RAYMOND JAMES

Green Shoots

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It might strike readers as odd, or at the very least premature, that in the midst of a dark and tempestuous mid-winter thoughts might already be turning to a brighter spring, but that is how the financial markets work. Stock and bond prices occupy the future as much as, if not more so, than being informed by the present. For the holders of broadly diversified portfolios of financial assets, January has proved another very successful month in the round as markets built on the gains achieved at the end of 2023 in anticipation of better things to come.

The US stock market has enjoyed a series of new all-time highs, in large part inflated by that economy's ongoing resilience and investor enthusiasm for the promise offered by the roll-out and application of artificial intelligence (to which benchmark indices are heavily weighted towards). Meanwhile, the Japanese stock market has tracked further to the upside, the main benchmark index hitting levels not seen since way back in early 1990. Arguably even more strikingly, European bourses have continued to strengthen, carried higher by falling energy prices from the elevated levels of last winter and the expectation that the single currency region's central bank will soon begin lowering interest rates in an effort to breathe new life into an otherwise moribund economy. In the context of eye-catching gains elsewhere, the UK stock market has failed to keep pace. News relating to the domestic economy's recent performance has been downbeat and in addition to which the uncertainty associated with an election, that must now be held within the next twelve months, is casting a long shadow.

There are, of course, exceptions to every rule and while few investors are likely to have much direct exposure to China, the fate of the world's second-largest economy does matter to the global economy more generally and to international businesses that thrive on a broad-based revival. Although it has been confirmed that that country's economic activity grew strongly in 2023, that was always likely against a comparator year in which much, if not all, key hubs were in pandemic-induced lockdown. While stock markets elsewhere have hit multi-year, and in some cases, all-time highs, the Chinese stock market has floundered, dropping to levels last seen prior to the pandemic's onset. Investment, hitherto the driver of economic growth has stalled, consumers have retrenched, world trade is slowing, and overseas investors have pulled out. On top of that, a Hong Kong court has ruled that property giant Evergrande must liquidate, adding to fears regarding the health of a sprawling real estate sector accounting for one-quarter of all economic activity. In response the country's central bank has cut key interest rates, Beijing's plan being to flood the banking system with reserves by pumping cash into household and business accounts. If the plan works, adding credit to the economy should encourage increased spending, presaging a revival in due course.

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If China's experience teaches investors anything it is the further confirmation that it is central bankers' approach to monetary policy that holds the key to future market

performance. Sovereign bond markets have not, so far, built on the gains achieved late last year, prices slipping and yields edging higher in response to senior central banking officials' insistence that while lower interest rates will very likely come, the promise of "jam tomorrow" does not always mean "jam today". Inflation is falling around the world, but remains, for now, above target and still too high for comfort. But while the markets may have over-anticipated the point at which the rate-cutting process might begin (and the extent of that process thereafter), the prospect of policy loosening allows both households and businesses to plan for the future with greater confidence and bond yields should resume their fall as inflationary pressures diminish as 2024 progresses.

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None of this is to say that the future will not hold challenges, gains in financial asset prices are typically hard-won and achieved often in the face of demanding hurdles. Investors fully aware that the best returns are typically achieved over medium and longer-term time periods have grown used to the reality that prices seldom rise in a prolonged straight line and are subject to periodic corrections from time to time. Is it too insouciant simply to assume that inflation will keep falling, interest rates will fall and global economic activity revive? Perhaps the biggest challenge lies in the political and geopolitical environment. Financial markets have historically struggled effectively to discount uncertain outcomes associated with both, typically erring on the side of optimism when forced to decide. This triumph of hope over experience is being put to the test; conflict in the Middle East threatens escalation, drawing ever more powerful *dramatis personae* into direct confrontation, adding to supplier delivery times and potentially pushing up prices over and above the very obvious impact on crude oil. As a far-from-irrelevant aside, 2024 is a big election year in many places, not least of which in the United States. At a time when the world needs forceful (but not inconsiderate) and assertive (but not arrogant) leadership the front-running candidates in a presidential race showdown remain a cause for concern.

Thus are the contours of the investing landscape taking shape. Financial markets are facing up to the challenges that lie in wait with both bravery and resolution. There may be more storms ahead in coming months but there is a pathway to a brighter future and it remains our view that when 2024 comes to a close the green shoots of spring will have grown into something more lush and verdant; financial asset prices should end the year higher than where they began it.

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