

# CIO Weekly – Featuring Eli Lee of Bank of Singapore

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*This week: Bank of Singapore: Clients have already started hedging against the possibility of inflation; UBS Chief Investment Office: No withdrawal of monetary easing anytime soon; BlackRock Investment Institute prefers taking risk in equities over credit from a “tactical” perspective*

## **Bank of Singapore: Clients have already started hedging against the possibility of inflation**

Worries about yields rising, at least on long-dated paper, abated a little after the May US jobs report showed vacancies were getting filled slower than expected, prompting predictions that a full recovery in the jobs market there [could be delayed to “well into next year”](#).

Yields on the benchmark 10-year Treasurys closed at its lowest level in more than three months to below 1.5% on Wednesday. But with fiscal stimulus upending traditional economics, the US jobs data showed a perplexing trend — though job openings surged by nearly a million in April, the most since the [Bureau of Labor Statistics](#) started tracking the data in December 2000, some 4 million people quit their jobs in April, according to the Labor Department’s [Job Openings and Labor Turnover Summary](#). That has led to a record 9.3 million vacancies remaining open, higher than the 8.3 million estimated by economists polled by Refinitiv.

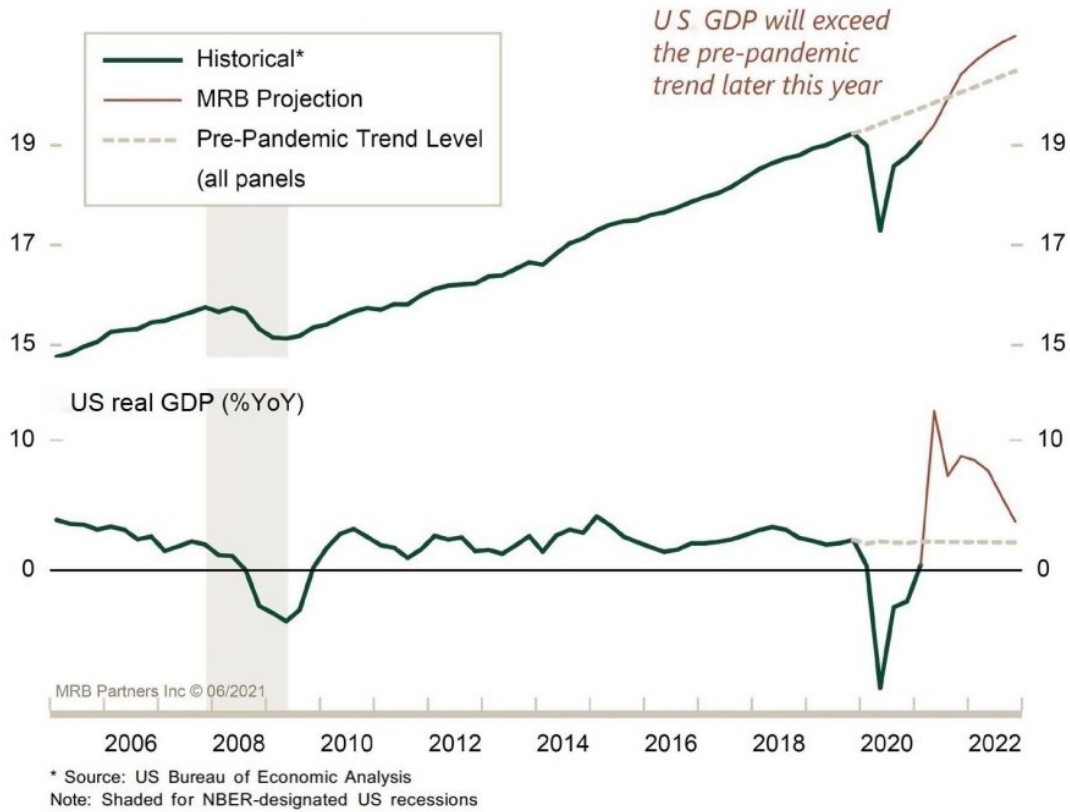
As people hold out for better-paying jobs, thanks to stimulus checks, economists expect wage inflation to add onto oil price increases.

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### US real GDP (Chained 2012 US\$ trillion)



Source: MRB Partners • [Click on image for PDF file](#)

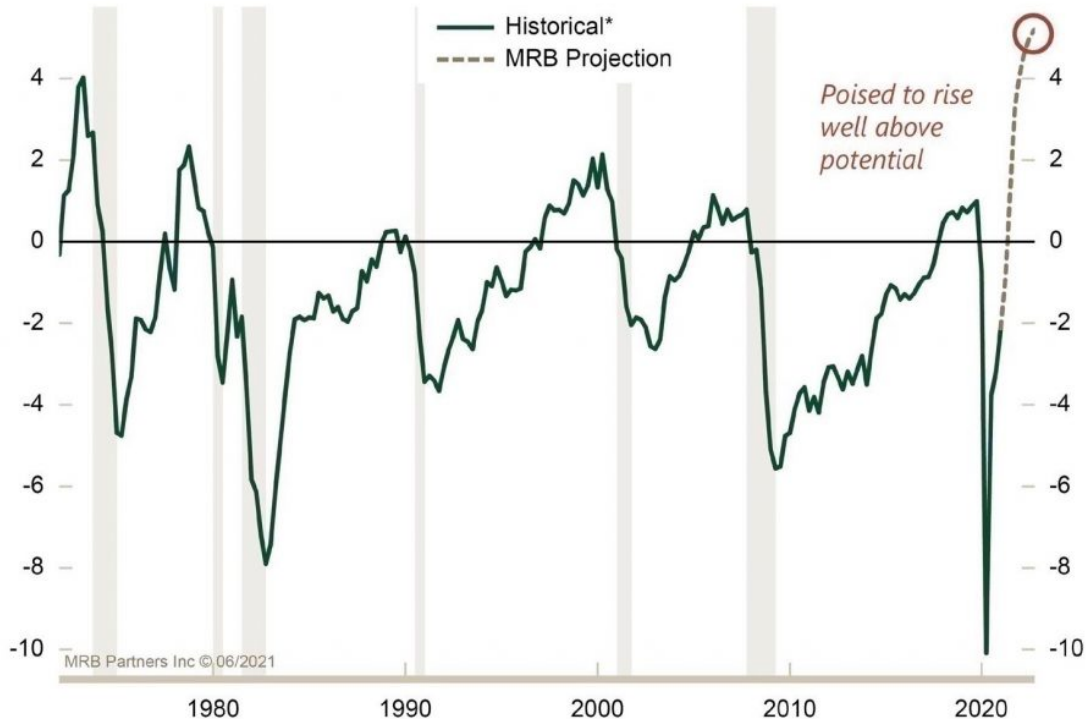
“Inflation will not be as ‘transitory’ as many investors believe, or the Fed hopes will be the case,” cautioned Phillip Colmar, global macro strategist at The Macro Research Board, a US-based independent global top-down research firm.

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## US real output gap\* (% YoY)



\* Percent deviation of real GDP from its potential level; Source: Congressional Budget Office & US Bureau of Economic Analysis  
Note: Shaded for NBER-designated US recessions

Source: MRB Partners • [Click on image for PDF file](#)

“Most drivers are currently contributing to higher price pressures, and many are expected to persist, at least until the next recession,” Colmar wrote to clients. “This will become more evident later this year and in 2022, as the primary influence shifts from cost-push to demand-pull inflation.”

“US Treasuries do not provide enough compensation for sticky price pressures, and another up-leg in bond yields is likely to begin later this year,” Colmar said.

Speaking to *Asian Private Banker*, Eli Lee pointed out that clients have already started hedging against the possibility of inflation rising, despite the “escalation in inflationary pressures” likely to be temporary.

“The bout of inflationary pressures that is about to escalate are very likely to be temporary,” said the head of investment strategy at the Bank of Singapore. “I do think that clients are already starting to hedge against

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inflationary pressures.”

“Prices are surging because of temporary shortages due to the COVID 19 pandemic, but this is expected to ease over time,” he explained. “We are seeing some signs of labour scarcity in the market.”

“This is holding back production and driving price pressures, but again, we expect workers to return as unemployment benefits expire, and as the rate of vaccination increases in the community over time,” Lee opined.

Buttressing his prediction, Lee said “various very powerful long term structural forces” — such as technological disruption and demographic trends — will likely continue to exert downward pressure on prices. “So the base case is that we will see inflationary pressures over the next few months — a lot of that is due to base effects as well — but they will ease over time.”

### **Mitigating risk**

**“There is a risk that inflationary pressures could turn out to be more worrisome than anticipated,” Lee said. The private banking unit of Singapore’s OCBC Bank believes in risk management as a key component in investing and therefore advocates hedging against “downside” scenarios, he said. “We do think that it is sensible for our clients to incorporate inflation hedges into portfolios.”**

The pace of the recovery in the global economy is one reason why investors worry that inflation will rise persistently, explained Lee. Inflation in the US fell back to low levels in 2013 despite the quantitative easing and monetary stimulus from the US Federal Reserve in the wake of the 2008 global financial crisis, he noted. This time around though, the quantitative easing from the Fed along with the expansion in its balance sheet is “actually several magnitudes more substantial than during the 2008 global financial crisis,” Lee said.

“This year alone, the US government is proposing more than US\$6 trillion of new fiscal stimulus which is unprecedented,” Lee told *Asian Private Banker*. “So I think these various factors point to the risks that inflation could turn out to be more worrisome and persistent than anticipated ... and we do think that it is worth hedging against.”

In terms of portfolio allocation, Lee suggested investing in companies that tend to do well during periods of inflation, with strong pricing power and resilient profit margins when the cost of inputs increases. “We continue to be bullish on sound and attractively valued stocks in the financials, commodities, energy and real estate sectors,” particularly those with strong earnings profiles, Lee said.

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## UBS Chief Investment Office: No withdrawal of monetary easing anytime soon

The fresh record notched by the S&P 500 and US payrolls data pointing to accelerating employment growth are not at a “sufficient” pace to prompt a withdrawal of monetary easing any time soon, said the Chief Investment Office of UBS.

The US economy created 559,000 jobs in May, slightly below a consensus forecast of 650,000 yet above the 278,000 posts added in the prior month, noted UBS. “The improving outlook for growth was supported last week by the US ISM Services Index, which hit a record high of 64.0 in May, up from 62.7 in April, underlining the return to normality in the US economy as consumer spending on services recovers.”

**“While the survey pointed to rising prices due to supply bottlenecks, we believe these will fade as businesses adjust to the reopening,” UBS said.**

“Another positive sign for US business came from reports that the Biden administration was willing to set aside its proposal to raise the top corporate tax rate to 28% to win Republican support for greater infrastructure spending,” the Swiss banking major said.

## BlackRock Investment Institute prefers taking risk in equities over credit from a “tactical” perspective

“We see the US and UK leading the developed world’s economic restart — with the euro area catching up — powered by pent-up demand and sky-high excess savings,” notes the think tank of the world’s largest asset manager. “The [immense] growth spurt will be transitory, in our view.”

Any possible restart is not likely to be a recovery as the more activity restarts now, the less there will be to restart later, opined BlackRock.

**“Our new nominal theme — that nominal yields will be less sensitive to expectations for higher inflation — was confirmed by the Fed’s recent policy meetings,” BlackRock said. “The Fed made it clear that the bar for reassessing its policy rate path was not met, and that it was too soon to talk about tapering bond purchases.”**

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“We believe this clear reaffirmation of its commitment to be well “behind the curve” on inflation has helped the Fed regain control of the narrative — for now.”

BlackRock favours inflation-linked bonds amid inflationary pressures in the medium term while preferring to take risk in equities over credit amid low rates and tight spreads from a “tactical” perspective.

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