

NEWSLETTER

January 2024



M & M FINANCIAL GROUP
WEALTH CREATION | INSURANCE | RETIREMENT

Introduction

Happy 2024! We hope that this year is all you want it to be – and we hope we can continue to add value to your financial planning over the coming 12 months. This month, we do a simple recap of what happened in the major markets in 2023, with some thinking from the RBA about what to expect in 2024. Enjoy!



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The Share Market in 2023

Let's commence 2024 by looking back at what happened in the share market in 2023. The Australian share market performed quite nicely in 2023. The total average market return was 13.0% (comprising price rises of 7.8% and average dividends of 5.2%).

Adjusted for inflation, the annual return was 8.5%. This is a good return – if this return was experienced each year, and dividends were reinvested, then an investment would double in value every 8-9 years.

Market analyst [First Links](#) provide some insightful analysis of the market's performance, especially in its historical context. Going all the way back to 1900, for each calendar year First Links report that the average annual inflation-adjusted market return for Australian shares is 7.9%. This means that 2023 was slightly better than average. Bear in mind, however, that this strong return is only *slightly* better than average – which underscores the benefits of investing in general. The long-term average return of 7.9% would also see an investment double in size every nine years or so, as long as dividends were reinvested.

An investment that doubles in value every nine years will quadruple every eighteen years. The value will rise by a factor of eight every 27 years and by a factor of 16 every 36 years. These numbers are inflation-adjusted – so the factor of 16 represents the actual increase in purchasing power made available by the average rate of return. If you average a return of 7.9%, then giving up \$1 of purchasing power today will buy you \$16 worth of purchasing power – in today's prices – in 36 years or so.

Were you to achieve this rate of investment return, the only thing that would reduce the amount you receive in your hand is tax. Because the tax payable varies according to (i) who the taxpayer is, and (ii) the type of return (capital gains tend to be taxed more lightly than dividends), it is not possible to state precisely what the after-tax rate of return would be long-term. However, it is obviously going to be the case that the less tax paid, the better the return.

For most people, this tax element makes superannuation a key part of their planning. Superannuation has the obvious benefit of being a long-term investment – 36 years is less than the average working life. Superannuation is also a relatively lightly-taxed form of investment. Dividend income is taxed at just 15%, and capital gains are taxed at either 10% or 0%, depending on when the gain is realised. If a super fund makes a long-term investment into something like an index fund, for example, and sells that investment only after it has entered 'pension phase,' then there could be decades of capital gains that are untaxed.

Interestingly, First Links also point out that 2023 was a 'middling' year in terms of market performance across the past five years. The 'worst' performed year in the past half-decade was 2022, when the inflation-adjusted return was **-10.1%**. The 'best' performed year was 2019, when the inflation-adjusted total return was **21.8%**. 2020 saw a slight rise of 2.7% while 2021 saw a larger rise of 13.8% after inflation. Returns were positive in four of the five years, which is also in line with the long-term experience where returns have been positive in 72% of years since 1900.

In the above paragraph, we put the words 'best' and 'worst' in quotation marks, however, to highlight that investors should usually think differently about returns across a period as short as one year. The market fell by more than 10% in 2022. This is the 'worst' return for the last five years. But the lower prices actually made 2022 a really 'good' year in which to have *purchased* an investment that tracks the average. Lower prices are better for buyers, and these periodic 'falls' in

yearly returns are actually a great opportunity for people who choose to invest regularly over time. This group includes, of course, people who regularly receive super contributions.

Annual returns are one thing. But markets fluctuate within a year, as well. In this sense, 2023 was no different to any other. Indeed, 2023 was a particularly volatile year. Here is a graph of the ASX 200 for the last five months of 2023 and the first month of 2024:



As you can see, the index fell to 6,772 at the end of October 2023. It rose again to end the year on 7,590 – a rise of 12% from point to point. The fall to the end of October was itself a fall of 8.4% in just a few months since late July.

This means that the best time to buy during 2023 was late October.

All this data lends itself to a recommendation for one of our favourite investing strategies – regularly investing over time, or **dollar cost averaging** (DCA) as it is sometimes known. You will probably have read about this on our website before, but as we commence this new year, following on from an ‘averagely good’ year, it is worth thinking about DCA some more. It turns out that being average is a good thing.

Dollar cost averaging (DCA) is an investment strategy that involves consistently investing a fixed amount of money at regular intervals, regardless of the ups and downs in the market. This approach is designed to reduce the impact of short-term market volatility and takes advantage of the long-term trend of the investment. This trend, as First Links’ data shows, is a positive one.

Here's how it works: Let's say you decide to invest \$100 every month in a particular index fund, such as an ASX 200-tracking fund. In some months, the price of that investment might be high, and your \$100 will buy fewer units. In other months, when the price is lower, your \$100 will buy more units. Over time, this strategy averages out the cost of your investment. You actually end up with a relatively lower purchase price, as you automatically buy more units when prices are low, skewing the average price downwards.

The key benefit of DCA is that it removes the need to time the market – that is, to predict before hand which years will be good (and, more importantly, which ones won't in terms of market returns). Instead of trying to predict the ‘best’ time to buy, you simply take advantage of the fact that it is ‘better’ to buy when prices are low. This smooths out the impact of market fluctuations and reduces the risk of making a poor investment decision based on short-term market movements.

DCA is particularly useful for younger people who may not have a large lump sum to invest upfront. By contributing a fixed amount regularly, you're able to enter the market incrementally, potentially benefiting from the long-term growth of your investments. It is also magnificently well-suited to superannuation, where the combination of regular investment and long investment horizons give you a great chance of substantial long-term gains.

The thing we like most about DCA is that it is a very low-stress way of investing. If you watch the nightly news and see that the market is falling, you can remind yourself that lower prices are good news because you will be doing some buying next month anyway. If prices have risen, well, the investments you have already made have now gone up in value, making you wealthier than you were yesterday. This makes almost all news from the share market 'good' news, leaving you nice and relaxed about your long-term goals.

All that said, as 2024 kicks off you might be interested to know our thoughts for the market for the year ahead. Well, simple mathematics tells us that if we predict the market average we will be quite close most of the time, especially over the longer term. Over the past 123 years the average return has been just below 8%, inflation-adjusted.

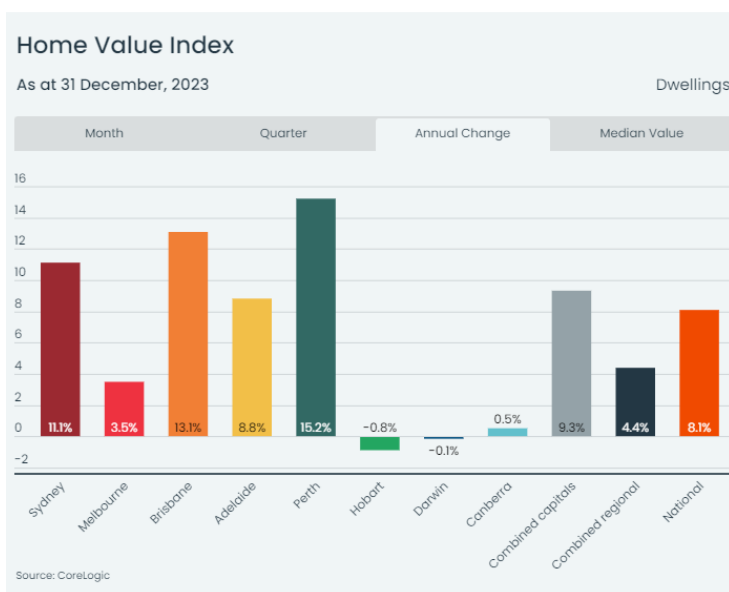
So, here's hoping for an average year!

The Residential Property Market in 2023

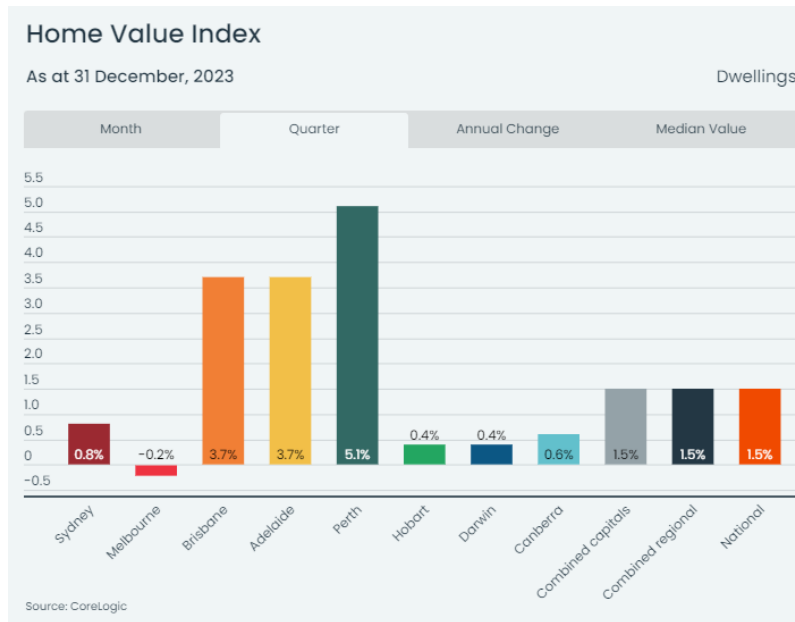
As 2023 has come to an end, once again we can draw on some market insights from [Corelogic](#) to look at what happened broadly to the value of residential property in 2023.

Nationally, there was an overall 8.1% increase in housing values. However, this national figure masked significant diversity across regions. For example, Perth experienced a 15.2% increase in property prices, whereas regional Victoria experienced -1.6% decline. The most prominent trend was the widening gap in home value growth rates among capital cities. Perth, Adelaide, and Brisbane consistently saw monthly growth rates above 1% since May, while Melbourne and Sydney experienced a slowdown, with Melbourne values declining in November and December. Sydney home values stabilized, showing only a 0.2% monthly growth rate in the last two months of the year. Smaller capital cities, such as Hobart and Darwin, recorded annual declines, while the ACT had a modest 0.5% increase in values for the year.

Here is how prices moved in all Australian markets for the 12 month period to the end of 2023:



2023 was really a tale of two half-years, however, especially in the larger Melbourne and Sydney markets. For the past three months of 2023, for example, prices were much less bullish, as a market correction started to take hold. Here is what happened with prices in Australian markets during spring and the first month of summer:



As you can see, Melbourne prices actually fell and Sydney prices probably rose slower than the inflation rate (the inflation data for the last three months is not in yet).

Undoubtedly, the big factor here was the substantial increases in interest rates over the last eighteen months or so. Interest rates rose at a rate faster than any time in recent history. So, a key question for the residential property market in 2024 is what is going to happen to interest rates. For that, we can look to the thoughts of the RBA itself – see our next article.

Inflation and Interest Rates in 2024

In November 2023, Acting Assistant Governor of the RBA, Marion Kohler, gave a speech in which she laid out the RBA's thinking about the Australian economy in 2024. As the RBA sets interest rates, we thought summarising her speech would be a good way to indicate what might happen with inflation and interest rates in 2024.

Kohler's speech discussed the trajectory of inflation, highlighting its recent decline and the factors contributing to this trend. During 2023, inflation decreased as the direct impacts of earlier supply shocks diminished. This decline is expected to continue due to below-trend economic growth, which will bring lower demand into 'synch' with increasing supply – remember, if supply equals demand, there is no pressure on prices to rise. That said, Kohler observed that this process is expected to be more gradual than the RBA initially thought, due to persistent domestic demand – a reflection of that fact that higher interest rates only suppress demand in one part of economy (home loan holders and new businesses), while potentially stoking demand in other parts (eg savers).



The fall in CPI during 2023 was driven mainly by lower goods price inflation, aided by improvements in global supply chains and a decrease in raw materials price inflation. This trend is expected to continue as supply chain cost reductions are passed on to final prices, and demand growth slows. Conversely, domestically sourced inflation, particularly services price inflation, has been slow to subside, with market services prices rising briskly.

Despite what was presented as a recent increase in wages growth and cost pressures such as energy, rent, and insurance, the RBA forecasts assume a gradual decline in wages growth over the next few years as labour market conditions ease. The speech emphasizes the importance of productivity growth returning to pre-pandemic levels for wages growth to align with the inflation target. One measure of productivity refers to the amount of goods or services that a single worker can produce in a given period of time. If that amount increases, the worker is becoming more productive. The RBA likes productivity of this type to occur before wages rise, as the increased productivity allows the employer to generate more revenue to 'cover' the increased wage cost.

The speech acknowledged that the 'last part' of bringing inflation back to the RBA's 2-3% annual target might take longer than the falls observed so far, as this has been the experience of other advanced economies. Potential CPI risks include any impact of further supply shocks, as exemplified by the recent increase in fuel prices. That said, this is always a risk. The RBA also maintains its concern about the possibility of high current inflation leading to expectations of sustained high inflation, as it worries that this can place upward pressure on actual prices and wages. Once again, though, the RBA always has this concern, even though wages and salaries have not risen by as much as the inflation rate over the last couple of years.

Since the speech in November, there has been new data available on prices rises for the month of November. The annualised CPI inflation rate to the end of November (that is, the change in prices between 1 December 2022 and 30 November 2023) was 4.3%. This was significantly lower than the figure for the 12 months to the end of October 2023. (We might also brag a little and remind readers that, back in mid-2023, we predicted inflation in the 4-5% range by the end of 2023).

The upshot of all this is that inflation is continuing to fall. This should prevent the need for any further interest rate rises in the coming months. As long as nothing unexpected happens!

The Legal Stuff

General Advice Warning

The above information is general in nature and does not take into account your personal situation. You should consider whether the information is appropriate to your needs, and where necessary, seek professional advice from a financial adviser.

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