Lessons from the FTSE at 40

As the FTSE 100 turned 40 on 3 January 2024, we look at how it compared to its predecessor and the lessons learned from four decades of growth versus inflation.

Source: Google Finance

The Financial Times Stock Exchange (FTSE) 100 Index, to use the Footsie's full name, has celebrated its 40th anniversary. It is a significant milestone and an opportunity to take stock of the index's history and position.

The UK's benchmark stock market index was launched in 1984 by the London Stock Exchange, designed as a modern successor to the FT30 Ordinary Share Index produced by the *Financial Times*. The FT30 was a product of a pre-computer era and once calculated using a slide rule. There are other starker comparisons with the 100-share FTSE 100:

- The FT30 shares were hand-picked by an editorial team at the *Financial Times*. The index was prone to age poorly given its data was only changed if there was a merger or bankruptcy. In contrast, the FTSE100's constituents are selected according to a detailed set of rules, largely driven by company size, and reviewed quarterly.
- Weighting played another key difference. To make life easy for the slide rule user, each company in the FT30 had an equal (3.33%) weighting in the index, regardless of its market size. In contrast, the more sophisticated FTSE100 weighted each share according to corporate value. That means that just five companies – Shell, AstraZeneca, HSBC, Unilever and BP – account for nearly one third of the index.

From its initial launch value of 1,000, the FTSE100 has climbed to 7,721.52 by its 41st year on 3 January 2024. That equates to an annual growth rate of 5.2%. Inflation over the same period, as measured by the Retail Prices Index (RPI – the CPI does not go back beyond 1988) averaged about 3.7% a year.

Like most indices, the FTSE100 measures only capital values and does not include dividends. When dividends are considered, the total return on the FTSE100 rises to 8.2%, an annual 4.5% outperformance of inflation. Dividends are still a key factor in the returns from the FTSE100 today, with the Index offering a dividend yield of close to 4%.

If there is one lesson from the FTSE100's legacy of the past four decades, it is that next time you see or hear its performance being quoted, check whether dividends have been taken into account.

On your marks – an early Spring Budget for 2024

A date to note in this year's calendar is the early Spring Budget on Wednesday 6 March.

The Treasury issued a press release in the time between Christmas and the New Year revealing the Spring Budget date, a week earlier than in 2023. The unusual timing of the announcement may seem strange, but there were two inter-linked reasons which could explain it:

- First, local and mayoral elections will be held in England on 2 May 2024. If – and it looks unlikely at present – the Prime Minister Rishi Sunak decides to call a general election for the same day, then Parliament would have to be dissolved 25 working days earlier. That would mean the week beginning 25 March, allowing for the Easter holiday which follows. Given all the work to be rushed through in the 'wash up' period before dissolution, a Budget on the first Wednesday in March is about as late as possible.
- Second, the Chancellor is normally required to give the Office of Budget Responsibility (OBR) at least ten weeks' notice to prepare its Economic and Fiscal Outlook, which is published alongside the Budget. Ten weeks backtracked from 6 March 2024 arrives on 27 December 2023.

If you feel like you have been here before, that is because the OBR issued its last Outlook on 22 November – only fifteen weeks before the next one is due. It is doubtful much will have changed in the interim to make much difference to the OBR's five-year projections.

The Chancellor and Prime Minister will likely be hoping that the OBR will discover some extra money down the back of the sofa as they did in November, thanks to higher-than-expected, inflation-boosting tax revenues. However, as an OBR head once memorably remarked, "What the sofa gives, the sofa easily takes away."

In most years, the date of the Budget is a factor to consider in your year-end tax planning. In 2024, with an election looming, it is probably less of an issue with the Chancellor aiming to please the electorate. However, the earlier you can plan, the better, as certain aspects may require information that can take a while to obtain.

HMRC, eBay and second-hand news

The media storm surrounding HMRC taxing eBay and other online sellers from the start of 2024 was, in fact, itself counterfeit goods.

A crop of stories across social and traditional media swirled across the start of the new year about HMRC cracking down on 'side hustle' tax from 1 January, leaving sellers using sites like eBay and Vinted feeling uncertain. Coming after an early December announcement that HMRC had effectively closed its main self-assessment helpline until 1 February 2024, the story only fuelled the outrage directed at the Revenue.

Except that it was not fresh news or, even, news at all. There was no new 'side hustle' tax. HMRC was starting the first year in which digital platforms, such as eBay, would be required to automatically report details of sellers who in a calendar year:

- Had sales of at least €2,000 (about £1,725 at current exchange rates); or
- Made at least 30 sales.

Further, this was not a UK-led law as revealed by the denominating currency. The initiative started with a set of model rules published in July 2020 by the Organisation for Economic Co-operation and Development (OECD), of which the UK is a member, aimed at reducing tax avoidance via digital platforms. The first reports from platforms will not be sent to HMRC until January 2025 and will cover only the current year.

Contrary to fears raised online in the New Year, neither HMRC nor the OECD have any interest in the sale of personal items no longer required, whether clothing or mobile phones. The new reporting requirements are for people who are trading – buying and selling goods with the aim of making a profit, something that has always been taxable.

It's worth bearing in mind that there is also a little-known trading allowance, which exempts from tax £1,000 of trading income (before expenses) in a tax year. A similar £1,000 allowance applies to property income (also before expenses), which matters here because Airbnb falls within the scope of the reporting regime.

There are a couple of lessons to learn from this saga of the 'side hustle' tax. The first is that tax is rarely simple and media information – especially social media – can be misinformation. The second is that HMRC's ability to gain insight into your sources of income is ever-expanding.

You have been warned…

The future of the State pension

Public opinion is pessimistic about the future of the State pension.

Ask yourself these two questions:

1. Do you believe that the State pension will be around in 30 years' time?

2. Do you think that the State pension will keep pace with prices over the next ten years?

If you said 'no' to both, then your view places you in the minority, although a sizeable one. Polling research undertaken for the Institute for Fiscal Studies (IFS) last year revealed that a third of working-age people answered 'no' to the first question. Pessimism rose with age and women were consistently gloomier than men: in the age range 45–54, about 42% of women said 'no' compared with 31% of men. The State pension has existed since January 1909.

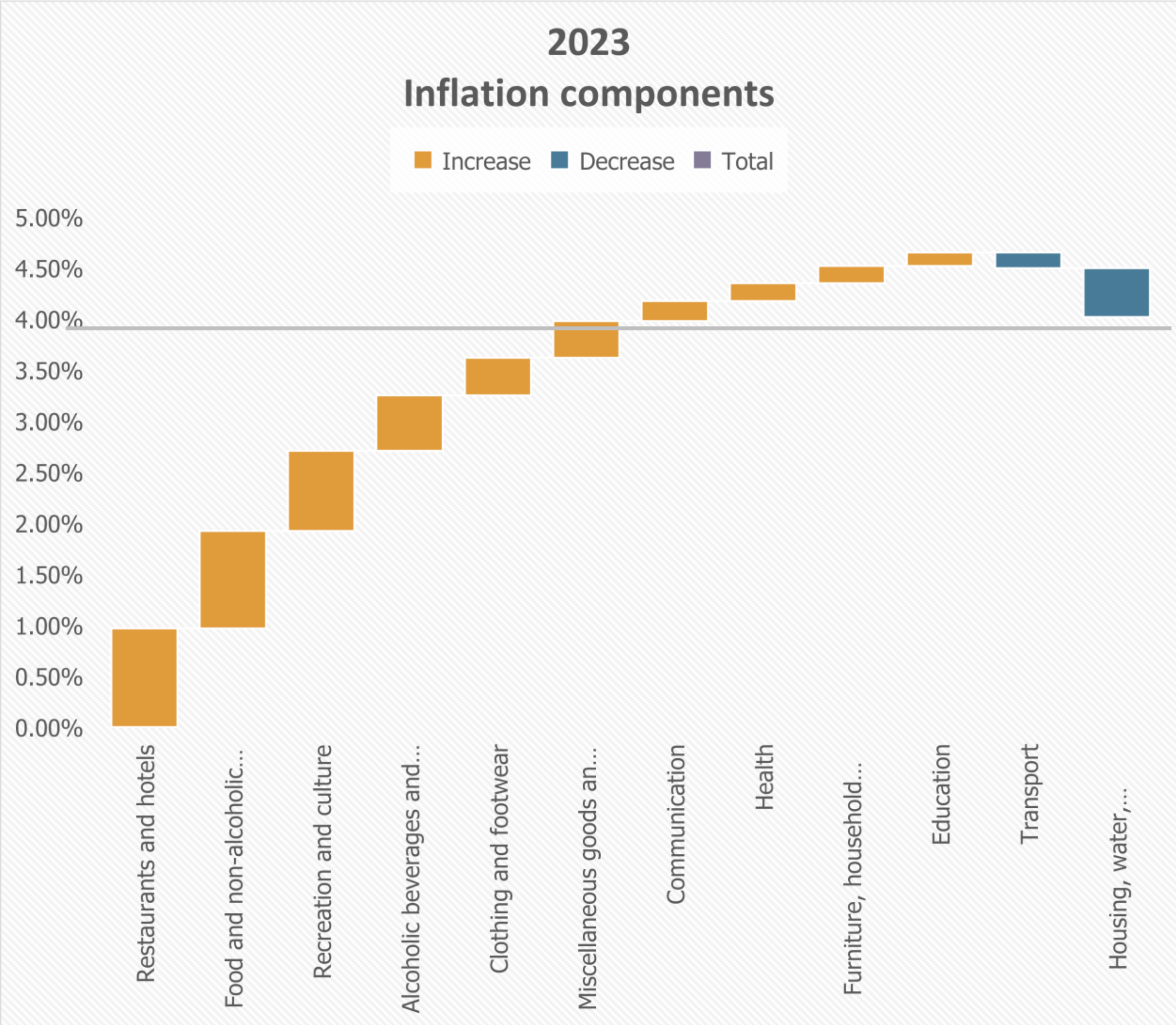
The perceived failure of pensions to keep pace with price inflation through to 2034 attracted 38% support, even though the opposite has been the case since 1975. Just 11% thought the pension would outpace price inflation, when that is near the guaranteed effect of the infamous triple lock, which has been in place since 2010.

The poll results may reflect a poor understanding of the State pension, as the IFS notes. This is forgivable, as the State pension has undergone several changes in recent years. For example, there has been the introduction of the new State pension regime in 2016 and ongoing rises in State pension age. Nevertheless, the State pension remains an important foundation for retirement planning. It accounts for more than £7 in each £10 of income for the poorest fifth of retired households and is close to a quarter of all income for the richest fifth, according to the IFS.

The UK's State pension system is much less generous than many of its European counterparts, but that means it is also more readily affordable in terms of Government expenditure. The public's pessimism is overdone because the subsistence level at which the State pension is pitched makes its survival more likely. However, while you should not ignore the State pension in your long-term planning, neither should you rely on it alone for a comfortable retirement.

2023: The year of disinflation

At the start of 2023, the Prime Minister pledged to halve inflation. The goal was reached, but how much credit can he take for the achievement?



Source: ONS

Inflation across 2023, as measured by the Consumer Prices Index (CPI) ended at 4.0%, a far cry from the 10.5% of 2022 and the October 2021 peak of 11.1%. The drop had been widely predicted, although in the final month of the year there was a small surprise: the rate rose 0.1% whereas the pundits had forecast a fall of the same amount.

The rapid decline in inflation – disinflation to use economists' jargon – does not mean prices have generally fallen (deflation), although there were a few exceptions such as in electricity and gas prices. The absence of widespread price falls is one reason why the cost-of-living remains a live issue for politicians for the forthcoming general election.

The story behind the CPI's fall in 2023 should give those same politicians something to consider before claims are made to conquer inflation:

- For example, the main driver of double-digit inflation in 2022 was energy prices. That meant higher fuel prices for all forms of transport – air fares rose by over 44% in 2022. It also pushed up domestic gas and electricity prices, by 128.9% and 65.4% respectively.

- In 2023, the opposite was true as energy prices declined: air fares rose by just 0.8% while gas prices tumbled by 31% and electricity by 15.4%. Those reversals were a major part of the overall decline in inflation. Energy prices are set globally beyond the influence of UK politicians.

It was a similar story with the rising prices of food. In 2022, food prices rose by 16.8% whereas a year later the annual increase was 8.0%. However, that was still double the overall inflation rate and left average food prices more than 26% up over the two years. On the fringes of food, there was an example where the government does have limited control over prices – alcoholic drinks. Here, the 2023 price rise was 9.6%, against 3.5% in 2022, in large part because of increases to alcohol duty.

The good news for 2024 is that inflation is expected to continue falling, with the consensus forecast for the final quarter of the year being just under 2.5%. However, it remains important to review the impact of past inflation on your financial planning: prices are up 21.8% since the end of 2019.