

## Macro Outlook Summary

January 2025

Monetary policy has a proven track record of managing consumer and business demand which in turn manages growth and hopefully inflation. Central Banks refrain from pointing out that inflation is however not a pure 'demand side' phenomenon and can be equally if not more acutely affected by the 'supply side' over which monetary policy has little influence. The Covid pandemic highlighted this with issues about supply chain disruption, shortages and price hikes - in some cases due to excess demand but in most instances due to shortage of supply. Globalisation arguably peaked around 2010 but the inflection turn was slow and passed largely unnoticed.

As years went by so quality control issues in global supply chains, shrinking labour cost savings and IP infringements led companies to re-shore their production, slowly to begin with and then with gathering pace. Nationalism resurfaced as some questioned whether multi-culturalism had gone too far and national identities were being diluted or lost. Immigration, always a source of cheap labour, became the focal point of this change in sentiment and the UK's story and Brexit reaction has dominated the headlines for years.

UK authority and society has wrestled with the historical, moral, ethical and social issues arising without clearly finding an appropriate and right new stance to take. And then the US elected Donald Trump who spelt out a hard-line view winning mass support. Nationalism has come mainstream and with it comes tariffs, anti-immigration and de-globalisation in steady earnest steps.

The impact of this change is on supply chains where a foreign supply will be substituted for domestic but at a higher price. Interestingly tariffs and sanctions have a very similar effect. The Russian economy was hammered into change by sanctions imposed by others and went through cathartic changes as foreign supplies were cut off and the domestic economy was forced to create replacement. It took many years of limited consumer choice, empty shop shelves and inflation before domestic substitution products often of inferior quality were brought to market.

Now the world seems set on embarking on a similar process, this time of self-harm, as a rising tide of tariffs and counter-tariffs force change. But before those sourcing changes come through, inflation is the natural consequence of supply constraint. Every major central bank is confronted with weakening business and consumer demand as a result of higher interest rates but also rising inflation as a result of nationalism. Whether they choose to tolerate inflation and support the consumer or try to suppress cost push inflation at the expense of the consumer will be the pivotal issue for bond markets and therefore equities in 2025 and beyond.