JIGSAW TALENT MANAGEMENT

Opinion Piece – Global Economy

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Looking at the market today it seems the global financial and monetary system is in crisis. We are now at the pointy end of a 50-year deflation cycle for western economies where the fine balance between growth and rates have been purposely distorted to financialise the global economy. By placing R (cost of capital) below G (economic growth) we have devalued currencies and accelerated asset bubbles. In a healthy economy the cost of capital should exceed the GDP growth rate. For instance, if the GDP (G) for the economy is 3%, the interest rate (R) should be 4-5%. This fine balance between G and R ensures investments are productive for the economy, malinvestment is limited and so are asset bubbles. In addition to the relationship between G and R, 30-year government treasuries should be the asset group to which all risk assets in the economy are pegged, yet the 30-year treasury got as low as 1.9% yield only a few years ago.

We can see the 10-year bond yields rising in all countries once again after initially retracing in key markets as investors attempted to front run the central banks pivoting back to QE re weak economic data. Yet it seems the US FED are going to continue to tighten, using NAIRU (non-accelerating inflation rate of unemployment) as a benchmark to assess inflation. If NAIRU is correlated to demand side inflation (we are not in this cycle today), then evidently Keynesian economics is flawed. If NAIRU creates inflation, then the employment in the economy must be of little to zero productivity. This suggest that Keynesian economics by default does not work. Injecting money into a flagging economy to spur nonproducing employment is a doom cycle that creates demand only, which in turn requires employment destruction to fix and the cycle continues. The Keynesian economy is engineered to collapse in boom and busts cycles. An economy weighted to private sector employment is efficient, synced to equal supply and demand creation. This equates to NARIU being an obsolete theory. High employment in a private sector weighted economy both lowers prices and the overall cost of living.

The FED's conviction in monetary tightening will continue to cause issues for the rest of the world as it guarantees a stronger US dollar in the short term. This is inflationary for any country requiring trade in US dollars or to service debts. As an example, we can look at Europe and the EURO USD. Many US dollars are issued by banks in Europe for investments/bonds even though its common assumption USD dollars are only issued by US banks and the FED. The reality is US dollars can be issued by any bank in the world the US allows. The EURO is today weaker than the USD at 0.97 – 1. This weakening of the European currency requires more EURO's to be dumped/printed in exchange for US dollars, increasing demand for USD and further weakening the EURO. This is just one of the many doom cycles that all fiat currencies are experiencing around the world. As the US dollar climbs the DXY it weakens other currencies it is measured against. As these currencies weaken inflation surges. Imports get more expensive for energy and food, while exports are contracting due to supply chain disruption, rising prices and asset deflation crippling overall wealth and consumption.

Here in Australia the AUD is also under pressure for similar reason and here at Jigsaw we forecast it dropping under 60 by Xmas. Weakening direct trade from Japan, China, South Korea are impacting demand for our currency at the same time as investors are putting capital into the US dollar. China and Japan's production is at the mercy of US and Europe's economies which are in a dire situation. With the RBA raising rates by only 25 base points in the last round of tightening, this further indicated to markets that Australia's housing market was more important than its inflation problem, further weakening the AUD ensuring our import costs escalate while our exports peaked in June 22. The balance of trade is looking sick. A weakening currency is only good for exports if the demand for exports exists, creating revenues to fund imports. Australia has increasing import demand, lowering export demand and little in the way of domestic production to exploit the situation.

So, the world has an inflation problem, and it seems there is nowhere to escape. Governments seem to be executing plans that seem to go against economic logic. As it stands, we have the madness of countries offering more stimulus to assist with inflation, which is the core problem causing inflation in the 1st place. If supply is crippled there is more money chasing fewer goods, this increases prices and devalues the currency, creating even more higher prices. The only way out of inflation is to raise interest rates above inflation, in turn changing consumption into savings or to increase supply (production) while contracting the money supply. If interest rates are raised but still sit below the rate of inflation, the only thing being achieved is supply side inflation which will be passed on to consumers. It seems every developed country is selecting the former (except the US), creating more central bank distortions re stimulus and QE to combat energy and food issues that were created by these countries in the 1st place with sanctions, ESG and COVID policy. The choice for each country is a game of Russian roulette with a two chambre gun and two bullets. You can pick a quick death by destroying the asset bubbles and wiping out people's wealth with rising rates or you can continue the Ponzi scheme until the currency is so weak you require a million dollars to by chewing gum. The UK is at this point and investors are starting to realise the currency will be thrown under the bus. Therefore, bond yields are rising. Even the US with an apparently strong USD is not out of the woods as its currency is only strong compared to other currencies but weak relative to product.

The question is - can the DXY keep on rising. Many economists believe it can, at least in the short term, as it is the go-to asset class for safety after US Treasuries (which are plummeting). The US dollar has privilege above other currencies due to its issuance in global investment markets and trade. For instance, if we look at Japan whose economy is in the same position as the UK to some degree, they have a weakening Yen, huge debt to GDP percentage (most debt is domestic), contracting exports (which is a big problem as they are a creditor nation) and imported inflation re energy and food costs. The Japanese government has stepped in to slow down the depreciation of the Yen by dumping their dollar reserves which amount to circa $1 trillion and buying Yen. This can work in the short to medium term, but US Dollars will not flow into the country so easily as global trade slows and the reserves in dollars Japan holds are needed for their own imports of commodities of which energy is a big component.

Another consideration re the US dollar is its inverse relationship to all other markets. If the USD is strong, it weakens other nations economies by increasing debt commitments, inflation, unemployment and decreases production. If the USD is weak, it bolsters other nations economies for the inverse reasons whilst improving US exports and strengthening US domestic interests. If we consider this, does it mean the US dollar is safe and has no risk of collapsing like other fiat currencies? The biggest threat to the USD is the BRICS nations who are developing their own reserve currency for trade and attempting to take the US pro-actively out of the supply chain. If this transition is successful, the US dollar could be under serious threat. If the US dollar is no longer the global currency to trade with then countries do not require to invest trade surplus in US dollars or treasuries. A core reason USD is held is to secure imports and gain a yield on reserves. A new reserve currency backed by commodities or gold will pivot bond holdings to gold holdings. This will be a catalyst for US treasuries and dollars being dumped at a rapid pace, creating an influx of dollars flooding back into the US economy possibly resulting in stagflation. This event, if it occurs, will also ensure there are no buyers (demand shock) for US government debt. The only buyer being the FED.

To finish this market snapshot let's look at the procurement and supply chain landscape. Supply side pressure in the procurement talent market will likely ease as inflation and cost of capital pressure contract demand for consumer goods and retail forcing businesses to strip out opex where possible. Candidates that will be in surplus will mostly have opex category exposure. In addition, supply will also likely increase for talent in the banking sector as risk is this sector is increasing by the day. Credit Suisse and Deutsch Bank are just two of many who are under huge financial stress as bond deflation causes havoc to balance sheets and too much leverage is exposed (margin calls). Again, the procurement talent will be opex and ICT focussed. Procurement demand has not changed in recent months and continues to be capex, raw material, infrastructure focussed even in NSW which has a bigger services focused economy. Another growth area is ESG and sustainable procurement where there are over 40% more roles registered with us in 2022 than 2021, this trend is set to continue as the world strives to reduce its carbon emissions. As time moves forward, Jigsaw predict will have additional demand for post and pre deal M&A experience as private capital exploits market conditions or listed corporations look at mergers and take overs.