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Weekly Market Commentary
June 13th, 2022

Inflation Runs Hot Again…What Does It Mean?

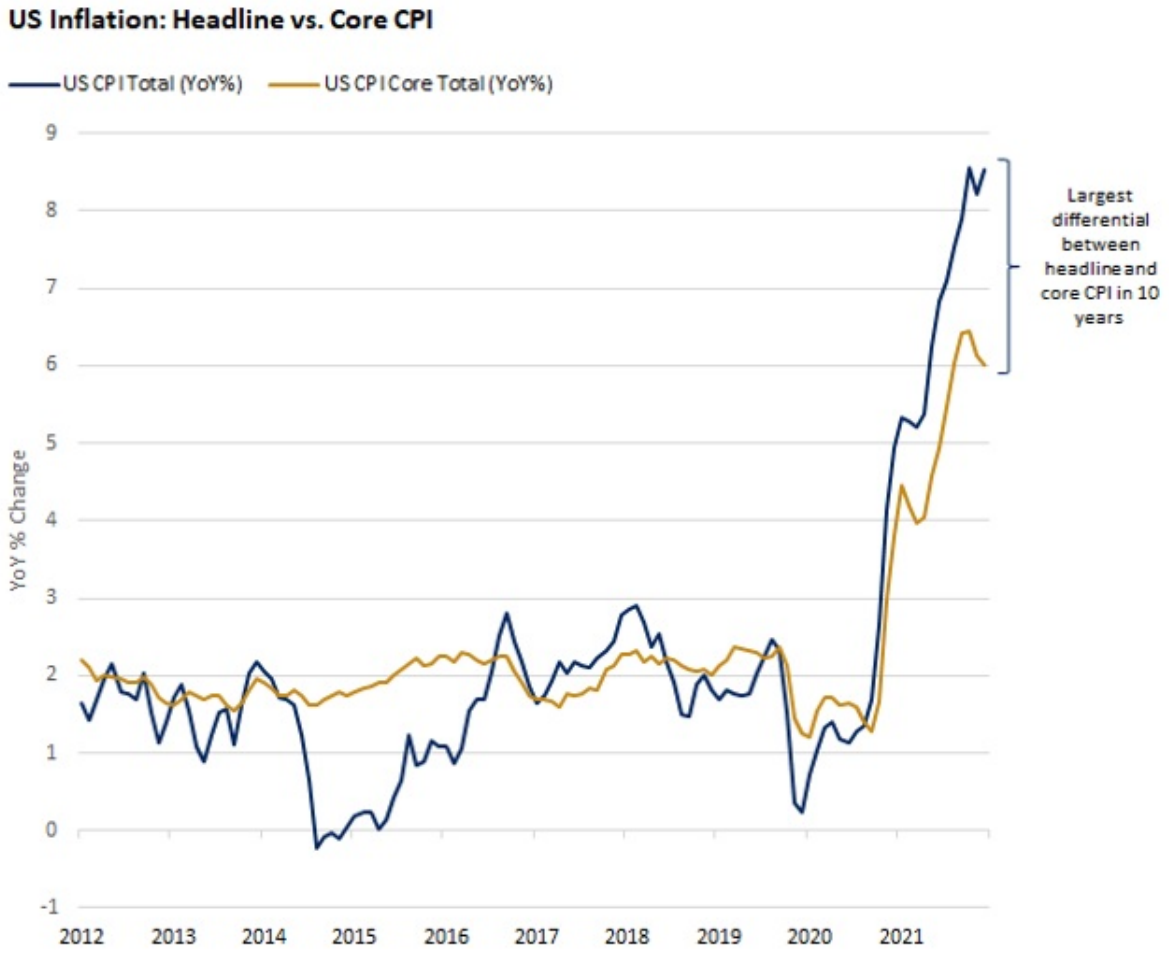
This week the biggest market-moving economic data arrived on Friday, with the release of the U.S. consumer price index (CPI) inflation reading for the month of May. The inflation data broadly came in hotter than expectations, with the headline figure coming in at 8.6% year-over-year, above expectations of 8.2%, while core CPI (excluding food and energy) came in at 6.0%, slightly above the 5.9% forecast.

While markets fell nearly 5% this week as risks to growth rise, we do not believe a recession is inevitable here, and with the market pullback already pricing in a fair amount of pessimism toward the economic outlook, we view the upside versus downside in markets as more compelling today.

Headline and core inflation diverge meaningfully

Headline inflation, driven by rising oil and food prices, has moved substantially higher over the last few months, while core inflation has shown signs of very gradual easing. Of note, this month we saw the widest differential between headline and core inflation that we've seen in the past 10 years.

Figure 1. Headline and core inflation have diverged meaningfully



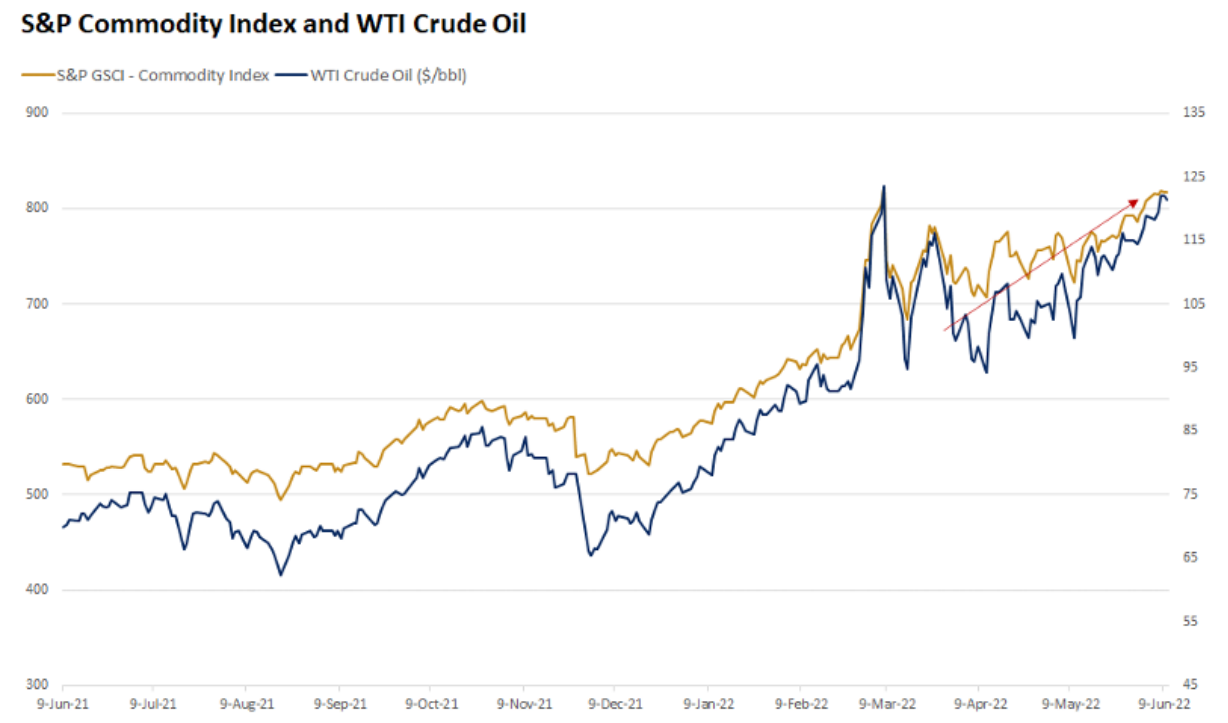
Source: FactSet

This chart shows the widening gap between core and headline inflation as food and energy move higher.

What is driving headline inflation higher?

The key driver of headline inflation continues to be rising global food and energy prices. With uncertainty in the Ukraine war (which continues to be difficult to handicap) and China's reopening driving demand, commodity prices may remain stubbornly elevated over the next several months. WTI crude oil prices, for example, were up nearly 9% in the month of May, and now are up about 7% in the first few days of June alone, hovering around $120.

Figure 2. Food and energy prices continue to trend higher



Source: FactSet, past performance is not a guarantee of future returns.

This chart highlights the increasing correlation between the price of oil and the move higher in commodity indexes

However, while the Federal Reserve may attempt to temper consumer-discretionary demand by raising interest rates, its actions generally do not impact global commodity prices or the demand for consumer staples, like food and energy. Thus, the Fed's focus tends to lie more on fighting core inflation, which is starting to see a downward trend, albeit very gradually.

What could drive core inflation lower?

Perhaps the one silver lining in this month's CPI report is that we saw a modest decline in core inflation, from 6.2% to 6.0% year-over-year. This was driven in part by better prices for medical care and transportation services. However, there may be an opportunity for further reprieve in areas like used- and new-car prices and airline fares, which remained high in this reading but could trend lower in the months ahead.

More broadly, we could also see higher mortgage rates starting to cool the housing market (which will, over time, impact the shelter/rent components of CPI), and early signs of layoffs in areas like the technology sector may ultimately cool the upward influence that wage growth has on inflation.

Overall, the base-case scenario continues to call for inflation to moderate somewhat by year-end, driven by base effects (more favorable yearly comparisons) and better trends in core inflation. However, given rising food and energy prices, risks for a bear-case scenario are rising in the near term as well.

(Source: oXYGen & Jones)

Markets For The Week

INDEX	CLOSE	WEEK
Dow Jones Industrial Average	31,393	-4.6%
S&P 500 Index	3,901	-5.1%
NASDAQ	11,340	-5.6%
MSCI EAFE	1,992	-2.8%
10-yr Treasury Yield	3.16%	.2%
Gold	$1,872	.1%
Bonds	$101.26	-1.5%

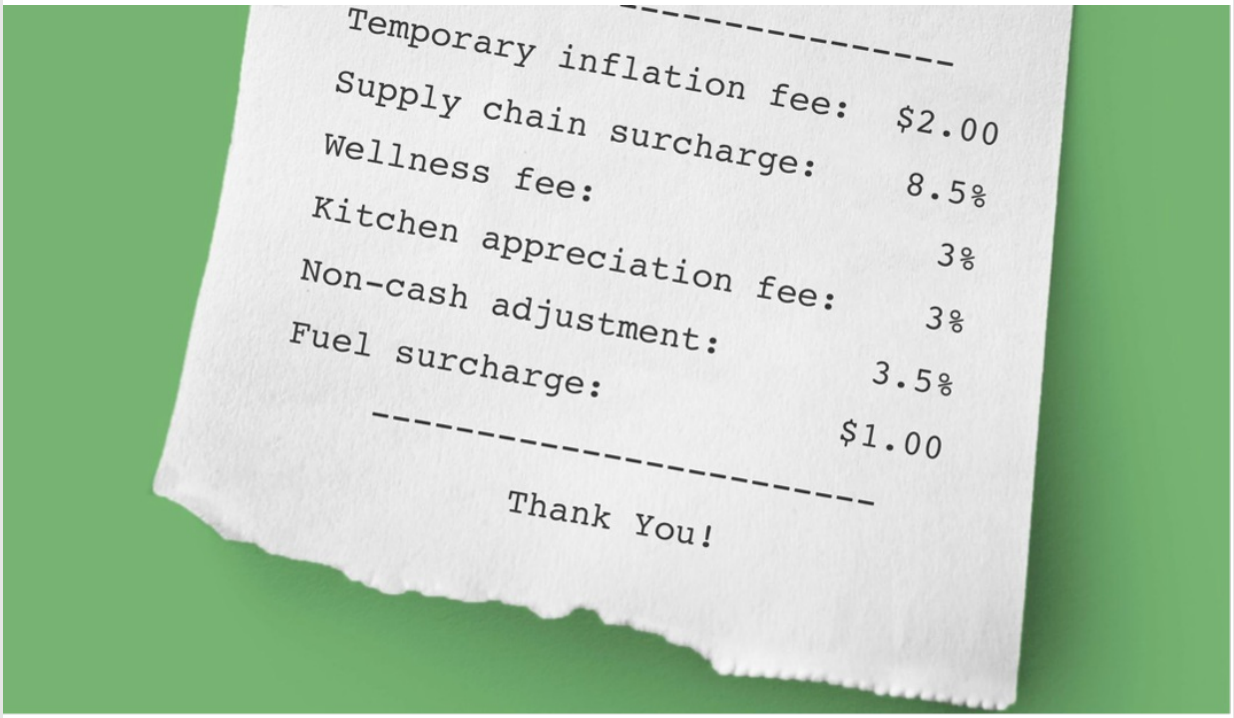
Source: Reuters/Wall Street Journal

Restaurants Add New Fees To Your Check To Combat Inflation

Fees for a "noncash adjustment," "fuel surcharge," or "kitchen appreciation" have been showing up on more bills lately. Industry analysts say this wave of surcharges is mostly being driven by restaurants trying to cope with the impact of rising inflation and a tight labor market on their bottom lines. In addition, Mastercard and Visa in April raised transaction fees for many merchants.

Lightspeed, a global developer of point-of-sale software, said fee revenue nearly doubled from April 2021 to April 2022, based on a sample of 6,000 U.S. restaurants that use its platform. The number of restaurants adding service fees increased by 36.4% over the same period.

The practice is like shrinkflation, when snack-food companies reduce the size of packaging or portions to make it harder to spot a price increase. Be careful, there could be a wellness fee on your bill the next time you eat out.



Earnings Highlights This Week

DocuSign: DocuSign delivered 25% revenue growth from a year earlier, but investors are increasingly concerned with profitability. The stock sank in extended trading, continuing its downward trajectory for the year.

Credit Suisse: Credit Suisse said despite the trading revenues benefiting from the spike in volatility, the impact of these conditions, combined with "continued low levels of capital markets issuance" and widening credit spreads, have "depressed the financial performance" of the investment bank in April and May. This is "likely to lead to a loss for this division as well as a loss for the Group in the second quarter of 2022," the trading update said.

Target: Target said it will take a short-term hit to profits as it cancels orders and marks down unwanted merchandise. CEO Brian Cornell said the big-box retailer wants to clear room for the merchandise including groceries and back-to-school supplies. Target anticipates its operating margin rate for the second quarter will be around 2%. That's lower than the outlook it gave less than three weeks ago. The company also reiterated its forecast for sales growth and said margins will look healthier in the back half of the year.

News and Notes

Are People Refusing To Return To Work?

Is the great resignation still happening and why are people still quitting their jobs?

- 4.5 million people quit their job in March. 4.0 million people quit their job in April, and we've got 10 million job openings. So, employees can be picky right now.
- 64% of workers in America right now said they would look for a new job if a full-time return to work was required.
- With unemployment hovering around a record low of 3.6% and some states at 2%, this may be one the toughest markets ever for finding employees.

You say there is a new trend in the workplace called- The Great Resistance -what is that?

- As life returns to some normality, some employers are calling for employees to return to work full time.
- Employees are resisting coming back to work full time, some saying it's costing them 2 to 3 hours a day in their life due to driving time.
- Many are saying they are losing quality time with their kids, it's affecting their wallet, and employees are digging their heels into their sofas so to speak.

What can employees do if they are negotiating a return to work right now?

- Talk to your employer about the rising commuting costs. Gas prices are soaring. Ask for a raise or a stipend to cover.
- Ask for a hybrid schedule or a certain number of weeks where you work at home in lieu of a hybrid schedule.
- Some companies like Airbnb are allowing workers to have a complete choice of where to work, including 170 countries up to 90 days at a time at Airbnb.

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