THE JANUARY BAROMETER

When the market surprises, whether positive or negative, the perplexed investor often seeks solace in historical statistics. If he then finds himself at the dawn of a new year, past numbers turn into hope. In January, the S&P, Wall Street's flagship index, rose by 1.6%. If one then considers that it has performed positively in twelve of the last thirteen weeks, rising by almost 20%, some tremors of uncertainty are inevitable. And so consulting the 2024[1] Stock Market Almanac becomes reassuring reading, before moving on to other considerations. The 'January Barometer', as it is called, tells us that if January is positive, with a probability of 83.6%, the whole year will be positive as well. [2] If this optimism is not enough, then the four-year presidential cycle projections can also be analysed: 2023 and 2024 will be positive. More precisely, the first quarter of this year will grow, while the middle two quarters will be negative or sideways, before taking off in the latter part of the year.[3] So all is well? We will see over the course of the year, but the start is encouraging. Underlying the optimism, in addition to the Almanac statistics, is the macroeconomic and financial reality, especially in the world's most important economy, the United States. But there are also risks, given by geopolitics and imbalances in the financial markets.

Over the past two years, central banks have undertaken the most extensive and synchronised tightening of global monetary policy, surprising an entire generation. Financial assets reacted violently during 2022, surprised by the power of the change of course: from the fear of deflation, the world found itself having to fight the explosion of inflation. Nevertheless, economic activity has remained surprisingly resilient to the point that there is now talk, without excessive fear, of a soft landing. If this path is confirmed, giving reason to the markets that aligned to this idea in 2023, the fight against inflation has come at a remarkably

[1] Jeffrey A. Hirsh, Christopher Mistal, *Stock Trader's Almanac, 2024*, ed. John Wiley & Sons, Inc., New Jersey.

[2] *Ididem*, p. 18.

[3] *Ibidem*, p. 11.

low cost in terms of lower Gross Domestic Product (GDP) growth or higher unemployment. How many financial analysts and economists, from 2021 onwards, seeing rates rise relentlessly between central bankers' meetings, predicted a major blow to economic activity, or even a recession? Given the already high debt levels and accumulated vulnerabilities, it was plausible to expect a significant increase in defaults and bankruptcies, or even a global financial cliff: not even the Credit Suisse and US small and medium-sized bank crises have really succeeded in opening up the abyss of fear. So much so that in November and December 2023 even the most cautious professional investors capitulated, lighting the fuse to the powerful rally that did not stop even in January 2024. This shift in outlook reflects the success of the Federal Reserve and, perhaps, Joe Biden's policies, which together have introduced the tools to turn the global rise in inflation around. Advanced economies had started 2023 with inflation averaging 7.5 per cent, while it now hovers around 3.2 per cent. Emerging markets, with a few exceptions, saw average inflation fall from 8.1% to 4.1%.

Part of the drop reflects the decline in commodities after the 2022 increases and the normalisation of post-pandemic supply chains. China, due to Xi Jinping's policies as well as its demographics, is no longer able to exaggerate commodity prices. Green Joe Biden nipped in the bud the attempts of Russia and Saudi Arabia to manoeuvre energy prices by pushing domestic oil and gas production: the US produced 13 million barrels of oil per day against Saudi Arabia's 10 million. But even the stickiest part of inflation, that of services (excluding housing), fell last year from over 5% to around 4% (from 9% to 7% in emerging countries). This environment has curbed, or at least delayed, the price-wage spiral.

Although not to the level imagined by many economists, the generalised rise in rates weighed on aggregate demand, contributing to the slowdown in global growth in 2023. China's recovery has been weaker than expected and Europe, with Germany at its centre, has come close to recession. The real engine of the world economy is the United States. While Jerome Powell has continued to raise rates to curb demand and inflation, Joe Biden's team has used fiscal leverage, and

indirectly geopolitics, to support it. The budget deficit in 2023 exceeded 7%, while the military industry, with its spill-over that today often takes the form of digital technology, stimulated demand. For their part, the oil companies have been happy to make the most of the shale oil wells reopened after the price flare-up following the outbreak of the war in Ukraine.

Another support for the economy is post-pandemic employment. Despite the economic slowdown, the labour market has remained robust: unemployment rates are hovering around historic lows. Many baby boomers, those born in the late 1950s and early 1960s, have retired, still enjoying the means to live and spend: labour supply now exceeds demand, especially in the US. The combination of strong labour markets and low GDP growth implied weak labour productivity growth: output per hour remained stagnant, even though employment expanded robustly.

Faster productivity growth, as labour markets normalise, "would make it possible for workers," according to Agustín Carstens, General Manager of the Bank for International Settlements, "to compensate for the reduction in real wages that many have experienced over the past two years, without a significant squeeze on corporate profits. This, in turn, would reduce the likelihood of wage-price spirals emerging". [4]

In such a framework, according to Carstens, "the path over the next six to nine months should be characterised by a continued decline in inflation, subdued but stable growth, a modest weakening of the labour market, and a gradual recovery in productivity growth. And, eventually, inflation would return to target and growth rates would converge to potential'. [5]

And indeed the stock exchanges espoused this view. Not only the US S&P has grown since the beginning of the year, but also, among others, the indices of Europe (+2.8%, Eurostoxx50), Switzerland (+1.76% SMI) and Japan (+8.4%). Of course, the real driving force was, also in January, stocks related to digitalisation and artificial intelligence, which grew by 3.5% (Nyse FANG Index).

[4] Agustìn Carstens, "Where are we on the journey towards price stability?", discorso alla Statistisch-Volkswirtschaflischen Gesellschaft (SVG), Basilea, 22 gennaio 2024.

[5] *Ibidem.*

What moved them was the belief, nurtured by Jerome Powell in late 2023, that inflation is now under control and that rates will fall soon, very soon indeed, as early as March. The Federal Reserve had indirectly announced three cuts, the market immediately discounted six. Agustín Carstens believes that among the risks that could arise is that 'the financial markets may begin to discount a more pronounced and rapid monetary easing than they should. As long-term rates have fallen recently, stock indices have rebounded, some hitting all-time highs. Housing prices have also rebounded in several economies and are not far from their highs. This would lead to a premature easing of financial conditions that could reignite inflationary pressures. [6]

Inflation will also remain a dominant theme in 2024 because “letting it restart, even if due to a temporary shock, would be an extremely risky strategy”. Deglobalisation and a return to domestic production (reshoring), geopolitical difficulties affecting international transport and energy costs as well as environmental costs will remain on the agenda. In addition, the resilience of economies will provoke claims in all those sectors that have suffered during the years of globalised liberalism and that now, by reverting to more localised and politicised approaches, are discovering privileged places to demonstrate (see the strikes in the car industry in the US and those of farmers in Europe).

Markets will continue to be buoyed by expansionary fiscal policies, albeit more moderate than in recent years. And more or less broad threats of monetary tightening will counterbalance the excesses of optimism, as witnessed by Powell's latest speech. This should help to avoid the much feared recession in the United States where, in a year in which a president is elected, there are unlikely to be any serious attempts to weaken growth, perhaps to contain the enormous public debt.

The current dynamic seems to hold. It is, however, based on a delicate geopolitical assumption. The United States, no longer an absolute but a relative power, has decided to exert all its power to dominate the growing international tensions. The markets will only believe the almost

[6] *Ibidem*.

goldilocks scenario if Washigton manages to handle the various ongoing international crises with credibility. In the Western bloc, Joe Biden's country is the only real decision-making centre. Just as in the last thirty years centred on economics, Europe was absent, now, that politics is back, Europe is even more marginal. Its genetic peacemaking function, sworn by the founding fathers of the European Union in the aftermath of the Second World War, today lacks the substance that would serve to contain the headlong rush of the powerful American ally, which in its strength also drags that digital technology that dominates the stock market and the world. This force has the inherent power, at least in the medium term, at least in 2024, to sustain that cavalcade that links political power and artificial intelligence and is reminiscent of the advent of the Internet at the turn of the millennium.

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