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Six minute strategy

Are we winning the war against inflation?

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May 2023



2023 global asset performance

Asset markets broadly stable despite US banking risks & rate rises

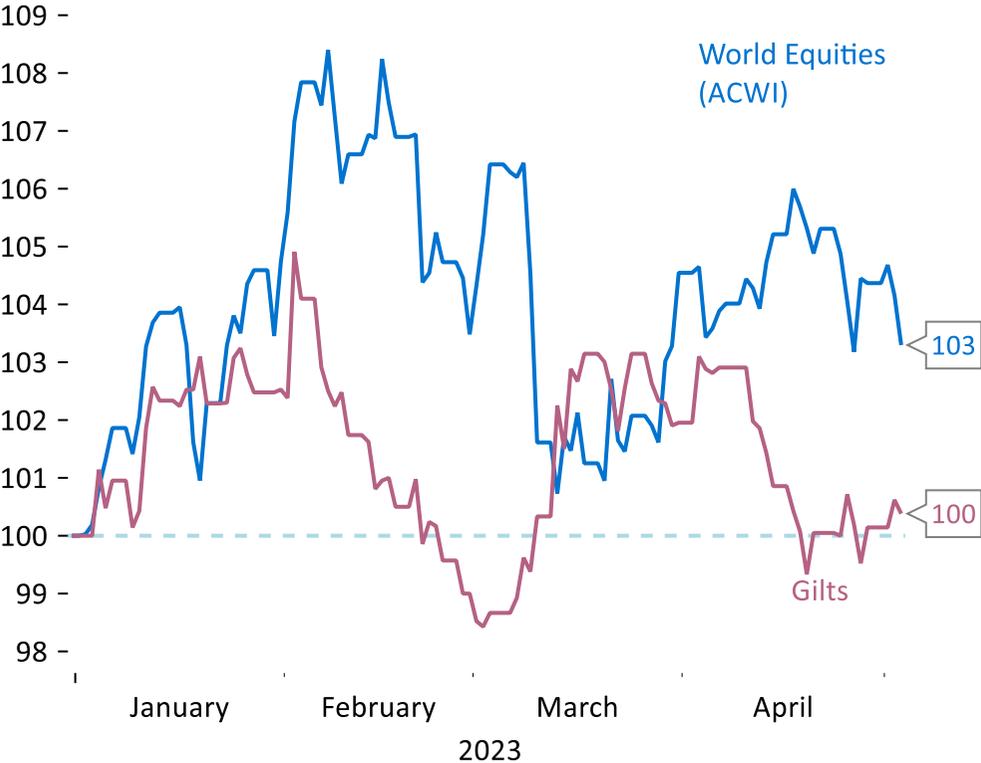


Global asset class returns stable as US rates rise



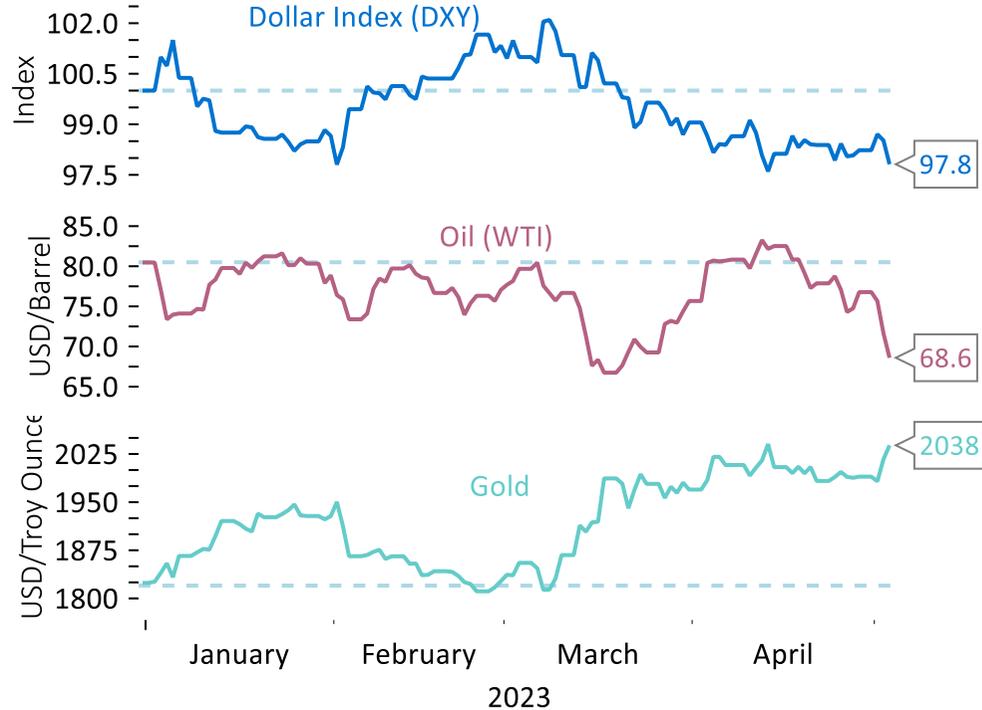
No significant dollar safe haven flows – oil recovers

Asset class performance 2023 (STG)



Source: Macrobond, 04.05.23

Asset class performance 2023



Source: Macrobond, 04.05.23

Core inflation still has not fallen yet – Why?

UK headline inflation highest in G7 – Core rates flat in Europe and US

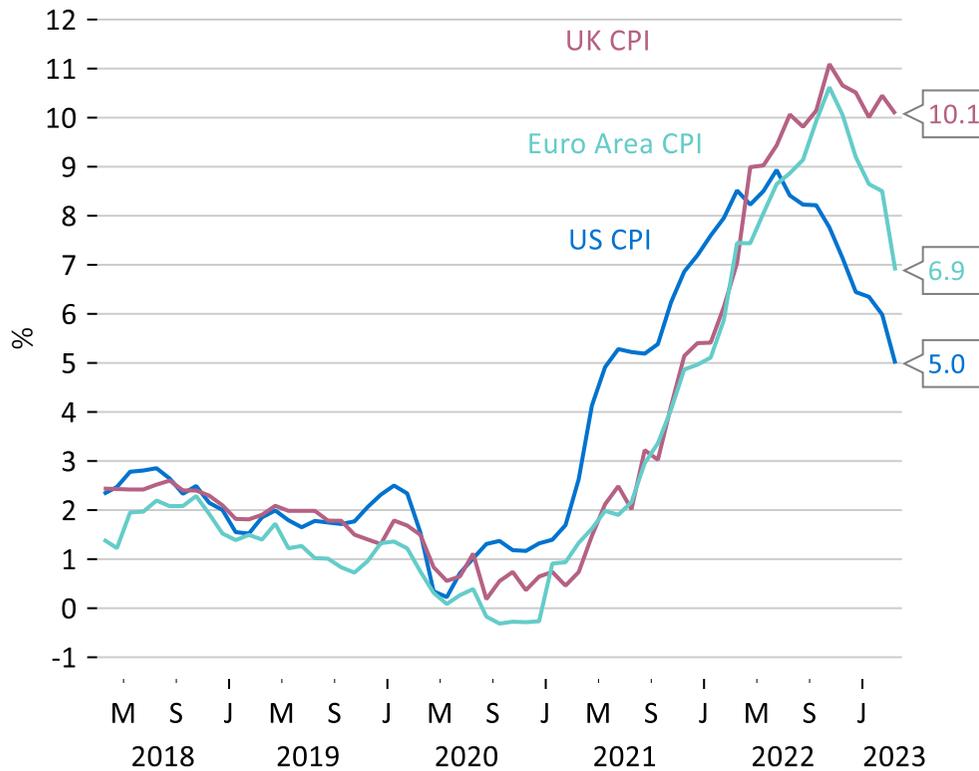


Headline inflation rates moderating except in the UK



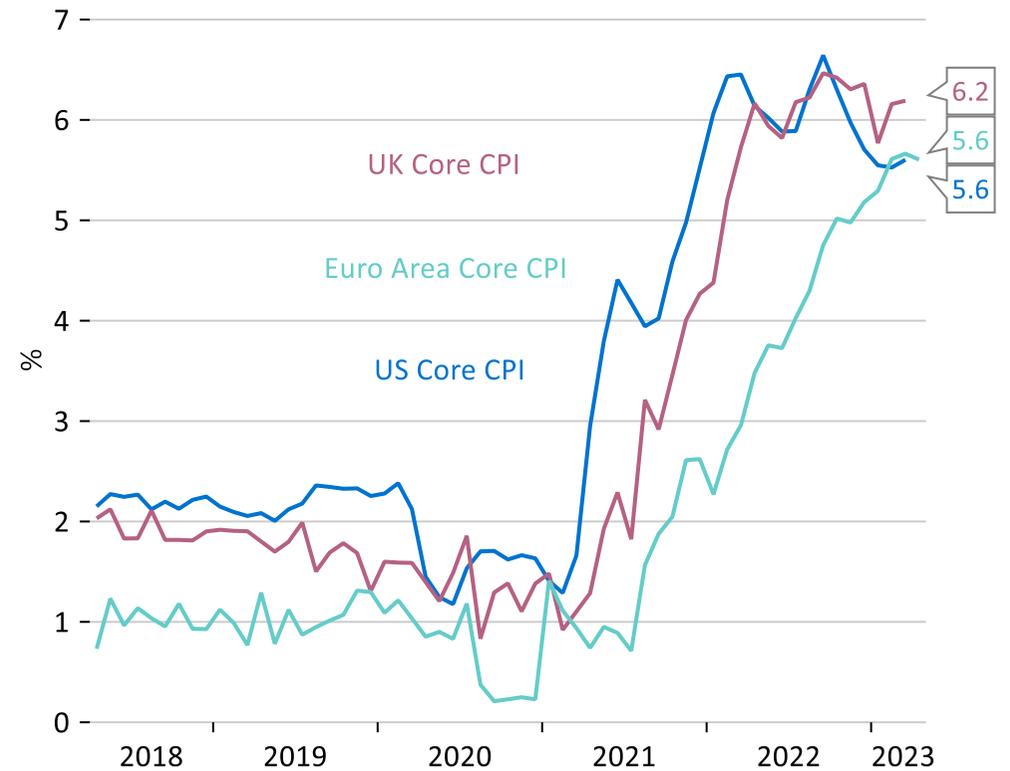
A long journey back to 2 percent...

Headline Inflation Rates



Source: Macrobond, 04.05.23

Core Inflation Rates



Source: Macrobond, 04.05.23

1.'QT' & tighter lending only now constraining activity

Shrinking central bank balance sheets & a rolling US regional banking crisis are disinflationary

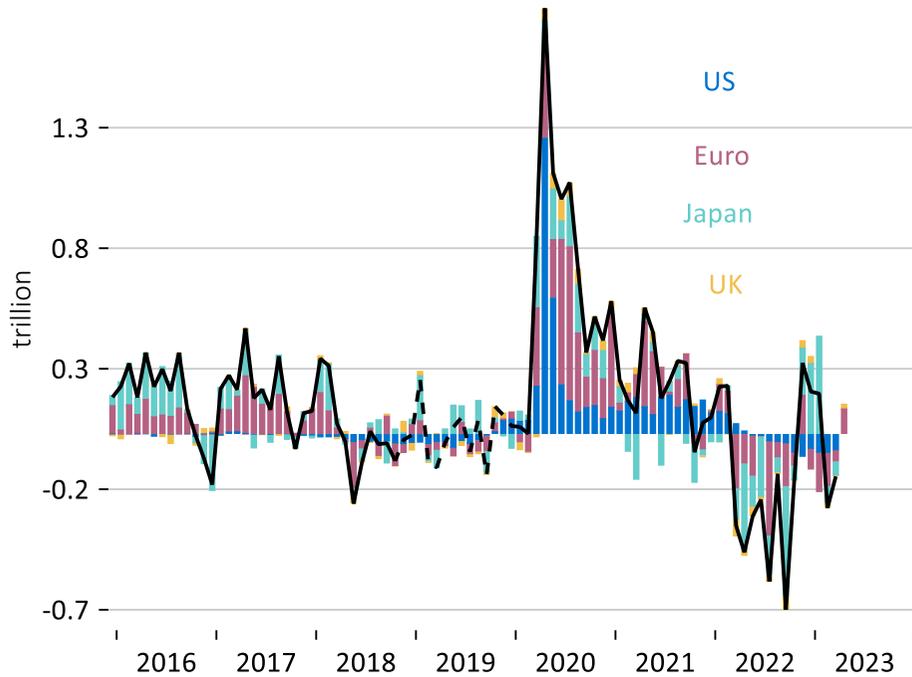


Central bank assets contract again after BoJ intervention



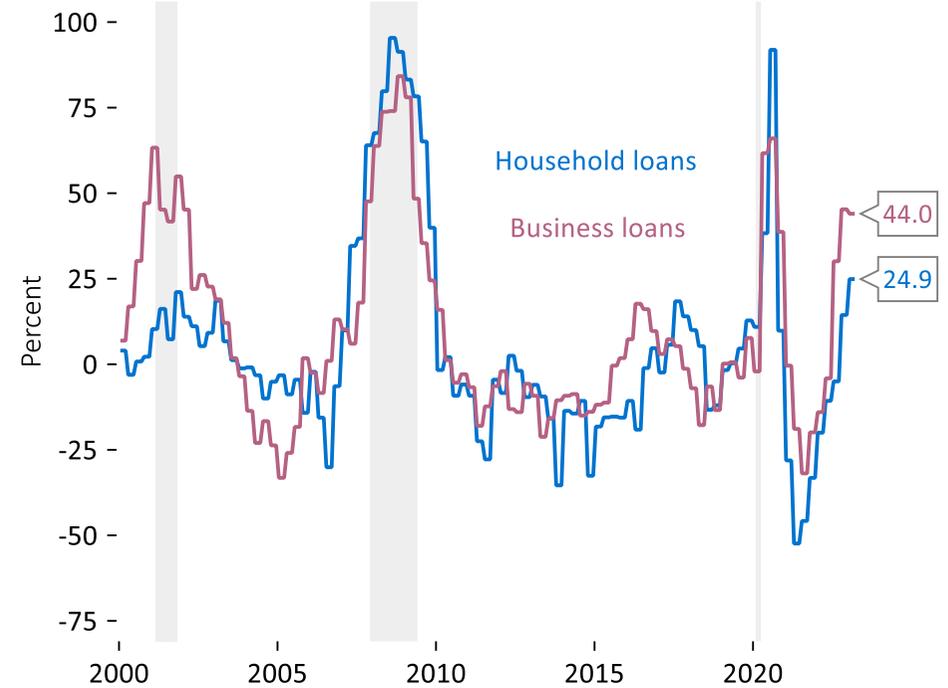
Loan conditions especially for real estate are tightening

1 month change in Central Bank Assets
USD trillion



Source: Macrobond, 04.05.23

Senior Loan Officer Survey & US Rates
Shaded = US Recessions



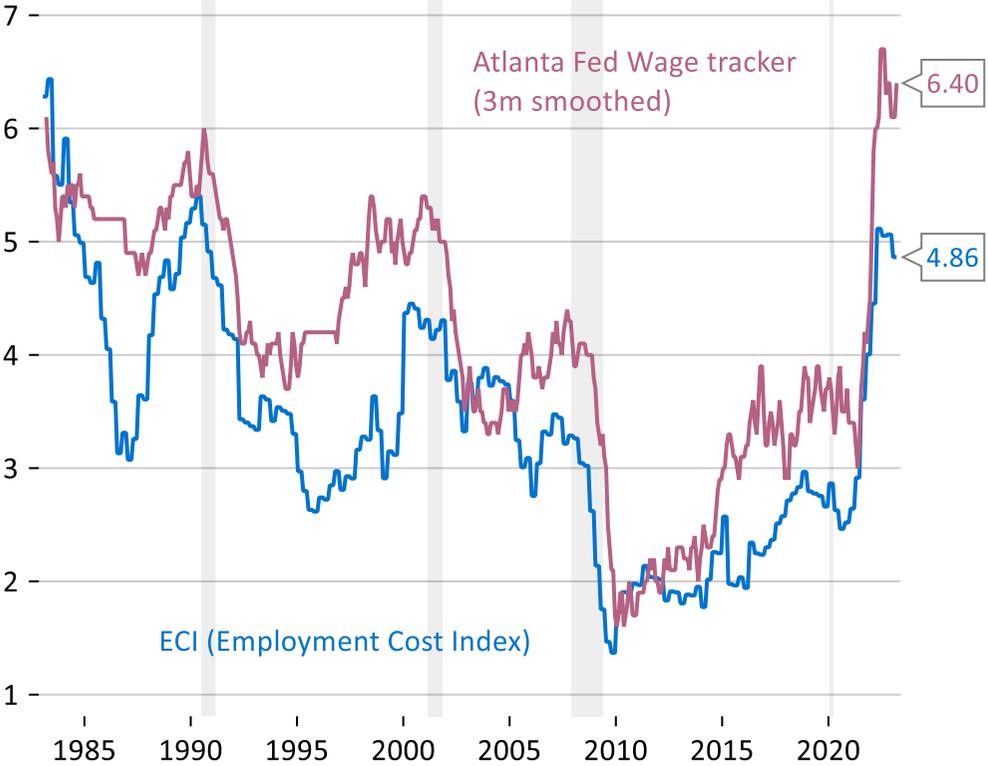
Source: Macrobond, 04.05.23

2. US wages easing only modestly - Vacancies just starting to fall

For the last 40 years a sharp fall in US wages has always been triggered by recession

US wage costs still elevated

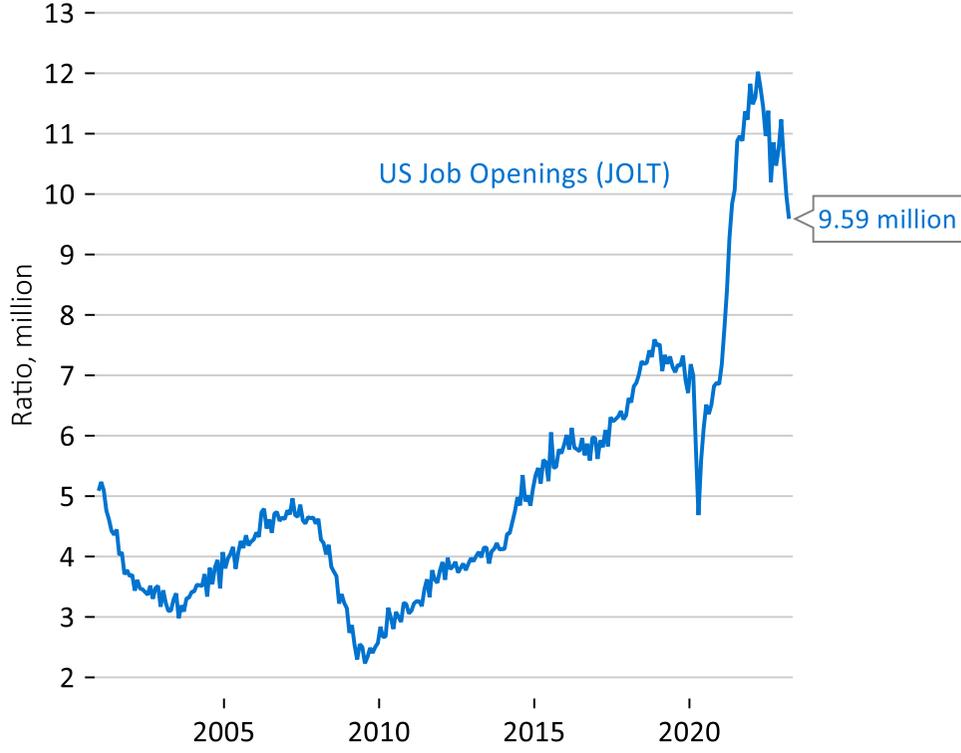
US Wage Inflation & US Recessions (shaded)



Source: Macrobond, 04.05.23

US labour market just starting to ease

US Job Openings



Source: Macrobond, 04.05.23

3. Commodities prices falling but this isn't yet helping companies

'Pricing pressures continue to plague daily operations' - ISM respondent April 2023

 Commodity price declines across industrials and foods

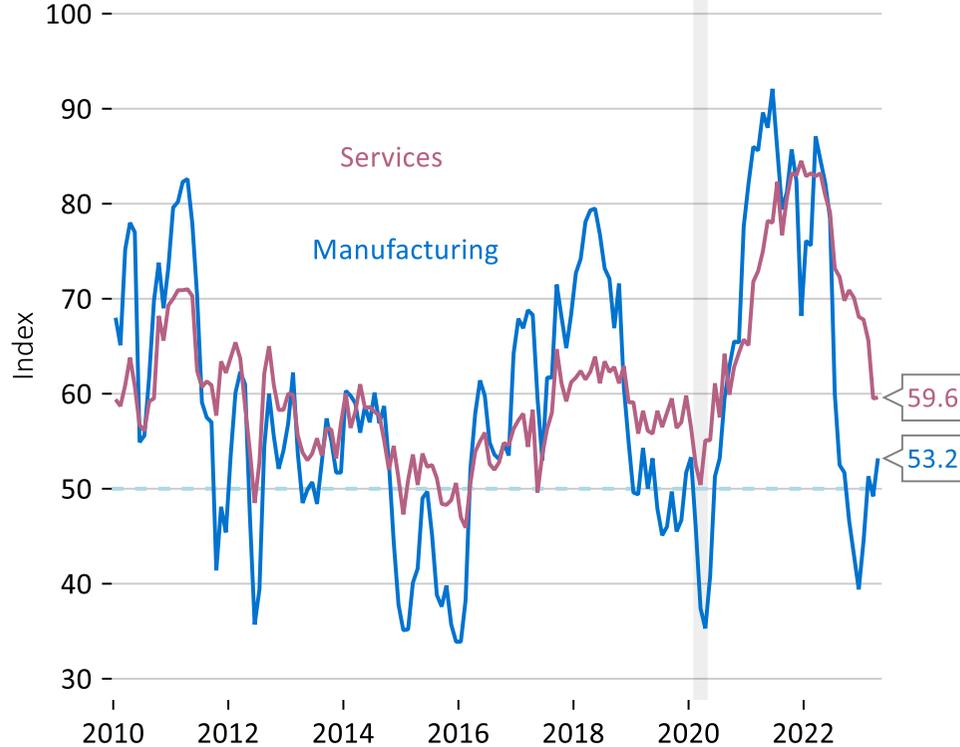
 Companies prioritising pricing over volumes – Greedflation?

World Commodity Indices, The Economist
Annual % Rate



Source: Macrobond, 04.05.23

US - ISM Prices Paid



Source: Macrobond, 04.05.23

4. UK: Headline inflation should finally start to fall

UK household energy bills reset only every 3m while food price inflation should subside

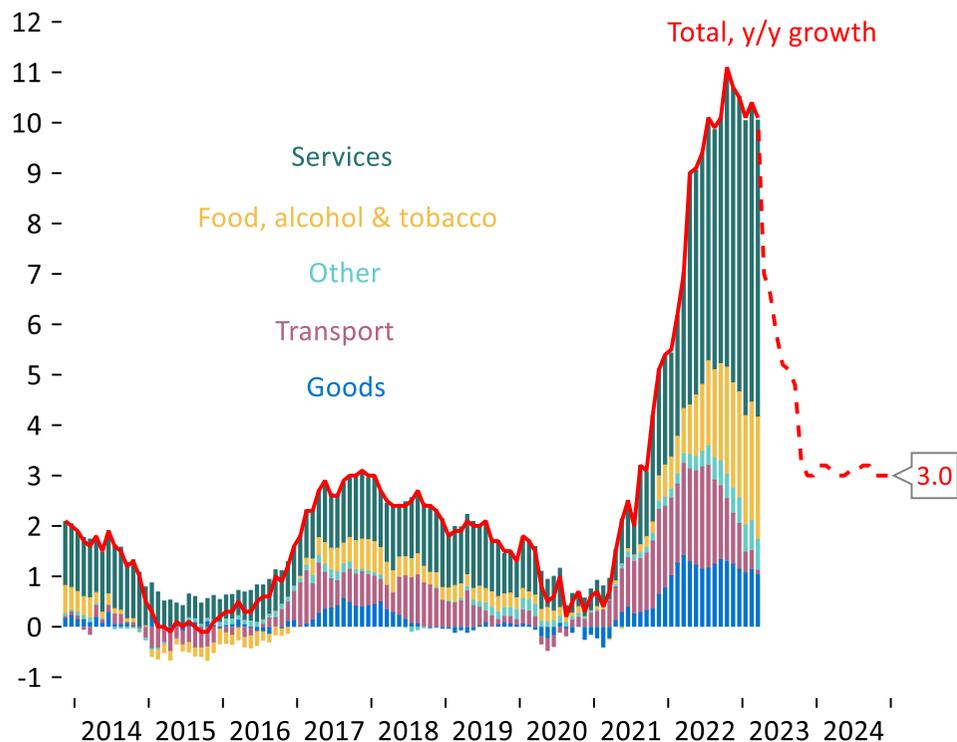


Food price inflation of 19.1% the big shock



High inflation today is driving real wage demands

UK Consumer Price Inflation

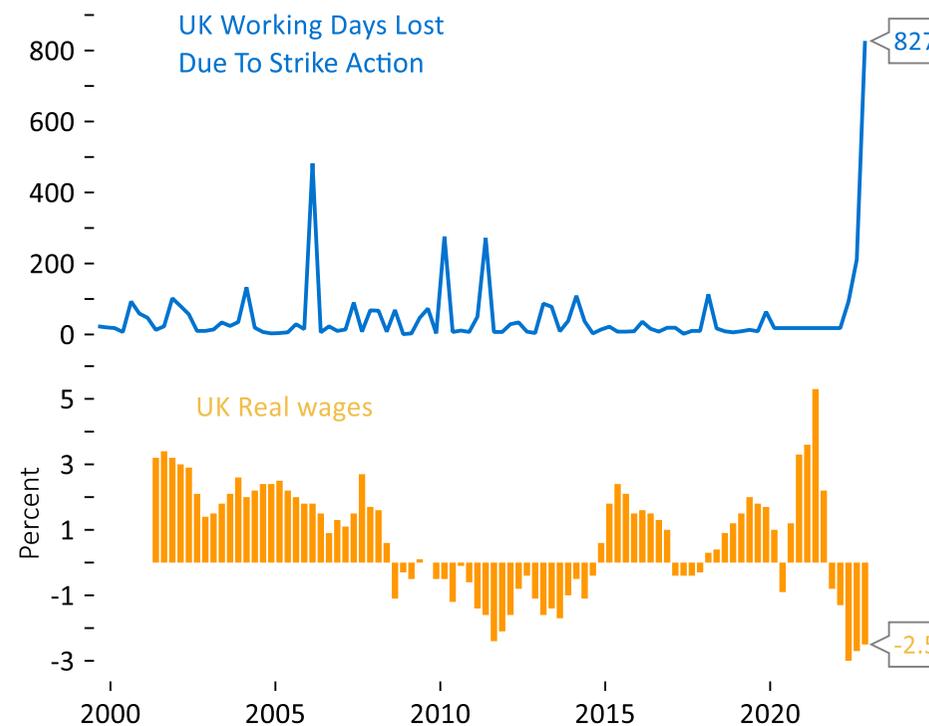


Source: Macrobond, 04.05.23

'All else equal falls in food & energy prices should lower UK inflation from 10.1% to 6% by September 2023'

Bloomberg May 2023

UK real wages & strike action (Quarterly)



Source: Macrobond, 04.05.23

Bank of England forecast of UK CPI 2024 Q1 3% & 2025 Q1 1.0%

Monetary Policy Report Feb 2023

5. UK: Stronger pound will help lower import price inflation

Focus: Sterling can rally 10% to reach (PPP) fair value – our estimate is U\$1.35

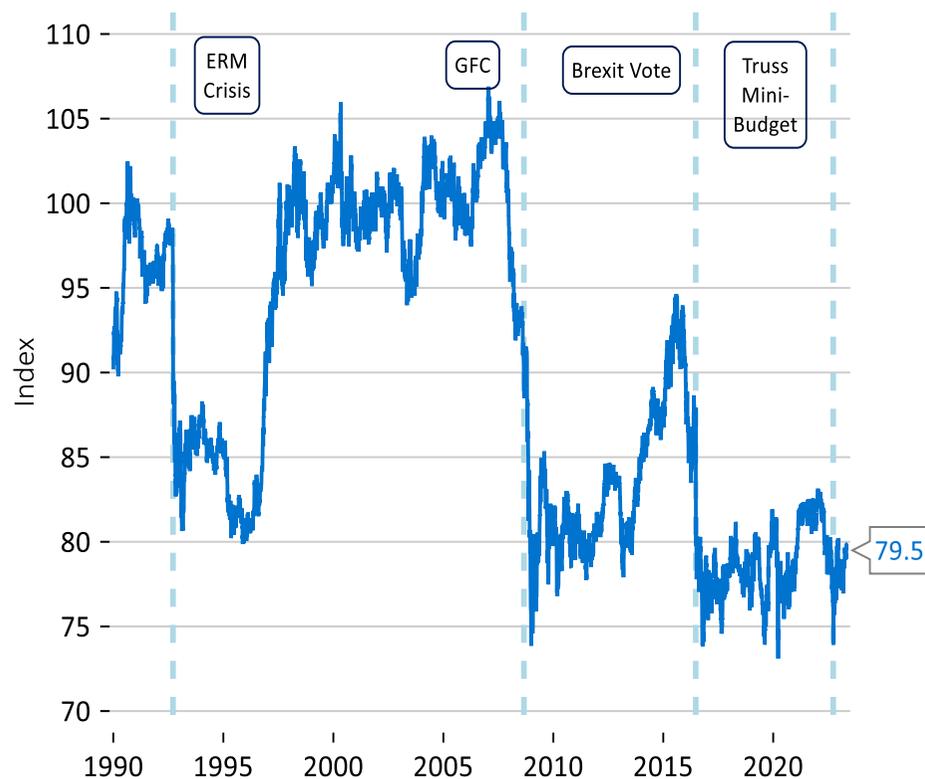


Political & financial stability should help Sterling



UK 10 year gilts now yield more than US treasuries

Sterling Trade Weighted Index (BoE)



Source: Macrobond, 04.05.23

10 Year Government Bond Spread US minus UK



Source: Macrobond, 04.05.23

'UK outlook revised to stable from negative on moderating fiscal risks' - Rating AA

S&P Global Ratings 21/4/2023

Summary: Core inflation should start declining but it's a long journey back to 2%...



Disinflationary forces argue for at least a pause in US rate rises – UK and Europe still two meetings away

1. Inflation in the **Developed World** should continue to decline in the wake of falling energy & food prices. Key risks lie in labour markets & in the pricing decisions of corporates which may not yet be passing on lower input prices ('Greedflation').
2. Tighter loan standards following the US regional banking crisis are broadly deflationary, while higher rates are now starting to impact real estate and shelter pricing. We expect the **May rate rise to be the last** as the Fed pauses & assesses the impact.
3. **UK March inflation** surprised on the upside, coming in at 10.1% instead of 9.2% forecast in the Feb inflation report. PMI's and growth have surprised on the upside while lower utility bills should help with the disinflationary trend in the second half. Around **two more 25bps rises expected from the Bank of England**.
4. **Euro area core inflation** fell to 5.6% from peak of 5.7%. Core goods fell but core services remain very sticky. Overall, growth has been more resilient and inflation more stubborn - **ECB likely to raise rates by 25bps over the next few meetings**.

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