June 2021

The Inflation Debate

The topic of “inflation” has dominated the conversation within markets since the start of the year. The reopening of economies has created a demand shock that occurred at a time when inventory levels were low across many sectors. The outcome has been price increases across the spectrum with food prices showing their largest increases in a decade, oil prices on an upward path, with many commentors calling for $100 oil and headline grabbing price spikes in critical inputs to the global economy such as iron ore, lumber and semiconductors. This has led to a debate as to whether this inflation is transitory and will calm down to a sustainable level as economies normalise or are we about to enter an era of stagflation similar to the 1970’s. The most important element of the inflation debate is that it has moved on from where it has been for much of the last 15 years which was whether the low inflation environment would become deflationary. Now the debate is what type of inflation and how much.

The argument for inflation being transitory at the moment holds a lot of weight as the price spikes that have occurred are largely explained by supply and demand shocks which will largely abate over the next 6-12 months. Central banks had appeared to be of the view that the current inflationary pressures were temporary and were willing to be “behind the curve”. However, a question mark was placed over central banks thinking recently as the Federal Reserve (the Fed),appeared to be prepared to speed up its rate normalisation/raising timetable with the first rate rise for this cycle set to be in 2023 instead of 2024. This caused tremors across financial markets and long-term yields fell as investors began to ask if the Fed would move away from its easy monetary policy in order to tackle higher inflation.

It’s likely market participants are reading too much into the recent move in the dot plots by the Fed. Central banks still remain on track to wait for inflation to pick up for a sustained period before raising interest rates materially. The question that has to be answered is not whether the current inflationary spikes that we are seeing are temporary but rather whether the conditions are in place for a sustained pickup in inflation after economies have been restored to post-covid normalisation, whatever that may look like. For the last year, we have argued that the response to the global pandemic in the form of increased fiscal policy and increased stimulus by central bankers was set to usher in a more reflationary economic cycle than the one that followed the financial crisis. Everything that we have seen over the last twelve months supports this. We expect the argument for a more reflationary cycle to strengthen as consumers spend their pent-up savings and this

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along with central bank support and increased levels of government spending creates an environment where corporates are willing to invest in their businesses and banks are willing to lend. In effect, we are expecting the velocity of money within the economy to accelerate.

As we enter this new reflationary cycle, the risks are different than the previous cycle. The first risk is obvious, holding the wrong assets. The assets that worked in the last disinflationary cycle, most notably fixed income bonds and growth stocks can't work in an inflationary cycle. The second risk is that inflation runs out of control, forcing central banks to raise rates and end the cycle prematurely. We believe we are a long way off this and the likelihood is that we will be in a reflationary cycle for years before such an end game materialises. It is, however, a risk and one that we monitor and stay ready to act upon.

The opportunities are also different this time around. The opportunity for investors through the last cycle was that the backdrop of low inflation, low growth and low interest rates would continue, boosting asset valuations (or some may say creating asset bubbles). The opportunity through the next cycle is for substantial appreciation to occur in areas of the market that benefit from inflation. These include commodities, financial stocks and industrial stocks. The Inflationary assets have been working for the last twelve months and we expect that to continue.

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Appian
Asset Management

Monthly Monitor

Appian AM NAV's Fund Prices 30-05-2021

NAV		MTD	QTD	YTD	SI
		%	%	%	%
AMAF	171.6770	0.89%	1.06%	9.85%	71.68%
AGDGF	234.7325	1.45%	1.98%	18.03%	134.73%
AGSCOF	231.6201	1.59%	6.36%	20.83%	131.62%
AIF	131.3781	2.68%	3.79%	11.13%	31.38%
AELF	102.5117	-	-	-0.53%	2.51%
ABPF	126.69	-	-	2.44%	26.69%

Appian Asset Management Limited is regulated by the Central Bank of Ireland.

Warnings

- **If you invest in any of the funds you may lose some or all of the money you invest.**
- **Past performance is not a reliable guide to future performance.**
- **Appian Funds may be affected by changes in currency exchange rates**
- **The value of your investment may go down as well as up.**

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