INVESTMENT STRATEGY INSIGHTS

Nothing Says Happy Valentine's Day Like…

February 14th, 2022

Still Talking About Inflation

- Higher inflation may be a regime change but is still unlikely to be a repeat of the much-feared inflation surge of the 1970s

From Pandemic to Endemic

- Transitioning from the emergency phase of the pandemic should enable economic normalization to continue

Keeping an Eye on Eastern Europe

- Investor anxiety around geopolitical tensions should be expected, but markets have a history of longer-term resilience

GLENMEDE

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Still Talking About Inflation

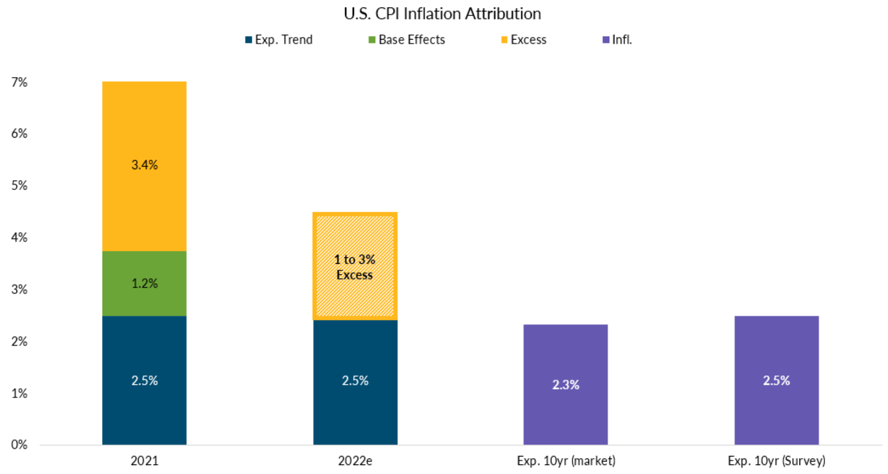
- **Hotter Than Expected Inflation Print.** Consumer Price Index (CPI) inflation hit the 7.5% mark for January, the fastest pace of annual inflation in the U.S. since Michael Jackson's *Thriller* hit record stores. Many of the standout items from the CPI basket over the last year continued their torrid pace of inflation, with prices on fuel oil and used cars/trucks continuing to grind higher. Looking ahead, Glenmede expects inflation to moderate over the year to near 4%, a level still above the Fed's longer-term 2.5% target.
- **Supply Chainflation.** Ongoing supply chain disruptions are one of the culprits behind hotter-than-normal inflation, as the supply of goods has been outstripped by record demand in some industries. There are some signs that these impacts may be abating – for example, the WCI freight rate, a benchmark rate per 40 ft container, has started to show signs of a near-term peak. Clearing the backlog of shipments may be key to boosting inventories and wrestling inflation under control.
- **Higher Inflation, Faster Tightening.** With CPI coming in hotter than expected, the Fed may be justified pursuing a relatively brisk pace of monetary tightening. There's still one CPI and PCE* report on the docket before the next FOMC meeting. All else equal, more fuel to the inflation fire should harden the Fed's resolve to begin raising interest rates at its next meeting in March. It likely raises the odds of a half-percent rate hike in March at the margin, though a quarter-point hike should remain the base case.

Higher inflation may be a regime change but is unlikely to be a repeat of the much-feared inflation surge of the 1970s

*The Fed's preferred measure of inflation is Personal Consumption Expenditures (PCE)

Chart of the Week:

Inflationary pressures persist into 2022, but should moderate as the year progresses



Source: Glenmede, FactSet
Data shown are various historical and projected figures for the U.S. headline consumer price index (CPI), which measures the change in the price of a basket of goods and services consumed by U.S. households. "2021" is actual results and "2022e" is Glenmede's expectations, broken down into long-term expected trend rate inflation, base effects and excess factors due to labor shortages and supply-chain disruptions. "Exp. 10yr (Market)" is derived via market-based inflation expectations, which includes breakeven inflation rates on 10-year Treasury Inflation Protected Securities (TIPS) and 10-year inflation swap rates. "Exp. 10yr (Survey)" includes all the market-based inflation expectation components, alongside survey-based expectations via the Fed's Livingston survey. Past results may not be indicative of future results. Actual results may differ materially from projections.

Nothing Says Happy Valentine's Day Like…

From Pandemic to Endemic?

- **U.S. Cases Declining.** Reported COVID-19 case counts have dropped significantly as the wave of omicron infections continues to recede. Hospitalization rates appear to be following case counts lower, though the fatality rate, a lagging indicator, has not yet turned the corner. Dr. Anthony Fauci struck an optimistic tone last week, suggesting that the level of protection via vaccines, boosters and previous infections means the U.S. could be reaching the end of the pandemic's emergency phase. Accordingly, the number of states with an active COVID-19 emergency order have dropped from fifty at the height of the pandemic, to around twelve.
- **Transition to Endemic COVID-19?** Omicron's impact appears to be receding as quickly as it rose, but it may be unreasonable to expect COVID-19 to disappear altogether, raising the question of whether COVID-19 will become endemic. Instead, enough people may have immunity from vaccines and natural infection to keep a lid on transmissions, hospitalizations and deaths, even as the virus continues to circulate.
- **Window into a Post-COVID World.** Denmark removed all COVID-19 related restrictions last week, despite recently rising case counts due to the now dominant BA.2 omicron (high transmissibility but low virulence) variant. In general, more widespread vaccines and the use of anti-viral treatments have together pushed the case fatality rate of COVID-19 to below the level of influenza, reaching a potential state of endemic equilibrium. The result might be a more manageable endemic phase of the virus in 2022, which may allow for a return to more normal daily lives.

Transitioning from the emergency phase of the pandemic should enable economic normalization to continue

Keeping an Eye on Eastern Europe

- **Tensions Remain High.** Tensions on the Russia/Ukraine border remain a notable geopolitical threat, with U.S. Secretary of State Blinken noting "an invasion can begin at any time." A recent poll* of foreign policy experts in the U.S. showed 56% of respondents expecting Russia to use military force against Ukraine. From an economic and market perspective, the direct impact of armed conflict is likely small, as Russia and Ukraine combined represent less than 3% of global GDP and 0.5% of global equity market capitalization.
- **Following Flow-Through Effects.** Open hostilities between the two countries may have other, secondary impacts. For example, the European Union relies on Russia for more than a third of its natural gas supply. Also, Russia and Ukraine combined account for a quarter of global wheat exports. Such large presence in these markets could cause more disruptions to already strained supply chains. In addition, western threats to impose financial sanctions could cause issues for banks that have extended credit to Russian guarantors, though the scale of this exposure in aggregate appears low.
- **Reacting to Geopolitical Risk.** Global equity markets have a track record of longer-term resilience in the face of geopolitics flareups. However, this does not mean that markets are immune to the risks of armed conflicts over the near-term. For example, in reaction to support for Israel in the Yom Kippur War, the OPEC oil embargo unleashed sizable inflation pressure in the U.S. However, the U.S. economy appears notably less vulnerable to similar risks this time around, especially since the U.S. has lately been producing enough energy of its own to become a net exporter.

Investor anxiety around geopolitical tensions should be expected, but markets have a history of longer-term resilience

*Conducted by the TRIP (Teaching, Research & International Policy) Project at the College of William & Mary's Global Research Institute and the Sie Center at the University of Denver. The results are based on responses from 362 experts between 12/16/2021 and 1/27/2022

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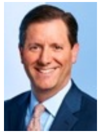

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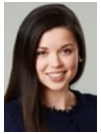

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GLENMEDE CORPORATE FACTS

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