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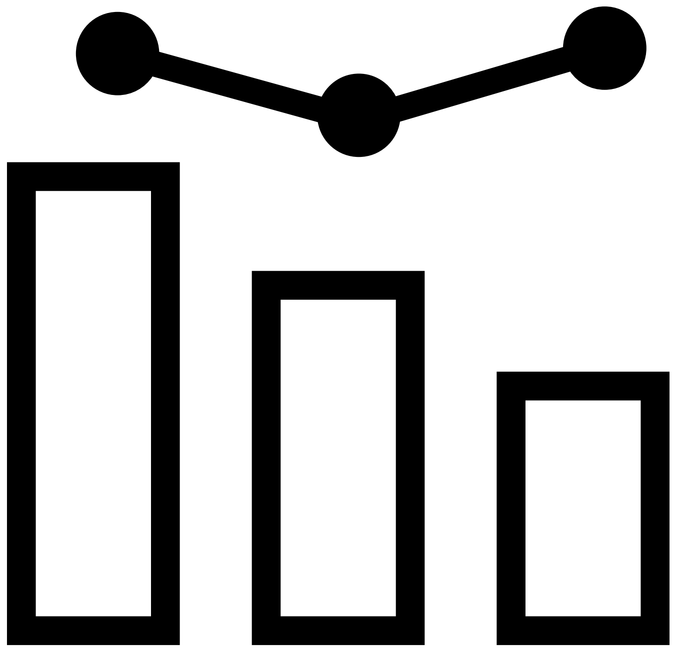

Marketupdate

January 2024

January 2024: a good month for stocks, after a hesitant start

Stock markets got off to a hesitant start in 2024, but gradually found their way to the upside as the month progressed. Government bond yields actually started the year higher, but declined again slightly towards the end of the month.

For investors, 2024 initially featured a reversal of the last quarter of 2023, with rising interest rates and generally falling share prices. But this picture already changed during January. Led mainly by US technology stocks, stock markets resumed their upward direction, while bond yields declined slightly towards the end of the month. On balance, European government bond yields were still slightly higher at the end of January than at the beginning of the year, showing a negative monthly return of 0.5%.

In the stock markets, the picture for the whole of January was ultimately mostly positive, but this was not the case for all categories and regions. US equities were ultimately the winner, as they were in 2023, with a monthly return of almost 3.5%. The return differential with European equities, which appreciated ‘only’ 1.6% in January, was largely due to the depreciation of the euro against the US dollar (-1.9%). Chinese equities underperformed heavily in January, also depressing returns for emerging markets as a whole (MSCI Emerging Markets index -2.8%). The problems in China also had an indirect

effect on Asian equity markets, but this was partially offset by a positive price performance in Japan. On balance, the MSCI Asia Pacific Index delivered a return of +0.3%. Listed real estate, (last quarter's big winner with a return of +25% in Q4 2023), was the biggest loser in January, with a negative monthly return of 3.0%.

Finally, European corporate bonds achieved yields between those of European government bonds and equities, as is usually the case. Investment grade corporate bonds delivered a monthly return of +0.1%, while more risky high yield bonds posted a return of +0.7%.

The returns on the various asset classes were as follows:

Rendementen (total return, in euro's)	januari	1st quarter	2024	12 months
Bloomberg Barclays Eurozone Government Bonds	-0,5%	-0,5%	-0,5%	4,1%
Bloomberg Barclays Euro Corporate Bonds	0,1%	0,1%	0,1%	6,0%
Bloomberg Barclays Euro High Yield Corporate Bonds	0,7%	0,7%	0,7%	9,5%
FTSE/EPRA Europe Real Estate	-3,0%	-3,0%	-3,0%	0,4%
MSCI Europe Shares	1,6%	1,6%	1,6%	10,2%
MSCI North America Shares	3,4%	3,4%	3,4%	19,7%
MSCI Asia Pacific Equities	0,3%	0,3%	0,3%	1,6%
MSCI World Developed Markets Shares	3,1%	3,1%	3,1%	15,1%
MSCI Emerging Markets Shares	-2,8%	-2,8%	-2,8%	-3,0%

Source: Bloomberg

US economy continues to surprise to the upside...

Most of the major economies traditionally publish their fourth quarter growth figures in January. There were no immediate surprises regarding the state of the global economy, apart from the figures released for the US economy. The story of 'the recession that never materialised' continued in the fourth quarter as well. The US economy grew 0.8% quarter-on-quarter in the fourth quarter, slightly less than the 1.2% seen in the previous quarter, but still well above the consensus forecast of 0.5%. Over the whole of 2023, the US economy thus posted very decent growth of 2.5%.

A particularly striking feature of US growth in the fourth quarter was that consumer spending held up better than expected. So far, higher interest rates and the depletion of 'corona savings' do not appear to have had any significant effect on US consumer spending. Of course, it helps that unemployment was still historically low at 3.7% at the end of 2023, and that hourly wages have been rising faster than prices for some time now. Seen in this light, it is no surprise that US consumer confidence rose sharply in December, although it should be noted that this was mainly due to the measure of confidence 'in the current situation'. The 'expectations' component was at a considerably lower level, which is less good news for President Biden's hopes of re-election in November. The huge gap between consumer confidence among Democrats (high) versus that among Republicans (low) will be an additional source of concern for him. These two voter groups now seem to be living in completely different economic realities.

...While Europe continues to teeter on the brink of recession

Europe on the other hand is clearly in a truly parlous economic reality, with the eurozone posting no economic growth at all in the fourth quarter. This was slightly better than the consensus growth forecast of -0.1%, and moreover meant that the eurozone narrowly escaped a recession, at least according to the formal definition of two consecutive quarters of negative economic growth. Over the whole of 2023, growth here was 0.5%, which is certainly not particularly impressive when compared to the growth rates of 2021 (5.9%) and 2022 (3.4%).

The most notable aspect of the European economic growth figures is the continuing malaise in Germany. Whereas concerns about the eurozone 10 years ago mostly focused on the southern European economies, Germany is the weakling today, as was the case 20-30 years ago. The German economy contracted by 0.3% on a quarterly basis in the fourth quarter, but has in fact been teetering on the brink of recession for around two years. The previously much-vaunted but also highly conservative German (car) industry is apparently finding it very difficult to adapt to rapid technological developments elsewhere, while much-needed structural reforms failed to materialise during the lengthy Merkel era and are not (or at least not yet) really getting off the ground under Chancellor Scholz's unstable administration either. Compared to the poor performance in Germany, economic growth rates in Italy (0.2% quarter-on-quarter in Q4) and Spain (+0.6%) were particularly striking. Growth in the French economy was in between the above figures mentioned, posting exactly zero growth.

Chinese economy meets expectations, but with increasing difficulty

China's fourth-quarter growth figures did not produce too many surprises. With quarterly growth of 1.0% and 5.2% for the whole of 2023, the economy met the Chinese authorities' growth target as expected. Especially given the ongoing problems in China's real estate sector, it is questionable whether some manipulation has been applied to achieve this growth, and in particular whether the Chinese authorities will be able to maintain the desired rate of economic growth in the future. The Chinese authorities announced a further package in January to support the economy, especially the ailing real estate and

banking sectors, and to halt the free fall in the Chinese stock market (now down more than 40% from its peak in spring 2021). The latter aim has not yet really been achieved, but most economic indicators are not at this point suggesting that China is facing a sharp slowdown in growth either, at least not in the short term.

Reasonable growth outlook does not argue for too many interest-rate cuts in the short term

All in all, the outlook for global economic growth has not changed radically from a quarter ago, and has even slightly improved rather than worsened due to the better-than-expected performance of the US economy. This is also the conclusion of the IMF, which in the latest quarterly update of its ‘World Economic Outlook’ has slightly upgraded its growth forecast for the global economy in 2024 from 2.9% to 3.1%. In doing so, the IMF assumes that the US economy will grow by 2.1% in 2024 (from 1.5%) and the European economy by 0.9% (from 1.2%). For China, the IMF now expects growth of 4.6% in 2024, higher than its previous forecast of 4.2% but lower than the target set by the Chinese authorities.

For the central banks, and certainly the US Fed, the latest economic data do not give reason to be in too much of a hurry to cut interest rates, even in the face of steadily declining inflationary pressures. The latest inflation figures indeed show a rather mixed picture. Headline inflation has picked up again recently, from 2.4% year-on-year in November to 2.9% in December in the eurozone and from 3.1% to 3.4% in the US. This was not entirely unexpected, and looks more like a temporary uptick rather than the start of a new upward trend. Core inflation, which excludes volatile food and energy prices, is still declining in both the US and the eurozone. In the eurozone, this measure declined from 3.6% year-on-year in November to 3.4% in December and 3.3% in January. Core inflation in the US also declined slightly further in December, from 4.0% to 3.9%.

Turn in the interest-rate market: rates to stay high for slightly longer, and fewer rate cuts in 2024

While inflationary pressures are and will continue to be expected to ease further towards the US and European central bank 2% inflation targets in the coming period, the diminished chances of a recession (especially in the US) and the still tight labour markets in the US and the eurozone (with accompanying expectations of more wage increases) could throw a spanner in the works. Meanwhile, the interest-rate market has also realised that expectations of initial rate cuts by both the Fed and the ECB as early as March this year that were still widely held in December are probably not that realistic after all, barring exceptional circumstances. These expectations have now been pushed back to the subsequent interest-rate meeting for both central banks. This means that the ECB would cut its base rate for the first time in April, probably by 25 basis points, and the Fed in early May.

The interest-rate market therefore currently assumes that the ECB is likely to cut interest rates before the Fed, which would be fairly exceptional historically but looks to be more realistic given the relative state of these economies. The European economy is clearly in worse shape than the US economy, and at this point would therefore benefit more from lower interest rates than the US economy, which is performing well. Incidentally, the interest-rate market also assumes that both central banks will cut base rates by a total of 150 basis points this year, also slightly less than previous expectations at the end of 2023.

In our view, the market's expectations of central bank interest-rate policy are more realistic now than they were a few months ago. For government bond yields, we still see some room for further gains, even after the increases seen in January. In other words, we still expect to see a gradual steepening (or normalisation) of the yield curve. For more risky investments, such as equities, the slightly improved economic outlook is a plus. However, much will depend on earnings forecasts, especially for the big US tech companies. These do seem to be a bit far ahead of the supposed future possibilities of artificial intelligence, meaning that these stocks are anyway not particularly attractively valued. Valuations in the

European stock markets look to be relatively more attractive in this respect, but the economic outlook is less favourable in this region.

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