Inflation bogey is only 'transitory'

Money Matters

Mark Williams

The financial world loves coming up with new buzz words to encapsulate what is trending.

Alan Greenspan famously referred to "irrational exuberance" in describing the property bubble of the early 2000s. "Green shoots" was used extensively in the aftermath of the great financial crisis in describing the early signs of the recovery. "Taper Tantrum" was used in describing the sharp rise in US treasury 10-year yields in 2013 and a sharp market sell-off when the US Federal Reserve spoke of tapering its quantitative easing (QE) programme. "Asian Contagion" was very descriptive of the currency crisis in 1997, which spread through Asia like a virus affecting the entire region.

So, what is buzzing now?

For some reason, the current word trending makes me think of sci-fi and, according to Google, there was a book published in 2016 entitled *Transient Echoes*, which is described as a dystopian sci-fi novel. Not that I ever read the book, but I digress …

The word is "transient" or "transitory", which was recently used by US Federal Reserve chairperson Jerome Powell to describe the country's view of its inflation. The 101 economic theory distinguishes between structural and cyclical inflation, which I guess the latter is now trending as transitory. But enough of the fluffy banter as this is serious stuff.

Inflation is a big deal and something the world has almost forgotten about since Paul Volcker was elected US Federal chairperson in 1979, when he single-handedly set about taming the inflation dragon, which had ruled from 1965 to 1982.

The Fed believes the current spike in inflation is transitory and has been driven by the base effect (measuring off a previous low point), once-off consumer spending of the Covid fiscal hand-out and temporary supply constraints, which given the slack in the economy will see the inflation number peak and then fall back within range. Based on this view the Fed has no intention of changing its accommodative policy stance, which is supportive of risk assets.

Bear in mind the Fed has a dual mandate of maintaining price stability (inflation targeting) and promoting full employment, which it considers at or below 3,5% unemployment. It employs the best and brightest, and they have unlimited access to the most valuable up-to-date market data.

So, the odds are that they are correct, but what if they are wrong?

In fact, policy error is probably higher now than ever before given the uncharted waters the world finds itself in.

The rise in US 10-year yields is a barometer for future inflation risks and should be closely watched by investors. Having bottomed at around 0,6%, the sharp move to the current rate of about 1,7% indicates a market worried about future inflation risk. – *www.mwwealth.co.za*