

M&CO Newsflash

Look for the silver linings

MORTGAGE holders will be about \$1000 a month better off in total this month, after the Reserve Bank resumed its most aggressive interest rate-cutting campaign in decades against the most bleak global economic backdrop since World War II...

Updated forecasts released by the International Monetary Fund (IMF) continue to highlight the precarious outlook for the world. Advanced economies are expected to shrink by 2 per cent this year, the first contraction in more than 60 years. Chinese growth forecasts have also been slashed to 6.7 per cent. But the IMF expects strong action from governments and central banks to help restore global growth to 3 per cent next year, after only 0.5 per cent this year.

Consumers will also benefit from falling prices resulting in the biggest three-month fall in the cost of living for more than a decade. An official survey of consumer prices found they fell 0.3 per cent in the final three months of last year, making the annual inflation rate 3.7 per cent, down from 5 per cent in the previous quarter.

The 18 per cent plunge in petrol prices was largely responsible. Aggressive discounting by retailers also cut the costs of TVs and computers by almost 14 per cent. Cars are 3.5 per cent cheaper than a year ago.

But putting food on the table and a roof over your head is still expensive. Rents rose 8.4 per cent last year and food prices jumped 2 per cent in the December quarter, to be up 5.6 per cent over the year. The slump in the dollar is keeping upward pressure on prices for imported goods like furniture and clothing. But weak consumer demand is expected to keep rises in check.

During the 1929 to 1933 "Great Depression", the Australian share market fell a total of only 46 % (whilst the US's Dow Jones reportedly went down 89%). At our lowest point this time around, we were down precisely that amount.

Probably more importantly, though, the Great Depression saw 7 of the 10 biggest one-day rallies ever recorded. Sound familiar? We saw 4.5 per cent on September 22, the largest gain for nine months; 5.6 per cent on October 13, the biggest one-day surge for 11 years; and another 3.7 per cent on October 14.

This extreme volatility - we all know there have been spectacular falls, too - is known to typify the end of a bear-market phase.

Research shows not only that the average bear market lasts

just 15 months - but that shares usually chalk up significant gains in the 12 months after prices bottom. The average is a rise of 32 %.

We gained 27 % after the tech crash and 25 % after the Asian crisis but the market put on 35 % after the 1987 freefall and a spectacular 50 %-plus after the 1970s economic meltdown. All this still compares mildly with the 281% gains recorded, where else but in the US, between 1932 & 1937 (followed by a 50% downward "re-adjustment" by 1938)

So it's vital you don't miss the bounce by switching your super out of equities, perhaps in favour of the soon-to-be less-than-spectacular returns from cash.

While it's impossible to tell if we are at the bottom yet, markets usually recover before economies do because they price in coming slowdowns. And we're certainly a lot closer to it than we were this time last year!

So just hold your nerve and leave your super alone. If you are at least five years from retirement, you might even consider paying in more.

Cash to lose crown as asset class king

Interest rate cuts and rising investor confidence in equity markets will mean cash will no longer be viewed as king of the asset classes, according to Russell Investments chief investment officer Symon Parish. He said while investors seek the security of cash safe havens, there are now other emerging opportunities in the investment landscape for 2009. "Equity valuations look attractive relative to the significantly lower returns from cash as a result of the series of recent interest rate cuts," Parish said.

"Cash will no longer be king as risk aversion dissipates and investor confidence in equity markets picks up over 2009." Opportunities have emerged in Japan, with valuations at their lowest level. The country's banking sector in particular has weathered the financial crisis better than banks in Western countries, according to Parish. "The US will lead other international markets in recovery as they have experienced the financial turmoil and slowdown in productivity earlier and deeper than other countries,"

This year there will be plentiful opportunities for the most skilful active managers to add value against market benchmark.

SOURCE: - IFA, the Sydney Morning Herald 01 09

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