Firstlinks
a Morningstar company

Edition 606, 11 April 2025

Contents

Editorial

UniSuper's John Pearce manages $150 billion in assets and understandably has a lot on his mind.

In mid-February, he flagged a potential correction ahead, which has proven remarkably prescient. Back then, he said he expected a flat year for equities but wouldn't discount the possibility of a correction of 10% or more. However, he invested for the long term, and on this basis, he remained optimistic given the growth in the global economy, subdued inflation, strong employment, and the tech revolution:

"… if we do get that correction, UniSuper will be using it as a buying opportunity. We've got plenty of cash, and we intend to load up on assets when the price is right."

Now, he's not so sure. He says Donald Trump has effectively declared an economic war with his tariff hikes:

"The current crisis, it's man-made. And it's made pretty much by a single man. We know what the solution is here, the solution is for rational people to get around and understand the havoc that they have created and get to a sensible compromise. We know what the solution is, and let's hope that common sense prevails."

Yet, he's not banking on it. Pearce says the market has gone into meltdown because of the magnitude and breadth of the tariff increases. China copping whopping tariff rises hasn't surprised. What has is that few have been spared Trump's wrath. Even Australia, a staunch American ally, is facing a 10% tariff, and we got off lightly.

Pearce says tariffs are bad for global trade and are a tax on the US consumer. And the reason that markets have plummeting is because the odds of a US recession, and perhaps a global one, have gone up.

What will happen from here?

Pearce foresees a wide range of possible outcomes. At the pessimistic end, there might be a long drawn-out battle. That's where the likes of Europe and China don't come to the negotiating table. And we're already seeing that with China, which has announced retaliatory tariffs.

At the optimistic end, there have been a few countries which have come to the negotiating table. Vietnam says it will cut all tariffs on American imports to zero. And India says it won't retaliate but expects a bilateral agreement.

Pearce is leaning towards a long drawn-out battle. However, whichever way it goes, a lot of damage has already been done, with companies putting off investments and consumers getting nervous – both of which have already resulted in softening US economic growth.

There are potential positives

Pearce is not all doom and gloom, though. If Europe and China don't come to the negotiating table, they'll likely have to stimulate their own economies. We've already seen that with Germany, which has announced plans to significantly increase government spending on defence and infrastructure. And China is also making noises around stimulus, which could be positive for economies outside of the US, such as Australia.

Reducing US stock exposure

Pearce admits that he has some big asset allocation decisions to make. Priority number one is what to do with his large exposure to US assets.

Previously, he'd been a believer in American corporate exceptionalism, given its technology strengths. But Trump threatens all of that.

He says UniSuper is questioning its commitment to America and that, "I think we've seen peak investment in US assets."

He expects to reduce US stock exposure "over time", though now is "not the time to be reducing that exposure", given how far and fast the market has fallen.

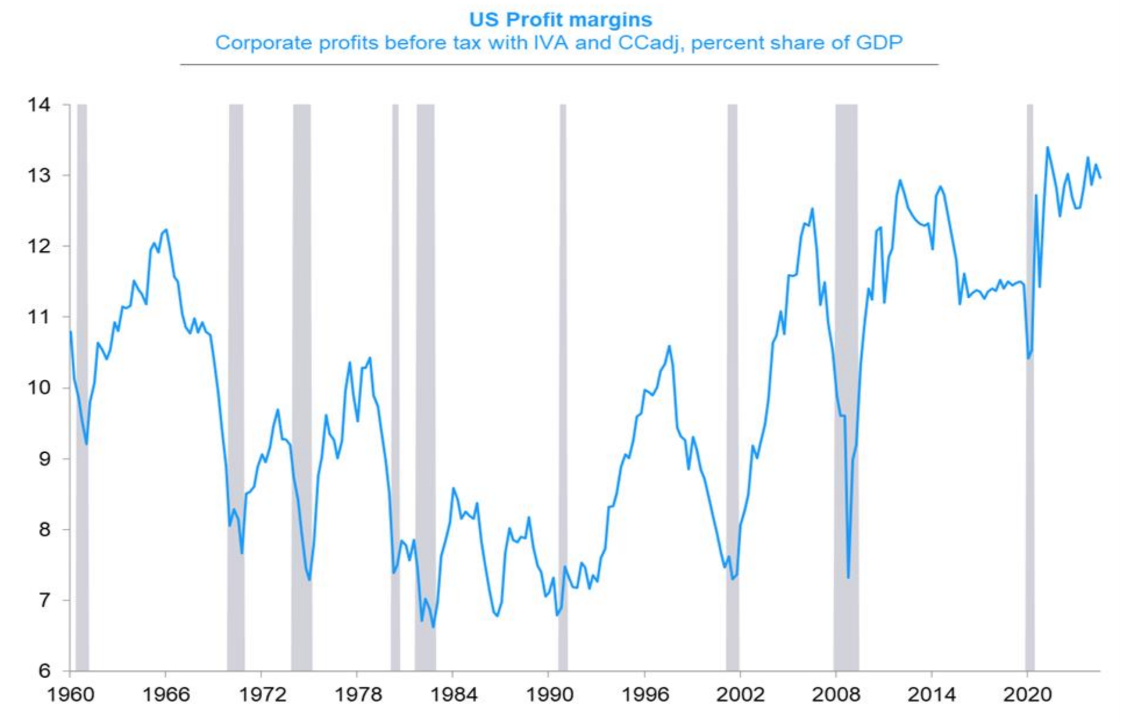
Should you follow suit?

Is it sensible for the average investor to follow John Pearce's lead and rethink their US stock allocation? I think it is.

Unlike Pearce, I've [questioned the notion of US market exceptionalism] over the past 12 months. Steep valuations, increasing concentration in the Magnificent Seven, record-high corporate profit margins, extreme institutional allocations to US stocks, speculative retail investor behaviour in AI and other tech-related companies, all pointed to a trend that had gone too far. Meanwhile, other countries had been largely left for dead, including Europe and those in Emerging Markets.

The problem is that the US remains expensive versus history, institutions like UniSuper are only just starting to reweight holdings out of America, retail investors remain overloaded with US shares, and corporate margins remain at peak levels.

It's the latter point where the greatest risk to US equities lies. Corporate margins have been abnormally high for more than a decade, and with the switch away from globalisation, US tech firms could struggle to maintain their high margins.



Source: BEA, EY-Parthenon
*Shaded areas represent recessions

You can now understand why all the US tech billionaires lined up at Trump's inauguration in January. Staying close to those in power might ensure that their companies maintain their monopolies and oligopolies. Unfortunately for them, it hasn't worked out as planned.

If corporate margins mean revert, that will prove a long-term drag on US earnings. Combined with still elevated valuations, it doesn't paint an optimistic picture for the US market over the next decade.

Meanwhile, other parts of the world remain cheap and countries like Germany are spending big, which could revitalise their economies.

Therefore, the global switch out of US equities into other markets may have only just begun.

**Disclosure: UniSuper is a Firstlinks sponsor.*

****

In my article, I look at famed investor **Howard Marks**' remarks that this is the biggest upheaval in markets he's witnessed in his 50-odd year career. We've switched from a globalised to a fragmented world, and this has changed the rules of the investing game, he believes. He says the new environment demands a different investment approach.

Meanwhile, a lot of investors are wondering whether it's sensible to start buying stocks amid this market volatility. To help with this, **Ashley Owen** has analysed almost 40 corrections of 10% of more in the Australian share market since 1920. And he answers the question: what would have happened in each case had you 'bought the dip'?

The uncertainty sowed by falling share markets can make investors panic and commit costly errors. **Leigh Gant** says that following the advice of an ex Navy SEAL commander can help you stay composed and focus on what really matters.

And **Greg Canavan** has gone back to re-read Charles Kindleberger's classic book, *Manias, Panics and Crashes*. The book details different booms and busts throughout history, and the commonalities between each episode. Greg thinks the recent AI-fuelled boom followed the classic patterns of the past and recent market ructions may be the beginnings of another bust.

James Gruber

Also in this week's edition...

For those of you who may be tired of hearing about tariffs and market ups and down, we have several articles with alternative topics.

Roger Montgomery explores why sales of electric vehicles - hailed as the future of the automotive industry - have stalled both in Australia and globally.

According to **Magellan's Lucina Martin**, travel is about to be transformed by a new technological force: AI-powered travel agents. These agents will independently navigate websites, make decisions, solve problems and adjust your travel itinerary on your behalf – just like a personal assistant.

Property investment in SMSFs is a popular strategy for retirement wealth. Compliance is essential to avoid risks like the sole purpose test, non-arm's length income, and property development issues, says Shelley Banton.

Lastly in this week's whitepaper, **RQI** looks at corporate culture, and how though it's intrinsically important to companies, it's also notoriously difficult to measure.

Howard Marks: The investing game has changed

James Gruber

Howard Marks is closely followed by investors, and for good reason. He's the Co-Chairman of Oaktree Capital Management, the world's largest distressed credit investor managing more than US$200 billion. He's best known for his client letters published since 1990.

Over the past week, Marks appeared on Bloomberg TV and he was both blunt and nuanced - as he was in a follow-up client memo.

In his TV interview, he was blunt about changes wrought by Trump and his tariff policies. He thinks they amount to nothing less than a regime change.

Mark says that we've lived in an era of globalisation since World War Two. There's been open trade, efficient supply chains, and cheap goods:

"I believe that the last 80 years since World War Two have been the best economic period in the history of mankind. And one of the major reasons was the growth of trade."

Free trade brought significant benefits, including greater productivity, broader access to goods, and lower prices. It helped keep inflation down, which aided central banks, consumers, and investors:

"Worldwide welfare is maximized when every country does the things it does best and cheapest and then sells them to the countries that need them, which do other things and sell them to other people. That's how trade works ...

… The good news is that Italians make the pasta and the Swiss make the watches. But if we stop world trade, and the Swiss have to make their own pasta and the Italians have to make their own watches … people in both countries will be a little worse off."

Marks believes the era of free trade is now fading.

In its place is a new world. One where countries are rethinking trade, tariffs are increasing, and domestic production is finding favour, even if it means higher prices for goods.

"Tariffs are an increased cost. Somebody has to pay them."

This will result in slowing trade, increased inputs and prices, and less efficient supply chains - all of which will hurt economic productivity.

Not prone to big statements, Marks makes one anyway:

"This is the biggest change in the environment that I've seen probably in my career."

How investors should play it

For investors, Marks says old models and playbooks need to be thrown out. Because what's worked over the past 80 years may not work in future. The new environment demands a different approach.

That approach shouldn't rely on forecasting. In the past, Marks has been scathing of macroeconomic forecasts, and he now thinks they're even less useful. He thinks forecasts can't work in an environment like this because the world is so uncertain. It's hard to predict what will happen the next day, let alone the next year:

"… the probability that we know what the future is going to look like is lower than ever."

So what should investors do?

At first glance, Marks isn't encouraging, suggesting that there's "no analysis you can do to determine whether today's asset prices are right for the environment ahead."

However, he doesn't just mean today's environment, but *any* environment. Put simply, we can't possibly know whether a market multiple of 20x earnings is appropriate pricing for what's ahead, or whether that multiple should be higher or lower.

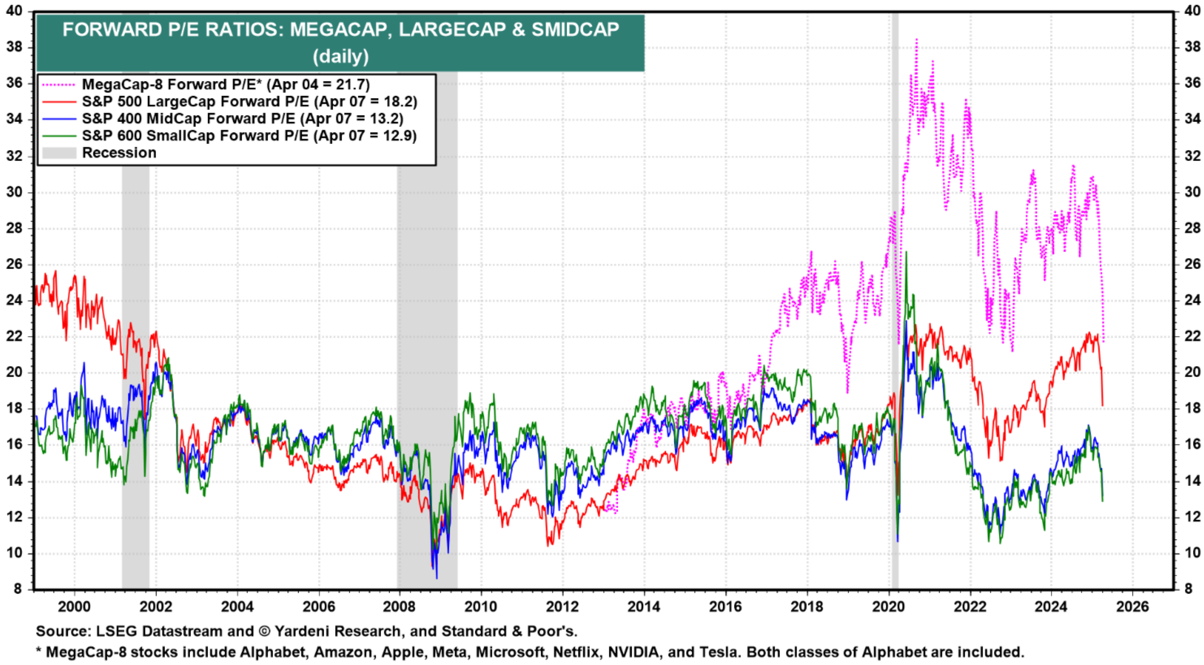
What Marks is saying is that given the enormous changes happening today, and the likelihood of higher prices and inflation, investors need to tread carefully. And more than ever, they should focus on probabilities and price.

He says the market falls should have investors thinking like a shopper at a sale. "Bloomingdale's just put everything on sale," he quips. "Prices have come down…It's on sale. That should encourage people to think about buying."

Notice that he doesn't urge investors to buy *now*, but that they should *think* about buying assets that have fallen in price, while being conscious of the risks brought by Trump and his tariffs.

Marks does say that he maintains his preference for credit over stocks right now. "The yields on credit are still very healthy," he notes, pointing out that high-yield US bonds have jumped from 7.2% to nearly 8% yields in just weeks, making those bonds cheaper.

His take on stocks is more cautious: "[US] Stocks have delivered an average of 10% a year for the last hundred years, but not when the P/E ratio was 19." With valuations where they are today, he thinks expecting historical returns would be a mistake.



Finally, as to whether the US remains a strong place to invest, Marks says that it's no long a given, especially given its large trade deficits:

"Can the events of the recent days … cause there to be a credit limit? Can they cause a bill to be presented at some point in time? And if the answer to either or both of those questions is yes, that's a real risk. If people don't like the [US] dollar, if they don't like investing in the United States, don't want to hold an unlimited number of Treasuries, if we just make people mad, and say "the US is still a great credit but I don't want to hold your debts because look how they're treating me", the fiscal situation would be very complicated."

James Gruber is Editor at Firstlinks.

Buy the dips?

Ashley Owen

[ed: This article was written on March 23 2025, based on Australian market data to March 20. The US article mentioned in the piece was written on March 18 with data to March 14. Markets have been volatile since then, with an initial rebound in the US followed by the recent fall into correction territory.]

A few days ago I published my review of the dips of -10% or more on the US stock market since 1900.

My findings on the US market 'dips' were:

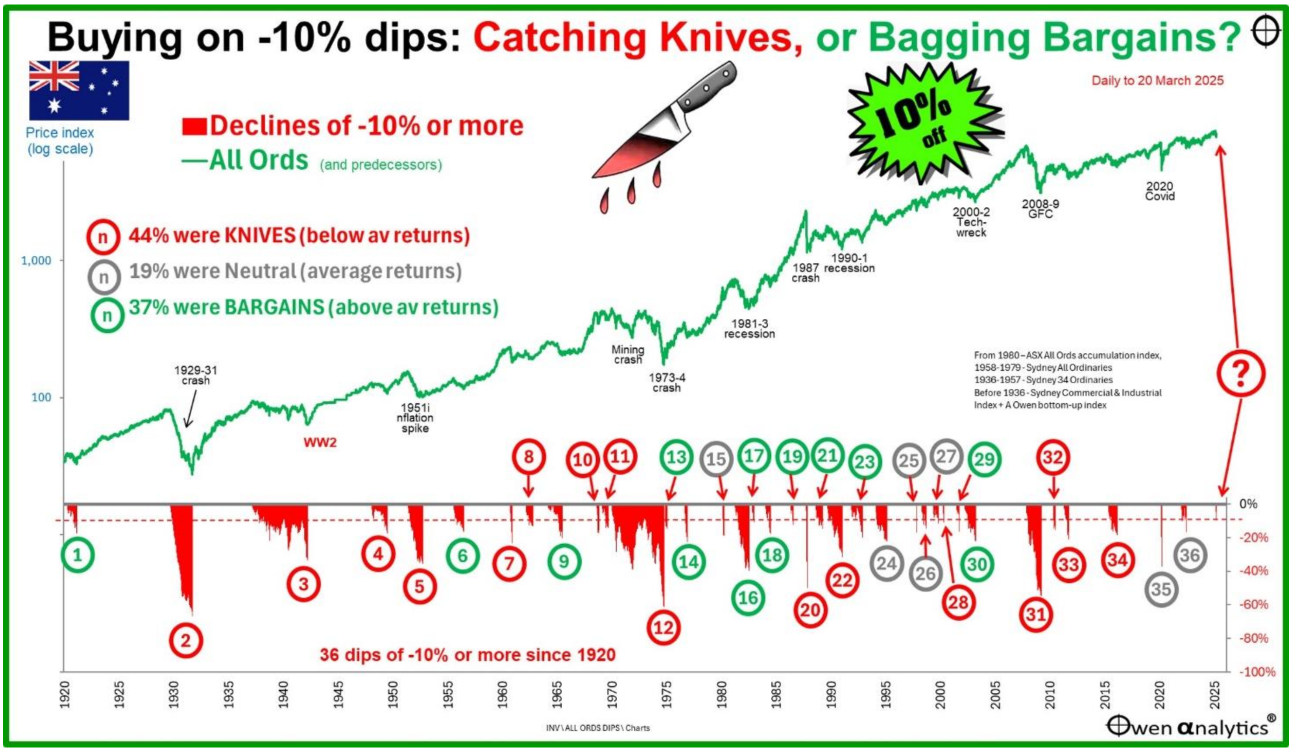
- In most cases, a -10% dip in the US market turned out to be just the start of a much larger fall (a further -15% fall on average), and for a much longer period (more than a year of further falls on average).
- Overall, buying the dips resulted in significantly below-average returns over subsequent 1, 3, and 5-year periods from the buy-in price, but there were several occasions when buying the dip resulted in above-average returns.

- Pricing was a critical factor – if the market was over-priced, a -10% dip mostly turned out to be the start of the bust that deflated the over-priced booms. Prime examples were the 1929 crash that ended the speculative 1920s boom, and the 2000-2 'tech-wreck' that ended the 1990s speculative 'dot-com' boom.

In the US story I outlined:

- The case for 'buying dips' – logically, buying at a 10% 'discount' should increase subsequent returns from the lower buy-in price.
- The case against buying dips - in reality, markets are not random – they trend, and -10% dips mostly turned into much deeper set-backs, resulting in significantly lower returns from the buy-in price. Bottom line – reality trumps logic.

Today's chart shows all of the dips of -10% or more on the ASX market since 1920 (which is as far back as my daily series goes. See end of this article for notes on data sources.



The worst sell-off was the 1929-31 crash, which was also the worst for the US market (but ours was not as deep, and a year shorter than the US).

Also like the US market, the recent -9.7% dip in the All Ords is so small in historical terms you need a magnifying glass to see it.

'Knives, 'Bargains', and 'Neutral' returns from buying 10% dips

The colour of the Dip number on the chart indicates the outcome for investors if they bought into the broad market at the point the dip reached -10%. As with the US story, I measure returns (price index return, excluding dividends) over subsequent 1-year, 3-year, and 5-year holding periods from the entry price on the day the dip reached or exceeded -10% from the recent high.

- 44% of dips turned out to be 'Knives' (below average subsequent returns)
- 37% of dips turned out to be 'Bargains' (above average subsequent returns)
- The remaining 19% of dips turned out to be 'Neutral' (around average subsequent returns)

This is better than the US market, where

- 55% of -10% dips turned out to be 'Knives'
- 33% turned out to be 'Bargains'
- 13% turned out to be 'Neutral'

What happened next?

The table below shows what happened next after each dip of -10% or more on the Australian market:

Buying on -10% dips: Catching Knives, or Bagging Bargains?

10% declines in the All Ords (and predecessors) since 1920 - What happened next?

	A	B	C	D	E	F	G	H	i					
	High	Date of -10% decline	Eventual Low	Days from -10% decline to bottom	% Decline top to bottom	Price move from -10% decline day: 1 year	3yr (pa)	5yr (pa)	Causes	KNIFE	NEUTRAL (market return)	BARGAIN		US Market (DJIA)
1	Mon, 19 Apr 1920	Thu, 18 Nov 1920	Mon, 28 Feb 1921	102	-17.3%	10.4%	13.2%	10.1%	post-war inflation spike, recession			BARGAIN	🇺🇸	KNIFE
2	Wed, 4 Sep 1929	Thu, 28 Nov 1929	Thu, 17 Sep 1931	658	-66.7%	-45.7%	-10.2%	-0.4%	1929-31 crash, deflation, gov default	KNIFE			🇺🇸	KNIFE
3	Thu, 11 Mar 1937	Tue, 19 Oct 1937	Tue, 31 Mar 1942	1,624	-33.5%	-1.8%	-0.7%	-1.4%	Steel export ban to Japan, Unions close BHP, wo	KNIFE			🇺🇸	KNIFE
4	Thu, 5 Feb 1948	Thu, 31 Mar 1949	Fri, 8 Jul 1949	99	-17.3%	12.3%	-2.2%	-0.8%	Bank nationalisation battle, Britain BOP/Pound cr	KNIFE			🇺🇸	KNIFE
5	Mon, 7 May 1951	Thu, 16 Aug 1951	Mon, 29 Sep 1952	410	-35.6%	-23.9%	-4.6%	-2.7%	Korean War escalation + 25% inflation spike	KNIFE			🇺🇸	(US fell -8%)
6	Tue, 26 Jul 1955	Tue, 8 Nov 1955	Tue, 19 Jun 1956	224	-16.9%	-0.5%	5.3%	9.6%	Petrov + Malayan communist scares, tax hikes,			BARGAIN		(US rose)
7	Fri, 16 Sep 1960	Fri, 21 Oct 1960	Wed, 16 Nov 1960	26	-23.2%	-4.0%	3.0%	0.4%	rate hikes, tax hikes, recession	KNIFE			🇺🇸	NEUTRAL
8	Wed, 21 Feb 1962	Wed, 20 Jun 1962	Wed, 10 Oct 1962	112	-13.0%	9.8%	2.2%	4.4%	Aust 1st troops to Vietnam, Cuban milline crisis (	KNIFE			🇺🇸	NEUTRAL
9	Thu, 27 Feb 1964	Tue, 2 Mar 1965	Tue, 29 Jun 1965	119	-20.4%	-5.7%	10.4%	12.4%	Inflation, rate hikes, credit crunch, recession			BARGAIN		(US rose)
10	Fri, 16 Aug 1968	Thu, 19 Sep 1968	Tue, 29 Oct 1968	40	-17.6%	0.8%	-6.0%	-2.9%	Soviet invasion of Czech, UK investors dump BH	KNIFE				(US rose)
11	Tue, 11 Feb 1969	Mon, 9 Jun 1969	Wed, 3 Sep 1969	86	-14.3%	-6.4%	2.8%	-6.2%	inflation, rate hikes, + UK+US inflation	KNIFE			🇺🇸	KNIFE
12	Tue, 6 Jan 1970	Wed, 1 Apr 1970	Mon, 30 Sep 1974	1,643	-61.3%	-15.7%	-1.8%	-10.1%	Mining crash + property/finance crash	KNIFE			🇺🇸	KNIFE
13	Tue, 12 Nov 1974	Tue, 19 Nov 1974	Thu, 9 Jan 1975	51	-15.0%	33.0%	13.7%	17.0%	Whitlam crises, Connor/Khemlani loans afair			BARGAIN	🇺🇸	KNIFE
14	Thu, 19 Aug 1976	Mon, 27 Sep 1976	Fri, 26 Nov 1976	60	-22.5%	-6.8%	13.3%	12.3%	inflation, rate hikes, UK IMF bail-out			BARGAIN	🇺🇸	KNIFE
15	Thu, 14 Feb 1980	Mon, 10 Mar 1980	Fri, 28 Mar 1980	18	-19.1%	15.7%	-2.9%	6.8%	Inflation, rate hikes, recession fears		NEUTRAL		🇺🇸	KNIFE
16	Mon, 6 Apr 1981	Thu, 9 Jul 1981	Thu, 8 Jul 1982	364	-39.9%	-33.1%	0.2%	11.4%	inflation, rate hikes, recession			BARGAIN	🇺🇸	BARGAIN
17	Wed, 20 Oct 1982	Mon, 20 Dec 1982	Tue, 21 Dec 1982	1	-10.9%	60.6%	28.0%	21.6%	inflation, rate hikes, recession			BARGAIN	🇺🇸	BARGAIN
18	Mon, 9 Jan 1984	Tue, 22 May 1984	Mon, 18 Jun 1984	27	-18.0%	28.2%	38.1%	17.7%	inflation, rate hikes, Sterling crisis, Continential Illinois bailout			BARGAIN	🇺🇸	BARGAIN
19	Wed, 7 May 1986	Wed, 9 Jul 1986	Mon, 28 Jul 1986	19	-12.2%	67.8%	10.8%	6.6%	Keating's 'banana republic' BOP crisis, rate hikes			BARGAIN		(US flat)
20	Mon, 21 Sep 1987	Mon, 19 Oct 1987	Wed, 11 Nov 1987	23	-50.1%	-24.1%	-13.4%	-7.3%	1987 crash	KNIFE			🇺🇸	KNIFE
21	Tue, 9 Aug 1988	Mon, 21 Nov 1988	Fri, 7 Apr 1989	137	-14.8%	10.3%	3.3%	6.7%	inflation, rate hikes, Rothwells, Equiticorp, Spedley, GPI			BARGAIN		(US rose)
22	Tue, 29 Aug 1989	Mon, 16 Oct 1989	Tue, 15 Jan 1991	456	-31.6%	-17.5%	-3.2%	4.7%	Collapse of US junk bond mkt, inflation, reate hike	KNIFE			🇺🇸	(US fell -7%)
23	Fri, 8 Nov 1991	Tue, 25 Aug 1992	Mon, 16 Nov 1992	83	-20.0%	26.8%	11.7%	11.6%	Westpac/ANZ bank losses			BARGAIN		(US rose)
24	Thu, 3 Feb 1994	Tue, 29 Mar 1994	Wed, 8 Feb 1995	316	-22.1%	-9.6%	4.9%	7.4%	Bond crisis, inflation scare, rate hikes		NEUTRAL		🇺🇸	(US fell -9.7%)
25	Wed, 1 Oct 1997	Mon, 27 Oct 1997	Tue, 28 Oct 1997	1	-17.3%	3.5%	9.1%	3.8%	Asian currency crisis	KNIFE			🇺🇸	BARGAIN
26	Thu, 16 Apr 1998	Wed, 10 Jun 1998	Tue, 1 Sep 1998	83	-14.7%	15.1%	9.1%	3.2%	Russian default, LTCM crisis		NEUTRAL		🇺🇸	BARGAIN
27	Tue, 27 Apr 1999	Mon, 18 Oct 1999	Tue, 19 Oct 1999	1	-11.6%	15.1%	1.8%	5.9%	US inflation, RBA rate hikes, GIO losses		NEUTRAL		🇺🇸	KNIFE
28	Wed, 22 Mar 2000	Mon, 17 Apr 2000	Mon, 17 Apr 2000	0	-10.8%	10.1%	0.3%	6.2%	Start of US Nasdaq crash		NEUTRAL		🇺🇸	KNIFE
29	Fri, 29 Jun 2001	Wed, 12 Sep 2001	Mon, 24 Sep 2001	12	-16.3%	1.5%	5.7%	10.3%	Sep 11 attacks in NY, Ansett collapse			BARGAIN	🇺🇸	KNIFE
30	Thu, 7 Mar 2002	Wed, 17 Jul 2002	Thu, 13 Mar 2003	239	-22.3%	0.1%	11.5%	15.7%	US tech-wreck			BARGAIN	🇺🇸	KNIFE
31	Thu, 1 Nov 2007	Wed, 9 Jan 2008	Fri, 6 Mar 2009	422	-54.6%	-39.5%	-7.9%	-5.1%	GFC	KNIFE			🇺🇸	KNIFE
32	Fri, 16 Apr 2010	Mon, 17 May 2010	Mon, 5 Jul 2010	49	-15.1%	5.0%	4.8%	4.7%	Greece 1 debt crisis, flash crash	KNIFE			🇺🇸	BARGAIN
33	Tue, 12 Apr 2011	Wed, 3 Aug 2011	Mon, 26 Sep 2011	54	-21.3%	-2.8%	8.0%	4.7%	Greece 2, US downgrade crisis	KNIFE			🇺🇸	BARGAIN
34	Tue, 28 Apr 2015	Tue, 18 Aug 2015	Fri, 12 Feb 2016	178	-18.7%	6.0%	6.5%	3.4%	China slowdown, comoditiesi crash	KNIFE			🇺🇸	BARGAIN
35	Thu, 20 Feb 2020	Fri, 28 Feb 2020	Mon, 23 Mar 2020	24	-37.1%	6.6%	4.6%	5.4%	Covid lockdown crisis		NEUTRAL		🇺🇸	BARGAIN
36	Tue, 4 Jan 2022	Thu, 27 Jan 2022	Mon, 20 Jun 2022	144	-16.6%	8.1%	6.8%	.	inflation, rate hikes, recession fears		NEUTRAL		🇺🇸	NEUTRAL
			median:	85	-18.3%	2.5%	4.7%	5.4%	= a little **below** market av.	44%	19%	37%		
			average:	220	-24.2%	3.0%	4.9%	5.3%	= a little **below** market av.					
			best:	0	-10.8%	67.8%	38.1%	21.6%	July 1986, May 1984, Dec 1982					
			worst:	1,643	-66.7%	-45.7%	-13.4%	-10.1%	Nov 1929, Oct 1987, Apr 1970					

Data sources -
From 1980 – ASX All Ords accumulation index,
1958-1979 - Sydney All Ordinaries
1936-1957 - Sydney 34 Ordinaries
Before 1936 - Sydney Commercial & Industrial Index + A Owen bottom-up index

Overall market returns

	1 year	3yr (pa)	5yr (pa)
median:	6.3%	5.5%	5.7%
average:	6.5%	5.5%	5.2%

23 Mar 2025

Owen analytics®

This table has the same columns as the US table in the US story – except this time at the far right of the table I added two columns M and N to indicate whether each ASX dip mirrored (ie followed) the US market.

A US flag in column M indicates that the US market was also falling at the same time as the dip on our local market. The far-right column N indicates whether the US dip at the same time as our local dip turned out to be a Knife, Bargain or Neutral for US shares (from my recent US story). I have done this because. . .

Majority of dips on our market were US-led

The Australian stock market almost always follows the US market. Both markets boom and bust together (with rare exceptions), but the extent of the relative booms and busts in each market vary with each cycle. The Australian and US share markets essentially take turns in having the bigger boom and then the bigger bust.

From the US flags in column M at the right of the above table, we can see that only 6 of the 36 dips on the Australian market does not have a US flag – ie only six of our dips were NOT accompanied/triggered by falls on the US market at the same time.

Here are the six dips on the Australian market that were due to local factors alone, while US prices rose –

- Dip 6 - 1955-6 – Petrov and Malayan communist scares (the Cold War comes to our backyard), plus tax hikes. (Bargain)
- Dip 9 – 1964-5 – inflation, rate hikes, credit crunch, recession (Bargain)
- Dip 10 – August-October 1968 – UK investors dump BHP and mining shares (Knife, because it preceded the 1970 mining collapse)
- Dip 19 – May-July 1986 – Balance of Payments crisis, Keating's 'banana republic' comment (Bargain)
- Dip 21 – 1988-9 – Inflation, rate hikes, collapses of Rothwells, Equiticorp, Spedley, GPI (Bargain)
- Dip 23 – 1991-2 – Westpac & ANZ losses due to bad debts from the 1980s lending binge (Bargain)

Note that five out of these six 'local factor' dips turned out to be 'Bargains' if investors bought in when the dip was at -10%, even though the market continued to fall in the short term well beyond the initial -10% dip.

Timing the bottom perfectly

As in the US table in the US story, starting from the left of the table, we have the date of the market high (column A), the day the -10% dip was reached or exceeded (B), and the day the market eventually bottomed (C).

Colum D shows the number of days of further falls after the -10% day to the eventual bottom.

There were four -10% dips that turned out to pretty much the bottom of the dip, so 'buying the dip' led to no further immediate pain on the downside. However, although these four -10% dips produced no more immediate downside, only two turned out to be 'Bargains'.

- Dip 17 – 'Bargain' - starting after the 20 October 1982 high (the trigger for the dip was high inflation, rate hikes, recession, after the late 1970s-early 1980s property and mining booms). The dip hit -10% on 20 December, and hit bottom only 1 day later on 21 December (down -10.9% from the high) then rebounded. Buying that dip turned into a tremendous 'Bargain' – returning 61% over 1 year, 28% pa over 3 years and 22% pa over five years from the buy-in price (not including dividends).

- Dip 25– 'Knife' - starting after the 1 October 1997 high (the trigger for the dip was the Asian currency crisis). The dip hit -10% on 27 October, and hit bottom just 1 day later on 28 October (down -11.6% from the high) then rebounded. Even 'though 'buying the -10% dip' almost picked the bottom perfectly, it did not turn out to be a bargain because subsequent returns ran into the 1998 Russian default crisis and then the 'tech-wreck' – which were entirely unrelated to the original 1997 dip.

- Dip 27– 'Neutral' - starting after the 27 April 1999 high (the triggers for the dip were RBA rate hikes and GIO losses, plus the US market was also showing the first signs of wobbles at the top of the 'dot-com' boom). The dip hit -10% on 18 October, and hit bottom just 1 day later on 19 October (down -11.6% from the high) then rebounded. Again, even 'though 'buying the -10% dip' almost picked the bottom perfectly, it again did not turn out to be a bargain because subsequent returns ran into the 'tech-wreck' – which was unrelated to the original 1999 dip.

- Dip 28– ''Bargain' - starting after the 22 March 2000 high (this dip was in response to the Nasdaq sell-off, which turned out to be the start of the long and deep US tech-wreck crash.) The dip on the ASX hit -10% on 17 April, which turned out to be the bottom of the dip on the local market (but not in the US). In this case, buying the dip picked the bottom of the local ASX dip exactly, and it turned into a real Bargain because Australia had a very mild 'tech-wreck compared to the US experience. Australia's 'dot-com' boom was much milder, and so our 'tech-wreck' was also much milder.

Aside from these four occasions when buying the local ASX -10% dip picked the bottom almost perfectly, in every other case, the market kept falling beyond the -10% dip. Some were only short periods of further losses, but most were longer:

- the median additional period of further falls after the dip was 85 days (bottom of column D), which is much better the US market, where the median was 252 days of further falls after the -10% dip.
- the average additional period of further falls after the dip was 220 days (bottom of column D). This was also much better the US market, where the average was 414 days of further falls after the initial -10% dip.

Although our experience has been better than in the US, these are still long periods of additional falls/pain after thinking you were getting a bargain by buying the 10% dip. If you buy a -10% dip, in most cases you ended up with several months more of further falls.

10% dips usually turn into much deeper sell-offs

Column E shows the total sell-off from each peak. In almost all cases, the eventual sell-off was a lot worse than the initial -10% dip.

- 42% of the -10% dips (15 out of 36) turned into sell-offs of -20% or more (65% in the US).
- 25% of the -10% dips (9 of 36) turned into sell-offs of -30% or more (42% in the US).

The bottom line is that stock markets (here and in the US) are not 'random' as finance textbooks and Nobel prize-winning theories proclaim. Markets trend, sometimes trending down for several years at a time.

In most cases, a -10% fall turned out to be the start of a much larger fall (a further -14% fall on average – column E), and for a much longer period (more than a few months of further falls on average – column D).

Where are we now?

On 13 March, the All Ords hit a -9.7% dip below the all-time reached on 14 February. Not quite -10% yet but close. As usual, the dominant factor driving our market is what is happening in the US of A. Our local market is over-priced on a variety of measures, but not as nearly as over-priced as the US market, driven by the 'Magnificent Seven'. (See links to recent stories about US market pricing below.)

It is very similar in a lot of ways to the late-1990s 'dot-com' boom that ended with the 2000-2 'tech-wreck'. On that occasion, the US had a much bigger boom than Australia, so it had a much deeper and longer bust. The dips on our market leading into the tech-wreck (dips number 26 to 30) turned out to be either 'Neutral' or 'Bargains' (but they were 'Knives' in the US market because the tech-wreck was much deeper and longer there).

Last time, what pricked the bubble and triggered the crash was a combination of inflation, rate hikes, stories of revenue-less dot-com stocks running out of cash, plus some major bankruptcies like Enron, WorldCom, and PG&E, and the 9/11 attacks. This time we have sticky inflation, plus the never-ending and ever-widening Trump chaos.

When (not if) the current US tech boom collapses, and even if the US suffers a long and deep economic recession and stock market crash (like last time), the local Australian market will also fall along with it, but probably not as heavily the US. The 'dips' in our market will probably turn out far less damaging than the US dips, like last time.

I have the hummus ready – bring on the dip!

Note on data sources: *From 1980 – ASX All Ords accumulation index; 1958-1979 - Sydney All Ordinaries; 1936-1957 - Sydney 34 Ordinaries; Before 1936 - Sydney Commercial & Industrial Index and Ashley Owen's bottom-up index. The original version of this article can be found here.*

Ashley Owen, CFA is Founder and Principal of OwenAnalytics. Ashley is a well-known Australian market commentator with over 40 years' experience. This article is for general information purposes only and does not consider the circumstances of any individual. You can subscribe to OwenAnalytics Newsletter here.

Shaky markets, steady mind

Leigh Gant

Markets are down, and everywhere you look, there's talk of panic. Some investors expect a quick rebound. Others picture worse declines. Neither camp is guaranteed to be right, but both are at risk of letting emotion override logic.

The best tool we have during times like these isn't a crystal ball - it's a clear head.

Emotions under pressure

In any market slump, fear spreads like wildfire. Even long-term investors can get antsy when their portfolios turn red. Meanwhile, confident voices emerge, claiming they timed the top, or they're about to catch the absolute bottom. Anxiety and envy swirl together, pushing people toward rash decisions. Price dips by 5%. Then, another 5%. At each step, folks wonder: *Should I just sell everything?*

All it takes is one ill-timed decision—rushed by panic or lured by ego—to lock in losses that could've been avoided. That's the hidden cost of emotional investing.

Instead of building wealth, you end up building regret.

Learning to detach with a Navy SEAL

Jocko Willink is a former Navy SEAL commander, decorated for his leadership in the Battle of Ramadi. He's now known for his bestselling book Extreme Ownership, where he champions the principle of "detachment"—stepping back before reacting so you can see the bigger picture and make better decisions. He illustrates this concept with a vivid moment from close-quarter battle training:

Each SEAL was focused on a specific field of fire, weapons trained and ready for orders. Although Jocko wasn't the designated leader at that time, he sensed the tension mounting. Every moment increases the tension, and panic would result in dire consequences. A young Willink lifted his rifle to high port, physically withdrawing from the immediate fray. That brief pause allowed him to scan the environment, catch a clearer view of threats, and make a decisive call. By detaching for just an instant, he dodged what could have been a costly error—and did it by simply taking a breath in the midst of chaos.

Investing doesn't have the life-or-death stakes of warfare, and it's no place for the bravado of comparing ourselves to special operators. Still, the underlying lesson stands. When markets tumble or headlines grow dire, emotions run high. Detachment means pausing before reacting to every price swing. Ask: "Is this business fundamentally broken, or am I just seeing fear play out?" Often, you'll find the situation is less dire than your adrenaline suggests.

A "pause rule" can reinforce this discipline. A small window, like Willink's "step back", creates space for rational thought.

Markets have seen it all

Global share markets can feel chaotic right now, yet this is hardly the first time investors have encountered unsettling headlines or tumbling share prices. Over past decades, crises of every sort—currency meltdowns, technology bubbles, wars, and pandemics—have tested the resolve of even the most composed investors. Long-term returns, however, have been remarkably resilient for those willing to look years down the road rather than days.

The Australian share market, for instance, transformed a notional $10,000 into over $130,000 across the past three decades. That growth happened alongside repeated corrections, a global financial crisis, and several episodes of geopolitical turmoil. There were no guarantees along the way. Yet the pattern of recovery emerged time and again, underscoring how human ingenuity and corporate enterprise often drive markets to surpass previous highs.

Opportunities in the chaos

Short-term pain is never pleasant. Portfolios lose value and emotions escalate. This environment, however, can create openings for patient investors who distinguish between genuine problems and fleeting panics. It's true - some companies inevitably falter. Many others remain fundamentally strong, yet their share prices drop alongside the broader market. Those willing to sift through the rubble can find promising businesses at valuations that suddenly seem more attractive.

This approach does not rely on heroics or a perfect forecast of the bottom. Rather, it hinges on the belief that enterprises tackling real-world problems and fulfilling customer needs will generate returns over time. Market downturns simply accelerate the process of separating hype-fuelled shares from more grounded opportunities.

Thinking beyond the headlines

Confidence does not require dismissing valid concerns. It means recognising that markets have repeatedly overcome significant challenges. Innovative companies continue to solve problems, make profits, and compound. While the short term may spark worry, this is often when disciplined buyers who hold a multi-year horizon can lay the groundwork for future gains.

Valuations may take time to reflect a business's true worth, but they tend to do so eventually. That is why steady compounding, buoyed by rational decision-making, forms the cornerstone of success for many experienced investors. Instead of being caught off guard by sudden declines, they adapt, evaluate new opportunities, and continue moving forward.

When the dust settles

Every sell-off feels unique, yet time and again, markets have shown resilience. Fear subsides, optimism returns, then innovative and quality businesses resume their climb.

No one is suggesting that decline is pleasant or that future events are guaranteed to mirror the past. The difference lies in staying rational, following through on solid due diligence, and keeping an eye on how profitable enterprises eventually regain their stride. That is the essence of prudent investing: not trying to dodge every dip, but retaining the conviction and clarity to make measured decisions when skies darken.

Stepping back for the long haul

A falling market can feel like a crisis or an opportunity, depending on your perspective. Detached investors often treat it as both. A crisis if you ignore valuations and trade on emotion. An opportunity if you've protected your downside and patiently wait to buy quality assets at attractive prices.

This approach doesn't guarantee you'll never see red ink in your portfolio. But it does increase your odds of thriving over the long run.

Rationality doesn't win headlines, but it wins in the end. Markets will always fluctuate, headlines will always sensationalise, and fear will always rear its head. Your job is to stay calm, stay humble, and stay in the game.

Do that, and you give yourself the best chance of turning turbulence into long-term gains.

Leigh Gant is the Founder and CEO at Unio Growth Partners. This article is for general information purposes only as it does not consider the individual circumstances of any person. Investors should seek professional investment advice before acting.

Is it time to pull the plug on EVs?

Roger Montgomery

Electric vehicles (EVs) have been hailed as the future of transportation – promising a cleaner and greener alternative to traditional internal combustion engine (ICE) vehicles. Governments worldwide have pushed EV adoption through subsidies, tax credits, and ambitious targets, while car manufacturers have invested billions to electrify their fleets. However, announcements from major automakers, as well as recent data and surveys in the U.S., Australia, and Europe, suggest EVs may not be the wisest purchase for consumers today.

From production pullbacks and the downstream impacts of consumer hesitancy and infrastructure woes, here's why the EV revolution is hitting a speed bump.

Major carmakers are hitting the breaks on EV ambitions

One of the most telling signs that EVs may not be the golden ticket they were once thought to be comes from the very companies building them. Large car manufacturers are rethinking their all-in approach to EV production, citing weaker-than-expected demand and staggering financial losses.

In the U.S., Ford and General Motors (GM) have made headlines with their retreats from aggressive EV plans. Ford, which has been transparent about its EV financials, reported losing US$18 billion on EV production over three years, equating to a jaw-dropping US$50,000 loss per EV sold. In response, Ford announced in 2024 that it's scaling back EV production and shifting focus to hybrids, delaying plans for an all-electric SUV (sport utility vehicle). GM followed suit, cutting its 2024 EV production targets by an estimated 50,000 units, acknowledging that consumers aren't transitioning to fully electric models as quickly as anticipated.

While Tesla is still an EV market leader, it has faced its own challenges, with price cuts and slower sales growth signalling a cooling market. In Australia, Tesla's sales slide continued in February, with the brand recording a significant reduction in sales compared to the previous year. The nation's best-selling electric vehicle brand recorded 1,592 sales in February, more than double the disastrous 739 deliveries notched in January. However, that was down 70% from the 5,665 sales of February 2024.

The picture in Europe is similar. Volkswagen, a key player in the European market, has tempered its EV targets. According to the European Automobile Manufacturers' Association (ACEA), Volkswagen recorded a 27% year-to-date drop in battery-electric vehicle (BEV) sales in Germany.

Volvo, which once pledged to go fully electric by 2030, has adjusted its timeline, admitting that market infrastructure and consumer acceptance aren't quite there yet. European manufacturers are increasingly pivoting to hybrids as a bridge technology, reflecting a pragmatic response to sluggish EV uptake.

Meanwhile, back in Australia, EV adoption remains in its infancy, with the pure electric market share declining precipitously. The latest data from the Federal Chamber of Automotive Industries (FCAI) and the Electric Vehicle Council (EVC) reveals a total of 5,684 full battery-electric vehicle were sold in Australia in February, compared to 10,111 in the same month last year.

A total of 96,710 new vehicles were sold in Australia during February, including cheap Chinese EVs, meaning EVs make up just 5.8% of sales. A year ago, EVs made up 9.6% of the market even when cheaper Chinese models were unavailable in significant quantities.

Major manufacturers like Toyota, dominant in the Australian market, have doubled down on hybrids rather than pushing EVs aggressively, citing the country's vast distances and limited charging infrastructure. Even Tesla's Model 3, which led EV sales in 2019, faces competition from more affordable internal combustion engine and hybrid options, dampening enthusiasm for a full electric switch.

Consumer sentiment: cost and convenience concerns

Surveys across all regions reveal a growing scepticism among consumers. This is driven by high costs, range anxiety, and inadequate infrastructure. In the US, a 2023 Pew Research Centre survey found that only 38% of Americans were likely to consider an EV for their next purchase, down from 42% in 2022. The same survey in 2024 revealed just 29% of Americans say they would consider an EV for their next purchase. And globally, 29% of current EV owners told McKinsey in 2024 that they plan to switch back to gasoline or diesel vehicles, with that figure rising to 38% in the US – highlighting dissatisfaction with the ownership experience.

Key concerns include the high upfront cost (EVs remain 10-50% more expensive than internal combustion engine equivalents) and concern about charging availability.

In Europe, despite a 62% surge in EV sales from mid-2022 to mid-2023 (Bloomberg), mass adoption is stalling. The Ernst & Young (EY) report notes that while subsidies have boosted sales, the average EV still costs over 25% more than an internal combustion engine vehicle, and consumers are often unaware of the long-term ownership costs. A 2024 S&P Global forecast slashed its 2025 EU battery-electric vehicle market share prediction from 27% to 21%, reflecting economic pressures and a lack of affordable models. Posts on X (Twitter) echo this sentiment, with users pointing to the steep losses manufacturers and owners face as evidence that EVs aren't yet viable for the masses.

In Australia, range anxiety is a major hurdle, especially outside urban centres. With EVs like the Tesla Model 3 commanding a premium price – around A$60,000 compared to A$40,000 for a comparable hybrid – the cost-benefit equation doesn't add up for many.

Infrastructure and market realities

The EV charging infrastructure – or lack thereof – remains a critical bottleneck. In the U.S., despite US$5 billion allocated in 2022 to build EV charging stations, only 17% of Americans in the Pew Research Centre survey were confident this would materialise effectively. In Europe, the ACEA warns that the EU's charging network isn't keeping pace with demand, with gaps in rural areas undermining EV practicality. Australia fares worse, with just 3,000 public chargers nationwide as of 2023, compared to over 12,000 in Norway, a country with a similar population.

The hybrid hedge and the bigger picture

Meanwhile, as we have reported previously, hybrids are emerging as a compromise, offering fuel efficiency without the full commitment to electric. Toyota's success with the Prius and Ford's pivot to hybrid F-150s suggest that consumers will accept greener options without the risks and inconveniences of EVs. Meanwhile, manufacturers face regulatory pressure – like the EU's 2035 zero-emission target or California's 2035 internal combustion engine ban – but recent data shows these goals may be out of sync with market realities. The International Energy Agency's (IEA) 2024 Global EV Outlook predicts EVs could hit 45% of global sales by 2030, yet this falls short of net-zero targets, and regional disparities mean progress is uneven.

Why EVs might not be the smartest buy today

For the average consumer in the U.S., Australia, or Europe, EVs come with too many caveats in 2025. They're expensive, lose resale value quickly, and depend on an insufficient and unreliable charging grid. Manufacturers are losing billions, signalling an unsustainable model without massive subsidies – subsidies that are shrinking, as seen with the U.S.'s tightened Inflation Reduction Act (IRA) credits and Europe's shifting policies. Hybrids, by contrast, offer a practical middle ground, while internal combustion engine vehicles remain cheaper and more versatile for now.

The EV dream isn't dead, but it's clear the hype has outpaced reality. Until prices drop, infrastructure catches up, and manufacturers stop bleeding cash, putting your money into an EV might be more of a gamble than a smart investment. And by then, alternative technologies may supersede lithium battery-electric vehicles. For now, the road ahead looks bumpier than the glossy electric vehicle advertisements suggest.

Roger Montgomery is the Chairman of Montgomery Investment Management and an author at www.RogerMontgomery.com. This article is for general information only and does not consider the circumstances of any individual.

The future of travel

Lucina Martin

Planning and booking travel have long been a frustrating and time-consuming process. Travellers must sift through countless flight and hotel options, read reviews, juggle different booking platforms and coordinate schedules – all while trying to secure the best deals.

However, the future of travel is about to be transformed by a new technological force – AI-powered travel agents. Unlike traditional AI, which waits passively for instructions from users, AI agents will independently navigate websites, make decisions, solve problems and adjust your travel itinerary on your behalf – just like a personal assistant, but fully automated. This isn't a distant dream; it's a reality we expect travellers to experience within the next decade.

This innovation is being driven by breakthroughs in hardware and software. Advanced computing chips, which power AI training models, and sophisticated AI algorithms such as OpenAI's ChatGPT, Google's Gemini and Meta's Llama, are key enablers of this revolution. The most recent advancement occurred in January when OpenAI launched its next iteration of ChatGPT, Operator, an AI agent capable of independently navigating websites. Its applications extend far beyond travel, handling tasks like online shopping, filing expense reports and making restaurant reservations. By mimicking human interactions, Operator marks a major shift towards truly proactive, self-sufficient AI.

These technological advancements have sparked a wave of investment and innovation across the travel industry, creating both exciting opportunities and new risks for investors. Established travel companies, agile startups and tech giants are all racing to build AI agents that could disrupt traditional travel search engines and capture significant market share.

Tailored trips: Let your AI agent handle the details

One of the most powerful shifts brought by AI agents is personalisation. Instead of users manually searching for flights and accommodation, AI agents will predict your preferences, suggest destinations and secure bookings without requiring constant input. Imagine telling an AI agent you'd like to plan a European getaway in July. Instead of browsing for hours, your AI agent will instantly:

- Find flights that match your schedule, budget and preferred airline.
- Book hotels suited to your style, whether charming boutique stays in quiet villages or centrally located hotels just steps from cultural landmarks.
- Recommend activities based on your interests, from vineyard tours in Tuscany to guided cultural walks through historic city centres.
- Adjust plans in real time if flights change or better options arise.

This reduces search time, eliminates decision fatigue and unlocks destinations travellers may never have considered.

AI now smarter, cheaper, everywhere

For companies looking to capitalise on the AI agent opportunity, the first step is securing access to leading AI algorithms from OpenAI, Google and Meta. As the cost of computing continues to decline, access will become more affordable. A prime example of this shift is DeepSeek, a Chinese AI company that has demonstrated that building and training AI models can be cheaper and more efficient. This is a great outcome for AI infrastructure users such as established travel companies, allowing them to develop proprietary models while minimising their investment requirements. As AI tools become increasingly ubiquitous, the barriers to entry for companies looking to integrate AI will continue to shrink, enabling broader innovation.

Data is the new travel currency

As advanced AI infrastructure becomes widely accessible, the important question for investors is 'Who will come out on top?' The power of AI lies in the underlying data. Companies with access to the richest datasets can generate superior customer insights and will dominate. For example, a company with a large user base and strong customer relationships understands a customer's travel preferences, spending habits, location history and real-time market trends - a valuable asset. For this reason, smaller competitors will likely suffer. Additionally, traditional players including shopfront travel agents, group tour companies and companies like TripAdvisor risk ceding share as AI agents eliminate the need for manual searches, directly connecting travellers with bookings and personalised recommendations.

Existing giants like Booking Holdings, the parent company of Booking.com, have massive user bases and loyalty programs, giving them access to vast customer data. Booking Holdings is already incorporating insights into its early-stage AI agent to enhance the customer experience and streamline the travel booking process. In an AI-powered world, travellers are encouraged to go directly to the Booking platform, strengthening its control over the customer relationship. In this scenario, Booking's business quality and profitability are likely to strengthen, supported by a stronger market position and reduced reliance on expensive search-engine traffic.

Hospitality experts the big winners in an AI-driven world

In addition to AI infrastructure and customer data, deep expertise in travel and hospitality is essential for building effective AI agents. In this environment, the biggest winners will be companies that maintain direct relationships with accommodation owners, giving them greater control over service standards, property presentation and pricing. This close partnership is exemplified by franchised hotel chains like Hilton and Marriott, which work directly with their vast network of hotel owners. Hilton and Marriott don't just connect hotel owners with travellers; they are deeply integrated partners, offering decades of hospitality expertise that is incredibly difficult for tech giants to replicate. They provide hands-on support for hotel operations, labour management and supply procurement, even guiding owners through the hotel development process. To secure this valuable expertise, hotel owners sign long-term contracts –

often up to 20 years – with these franchised giants, ensuring they maintain a vast network of properties for travellers to choose from in this era of technological change.

AI agents are here, and travel will never be the same

The future of travel is being rewritten, with AI agents at the heart of this transformation. As the industry evolves, a fierce data race will unfold, with new sources being used to infer traveller preferences. Companies that can capture, refine and apply the richest travel insights will gain the upper hand.

Tech giants are interesting in this context, as they already hold key insights into consumer behaviour: Google can scan your Gmail history for past travel bookings and requests, Apple has access to conversation data where you may be planning a trip with friends and family, and Meta, through Instagram, can analyse your travel-related posts and tagged destinations to predict future behaviours. While large tech companies may have information on the customer, they lack the operational knowledge, long-standing relationships and industry-specific insights that predicate success in the hospitality sector. Therefore, big tech's most viable monetisation path is through strategic partnerships with established travel players like Booking Holdings, Marriott and Hilton.

For investors, this period of rapid change offers exciting opportunities and new risks to consider. Those investors who back the right companies will be at the forefront of the next evolution of travel, where seamless, hyper-personalised experiences redefine the industry. Market leaders will strengthen their dominance, while those slow to adapt risk being left behind in an AI-first world. The winners of this transformation will not just survive the disruption; they will shape the future of travel itself.

Lucina Martin is an Investment Analyst at Magellan Asset Management, a sponsor of Firstlinks. This article has been prepared for general information purposes only and must not be construed as investment advice or as an investment recommendation. This material does not consider your investment objectives, financial situation or particular needs.

For more articles and papers from Magellan, please click here.

Navigating SMSF property compliance

Shelley Banton

Property investment within SMSFs remains a popular strategy for building retirement wealth. Navigating SMSF property compliance, however, requires a holistic approach to ensure that SMSFs operate within the legal framework administered by the ATO and ASIC.

One of the problems is that SMSF trustees investing in property do not appreciate how the superannuation rules interact. Areas that can cause the most concern are the sole purpose test, the non-arm's length income (NALI) provisions and property development.

The sole purpose test

The sole purpose test lies at the heart of a complying SMSF. It mandates that an SMSF must be maintained solely to provide retirement benefits to its members or their dependents in the event of a member's death.

Until then, SMSF assets must not be misused for personal or business purposes unrelated to retirement benefits.

Breaches of the sole purpose test can have severe repercussions because an SMSF can risk losing its complying status and be subject to higher tax rates.

Non-compliance may arise from various scenarios, such as:

1. occupying residential property by a related party for personal purposes
2. undertaking property development activities where transactions are not at arm's length
3. not leasing business real property at market rates if used by related parties

Where the trustees of an SMSF are involved in property development ventures in various capacities, they must demonstrate that their decision-making is solely pursuing the retirement purpose of the SMSF and is not influenced by other goals or objectives concerning those business or other entities.

Non-arm's length income (NALI)

NALI is another critical area of property compliance for SMSFs. The NALI provisions target income derived from arrangements not conducted on commercial terms. The provisions act as a powerful deterrent against arrangements that could unfairly increase member entitlements.

Where income is classified as NALI, it is taxed at the highest marginal rate instead of the concessional superannuation tax rate of 15%.

Identifying NALI involves examining transactions to ensure they are conducted on arm's length terms. For example, if an SMSF acquires an asset for less than its market value or receives income under non-commercial terms, such arrangements may be deemed non-arm's length triggering the NALI provisions.

ATO flags property development issues

NALI provisions are particularly relevant in the context of property development projects. The ATO has flagged concerns about property development arrangements where income gets diverted to SMSFs through non-arm's length dealings.

For instance, SMSFs may hold direct or indirect interests in entities that invest in property development projects that engage in non-arm's length transactions, such as entering into loans with related parties at a 0% interest rate, to maximise profits.

No specific prohibitions prevent an SMSF from investing directly or indirectly in property development. It can be a legitimate investment for SMSFs if the fund's property development activities comply with the superannuation legislation.

The ATO, however, is concerned about the structure of certain schemes and arrangements that divert income into super, creating potential breaches of the sole purpose test, other SIS issues and NALI.

The ATO has provided guidance to SMSFs through its regulatory updates cautioning that care needs to be taken by SMSF trustees.

Joint ventures

The ATO has affirmed that a joint venture (JV) agreement involving related parties is an 'in-house asset'. As a result, the SMSF must hold a proprietary interest in any real property being developed so that the ATO is comfortable with the SMSF investment being 'in' that property and not an investment 'in' the related party.

One of the leading indicators that the investment may be an in-house asset is that the fund provides capital for the joint venture and has no other rights than receiving a return on the final investment. The ATO has flagged that this will depend on the terms of the JV.

Where outside influences affect the trustee's decision, such as ceasing to pay a pension to make a cash injection into a struggling property development venture, a contravention of the sole purpose test may occur.

The SMSF should not be involved in ensuring the success of a property development joint venture at its peril.

Ungeared entities

Investing in ungeared entities is another area where compliance with the requirements is complex. Ensuring the ungeared entity does not borrow, all transactions are at arm's length, any related party acquisitions are at market value, and the entity does not operate a business can avoid the investment becoming an in-house asset. Once an in-house asset, the investment can never be returned to its former exempt status, even if the trustee fixes the issue/s that caused the assets to cease meeting the relevant conditions.

It can be difficult, therefore, for SMSFs to meet and maintain these conditions while undertaking property development investments.

Special purpose vehicle

The ATO has now set a higher bar for property development schemes by focusing on a 'controlling mind'. It makes the decisions for one or more property development groups by selecting the project and establishing an SPV who are typically the members of the fund.

The ATO has adopted a broader approach and is less prescriptive about specific arrangements and structures that could potentially fail SISA compliance with property development.

The ATO has acknowledged that non-arm's length dealings by any party, with respect to any step in relation to a scheme, can give rise to NALI as defined in the Tax Act.

It gives the ATO a much wider net to cast, which ensures that trustees cannot circumvent the rules and can try to get more money into an SMSF.

Conclusion

Understanding the connections between NALI and the sole purpose test is crucial for an SMSF's successful and compliant operation.

SMSF trustees must ensure that their funds are maintained exclusively for retirement purposes and that all transactions are conducted on arm's length terms. Non-compliance with these requirements can lead to severe consequences, including significant tax penalties and potential disqualification.

Shelley Banton is Head of Education at ASF Audits. Read more articles in this SMSF property development series.

History tells us that markets are at a high-risk juncture

Greg Canavan

"For historians each event is unique. Economics, however, maintains that forces in society and nature behave in repetitive ways."

- Charles Kindleberger, Manias, Panics, and Crashes

It's been around 20 years since I last read Kindleberger's classic book. But with the 25th anniversary of the dot.com bubble last month (March 10), I thought I'd dust it off. We are, after all, in another bubbly environment. And while every bubble is unique in its form and duration, as Kindelberger notes, each has common characteristics.

To be honest, the book was a tougher read than I remember. I ended up skimming a lot of it. It was packed with every crisis, panic and mini-panic you could imagine, including the obscure Kipper und Wipperzeit episode.

This occurred just prior to the Thirty Years War, which broke out in 1618. It wasn't a unique crisis. It was a story of currency debasement, a story as old as money itself.

This is what makes the book a powerful read. Each crisis is different, but at its core is the same range of human emotions. What you're seeing today is just the latest episode of humanity mixed with a torrent of money.

While there is a huge amount of information crammed into Manias, Panics, and Crashes, the gold is in chapter two. It provides a framework for the rest of the book. Titled 'Anatomy of a Typical Crisis', it starts with the crisis model of the late Hyman Minsky. Kindleberger writes (with my emphasis):

"Although Minsky was a monetary theorist rather than an economic historian, his model lends itself effectively to the interpretation of economic and financial history 'According to Minsky, events leading up to a crisis start with a 'displacement', some exogenous, outside shock to the macroeconomic system. The nature of this

displacement varies from one speculative boom to another. It may be the outbreak or end of a war, a bumper harvest or crop failure, the widespread adoption of an invention with pervasive effects – canals, railroads, the automobile – some political event or surprising financial success, or a debt conversion that precipitously lowers interest rates.

But whatever the source of displacement, if it is sufficiently large and pervasive, it will alter the economic outlook by changing profit opportunities in at least one important sector of the economy.

If the new opportunities dominate those that lose, investment and production pick up. A boom is underway. 'In Minsky's model, the boom is fed by an expansion of bank credit that enlarges the total money supply."

Kindleberger's book was originally published in 1978. At that time, the world of 'tech' didn't really exist as we know it. Personal computers were only just being invented.

But in this era, the 'widespread adoption of an invention with pervasive effects' is all about technology. The internet was an example of a displacement. And we know how that turned out.

According to Kindleberger, "Each day's events produce some changes in outlook, but few are significant enough to quality as displacements."

Displacement and euphoria

Artificial intelligence (AI) clearly qualifies as a modern-day displacement. You can see this in the charts below.

On 30 November 2022, ChatGPT came into the world. It was the first publicly available (and free) AI tool. It was the start of a mania. For evidence, look no further than Nvidia's share price…

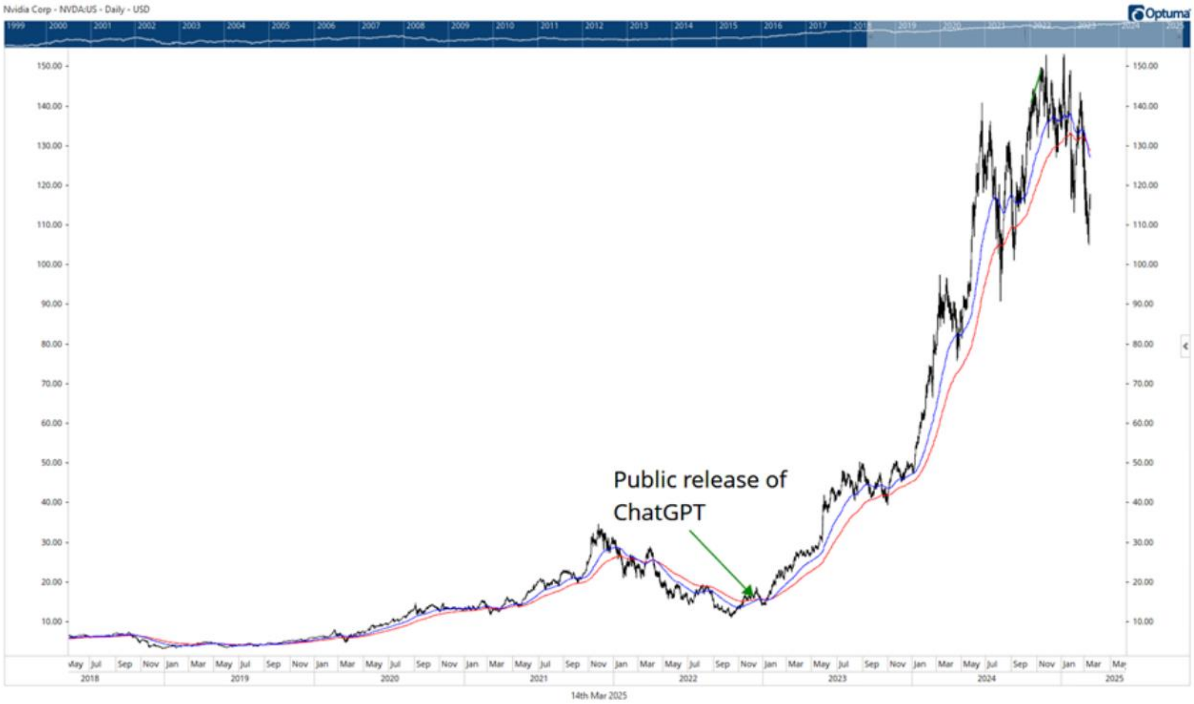


Figure 1: Nvidia share price chart. Source: Optuma

From the release date of ChatGPT to the recent peak, Nvidia's share price soared by around 830%. In the previous year, Nvidia's stock price had declined around 70% from the peak of the post-Covid monetary boom in late 2021.

ChatGPT, and AI in general, was the 'displacement' that stopped the bear market in its tracks. It allowed investor imagination to run wild.

Investment in chip technology and production ramped up…a boom got underway.

However, this boom didn't follow the classic Minsky model. It wasn't fuelled by an 'expansion of bank credit'.

Not exactly, anyway.

As I'll show you later in this article, the US Federal Reserve and Government, rather than private banks, provided ample liquidity to fuel the bubble.

Flush with cash from this liquidity surge and enjoying years of network effect dominance, the major tech companies went on an AI spending spree. Retained earnings and internal cashflows, rather than bank credit, fuelled this investment boom.

This is what makes this bubble unique. The huge investment in AI infrastructure didn't come with destabilising bank debt. Therefore, the argument went, it wasn't really a bubble. Moreover, the earnings were real. Therefore…again…not a bubble.

But one of the characteristics of bubbles and manias is the ability of investors to rationalise them at the time. As Kindleberger says, "forces in society and nature behave in repetitive ways". Somehow, this time is always different.

Historically, bubbles always have different characteristics. But at their core, they're all the same.

When it's a 'widespread adoption of a new innovation', like AI, the bubble represents a belief in something so new and profound that its possibilities and applications are endless.

In other words, the bubble is in investors' imaginations. Because the innovation is unique and groundbreaking, its imagined benefits are unlimited.

It's not just about Nvidia. You see it in the other 'Magnificent 7' stocks that are closely connected to AI too. Take a look at Meta…up around 560% at the peak from November 2022…

Figure 2: Meta share price. Source: Optuma

Or Microsoft, up 90% at the peak…

Figure 3: Microsoft share price. Source: Optuma

Or Alphabet aka Google…up 110%:

Figure 4: Alphabet share price. Source: Optuma

Or Amazon…up 160%:

Figure 5: Amazon share price. Source: Optuma

These are very large companies up significantly in just two years.

But, the argument goes, this isn't a bubble because the earnings are there to support these higher prices.

But maybe the bubble is in the earnings? Maybe the displacement caused by the emergence of AI led to a one-off investment boom that has momentarily inflated a select group of companies' earnings?

From 2022 to 2026 (forecast) Nvidia's earnings per share are expected to increase more than 1000%. Meta's by around 240%... Microsoft's by more than 50%... Alphabet's by 125%... And Amazon's by around 550%.

Maybe these earnings are sustainable. But Kindleberger's study of history and Minsky's model suggest we need to be critical of such a view.

In Minsky's model, euphoria follows displacement. While you haven't seen euphoria in the broader market, you can certainly see it in the share price charts above.

You've also seen it in 'quality' stocks. This is the 'sneaky bubble' that joined the bubble in tech and AI. Costco Wholesale is just one example. This US$400 billion company trades on 50x earnings! Several Aussie stocks also benefited from this 'quality' premium.

Figure 6: Costco share price. Source: Optuma

Distress

But let's get back to Kindleberger. After euphoria comes distress. Distress is brought about by changing expectations. Arguably, this is where we are now. Kindleberger writes (with my emphasis):

"Expectations in the real world may change slowly or rapidly, and different groups may wake up to the realization – sometimes at different rates and sometimes all at once – that the future will be different from the past. The period of distress may be drawn out over weeks, months, even years, or it may be concentrated into a few days. But a change in expectations from a state of confidence to one lacking confidence in the future is central."

I think it's fair to say that the first quarter of 2025 can best be summarised by the term 'changing expectations.'

There are two key events behind these changing expectations. The first is DeepSeek. This is the Chinese AI start-up that rivals ChatGPT and other Western LLM's (large language models). It's open-source and supposedly much cheaper run. Its release in January 2025 sent shockwaves through the industry.

Nvidia's share price plunged 17% on the news. DeepSeek was the catalyst for changing expectations towards AI-related companies.

The election of Donald Trump is the other event behind 'changing expectations'. This is more than just AI or tech-related.

The market initially welcomed Trump's election. But it's become clear he's not bluffing with tariffs. His attempts to engineer a renaissance of the US manufacturing sector and restore jobs to the working and middle classes are spooking markets.

This is not the environment where one of the most expensive stock markets in history will thrive. The market, both here and in the US, has gone from a state of confidence at the start of the year to one of uncertainty now. As Kindleberger says, 'a change in expectations from a state of confidence to one lacking confidence in the future is central.'

In his, or Minsky's model, this change of expectations brings about a period of distress. Here again, Kindleberger's study of history is instructive:

"Financial distress for an economy also has a prospective rather than an actual significance and implies financial adjustments or disturbances ahead. It is a lull before a possible storm, rather than the havoc in its wake."

He continues (with my emphasis)…

"Causes of distress are difficult to disentangle from symptoms, but they include demands on the capital market for cash when cash is tight, sharply rising interest rates in some segment or all of the capital market, balance of payments deficits, rising bankruptcies, the end of price increases in commodities, securities, land buildings, or whatever else may have been the object of speculation.

The end of a period of rising prices leads to distress if investors or speculators have become used to rising prices and the paper profits implicit in them. Of course, it is difficult—many would say impossible—to distinguish in advance a pause in a continued upward movement from a topping out that presages a downturn. Uncertainty on this score is itself a cause of distress."

Putting it all together

Okay…let's back up a bit and put all this together.

We've had the displacement of AI and the release of ChatGPT in November 2022. It reversed a bear market and resulted in an extended period of euphoria.

However, the euphoria wasn't widespread. It centred around tech and AI-related companies and industries, as well as 'quality' stocks. In a throwback to the 'Nifty Fifty stocks of the 1970s, these are high-quality earners that investors believed you could pay any price for.

But the emergence of a Chinese AI competitor and the real Trump agenda have changed investor expectations. We've now moved into the distress stage. As Kindleberger states, 'the period of distress may be drawn out over weeks, months, even years.' History isn't clear about how a period of 'distress' resolves itself.

Kindleberger writes:

"The essence of financial distress is loss of confidence. What comes next—a slow recovery of belief in the future as various aspects of the economy are corrected, a collapse of prices, panic, bank runs, or a rush to get out of illiquid assets and into money?

If there is no panic…financial distress may gradually subside."

And…

"When financial distress is followed by a crash or panic, there is no standard interval. It may be a matter of weeks or of years."

In other words, history is frustratingly vague about informing us as to what comes next.

Understanding this point is crucial. Otherwise, it's easy to let confirmation bias take over. If you're bearish, you're going to expect panic and a crash. If you're bullish, you'll hope things resolve themselves without too much damage.

But understand…no one knows how this will play out. What we do know is that history tells us that we're in a high-risk environment. We've had the displacement, the euphoria, and now, the distress.

Greg Canavan is the Editorial Director of Fat Tail Investment Research.