

MONEY

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Prices reflect probabilities

Investments: Future events always reflected in how shares fluctuate

Markets adjust to the unexpected, which is true for your investments as it is for Leicester City romping to the league title, says Barry O'Neill, investment director for Carbon Financial Partners in Aberdeen

One of the most common questions I get asked starts like this: "What do you think will happen to investment markets if...?"

You can finish the question with things like "we vote to leave the EU" or "Trump wins the election" or "interest rates go up".

My answer is invariably the same - that potential outcomes are already priced in. The beauty of well-functioning investment markets is all the available information is processed by market participants and finds its way into security prices.

The market does a very efficient job of incorporating information into prices. An example is when a company reports its



Barry O'Neill



REMARKABLE FEAT: Leicester City's 5,000-1 Premier League triumph can be compared to betting on the stock market

quarterly results to the market. There is often a near-instant change in price as the market reassesses how the information changes the company's future earning capability.

In order to understand more deeply what is going on in the stock market, you could do worse than think of how

another market, betting on the English Premier League, operated last season. It will probably not have escaped you that Leicester City won the league in May - a remarkable feat, considering they started the campaign with bookmakers offering odds of 5,000-1 on them being champions.

One confident bookmaker scrawled "pigs might fly" on an optimistic punter's betting slip.

As the season progressed, however, bookmakers quickly revised their odds every time new price-sensitive information came to light.

That new information reflected not only Leicester's results but also those of their title challengers, which of course had a significant impact on the Foxes' chances.

By Christmas, the odds had fallen to 10-1 and by mid-March Leicester were

10/11 odds-on favourites. The previously referred to "confident" bookmaker was probably recalling his flippant remark with trepidation every time he bit into a bacon roll.

Security prices are forward-looking in the same way betting odds are an expression of the likelihood of a future event occurring. Throughout the season, bookmakers were pricing and re-pricing their expectations of Leicester lifting

the trophy in the same way a market does when it collectively arrives at a security's price.

Company results, competitors' performances and a seemingly infinite number of other factors combine to set expectations of future security returns.

So why wouldn't you want your investment approach to harness this collective knowledge by putting the power of the market to work for you?

INSURANCE

Policies facing further tax rise

UK households are facing further increases in the cost of their insurance after a tax rate affecting millions of policies increased at the weekend.

The standard rate of insurance premium tax (IPT), which applies to most general insurance policies bought in the UK, went up from 9.5% to 10% on Saturday.

The rise is expected to push up the cost of new home, motor, private medical, pet and other types of insurance.

It is the second in-

"The rise will help fund new flood defences"

crease to the tax rate in less than a year.

According to the Association of British Insurers, the impact of both recent increases to the tax will add more than £16 to the average comprehensive motor insurance policy, more than £12.50 to the average combined home building and contents policy, more than £12 to the average pet insurance policy.

The UK Government has said the latest IPT increase will help fund new flood defences and maintain existing ones.

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