64/day or $388,502 as a lump sum from a low means resident. But if the ratio reaches 40%, they can receive $58.19/day or $518,033 as a lump sum. This may be very attractive, especially if their market price is below $500,000 as the market price doesn't cap what a low means resident can pay.

Changes to the home's funding don't just impact on what new residents can pay, they also impact on existing resident. A resident who moved in 2 years ago and is currently paying a DAC $43.64/day could find that their costs jump up to $58.19/day – as a lump sum the cost would increase by just over $92,000 from $276,059 to $368,100.

Many low-means residents think they can't afford great advice, we think they can't afford not to get it.

Jemma Briscoe is Head of Research and Technical Advice at Aged Care Gurus. This material is general information only and does not take into account your objectives, financial situation or needs. There is a free webinar on this topic on 14 July at 12.30.

Housing cost is biggest threat to a comfortable retirement

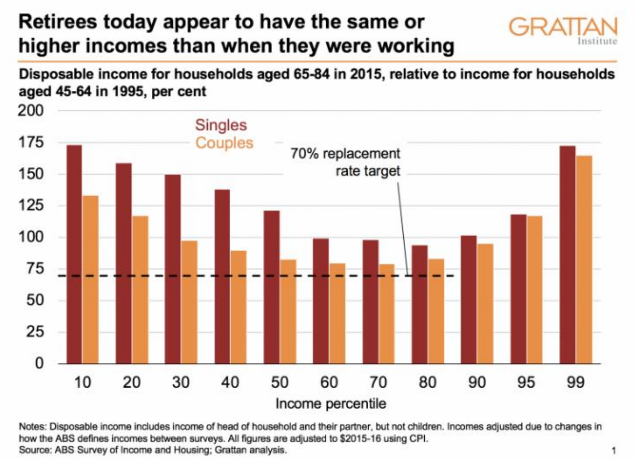
Brendan Coates

There's no shortage of issues facing people planning for their retirement. One that needs tackling is the threat worsening housing affordability and falling home ownership will present to the retirement incomes of many Australians.

How ownership critical for comfortable retirement

Most retirees today feel more comfortable financially than younger Australians who are still working. Retirees are less likely than working-age Australians to suffer financial stress such as not being able to pay a bill on time and are more likely to be able to afford optional extras such as annual holidays.

In fact, most people aged 65-84 today have as much or more income than they did 20 years ago when working. And while the age pension is by no means generous, it does keep most low-income retirees out of poverty – provided that they own their home.

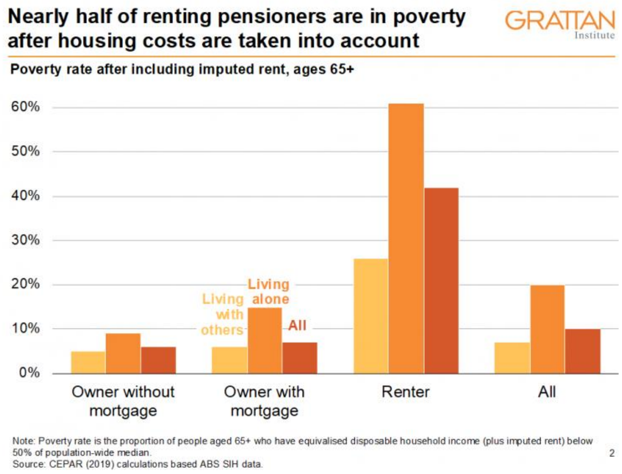


As for future retirees, Grattan Institute research shows that most working Australians today can look forward to a standard of living in retirement that's on par with their standard of living while working, and often higher. Retirement incomes also remain adequate for most Australians even when they work part-time or take significant career breaks, such as to care for children.

But we're failing retirees who rent

Not all Australians enjoy a comfortable retirement. Senior Australians who rent in the private market are much more likely to suffer financial stress than homeowners or renters in public housing. Nearly half of retired renters are in poverty once housing costs are taken into account.

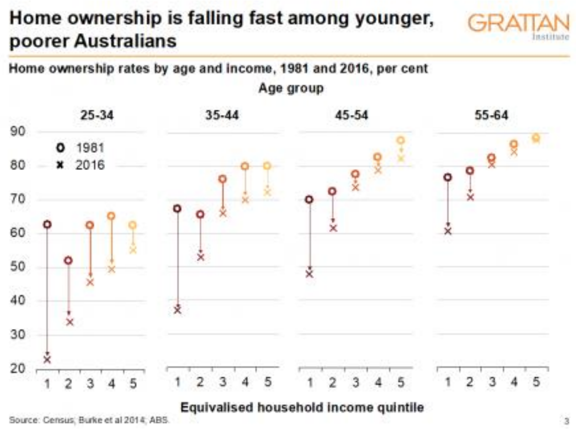
The explanation is simple: retirees spend a lot less on housing as they pay down their mortgage, but housing costs keep rising for retired renters. The typical homeowner aged over 65 [spends just 5% of their income on housing](), compared to nearly 30% for renters.



More retirees will rent in future

The proportion of retired renters in financial stress will increase because younger people on lower incomes are less likely to own their own home than in the past.

Between 1981 and 2016, home ownership rates among 25-34-year-olds fell from more than 60% to 45%. Home ownership has also fallen for middle-aged Australians. Home ownership now depends on income much more than in the past: for 25-34-year-olds, home ownership among the poorest 20% has fallen from 63% to 22%.



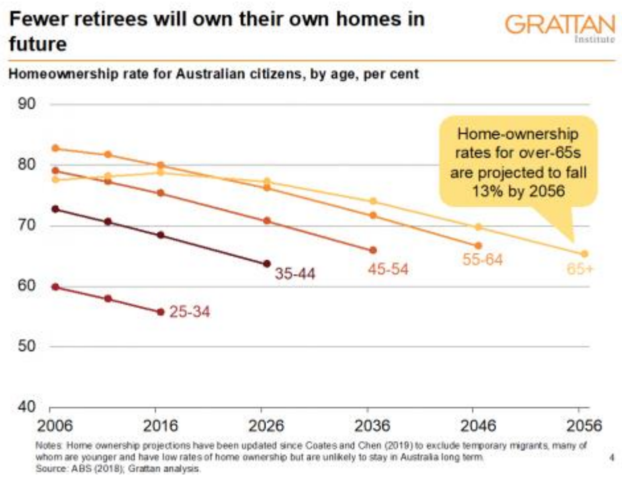
Today's younger Australians will become tomorrow's retirees. These trends suggest that by 2056 just two-thirds of retirees will own their homes, down from nearly 80% today.

So what should the federal government do?

Boosting Rent Assistance should be the priority

The government's first priority should be boosting Commonwealth [Rent Assistance](), which has not kept pace with rent increases over the past two decades. Raising Rent Assistance by 40%, or roughly $1,400 a year for singles, would cost just $300 million a year if it applied to pensioners, and another $1 billion a year if extended to younger renters as well.

And in future, Rent Assistance should be indexed to changes in rents typically paid by people receiving income support, so that its value is maintained. Boosting Rent Assistance would do much more to reduce poverty in retirement per government dollar spent than the alternatives, including lifting the age pension.



A common concern is that boosting Rent Assistance would lead to higher rents. But that's unlikely: households would not be required to spend any of the extra income on rent, and most would not.

More social housing is needed but not for everyone

There is also a powerful case for more government funding of social housing, including for vulnerable older renters at risk of homelessness. It would also be an [effective economic stimulus]() given COVID-19. But boosting social housing will be expensive. Increasing the stock by 100,000 dwellings would require additional ongoing public funding of about $900 million a year, or upfront capital expenditure of $10-$15 billion.

It would be prohibitively expensive to provide enough social housing to accommodate all renting pensioners, let alone all working-age Australians on low incomes. So any boost to social housing should be reserved for people at greatest risk of long-term homelessness.

Include the home in the pension assets test

The age pension exacerbates the divide between the housing 'haves' and 'have nots' in retirement by favouring homeowners over renters. Once a person is retired, their home is treated differently to their other assets. Under current rules only the first $210,500 of home equity is counted in the age pension assets test. Which is why $6 billion in pension payments go to people with homes worth more than $1 million.

It's time for more of the value of the family home to be included in the pension assets test, above some threshold such as $500,000 would be fairer and would save the budget up to $2 billion a year.

No pensioner would be forced to leave their home. Instead this change would primarily reduce inheritances. Pensioners with valuable homes could continue to live at home and receive the pension under the government's Pension Loans Scheme, which recovers debts only when homes are eventually sold.

A $500,000 threshold would ensure that homeowners would still have substantial equity to pass on to their beneficiaries. It would ask people with high levels of wealth that would otherwise be passed on to heirs to use some of this wealth to support themselves in retirement.

Higher house prices also mean that Australians are spending more of their lifetime incomes buying a house and paying it off by the time they retire. Yet few retirees draw down the value of their home to fund their retirement, either by downsizing or by borrowing against home equity.

Unless Australians are willing to draw on their home equity in retirement, rising house prices mean Australians will be left with lower living standards both while working and in retirement.

Brendan Coates is the Household Finances Program Director and a Fellow at Grattan Institute. This article is general information and not personal advice.

The populations of key countries are shrinking

Michael Collins

Released by US film producer Mike Moore, the documentary *Planet of the Humans* tells how renewable sources of energy are flawed solutions to mitigate the dangers of climate change.

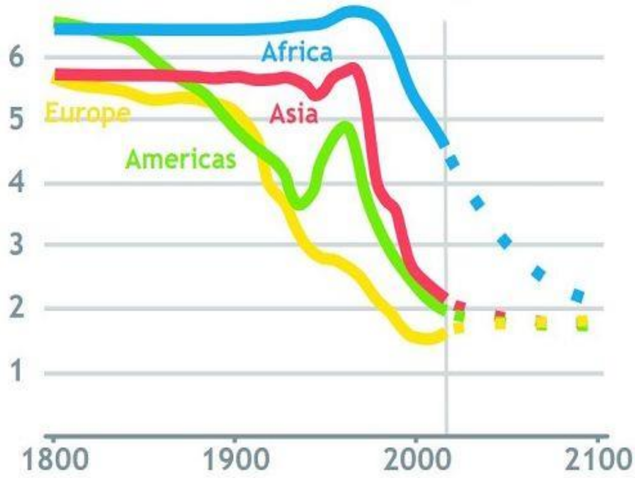
About halfway through the documentary, a scientist laments that the environment's biggest problem is that "*there are too many human beings using too much, too fast*". The warning here and elsewhere in the documentary is that only a reduction in the world's population can save the planet.

Declining birth rates

Well, in that case, the battle against climate change is winnable because the populations of many countries are shrinking. The OECD says that only three (Israel, Mexico and Turkey) of its 37 members have fertility rates above the replacement rate of 2.1 children per woman.

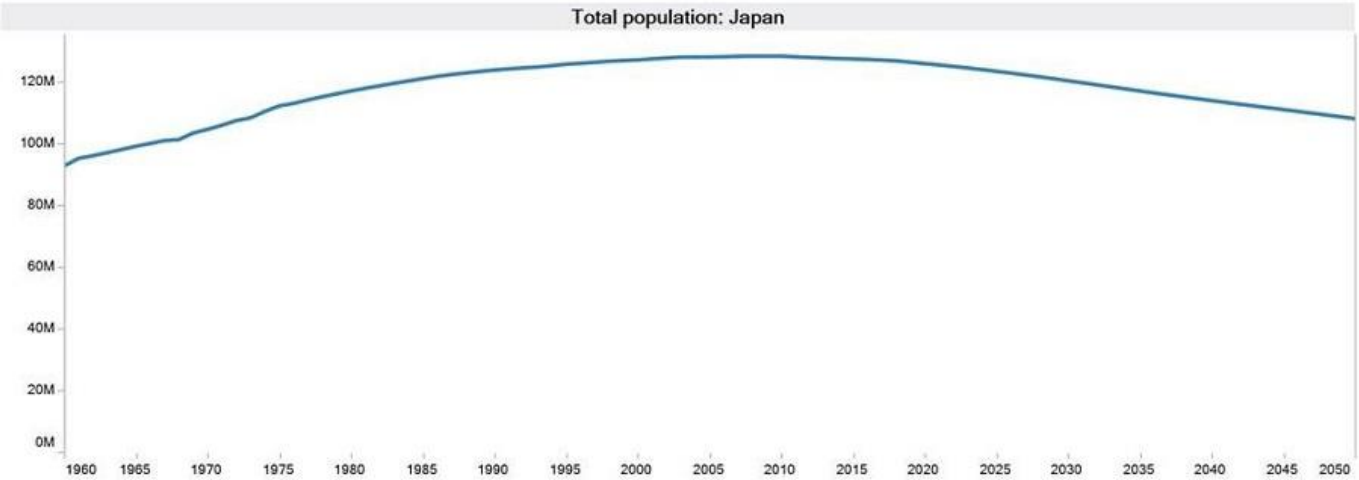
The UN reports the reproduction rates of all European countries are below replenishment levels. The EU forecasts that the populations of 12 of its 27 member countries will shrink in coming decades as only immigration props up numbers in the others. The World Bank predicts China's population will decline by 100 million people by 2050, that East Asia's will shrink from the 2030s and Brazil's will contract from the late 2040s by when India's population growth will be static.

Babies per woman (Total Fertility Rate)



Source: Free teaching material from www.gapminder.org. Period from 1950 to 2100. Data from UN's Population Division's publication World Population Prospects 2017.

Already dwindling are the populations of Russia (since 1992), Japan (first in 2008 and uninterrupted since 2010, see below) and Italy (since 2014). But for immigration, many Anglo countries with declining birth rates including Australia and the US would be shrinking population-wise too.



Many demographers say, if anything, the global bodies are underestimating the declines in population numbers. Social and economic forces that lowered birth rates in advanced countries are now universal across the emerging world. These factors include expectations of low infant mortality, rising female education, better career prospects for women, and urbanisation.

Fewer births in the emerging world, these demographers say, will see the world's population diminish from a peak of between eight and nine billion people from around the middle of this century, whereas the UN forecasts the world's population to increase another three billion to 10.9 billion by 2100.

The economic impact

The consequences of declining populations could be significant and mostly grim, any environmental benefits aside. Fewer births reduce what is probably the biggest motivational force in society; young parents seeking a better life for their children. In economic terms, declining populations are a bigger challenge than ageing populations because the former herald a lasting shortfall in private demand that points to lower output, even if GDP per capita might rise. Businesses will invest less if fewer people are consuming less. Such outcomes hint at the 'Japanification' of economies; deflation and almost permanent recessions for economies that prove impervious to stimulus.

Government finances face difficulties as the shrinking and ageing of populations accelerates because a smaller working-age cohort must support more elderly people who cost more health-wise. A stretched bunch of fewer workers could lead to reduced innovation and productivity gains. Government policy, especially with regards to taxation and social-security spending, could become skewed towards the elderly rather than productivity should older voters form a voting bloc.

For the countries affected, a drop in population numbers might undermine their global power, and any rejigging of the world order rarely happens without friction. To sustain population numbers, rich countries might rely more on immigration but that risks social and political strains (including in source countries), especially if long-dominant ethnic groups become minorities.

These outcomes indicate the biggest threat raised by shrinking populations; that the unprecedented change is a shock. Capitalist societies are geared for growing populations, as happened over the 19th and 20th centuries when the world's population increased eightfold from one billion around 1800. Over that time, all aspects of societies were designed to accommodate more people, a trend that engenders much optimism and dynamism.

Much might need to be adjusted as fewer people mean less of everything. Policymakers could no longer assume positive economic growth as a given. Companies could no longer reflexively plan to expand. Investors could no longer presume higher revenue by default. Town planning might be about shrinking social infrastructure. And so on.

Time to stop ignoring this change

In 1937, UK economist John Maynard Keynes foresaw the problem and cautioned that "*a change-over from an increasing to a declining population may be very disastrous".* At the very least, as many urge, it's time that society stops ignoring what might be an unrelenting challenge of the upcoming age.

To be clear, demographic projections largely extend trends, and birth rates could rebound at any time to make mockeries of such forecasting techniques. It barely needs to be said that a rising population is no guarantee of economic success and that younger populations come with bespoke challenges too. Declining populations could come with benefits. These could include reduced environmental damage, fewer clashes over the world's resources and reduced inequality if labour shortages boost wages. Perhaps changes might be less disruptive than expected because populations only shrink slowly.

Such musings reinforce how much is speculation when it comes to analysing a sustained decline in populations because the world has never undergone a voluntary mass depopulation. There's no guarantee either of the supposed benefits such as the better environment that *Planet of the Humans* assumes.

Michael Collins is an Investment Specialist at Magellan Asset Management, a sponsor of Firstlinks. This article is for general information purposes only, not investment advice. For the full version of this article and to view sources, go to: https://www.magellangroup.com.au/insights/.

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