



Year in review and outlook for 2025

January 2025

Rory Cunningham (00:00):

Welcome to The Ideas Exchange by ASX, connecting you with investment experts, market updates and ideas. I'm Rory Cunningham, Senior Manager of Investment Products at ASX, and this is our regular podcast covering everything from investment trends through to different ways to invest using a variety of products.

Speaker 2 (00:19):

A quick note about this podcast, information is provided for educational purposes only and is not intended to include or constitute financial product advice. You should obtain independent advice from an Australian financial services licensee before making any investment decisions. Please refer to ASX's full disclaimer with respect to this podcast on the section of the ASX website titled, The Ideas Exchange by ASX.

Rory Cunningham (00:46):

Hi everyone and welcome to The Ideas Exchange, I'm your host, Rory Cunningham from the ASX, and today we're very pleased to welcome David Bassanese, who is the Chief Economist at Betashares. David, welcome to the podcast.

David Bassanese (00:58):

Great to be with you today.

Rory Cunningham (01:02):

So, ASX has just been recently going almost around the country with Betashares and David gave a great presentation to the Betashares investor base that we thought that we had to get recorded in the podcast studio. And effectively, David your presentation is a review of what happened in markets and the economy in 2024, as well as your thoughts on what may unfold in 2025.

(01:25):

So, we thought we would sit down and have a conversation about that. Now starting with, let's start with 2024 year in review. Let's start with unemployment. David, how did 2024 end up for Australia and how did that compare to other countries?

David Bassanese (01:39):

Yeah, look, unemployment basically drifted up very modestly. Look, it's end of the year at 4.1% as of November. And really we've been in ... So, unemployment's been low and steady, I think would be the [inaudible 00:01:58], and look, we've had weak GDP growth but the employment market has been pretty solid. So, we've had very strong immigration, strong labor force growth, but we've been able to find jobs for the people coming into the country and that's kept the unemployment rate low.

(02:11):

But interestingly, it's also happened at a time when GDP growth has been very weak. So, weak GDP growth, solid employment growth, that means that productivity growth, output per worker or work hour has been quite weak. And I think part of the reason for that is a lot of the growth in employment these days as in what's called the non-market sector, things like aged care, disability care, which are wonderful important jobs, but the productivity at least as the statistician measures it, is pretty weak.

(02:43):

There's no productivity growth or they assumed very little productivity growth there. So, it's been a curious break in the sense that the labour market's been solid despite weak GDP. Now, how does that compare with other countries? Look, we're as good as the US, the US has got an unemployment rate also of 4.1%, and in fact, we're better than some of our peer countries in the UK, unemployment is 4.3, Canada a lot higher at 6.8% and New Zealand, 4.8%.

(03:10):

And I guess the key takeaway in terms of the real economy is why can the US, we've managed to avoid recession. It's helped that we've had big immigration so that's underpinned GDP growth. Certainly GDP per capita has been negative but we've avoided recession for another year. Whereas some other countries in the UK, Canada, New Zealand, at various moments in the past couple of years have tipped into recession.

Rory Cunningham (03:37):

Okay. What about inflation? I can't open the paper without reading about it, I can't go to the shops without experiencing it, where have we ended up in 2024 and have we got inflation under control?

David Bassanese (03:49):

Yeah, so there's two I guess key measures of inflation in Australia. One is the headline CPI includes all the items in the CPI, goods and services. That's at 2.8%, which you would think is great because it's in the RBA's target band, a two to 3%. Part of that is the government giving electricity

subsidies, which is sort of artificially reduced inflation, at least in the short run.

(04:14):

But so what many economists look at the Reserve Bank is what's called the trimmed mean. So, it basically chops off the most volatile price increases and price decreases, gives you more of a sort of an underlying sense of what prices are doing. And that's at 3.5%, so it's still above the RBA's target band.

(04:37):

It has come down and this year it's come down but it's come down more gradually than it did in '23. So, we had a faster decline in inflation and this year it's the rate of decline has slowed up and hence, so it's not where we want it to be yet, but it's gradually moving in the right direction.

Rory Cunningham (04:54):

Okay. So, is that why the Reserve Bank continues to leave cash rates where they are and then how does that compare to other countries, particularly the US?

David Bassanese (05:02):

Yeah, so we are one of the few central banks not to have yet cut interest rates after having increased them in '22 and '23. One of the reasons being inflation hasn't come down as much, the economy has held up better so we haven't tipped into recession, but also the RBA never raised rates as aggressively as some other countries, particularly the US.

(05:24):

So, the US raised their Fed funds rate up to five and a quarter percent, five and a quarter, five and a half, whereas we only raised our cash rate to 4.35%. So, they've went higher, now they've come down more quickly. So, the Federal Reserve have already cut rates 75 basis points and widely expected to cut interest rates in the final meeting in December, which will mean a full 1% cut from the Fed this year versus the RBA.

Rory Cunningham (05:58):

Okay. As we're recording this it's just before Christmas, which means that everyone's about to go to family barbecues, the favourite topic of conversation usually at family barbecues is housing prices. Now, it appears there's a little bit of a cooling off of housing prices, is this true or what is the data showing us?

David Bassanese (06:22):

Yeah, so the measure of house prices in Australia, there's a group called CoreLogic that measure this now, I guess it's the nationally recognized house price index, and it has flattened off over the last few months. In

Sydney and in Melbourne, you've had a small negative house price increase or you've had house price declines. The median price has come off a little bit in the last couple of months.

(06:46):

In other cities, Perth, Brisbane, Adelaide, prices are still going up pretty solidly. They're cheaper markets and so there's a bit more ... I think what's happening on the East coast are two things. A, we've just hit affordability constraints, people can't afford to pay anymore given the prevailing level of interest rates, the prevailing level of income, most home loan affordability indices are at record lows.

(07:10):

So, this just comes to limit to how much the average household can afford to pay for a home and we're reaching that at the moment. And the other thing going on with these high level of interest rates, some investors and maybe even some homeowners are selling, so listings have gone up. So, there's an increase of supply of housing on the market, at the same time as many people are struggling to be able to pay a lot more for the house. So, that's why we've seen it come off a little bit.

Rory Cunningham (07:38):

Okay. Let's move on to stock markets. Let's start with global markets, what are you seeing here?

David Bassanese (07:44):

So, it's been a good year for markets. So, the world market is up year to date, something like 20%. The US market, the S&P 500 is up at 27%, and it's a combination of both earnings growth. So, you're looking at round about 10 or so percent growth in what we call forward earnings, it's a weighted average of earnings for the current year and the expected level for the next year.

(08:10):

But yeah, so forward earnings are up something like 10%. We've also had valuations expand, so the P/E ratios, price-to-earnings ratios, I'm sure many of your listeners, I'm assuming they know what we're talking about being the ASX podcast, they've gone up as well. And so, the US market is now trading look at the highest levels really since the .com bubble, the late 1990s, we're looking at 22 times forward earnings.

(08:34):

The world market is trading 18 and a half earnings, so basically, it's been a combination of earnings and P/E expansion, which has driven the markets. In Australia we've had the similar P/E expansion, we've had a 12% increase in the P/E ratio, it's up around 18 and a half times earnings

as well, fairly high, but we haven't had the earnings growth. So, forward earnings in Australia were flat over the past year.

(08:59):

So, that's the difference. That's why our market this year is only up just over 11% in price terms, of course adding dividends gives you another 4% or so. But the big difference between Australia and the US and other markets this year just has been the flatter earnings growth, particularly in the energy and resources sector, which a big part of our market.

Rory Cunningham (09:22):

Okay. And then, in the Australian market, which sectors have done well in 2024?

David Bassanese (09:27):

Well, the banking sector of course, everyone knows I think the CBA has had a rocket under it. I think what's happened, the two things there, look, globally banks have been doing very well, globally with bond yields staying high, the net interest margins of the financial sector globally is good, their earnings have been good.

(09:49):

I think there's a lot also a bit of hope that with Donald Trump becoming the new president, which we'll probably talk about or being re-elected president, there's some excitement emerging on Wall Street that there may be deregulation of the banking sector. We know that can sometimes lead to trouble, but that's one of the things there.

(10:07):

And the other, I think just in terms of domestic reasons, there's been a lot of talk about the mortgage cliff that people maybe an increase in home loan defaults because of the high level of interest rates. And what we've seen is yes, home loan defaults have gone up a little but not as much as feared. And so, a lot of the banks made provisions for bad loans, and they've been able to write those back into their balance sheet.

(10:30):

The bad loan situation hasn't been as bad as they thought so I think that's been another factor. So, the financial sector has done very well. Pockets of growth also in our market, the S&P/ASX 200 Technology index has done very well as well, something like 30% I think this year. Only difference, and that again, the technology sector globally has done very well, difference is that it's 2% of our market and it's 20% of the US market.

(10:58):

So, that's why it's been a bigger catalyst in the US market. I guess, the dead weight in our market at least this year has been in the resources

sector, pessimism over China, the weakness of Iron Ore prices and as I said, the flatness of earnings has unwound. They had a couple of good years and this year, not a good year.

Rory Cunningham (11:19):

Yeah, okay. So, let's switch to the outlook for 2025 and let's discuss Trump. Now, his election victory has already had a big impact on markets as you mentioned, including Bitcoin, which I believe is still trading at over 100,000. Firstly, are there any lessons to be learned between his victory in 2020 versus 2024?

David Bassanese (11:43):

Well, I think the lesson is that he does go through with, he cut taxes, last time he was around he did engage in trade wars but the trade war situation last time around, I guess global economy wobbled but didn't topple over. So, I mean, I think he ultimately will pull back from doing anything that seriously risks the US economy, seriously risks Wall Street.

(12:11):

So, he'll talk tough, and he will implement some measures, there'll be some volatility in markets, but I don't think he would be crazy enough to do anything that would cause the economy itself to topple into recession or create a major bear market. But there certainly will be some volatility ahead depending on what he goes with.

(12:30):

I mean, the two big policies he's talking about are tax cuts, fiscal stimulus, but he's also talking about spending cuts as well. Elon Musk, his new buddy, reckons he can cut \$2 trillion of spending out of the budget. So, if he does that, it won't be as much fiscal stimulus as markets are expecting. I don't know if he will be able to cut spending as much, but they'll definitely be able to cut taxes so that will be sure about.

(12:58):

So, that's a positive for markets. The negative would be obviously the trade, if he jacks up tariffs and there's a tit-for-tat exchange in terms of tariff increases, which could hurt business sentiment. So yeah, I think they're the considerations for next year on the Trump front.

Rory Cunningham (13:15):

Okay. You mentioned a possible cut in US spending, let's talk a little bit about the US federal debt level, it's at historic highs. What do you see happening there in the future? How does that impact markets?

David Bassanese (13:30):

Look, it's a simmering issue for markets. Debt in the US is running at almost 100% of GDP close to the levels of World War II. And they're not at

war, and in fact, they're at full employment. So, the fact that debt in the US is so high, I mean obviously COVID was a part of that massive fiscal stimulus due to COVID, but they haven't really cut back on the deficit.

(13:53):

So, the deficit is running at 6% of GDP, debt is 100% of GDP, tax cuts would just add to the deficit. So, I mean, there is always a risk that people worry that, investors worry that there'll be a bond market backlash one day and bond yields will go higher because investors will worry about the US ability to, I don't know, pay off its debt, but just given the risks around such a high level of debt that they would just demand a high level of interest rates.

(14:24):

But look, so far at least that hasn't happened, we haven't had a bond market revolt in the US market. And it's just one of those things that it's a known risk, but we just don't know when and if the bond market will ever call the US to task. And I think one of the problems is that realistically, I don't think Washington will ever really tackle the budget deficit until the markets insist they do.

(14:47):

So, it's going to keep festering until there is a problem. Will it happen next year? I don't know, but at some point I think there's going to have to be some reckoning.

Rory Cunningham (14:57):

Okay. Switching back to home. So, we talked about inflation before, we talked about cash rates, what's your outlook for inflation, what's your outlook for cash rates in Australia next year?

David Bassanese (15:07):

Look, down, I mean, I think, so I mentioned the trimmed mean measure is at 3.5%, I'm hopeful it'll be sub 3% this time next year. So, around just under 3% of the year-on-year measure by the December quarter. We don't need to wait for that to happen before the RBA will cut rates. It just needs to, I guess, have more confidence that it is moving back down toward that two to 3% band.

(15:35):

So, I anticipate certainly by mid-year we'll be getting interest rate cuts in Australia. There's a debate at the moment, do they go as early as February or do they wait 'til May? Even the RBA is changing its mind on that at the moment so I wouldn't get too hung up about the timing of it, whether it would be February or May. But certainly, I think by mid-year we'll have enough evidence of inflation coming down that they can join the rate cut party that other central banks are in at the moment.

Rory Cunningham (16:02):

Okay. And unemployment in Australia?

David Bassanese (16:05):

Look, unemployment I've got it going up a little from 4.1 to about 4.3 so not ... I mean, the RBA think full employment in Australia is 4.5 but I think we'll find next year that inflation will come down without unemployment needing to get that high. And they'll probably end up revising down what they think is the full employment rate.

(16:24):

The Treasury Department, I think full employment is closer to four than 4.5%, but I think the evidence is in inflation. If inflation comes down, wages come down at current levels of unemployment, then your so-called full employment rate is lower than what you thought it would be and I think that's what we'll find next year. So, a little bit of a drift up in unemployment, further declines in inflation, RBA cutting rates at least twice, possibly four times.

(16:54):

I think really around the world central banks, as inflation gets back to their target levels, they are "re-normalizing" rates and the normal cash rate in countries like Australia and the US is around about 3%. So, we're well above three so we'll just gradually move toward three as the inflation numbers permit.

Rory Cunningham (17:14):

Okay. So, those things happening from an economic point of view, your outlook for markets, let's discuss the US market and Australian market, what's your outlook for 2025?

David Bassanese (17:26):

Look, so going back to the drivers earnings and valuations, the earnings side is, the good news is earnings are looking quite solid, earnings expectations are still positive and certainly no signs of downgrades coming through globally, holding up very well in the US. So, at the moment, based on current expectations, forward earnings growth, as I said last year, grew by double digits in the US, expected to grow by double digits again and globally.

(17:52):

In Australia at the moment, they're expected to grow by 6%, so it's better than flat. There is an improvement. I think there'll be some upgrades there so we could get 10 per cent earnings growth in our market next year as well. The problem is on the valuation front, last year globally we had P/E expansion added 10% return to markets and to our market. And it's just

hard to see P/Es continuing to expand. And I think if anything, they may pull back a little.

(18:19):

So, I've got, again our market, the P/E ratio going from 18 and a half to 17 and a half, pulling back a little, which will take maybe 5% off the market return. So, earnings up by 10, P/Es down by five, you're getting like a 5% price return, adding dividends, you're getting just under a 10% return, which is I think a reasonable long run average kind of return for the market would be how I'd be characterizing things.

Rory Cunningham (18:46):

Okay. So, just in wrapping up David, what do you think is important for investors to consider in light of everything we've just discussed?

David Bassanese (18:55):

Well, I think the big risks next year and not so much on the activity front, I don't think that the risks that we were worrying about the last couple of years on the back of central banks raising rates, the global economy, the Australian economy could tumble into recession, I think those, never say never but I think that's not the major risk now.

(19:15):

The major risk is what Trump does in terms of the trade wars, what he does in terms of fiscal stimulus if there's a net fiscal stimulus and it puts upward pressure on inflation and bond yields in the US, that will put a lot of pressure on valuations given they're already quite lofty. So, it's really the key issue is going to be inflation needing to continue to come down. Even in the US it's still not where it needs to be.

(19:43):

Underlying inflation in the US is at 2.8%, the Fed's target is two so it's not there yet. And if it stays where it is, the Fed won't be able to cut interest rates that much next year, if at all. So, I guess that's the worry, it's inflation, bond yields and Trump, more so than recession.

Rory Cunningham (20:04):

Okay. David, thank you so much for joining us today.

David Bassanese (20:07):

Great to be with you.

Rory Cunningham (20:08):

And if you'd like to hear more from David or learn about Betashares, including their range of ETFs and also their newly launched Betashares Direct investment platform, I'd encourage you to head to their website

where you'll find a lot of educational material. And thank you all for joining us on the podcast, we look forward to you tuning in next month.

Speaker 2 (20:27):

Are you keen to learn more? Why not visit the ASX blog, asx.com.au/blog for a wide range of articles, videos and insights from ASX experts, listed companies and investment professionals.