Inflation - past, present, and future

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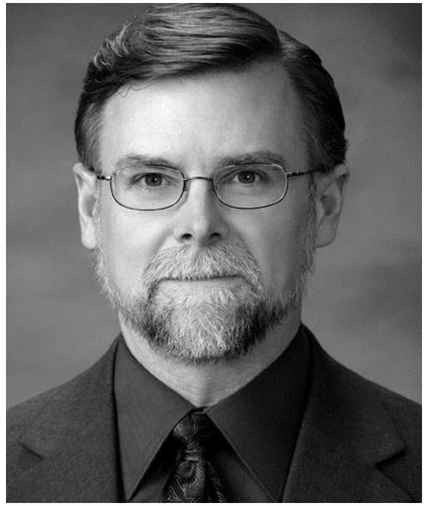

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Inflation . . . . definitions

- Standard traditional . . . Consumer Price Index
- Without modification
- NOT excluding food/energy
- Ignore the short-term . . . . several months

Baseline expectations for the future

- Continue to fall
  - but with significant volatility
  - from now through the bottom of the coming recession
- Then climb upward
  - for the following “15 years”

Inflation today

Just go to the U.S. Bureau of Labor Statistics

Inflation today

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Consumer Price Index

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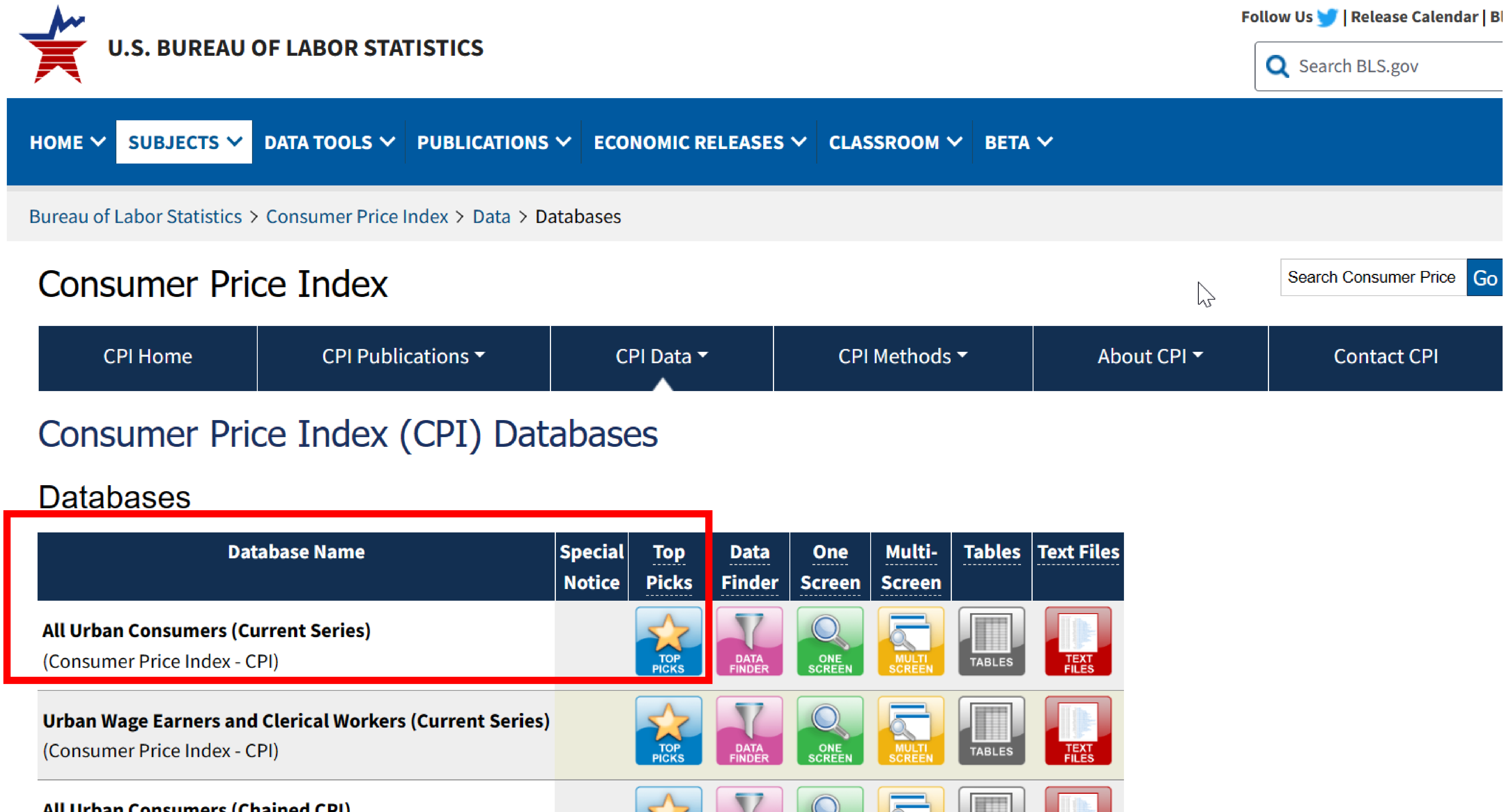
Consumer Price Index (CPI) Databases

Databases

Database Name	Special Notice	Top Picks	Data Finder	One Screen	Multi-Screen	Tables	Text Files
All Urban Consumers (Current Series) (Consumer Price Index - CPI)		TOP PICKS	DATA FINDER	ONE SCREEN	MULTI SCREEN	TABLES	TEXT FILES
Urban Wage Earners and Clerical Workers (Current Series) (Consumer Price Index - CPI)		TOP PICKS	DATA FINDER	ONE SCREEN	MULTI SCREEN	TABLES	TEXT FILES
All Urban Consumers (Chained CPI)							

Inflation today



Today . . . at this instant . . . inflation is running at

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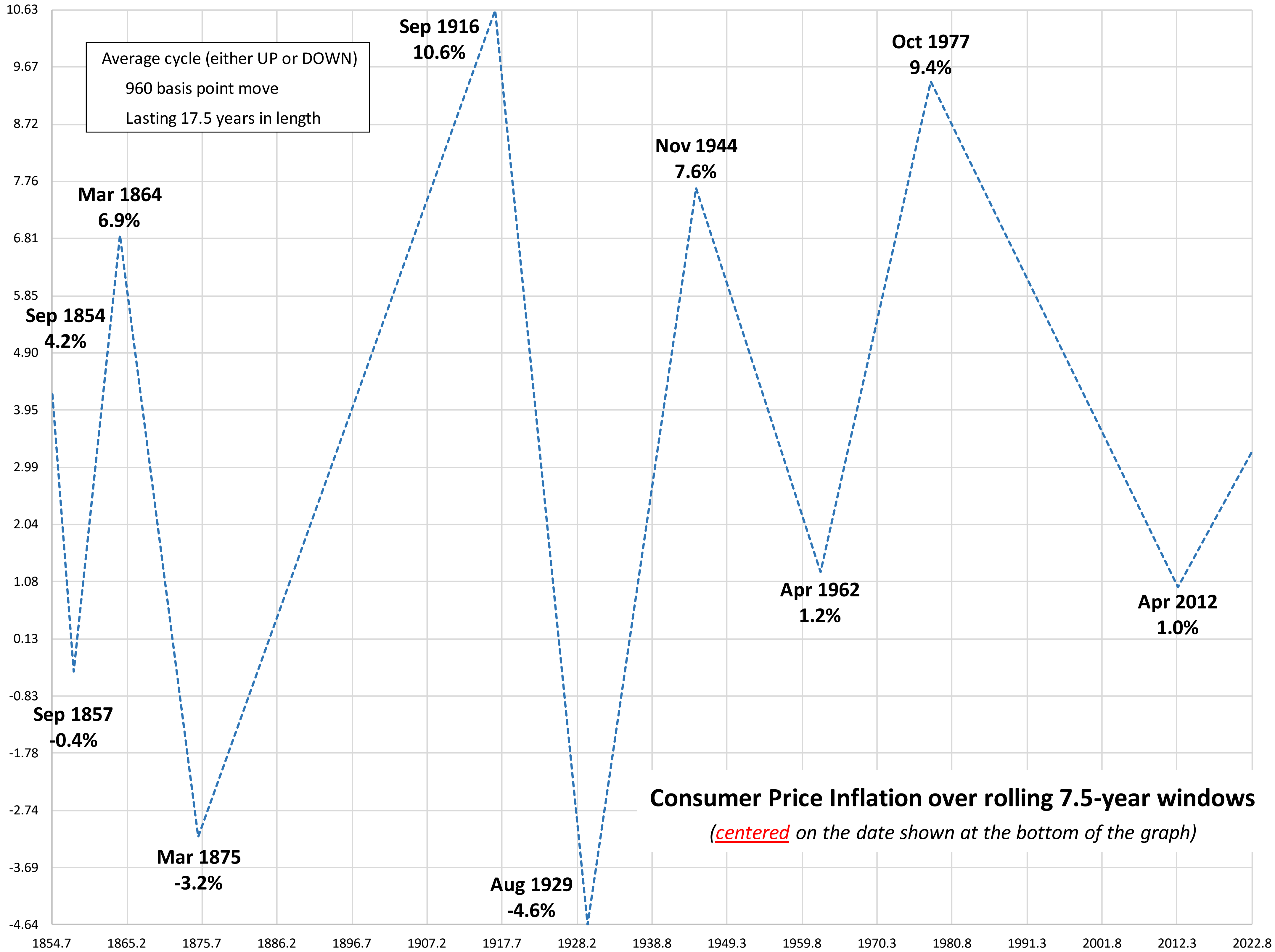
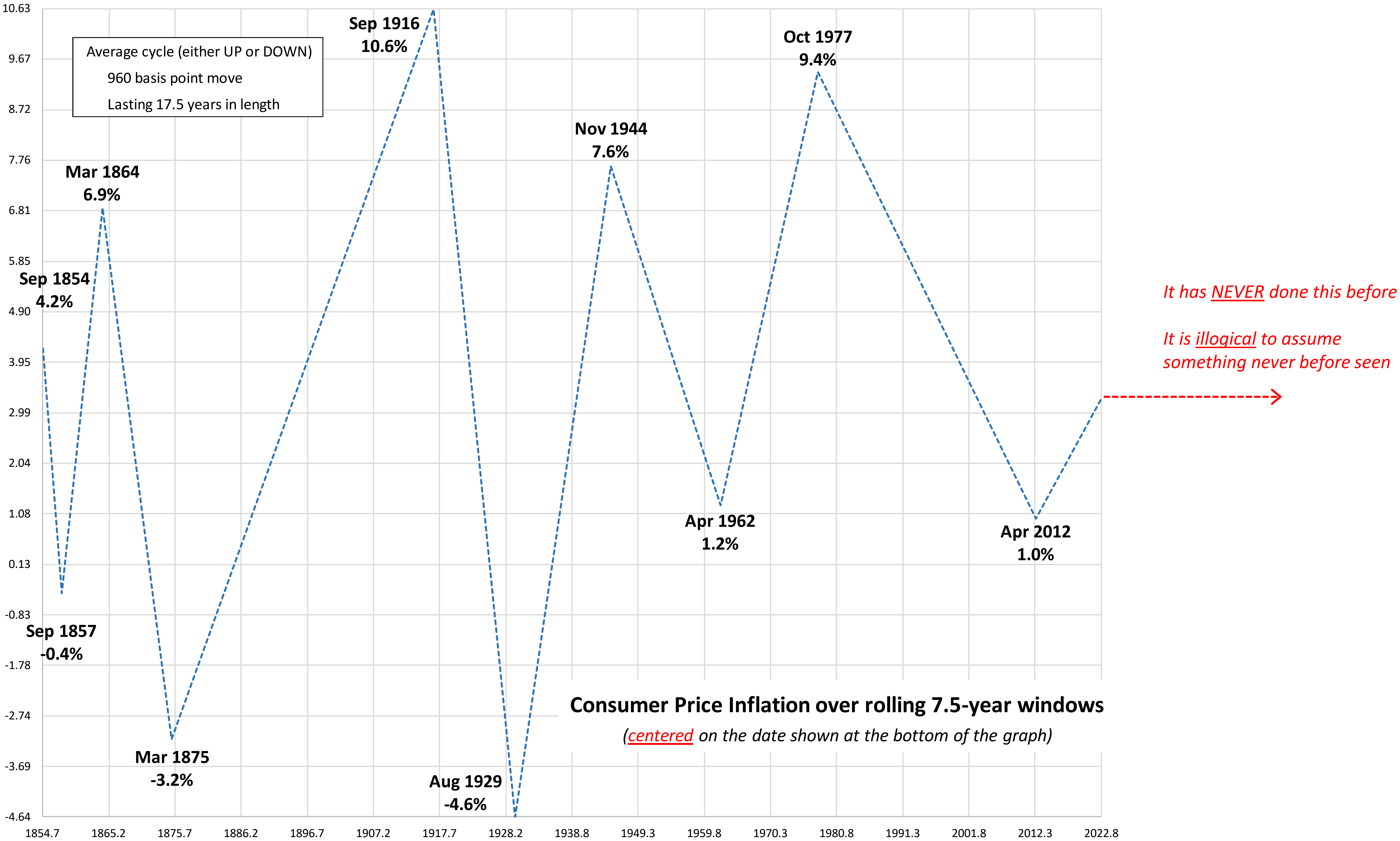
- Consumer Price Index . . . nothing excluded
- Year-over-year . . . as of Aug 31st . . . running at 3.6%
- That is UP from 3.2% . . . as of Jul 31st

Inflation over time



Average cycle (either UP or DOWN)
960 basis point move
Lasting 17.5 years in length
Sep 1854
4.2%
Sep 1857
-0.4%
Mar 1864
6.9%
Mar 1875
-3.2%
Sep 1916
10.6%
Aug 1929
-4.6%
Nov 1944
7.6%
Apr 1962
1.2%
Oct 1977
9.4%
Apr 2012
1.0%
Consumer Price Inflation over rolling 7.5-year windows
(centered on the date shown at the bottom of the graph)
10.63
9.67
8.72
7.76
6.81
5.85
4.90
3.95
2.99
2.04
1.08
0.13
-0.83
-1.78
-2.74
-3.69
-4.64
1854.7
1865.2
1875.7
1886.2
1896.7
1907.2
1917.7
1928.2
1938.8
1949.3
1959.8
1970.3
1980.8
1991.3
2001.8
2012.3
2022.8



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It has NEVER done this before
It is illogical to assume something never before seen
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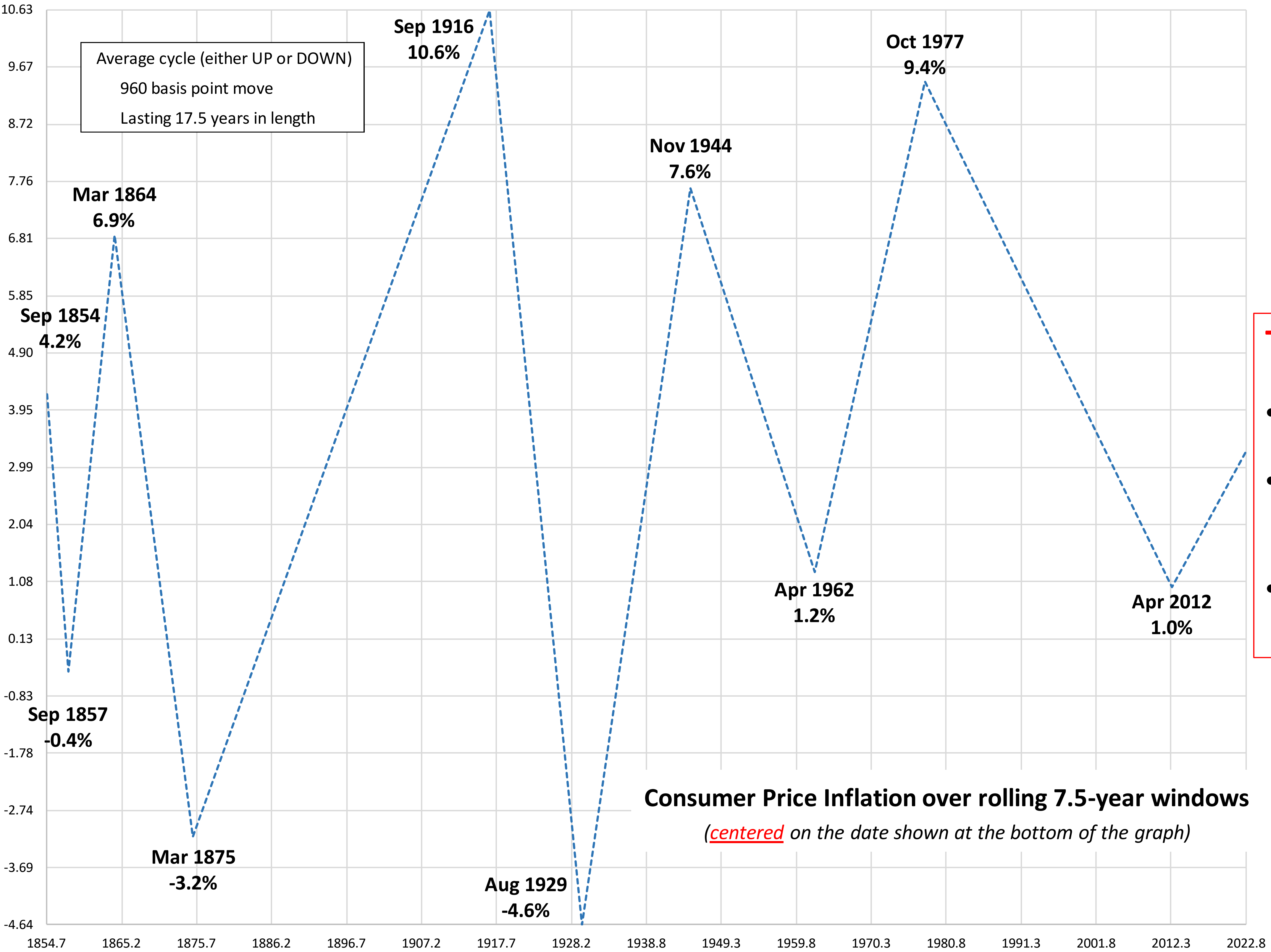

Takeaways . . .

- **Inflation is <u>never</u> constant**
- **Instead, it's either rising or falling**
- **Inflation . . . journeys through long episodic eras**

Why must inflation rise?

Over the long-term

A simple . . . obvious thought experiment

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- I am the government

- I need to pay for all of my programs
- As an elected representative . . . I desire to be reelected

- I can pay for my programs with
  - Taxes
  - Printing money . . . which sort of, hides the cost

- What is a logical prudent rational expectation
  - I will do some of both

Why inflation will rise for the next “20 years”

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- It’s all about funding (paying for) . . . “projects” . . . that’re already in play

- Society and governments have “projects” that they’re attempting to finance
  - Hot war with Russia
  - Cold war with China
  - Conversion from fossil fuels to renewables
  - Income inequality gap
  - Wealth inequality gap
  - Expanding social-support programs
  - Changing weather patterns
  - Deglobalization
  - Rising interest rates . . . i.e., debt service payments explode
  - Transitioning from one political structure . . . to a different structure

- Funding these projects . . . drives interest rates higher

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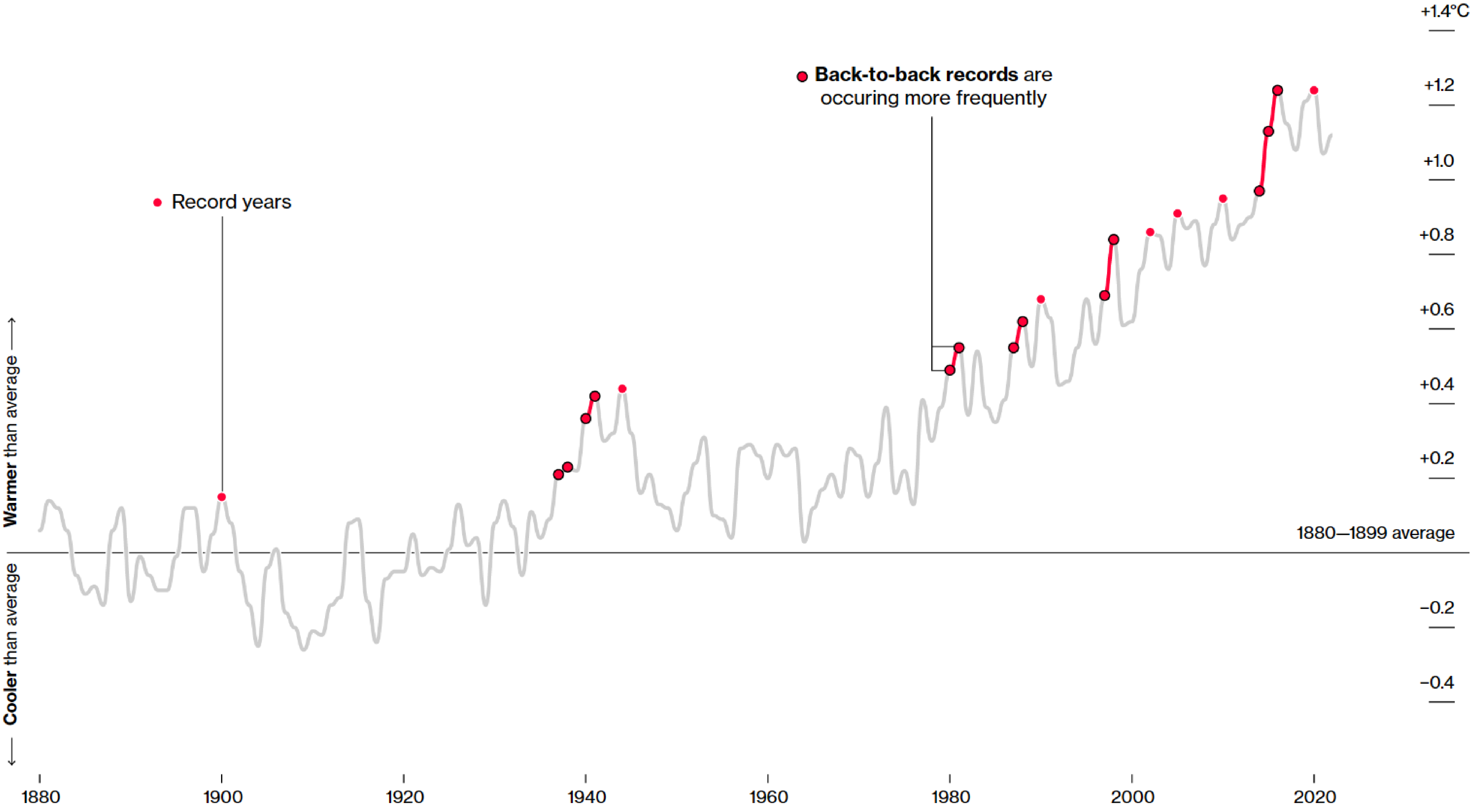
Rising Heat

Average annual global temperature deviation from 1880—1899 average



Source: NASA GISS Surface Temperature Analysis

Politics

- Just stop
- Just stop
- This has absolutely zero to do with which political party gains dominance
- The forces at play are <u>far far</u> larger . . . than any political party differences . . . which honestly are trivial

Review

The path forward

Baseline expectations for the future

- Continue to fall
  - but with significant volatility
  - from now through the <u>bottom</u> of the coming recession

- Then climb upward
  - for the following “15 years”

What's to be done

- The old irrelevant approach is dead . . . for goodness sake, just admit it's dead
    - MPT - Modern Portfolio Theory
    - Mean variance optimization
    - 60/40 portfolio
    - See the very nice piece on this by GMO . . . out of Boston

- What works . . . What's needed
    - Tactical asset allocation (TAA)
    - Serious, institutional, well-structured . . . alternative investments . . . If it's offered at a B/D it won't work

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  - See the v

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Julex has an article on their website addressing this point (soon to appear in *The Journal of Investing*)

Entitled "*The Emperor's New Clothes - Balanced Portfolio Construction*"

The Emperor's New Clothes - Balanced Portfolio Construction

Forthcoming in ***The Journal of Investing***

July 23, 2023

Rob Brown, PhD, CFA - Rob Brown is the Chief Investment Officer and a Senior Vice President for Integrated Financial Partners and Integrated Wealth Concepts, and an Advisory Board member for Julex Capital Management

1. INTRODUCTION

There's a generally accepted approach[1] (often titled "Modern Portfolio Theory" or "MPT") by which 60/40 portfolios[2] are constructed. The effectiveness of this approach, relies upon a set of assumptions regarding the inherent behavioral attributes of the asset categories utilized. If these assumed attributes hold, then the generally accepted approach works, and adds significant value.

The objective of this article is to provide significant evidence that these assumptions do not hold. That the underlying asset categories, just flat out, lack the assumed (and required) behavioral attributes. If true, then the generally accepted approach is suspect and probably misleading. Perhaps, we reached this unfortunate circumstance through myopic thinking . . . decisioning based on:

- **Cherry Picking.** We cherry-picked both an isolated time period (from out of history) and restricted ourselves to a non-repeatable and non-representative geography. We narrowed our vision (myopia) to U.S. asset class returns during the post-industrial era (the last 74 years). Which diverge shockingly from returns representing the great breadth of geographies over

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Risk managed deep value, a huge opportunity

Friday

August 25th

11:00 a.m. EASTERN

Important Disclosures

All data and statistics were provided by Global Financial Data, Inc. and NDR, Inc. (unless otherwise indicated in the exhibit)

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