

Running Hot – Will the Inflation Run Last?

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Consumers have only had to look at the gas pump or local grocery store the past few weeks to notice the increase in inflation and consumer prices. It seems like everything has gone up – consider:

- The U.S. consumer price index (excluding food and fuel) jumped by the most since the 1980s.
- The Canadian inflation numbers that followed suit were comparably high.
- Resources from cars and lumber to copper and oil have gone up in price.
- Producer prices – the input costs of components for goods producers – spiked.
- Wage inflation – a leading indicator of consumer price inflation – is accelerating.

The good news is our portfolios have benefited from exposure to inflation-sensitive areas like resources and other real assets, as well as underweight exposure to fixed income. Now the big question is – will this inflation be temporary as the U.S. Federal Reserve suggests?

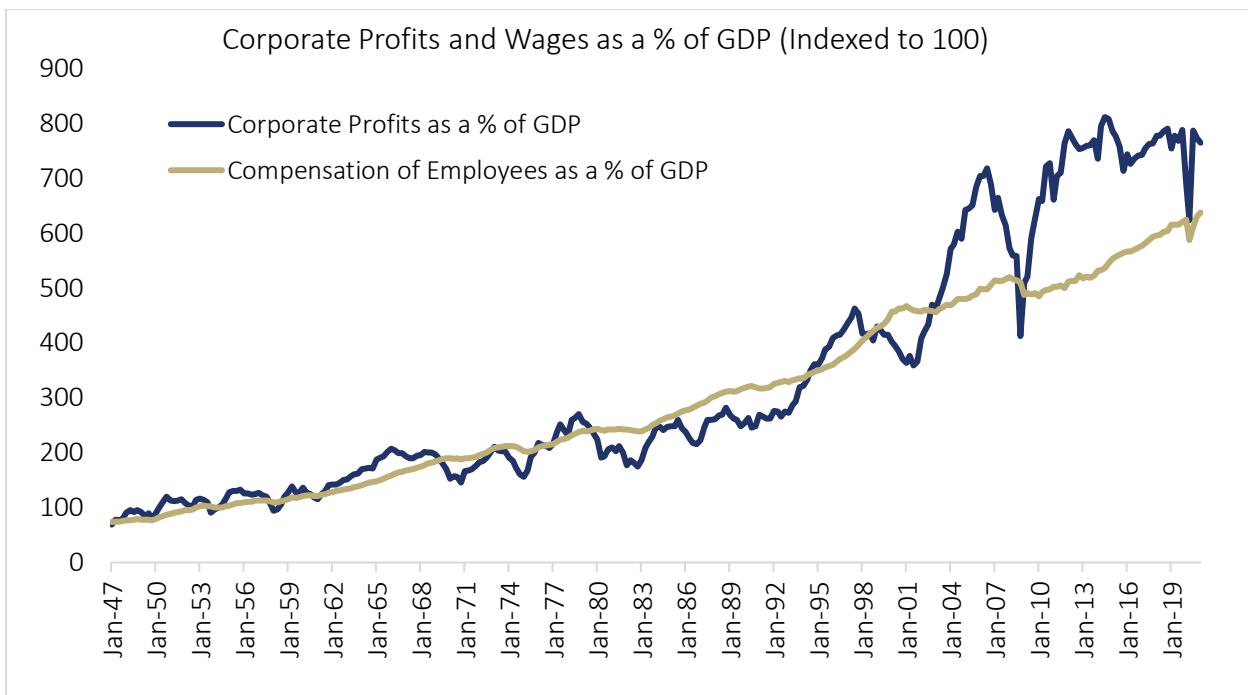
What drives inflation?

Before we answer the pending question, let's analyze the driving forces behind inflation:

1. **Scarce goods** – The shutdown of manufacturing and fast rebound have caused shortages of almost everything. In some cases, production can be ramped up quickly, but in other areas, like semiconductors, expanding capacity will take time if new factories need to be built.
2. **Scarce workers** – Employment reports show labour shortages are widespread. Some of this is due to unemployment benefits that are set to expire. Labour shortages should also recede as children return to school and health concerns subside as more people are vaccinated.
3. **Excess demand** – It's clear pent-up demand from lockdowns and excess savings (either from stimulus checks or reduced spending habits) are feeding demand. While unemployment benefits may stay elevated compared to the past, it's unlikely broad stimulus checks will continue indefinitely. The focus of major spending programs is shifting to things like infrastructure, which are still supportive of inflation.

How long will this run last?

While the price pressures from scarce goods and pent-up demand are clearly transitory, wage gains could drive things further. However, it's hard to imagine a sustained wage-price spiral where increasing wages lead to a vicious cycle of rising consumer prices and labour costs. One of the biggest reasons is the continued digitalization of the economy. While innovation creates new industries and jobs, there is increasing support for the view that the benefits are not evenly distributed.



Source: Federal Reserve Bank of St. Louis as at January 1, 2021

Monetary policy has a large role to play as well. Clearly, the U.S. Federal Reserve is letting the economy run hot, emphasizing that 2% is no longer a ceiling but an average inflation target. We are closely monitoring the situation as aggressive policy stimulus combines with rapid economic growth like almost no other time in history. Overall, we expect inflation to peak this year, but remain elevated for years to come.

One point worth making is that even if the pace of price increases slow, prices are still going up in the long run. That means the best time to invest is yesterday, as the adage goes. Cash that generates no income is not offsetting inflation. We continue to use our portfolios' flexibility to tactically allocate assets within our risk budgets and protect our investors' purchasing power. As investors, asset price inflation is one type of inflation you should welcome.

Combined top 15 equity holdings as of May 31, 2021 of the Assante Private Portfolios 40i60e Standard portfolio with Alpha-style exposure:

1. Microsoft Corp.	6. Mastercard Incorporated	11. Taiwan Semiconductor Manufact. Co Ltd.
2. Amazon.com Inc.	7. Alphabet Inc. (Class C)	12. Canadian Tire Corporation Ltd.
3. Alphabet Inc. (Class A)	8. Intact Financial Corp.	13. Prologis Inc.
4. Brookfield Asset Management Inc.	9. Facebook Inc.	14. Booking Holdings Inc
5. Royal Bank of Canada	10. Apple Inc.	15. iA Financial Corporation

Source: Bloomberg Finance L.P. and CI Global Asset Management as at May 31, 2021.



For more information, we encourage you to speak to your advisor or visit us at assante.com

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