# Investment Lessons from 2023

*No year in markets has ever been like any year preceding it. Each year's end gives us a moment to reflect on the year that was and assess our investment approach. Much will be written about what happened in financial markets last year, but there are three key lessons investors can take out of 2023.*

**Introduction.**

This time last year the official cash rate in Australia was at 3.1% - the first time it had been higher than 3% since 2013. The RBA had raised rates for the eight months in a row, and 2013 would see the hikes continue until reaching the current levels of 4.35%. Similarly in the US, the Fed funds rate was 4% at the start of 2023 on its way to its current level of 5.5%

These were among the fastest and steepest rate rises in history, and the market feared dire economic consequences. The US yield curve had been inverted since the middle of 2022, which historically was a leading indicator of a coming recession, and it was widely believed that the economy would crater under the weight of such a rapid increase in interest rates.

The consensus view among market commentators was that equities were going to have a tough time in 2023, as the slowing economy would drag the stock market down with it. In particular, the high tech stocks, which were down by more than 30% in 2022, would have further to fall as interest rates continued their upward path. High tech stocks are growth companies – those with high price to earnings ratios – and in theory these are more sensitive to interest rate changes than other stocks.

But none of that happened. The economy did not spiral into a hard landing and now looks to be gliding into a soft landing as we start 2024. Stocks did not crash and burn. The Australian market is up over 10% for 2023, while the MSCI world index is up 22.9%. The Nasdaq stocks, which were supposed to fall further, have had an amazing run helped by the AI craze, and are up a staggering 45% (in USD) in 2023, wiping out the bear market of 2022.
So, as we enter 2024, there are three important lessons investors can take away from the past twelve months.

**1 - Timing the market is a fool's game.**

This may be an investment idiom as old as investing itself but had investors listened to pundits and avoided the stock market in 2023, they would have missed out on some of the strongest returns in equities for many years.

To be fair, the investor who stuck went to cash at the start of 2023 may have felt vindicated by the end of September. At that point the Australian stock market (as represented by the ASX 200) had a year to date return of near zero, while the bond market was slightly negative. Cash was king. But in a sudden turn of events in the last quarter the market has witnessed a rally that no-one saw coming, and the ASX200 is now up over just 10% to finish the year – and all of that in the last quarter!

The cause of the rally was the long anticipated reaching of the terminal rate (particularly the US Fed Funds rate) and the view that the next rate change would be downward. This was reinforced by the Federal Reserve themselves, whose own projections after their December meeting indicated their could be as much as 75bps of rate cuts in 2024.

Stocks rallied and bond yields tumbled – meaning bond prices soared. The global bond index has finished the year at around 5.25% - about a percent better than the official cash rate and about par with what a 12-month term deposit was offering at the start of the year.

There is plenty of evidence – both anecdotal and empirical on why market timing doesn't work. The last 12 months gives us another example of how listening to market forecasts and trying to time when to get in – and when to get out - of the market is a sure fire way to lose wealth.

**2 – Diversification is key.**

The second key lesson from 2023 is also one of the oldest investment idioms – that diversification is the only free lunch in investing.

Technology stocks abroad soared in the first half of 2023 thanks to advancements in artificial intelligence, with many retaining this growth throughout the rest of the year, and now the Nasdaq is on the cusp of its strongest year in two decades,

The "magnificent seven" tech giants have seen a 99% surge in their shares over the year. Meta (the parent company of better known Facebook), Microsoft and Apple have all soared by more than 150%. while AI's demand for semiconductor chips has catapulted Nvidia 240% higher into the $1 trillion dollar club.

But any Australian investor in a portfolio that has a diversified exposure to international shares that is linked to market cap weights will include the "magnificent 7" stocks. Nearly 70% of the MSCI World ex-Australia Index (the standard benchmark for many Australian fund managers investing in international shares) is made up of US companies, and just under half of that US exposure is the Nasdaq companies.

The outstanding returns of this small cohort of US companies have helped propel the MSCI World ex-Australia index to a return of over 20% - one of the strongest returns in years. But it's not all due to the US tech stocks. Over the course of the year the Japanese market is up over 17% (in AUD), which seems odd given that the Japanese economy seems to be in a state of stagnation. And the European market – still contending with the conflict in Ukraine – is up around 18% (in AUD).

What all this means for investors is that a diversified exposure to companies and countries linked to market cap weights will deliver the returns of the global capital markets without having to time the market – or to pick which stocks, sectors or countries will be the best performers in any year.

**3 – Stay disciplined.**

There is no question it's been a wild ride in markets over the last two years. Inflation came back from the dead to reach its highest level in 40 years, and in trying to get inflation back to their preferred levels central banks took interest rates from essentially zero to levels not seen for years in record time.

Consequently, markets experienced a downturn in 2022, with tech stocks down near 30% and the bond market having its worst crash in history. A portfolio of 60% equities and 40% bonds – seen as a conservative portfolio – had one of its worst years ever.

For the past two years investors have been inundated with predictions of a recession, a repeat of the 1970s, stagflation, a housing market crash and worse. And yet none of this happened. Equity markets are now higher than they were 2 years ago.

The lesson is clear - investors need to look past the 'noise' of positive and negative commentary and concentrate on long-term goals. Anxiety, not information, is trying to get you to make short-term moves. So how do you stay focused on the long term? With the help of a trusted financial advisor, develop a financial plan you can stick with that is built upon a strong investment philosophy.

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