

Why is the Economic Cycle Important to Me?

When you're busy with your child's potty habits or the work you've yet to do, Economics may be far, far from your mind. Your concern is more the state of the house, not the state of the nation. But, if in the long run you wish to be a profitable investor, and live life with intention, then you better take a closer look at the **economic cycle**. I'll tell you why.

You see, it affects everything in our lives. Even if you don't invest per se, you would probably be concerned if mortgage interest rates (or rent) started rising, and your grocery and other bills seem much more than six months ago (a sign of strong inflation), as you are directly affected. At this point, you would feel a victim of the economic times.

But wait! You can take yourself out of the victim role, no matter what part of the cycle we are experiencing. If you are partial to investing, familiarity with the economic cycle and the lore of 'market sentiment' may even save your butt.

Market sentiment is the overall confidence of the investing crowd. It can often flow out to the mass media as well, reflecting the groundswell of excitement at a sudden growth area. Finance journalists are not as impartial as we would like them to be. The common mistake of Mum & Dad investors is to invest following this excitement phase, and therefore at the top of the boom. Thus any gains they make are usually wiped out when the bubble bursts and the reality of this sector and its problematic future comes to light. Investors start to bail out, causing the share price to plummet.

Knowledge of where Australia stands in the economic cycle is obviously going to aid your decisions on investing, and this bird's eye view will help you become a patient investor.

All three major asset classes: real estate, shares and fixed interest investments, have their boom time. Knowing which asset class is coming to the fore can make a huge difference to returns.

The Economic Clock (created circa 1925) is an easy diagram to understand how the market cycle works. This clock is composed of economic indicators such as interest rates, the Australian dollar, real estate and the share market, and it depicts the sequence of events in an economic cycle.

{Please see the Economic Clock graphic in *Sack Your Financial Planner*}

Looking at the clock, I estimate that we are about 3pm as commodities have just slumped. The property market is having a slowdown in most states. Each State capital, reflected by housing values and auction results, seems to be in different stages of the cycle. Perth for instance, had a boom in 2005/06, and is now levelling out.

Property Securities funds had huge gains in 2006 (35% average), but Listed Property Trusts (what these funds mainly invest in) are forecast for a lesser 9 per cent growth after three years of great returns. So where would a wise woman put her money?

The best advice I can offer is now is the time to take a long-term view, and review various tax-effective investments. It's a good time to gain more education about patient styles of investing, such as positive cash-flow property.

With consistency, the property cycle booms every seven to nine years. The last boom was in 2003. Property will most likely return to popularity as an investment quite soon (just as other classes of investing suffer), but I reason that you'll have to have bought your bargains by the end of 2008 to profit. This is because of the demand for rental properties in some areas that are benefiting from business expansion and others from lifestyle seekers. Property author Michael Yardney believes South-East Queensland and Melbourne will be in the first wave of housing growth. Those that sit on the sofa and moan about affordability will never gain a cent.

If you have an excess of profits, perhaps look into forestry managed investment schemes before the Government changes their mind and voids the 100% tax offset. There is a long investment term range of 17 to 25 years, but you do get income along the way. The tax perks of other non-forestry related managed investments (e.g. macadamias, olives) are already being phased out. Commission runs at 10% for these schemes, so research yourself with online brokers.

Warning: Research the viability of each investment long-term, and find out the risks and rewards. Assess in line with your attitude to risk and include as only a part of a well-managed portfolio.