

PANEL 2

Veranlagung im Inflationsumfeld

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CIRA Annual Conference 2022: Panel 2, „Veranlagung im Inflationsumfeld“

High Inflation, Global Growth Fragility and Market Stress?

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Kirkow
CONSULTING GmbH & Co KG

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CERCLE INVESTOR RELATIONS AUSTRIA

The “Great Reversal” into higher inflation

- *“Inflation is always and everywhere a **MONETARY** phenomenon”* (Milton Friedman), cf. stagflation of 1970s
 - Tightness of LABOUR markets – **distributional power struggles**
 - WAGE-PRICE-SPIRAL: national real income squeezed by current food and energy price shocks; **indexation** (Spain, Belgium, Brazil)
- SHRINKING WORKFORCE (demographics) and DEGLOBALISATION
 - Tilting the balance of power **BACK from capital to labour**
 - Very high **output & employment costs** of sharply rising rates
 - Massive expansion of PRIVATE & PUBLIC SECTOR DEBT
- DEBT TRAP raises issue of CENTRAL BANKING POLITICS
 - **Modest recession** is price worth paying („soft landing“)?
 - Risk of **new financial crisis**: HIGH DEBT + QUANT. TIGHTENING

Labour Market Cooldown

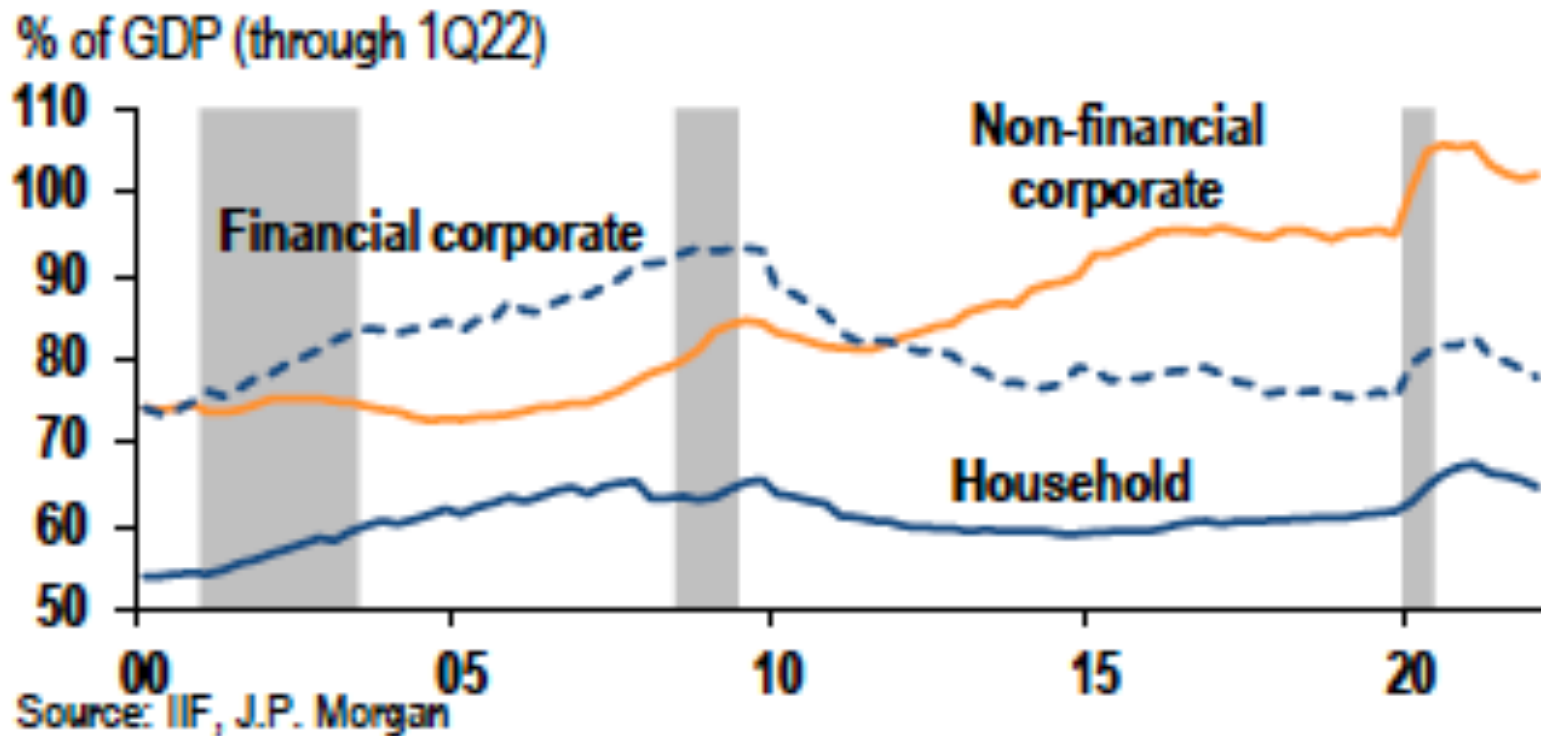
US labour market reports historic drop in job openings

Change in monthly job openings, millions, past 10 years



Sources: @_PeterWells, Refinitiv
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The Sharp Rise of Global Debt



How portfolios might cope in downturn?

- GROWTH/TECH STOCKS especially **susceptible to higher interest rates**
 - Diminish potential future returns, indiscriminate market sell-off
 - **Multi-year strategy** to ride out short-term volatility
 - SHORT TERM: reduce duration of investments (profits, cash flow)
- Reviewing BUSINESS MODELS towards **resilience & adaptability**
 - **Cash-generative** with market share, pricing power and less exposure to decline in consumer spending („recession proof“)
 - LONG TERM: massive investments in **intangibles, acquisitions and radical restructuring** – most VALUE FIRMS can't afford
- COMPANY EXPOSURE to **US-Dollar, China & Emerging Markets**
 - EUROPE: minimise structural damage due to HIGHER ENERGY COSTS
 - CHINA: political trap of Covid „lives-versus-livelihoods“

Growth vs Value Stocks

Growth investors' easy climb runs into trouble

Growth & Value indices on MSCI World index, \$ terms (Jan 1 2007 = 100)



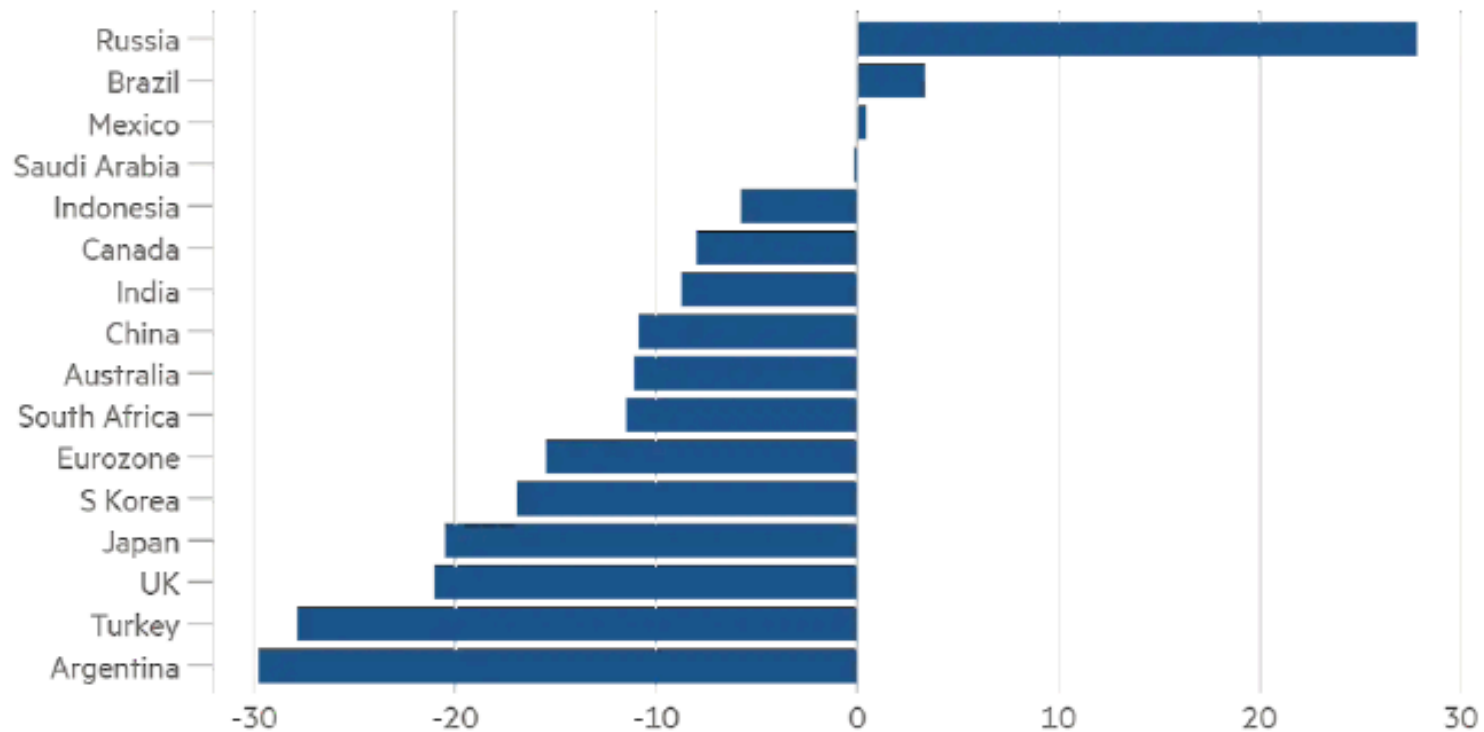
Source: Refinitiv
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Source: "After the tech sell-off: will growth investors keep the faith?," *Financial Times*, September 14 2022

The Strength of the US-Dollar

Nearly all G20 currencies have fallen against the US dollar

Currency change vs US\$ since Dec 31 2021 (G20 economies, %)



Source: Refinitiv
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"Why the strength of the dollar matters", Financial Times, September 27 2022

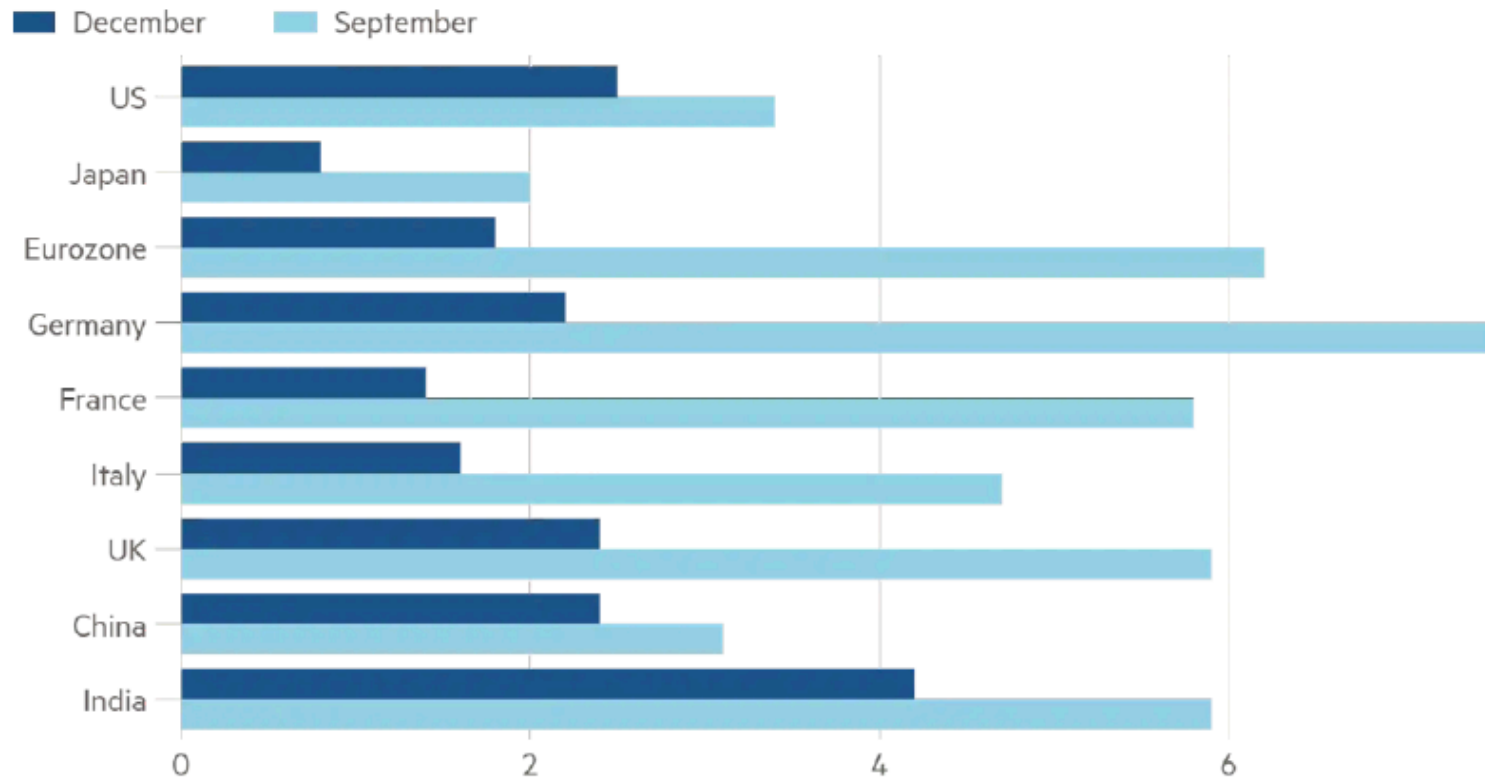
The illusion of investor knowledge?

- MODELS & FORECASTS as **standard practice** in investment industry
 - Models consist of ASSUMPTIONS, relationships and responses
 - COMPLEXITY necessitates **simplified assumptions**
 - **Predict behaviour** influenced by PSYCHOLOGY
- LIMITATIONS OF STATIONARITY: *“the past is statistical guide to future”*
 - **Extrapolation** forecasts – reflected in market prices
 - **Deviation** forecasts – potentially profitable but rarely correct
- WHY MAKE FORECASTS if they are **so easily rendered inaccurate?**
 - PROPER GOAL OF INVESTORS: *“do the best possible job in the absence of that knowledge”* (Howard Marks, Oaktree Capital Mgmt)
 - Time to **differentiate active fund management** vs passive?

Changing Inflation Forecasts

Inflation forecasts are worsening across the board

OECD forecasts for CPI inflation in 2023 (%)



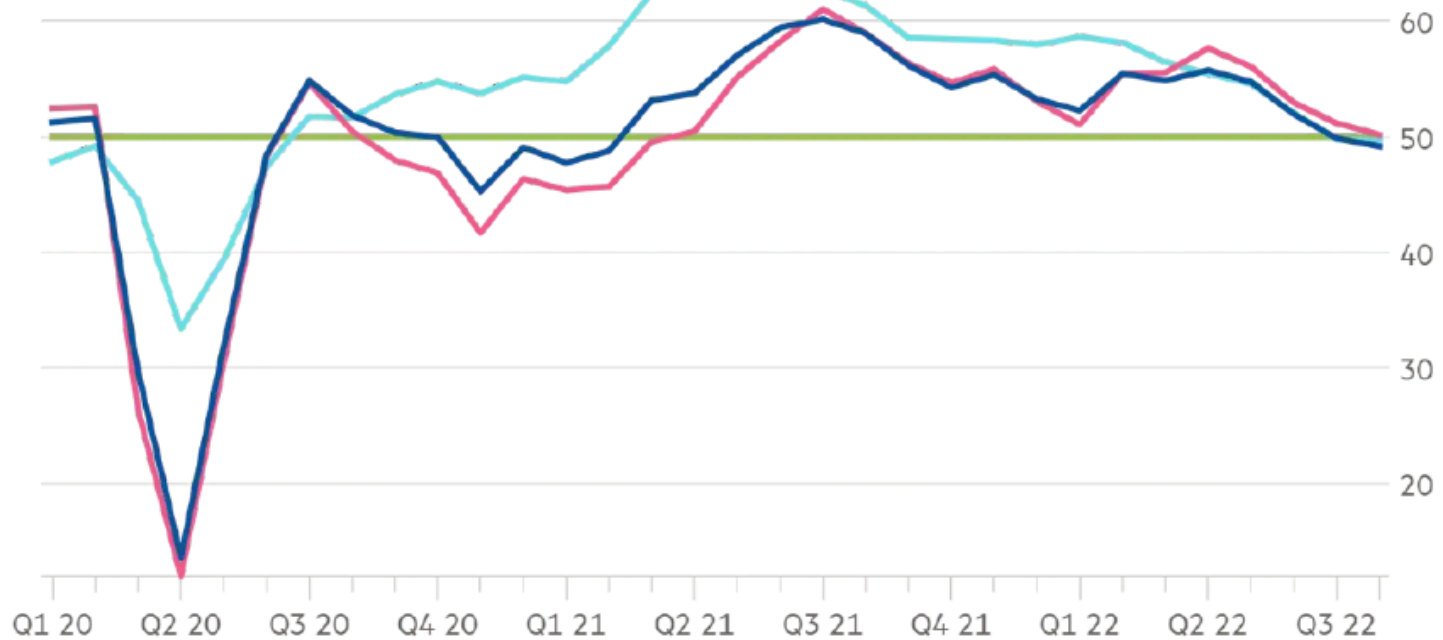
Source: OECD
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Eurozone PMI

Recession fears rise as business activity runs out of steam

Eurozone purchasing managers' index

Composite Services Manufacturing
The 50 mark separates growth from contraction



Source: S&P Global
© FT

List of Literature

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