Luna Investment Management

The Luna Perspective

Quarterly Market Update
January 2024

The festive cheer was firmly with investment markets in the final quarter, with gains registered across most major asset classes. The catalyst being a familiar one; continued falling inflation and crucially now an expectation that the global central banks will look to ease monetary policy and reduce interest rates in 2024.

Inflation continues to moderate and has fallen significantly from the highs in 2022. In December 2023 the Consumer Price Index (CPI) data release shows that it had fallen to 3.9% from the September level of 6.7%. The main catalyst for this big fall is that energy bills are a lot lower this year compared to last. Other aspects are also starting to moderate, from goods and services to alcohol and food. Interest rates were maintained at 5.25% by the Bank of England during the final quarter, meaning three consecutive meetings of no change. Against this backdrop UK government bond yields fell and, because of their inverse relationship, bond prices subsequently increased. To highlight this, the Bloomberg Sterling Gilts Index registered a total return of over 8.5% during the quarter.

Across the pond US inflation has been quicker to fall and US CPI is now at 3.1%. The main market moving event during the quarter was in December, when the US Central Bank, the Federal Reserve, hinted towards a pivot in interest rate policy and potential cut in 2024. The Federal Reserve has indicated that it is possible interest rates will be cut three times in 2024 and will settle at 2.5% in the coming years – half of the current level. This was stimulative to the global bond market with yields falling and prices increasing.

The oil price has also eased in recent months from the highs immediately after the start of the conflict in the Middle East. There was a slight spike in December due to tankers being forced to reroute after attacks in the Red Sea but as the quarter came to an end this reversed. To highlight the fall, the Brent Oil price was over $90 at the end of September and ended the year at $77. This should be another positive on the inflation outlook.

The feel-good factor in the bond market was also evident in global equity markets, which were buoyed with markets continuing to bounce from depressed levels. The FTSE All Share delivered a total return of 3.2% during the quarter, with the S&P 500 returning 6.9% and Nikkei 225 of 6.6%. These returns have pushed major stock markets to a whisker off their all-time highs. Another encouraging sign for investors is the breadth of the rally across market capitalisation and sectors. The exception was China, with the Hang Seng retreating during the quarter; it has now been a bear market for over three years.

In summary, inflation has fallen to lower levels quickly and interest rates look to have peaked and could be heading lower in 2024. The Bank of England will want to see inflation closer to their 2% target before likely following suit and cutting interest rates. Global economic growth has been a mixed picture with strong growth in the US being offset by weaker growth in China. Closer to home, UK economic growth seems to be flat-lining at zero and with the effect of interest rates filtering through the economy in 2024 the risk of a mild recession appears to be increasing.