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Athena Financial Solutions

Is inflation transitory? And how are the markets reacting to the latest inflation data?

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**Is inflation transitory?
And how are the markets reacting to the latest inflation data?**

James Brodie C.M.T.



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- With US CPI at 5.4% YoY September 2021 (Bureau of labour statistics) and world food prices up +32.7% YOY September 2021 (United Nations), inflation is looking less and less transitory with financial markets pricing more aggressive central bank hiking cycles (UK OIS pricing 108bp hikes by Bank of England by December 2022, Bloomberg). But the U.S. federal Reserve still expect PCE inflation (personal consumption expenditure) to be 2.2% or below for 2022, 2023 and 2024 (FOMC summary of economic projections). We investigate the difference between the central banks and the financial markets expectations, and also the impact this will have on asset prices.

8th November

- ECB's Lagarde: Confident higher inflation is transitory (Bloomberg)
- FED Evans ' Much of the current surge in inflation is temporary.' (Bloomberg)
- **Central banks - please define 'transitory'!**
- Jeremy Powell "Really for us, what transitory has meant is that if something is transitory, it will not leave behind it permanently or very persistently higher inflation."

U.S. September Inflation data (released 13th October)

CPI MoM and YoY both stronger than expected in October, and PPI continues to surge in November +8.6% YoY.

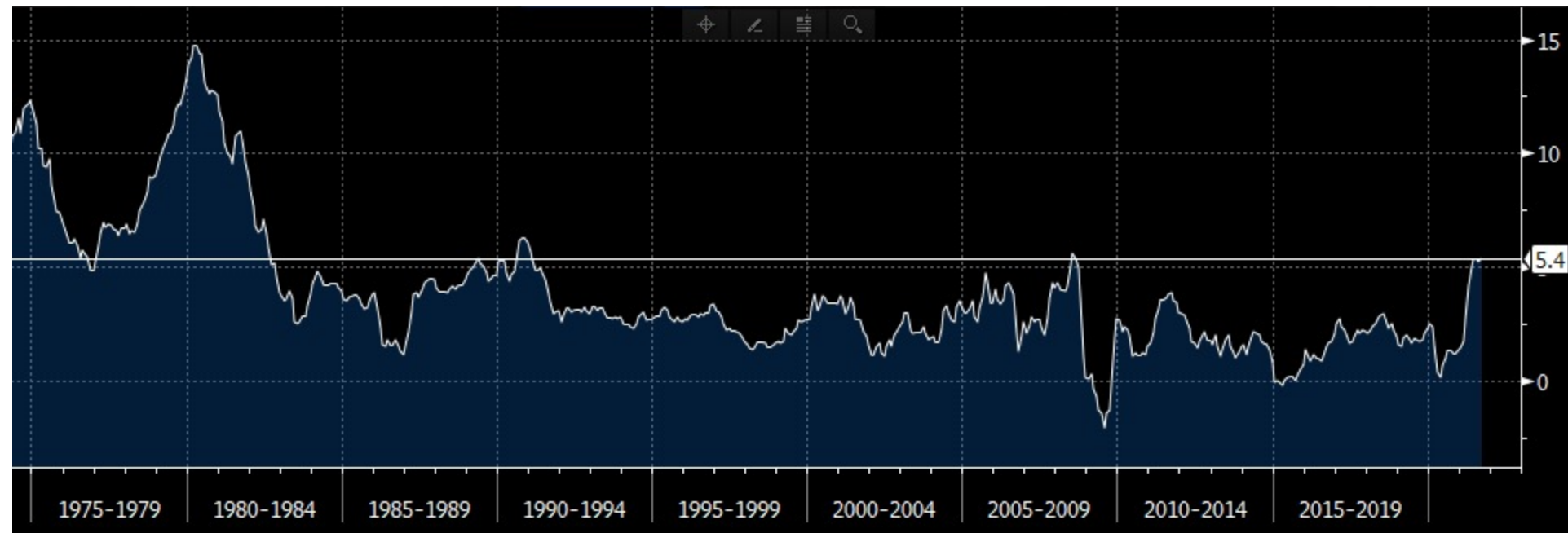
Date	Time	A	M	R	Event	Period	Surv(M)	Actual	Prior	Revised
36)	10/13 13:30				CPI MoM	Sep	0.3%	0.4%	0.3%	--
37)	10/13 13:30				CPI Ex Food and Energy MoM	Sep	0.2%	0.2%	0.1%	--
38)	10/13 13:30				CPI YoY	Sep	5.3%	5.4%	5.3%	--
39)	10/13 13:30				CPI Ex Food and Energy YoY	Sep	4.0%	4.0%	4.0%	--
40)	10/13 13:30				CPI Index NSA	Sep	274.172	274.310	273.567	--
41)	10/13 13:30				CPI Core Index SA	Sep	280.008	280.017	279.338	--
42)	10/13 13:30				Real Avg Hourly Earning YoY	Sep	--	-0.8%	-0.9%	-1.1%
43)	10/13 13:30				Real Avg Weekly Earnings YoY	Sep	--	-0.8%	-0.9%	-1.4%
44)	10/13 19:00				FOMC Meeting Minutes	Sep 22	--	--	--	--
45)	10/14 13:30				Initial Jobless Claims	Oct 9	320k	293k	326k	329k
46)	10/14 13:30				Continuing Claims	Oct 2	2670k	2593k	2714k	2727k
47)	10/14 13:30				PPI Final Demand MoM	Sep	0.6%	0.5%	0.7%	--
48)	10/14 13:30				PPI Ex Food and Energy MoM	Sep	0.5%	0.2%	0.6%	--
49)	10/14 13:30				PPI Ex Food, Energy, Trade Mo...	Sep	0.4%	0.1%	0.3%	--
50)	10/14 13:30				PPI Final Demand YoY	Sep	8.7%	8.6%	8.3%	--
51)	10/14 13:30				PPI Ex Food and Energy YoY	Sep	7.1%	6.8%	6.7%	--
52)	10/14 13:30				PPI Ex Food, Energy, Trade YoY	Sep	6.5%	5.9%	6.3%	--
53)	10/14 14:45				Langer Consumer Comfort	Oct 10	--	51.2	53.4	--
54)	10/15 13:30				Empire Manufacturing	Oct	--	--	--	--



Sources: Bloomberg, Bureau Labor Statistics

Inflation is rising?

- US CPI highest since 2008
- German import prices hit highest level since 1981
- Spain producer prices highest in 44 years at 23.6%
- Eurozone inflation hits 10-year high
- Federal reserves preferred PCE inflation gauge posting its fastest annual gain in 30 years



Source data and chart: Bloomberg US CPI

Or is it 'transitory'

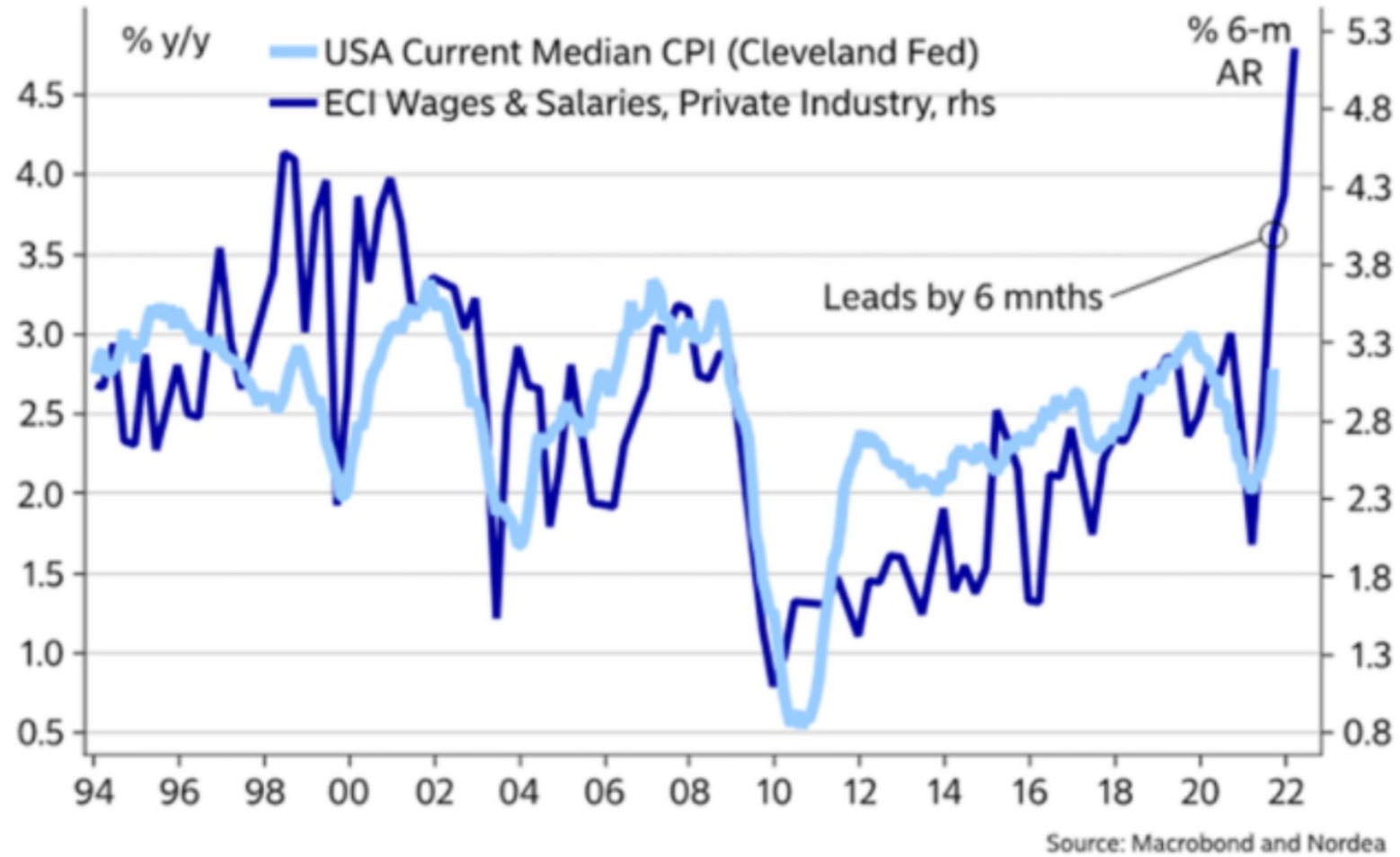
- Inflation in energy prices, food and asset prices.
- Continued supply chain bottle necks and shortages
- But many commodity prices are starting to ease
 - Global growth slowing
 - Global ISM data slowing
 - G3 credit impulse slowing
 - Chinese property sector slowing
- UK retail inflation falling consistently for 2 years (UBS).....



Source data and chart: Bloomberg, Chinese thermal coal prices

Will rising wages drag CPI higher?

Finding labour is a real problem in U.S.



Source: Macrobond and Nordea

Source: Macrobond and Nordea

Are inflation expectations driving CPI higher?

Correlations are hard to discount.



Source: Macrobond and Nordea

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ISM prices paid as a lead indicator

Will producers be able to pass on the rising price inputs?



Source: Bloomberg

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Wage inflation September NFP data



Source: Bureau labor statistics

JOLTS job openings (Nov 2021)

McKinsey – more than 19 million workers have quit their jobs since April 2021 & 3% have left the workforce

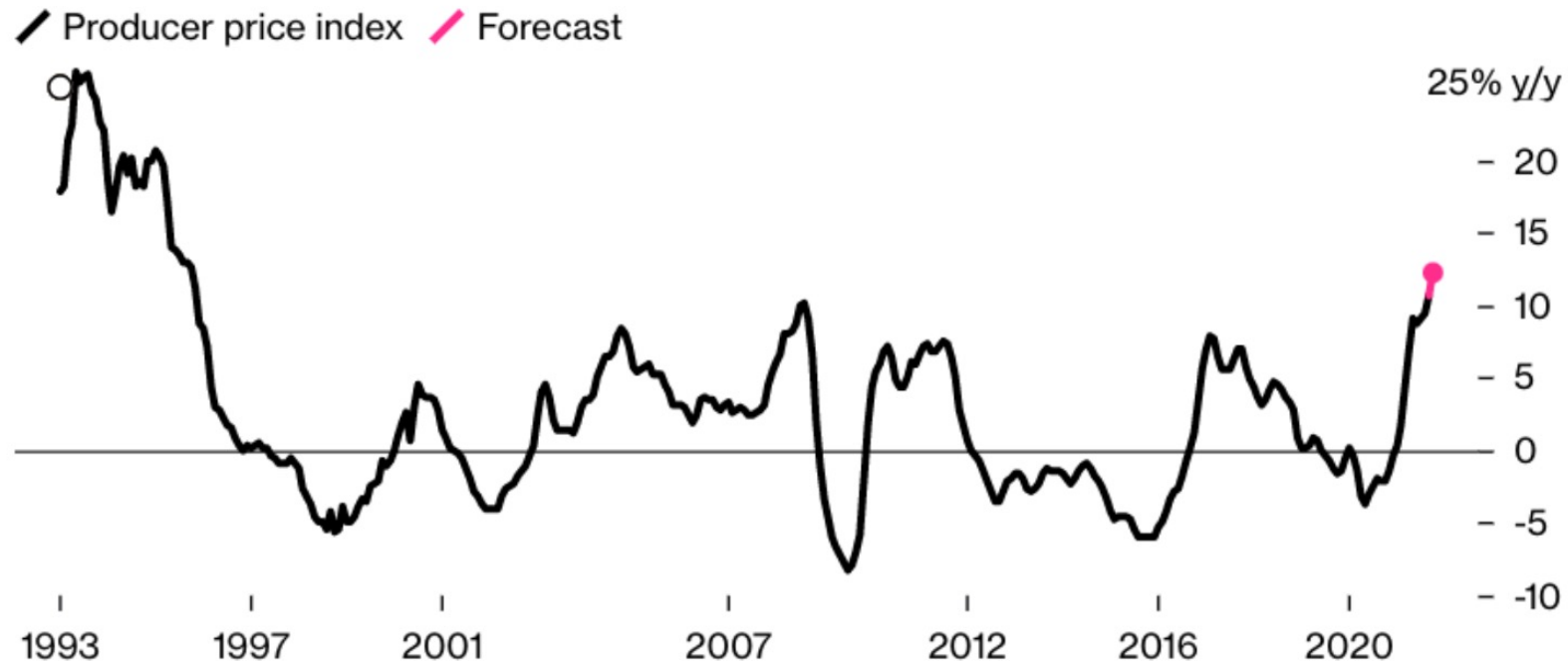


Source: McKinsey, Bloomberg

China's factory inflation soars

With electricity shortages in 19 of 36 provinces and renewed lockdowns & travel restrictions.

Price expected to have risen most since late-1995 in October



Source: China's National Bureau of Statistics, Bloomberg survey

Source: China national bureau of statistics, Bloomberg survey

United Nations World food price index – getting closer to record high

Higher food prices are positively correlated to social unrest

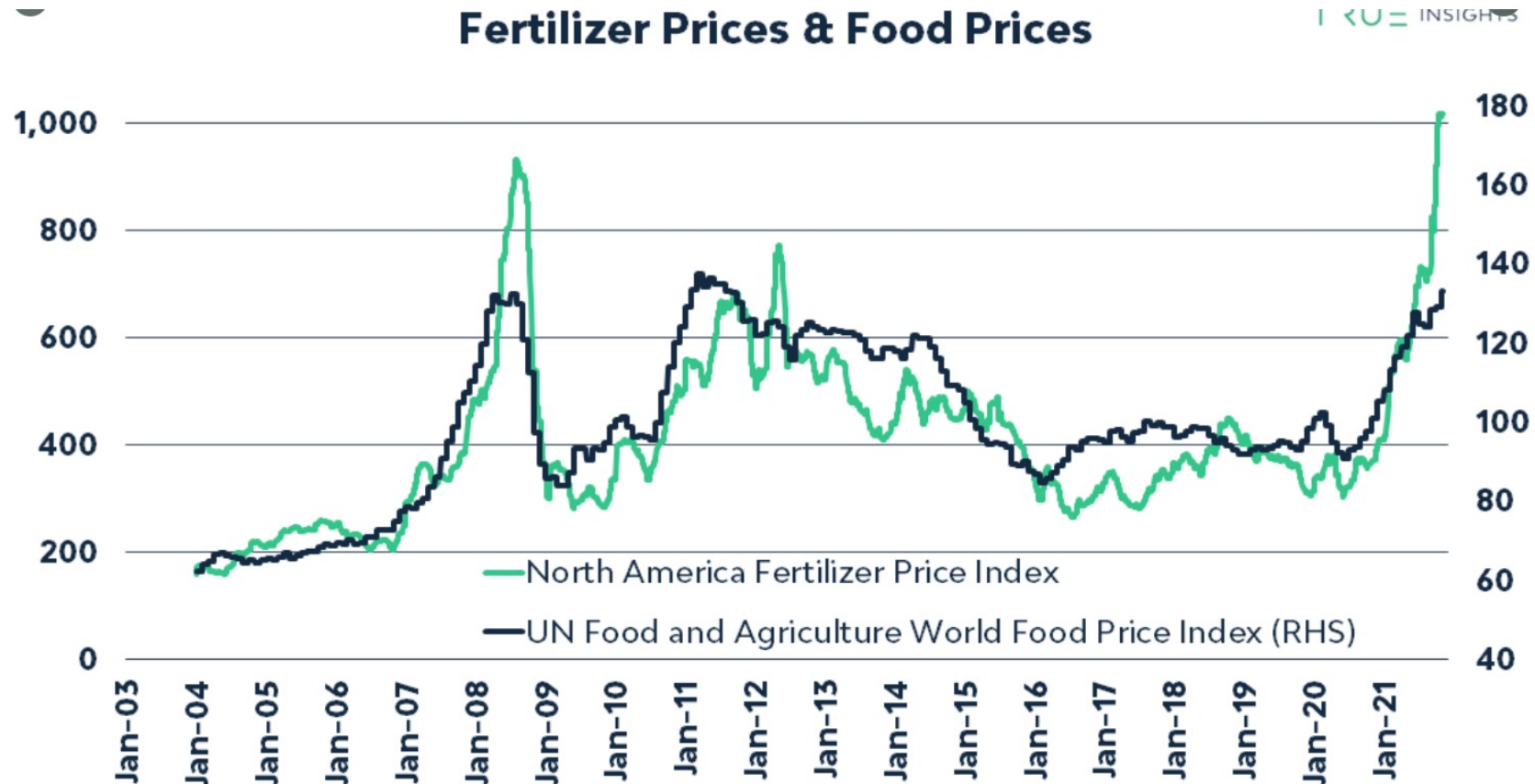


Source: Bloomberg

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Food prices & fertilizer prices

USDA – fertilizer prices have added 15% to the price of corn

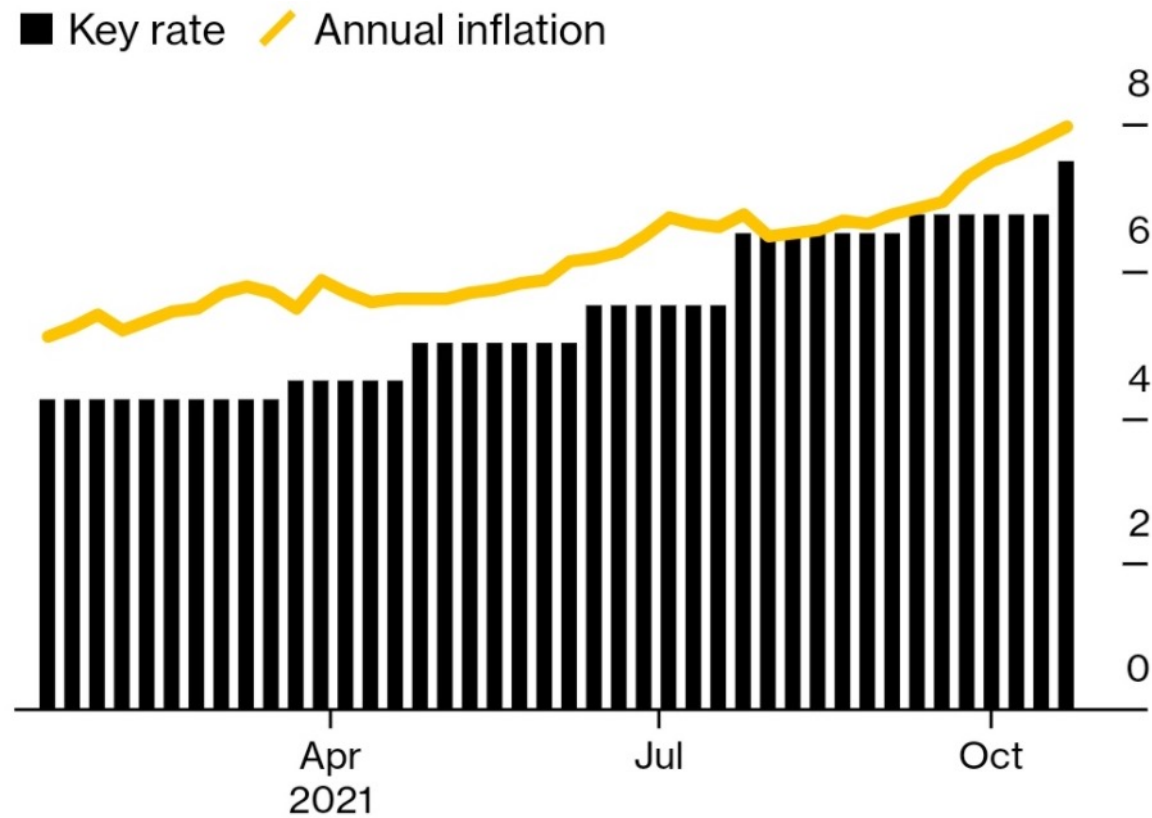


Source: True Insights, fred.stlouis.org, United Nations

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Russian inflation keeps rising despite rate hikes

Emerging markets have the added pressure of the stronger dollar



Sources: Bank of Russia, Ministry of Economy,

- Supply chain bottlenecks, lockdowns & electricity shortages
- Energy prices
- Food prices (& fertilizer)
- UK inflation expectations hit highest level in 25 years (UK office for national statistics)
- UK supply delivery times, 2nd worst on record (HIS market, CIPS)
- CAPEX for commodity producers declining 34% YoY (Bloomberg)
- 4% Americans have quit their jobs thanks to crypto gains (civicscience.com) but they are generally the lowest income brackets
- Dovish 'Taper' raising asset prices



- Shipping and commodity price spikes are mean reverting
- Global growth ISM and credit impulse slowing
- China September house sales fell 36.3% (value, YoY, China National Bureau of Statistics)
- China junk yields at all time high
- UK retail deflation (for over 2 years) (Paul Donovan, UBS)
- US Housing ?? Zillow looks to sell 7,000 homes for \$2.8 bio following algo failure (Bloomberg)

Baltic dry index



Chinese thermal coal prices



Sources: Bloomberg

Has the recovery trade peaked? Delta resurgence, supply chain constraints



J.P.Morgan Global Manufacturing PMI™

sa, >50 = improvement since previous month

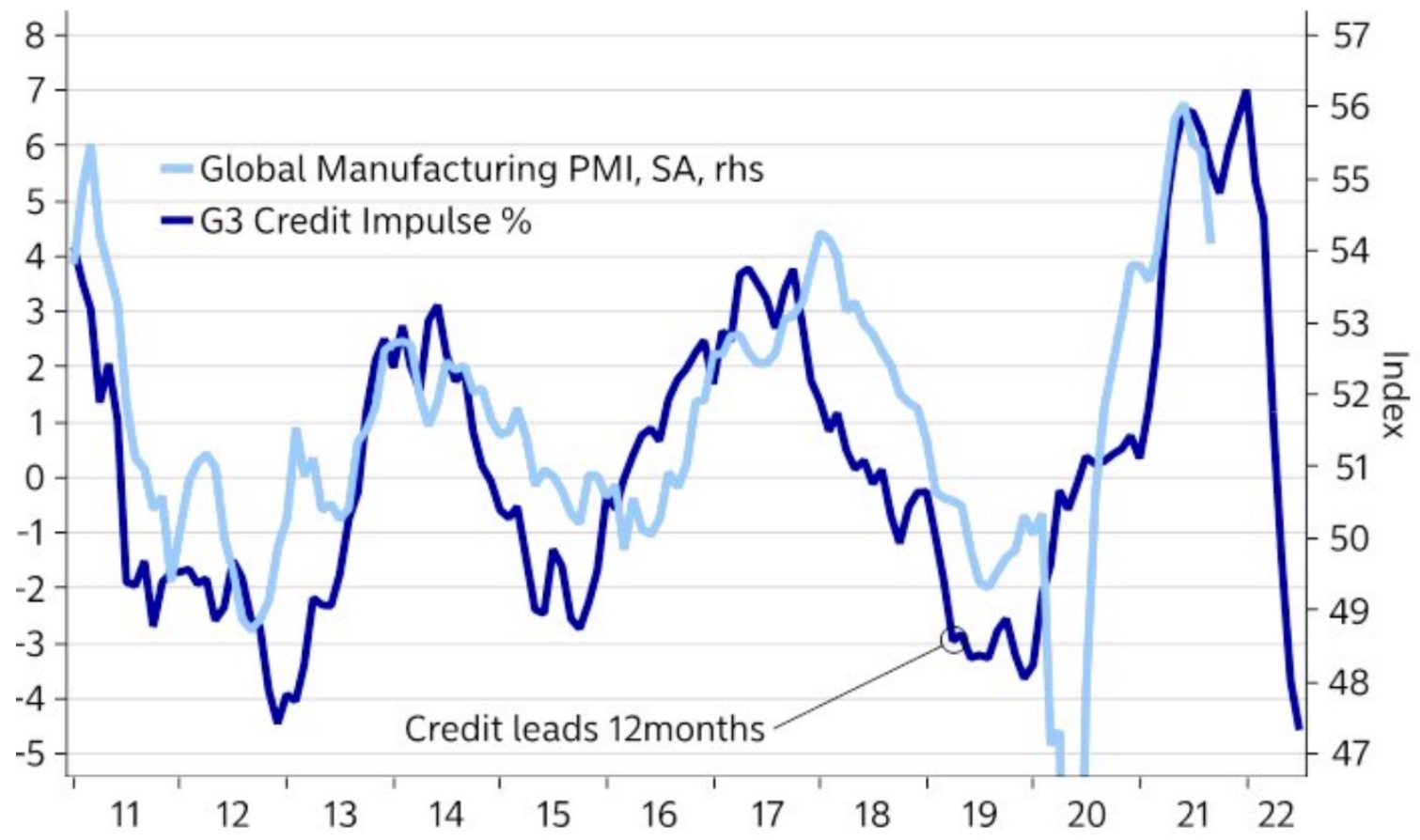


Sources: J.P.Morgan, IHS Markit.

Sources: Bloomberg, JP Morgan, HIS Markit

Deflationary forces – global credit impulse

Measures the impacts of new lending increments or acceleration of credits, to GDP growth.



Source: Macrobond and Nordea

Source: Macrobond and Nordea

Rebar (reinforcing steel)

Basic ingredient for every construction project



Source: Bloomberg

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Perhaps the most concerning data released last week

U.S. Q3 productivity plunged

- Productivity down -5.0%
- Unit labour costs up +8.3% both heading in the wrong direction

Source: Bureau of labour statistics

What do the charts say and how will the central banks reacting?

Sharp repricing of front end curves – here Australia 3yr IRS, with implications on debt and housing



Source: Bloomberg

U.S. 2yr 10yr yield spread hinting inflation IS transitory

So what do the central banks do?



Source: Bloomberg

And gold is starting to break out

\$1,831 is the key level, as real yields continue to fall.



Source: Bloomberg

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INTEUITION			HOME	COURSES	ABOUT US	CONTACT US	SIGN IN
CHAPTER 1 Introduction to fundamental analysis, technical analysis and behavioural finance The first chapter introduces fundamental analysis, technical analysis, behavioral finance and risk management. These are discussed with reference to current market structure, trends, themes and risks, immediately highlighting trading strategies and risk management techniques. <i>Duration 90 Minutes</i>	CHAPTER 1 Dow theory, intermediate trends and chart construction This tutorial looks at some key technical analysis concepts such as Dow Theory, trend lines and different chart types. Python back testing is used to support key concepts and Bloomberg charts are used to highlighting trend lines and candlestick price action. <i>Duration 50 Minutes</i>	CHAPTER 1 Building a trading process This tutorial introduces the importance of building a disciplined process using the tools and concepts covered on the course. Correlations between markets are also discussed and the first of many trading rules focusing on disciplined risk management. <i>Duration 80 Minutes</i>					
CHAPTER 2 Technical analysis concepts and trading strategies Chapter 2 continues to build on technical analysis concepts, trading strategies and risk management with a focus on Elliot wave theory, volume & open interest, Fibonacci analysis, volatility (Average True Range) and market psychology. <i>Duration 60 Minutes</i>	CHAPTER 2 Reversal patterns and trading strategies This tutorial looks at trend reversals from the perspectives of price action, market psychology and also trading strategies. <i>Duration 32 Minutes</i>	CHAPTER 2 Continuation patterns and trading strategies This tutorial looks at trend continuation patterns. Again, the focus is not so much on pattern recognition but the market psychology behind the price action, and above all identifying powerful risk/reward trading strategies. <i>Duration 56 Minutes</i>					
CHAPTER 3 Identifying trends, moving averages and trend following strategies In this tutorial we build and back test a trend following trading strategy in Python to highlight both its	CHAPTER 3 Trend following strategies In this tutorial we build and back test a trend following trading strategy in Python to highlight both its	CHAPTER 4 Oscillators, Bollinger bands and mean reverting strategies In this tutorial we discuss oscillators, Bollinger					



THANK YOU!

James Brodie



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