

**Erik:** Joining me now is Bloomberg macro strategist Simon White. Simon prepared a slide deck to a company. This week's interview, registered users will find the download link in your research roundup email. If you don't have a research roundup email, it means you haven't yet registered macrovoices.com. Just go to our homepage, [macrovoices.com](http://macrovoices.com).

Look for the red button above Simon's picture that says, looking for the downloads. Simon, it's great to get you back on the show. It's been too long. I want to dive right into your slide deck 'cause there's so much to cover today. Let's start on page two. You say Infl. Is a three act play that we really need to be thinking about a return to secular inflation.

And a lot of people said there was no catalyst. I think we got our catalyst, didn't we?

**Simon:** Yeah, in, that's I think that's that's absolutely right. Eric, I think this is playing out in a way that's very analogous to the seventies, which is why a there and I think most mispriced at the moment, I think mispriced before this war with Iran started, and I think it's even more mispriced now.

It certainly seems that transitory is back and forth. If you look at the CPI swaps, for instance, they show a quite sharp rise in inflation over the next few months, expected maybe peak out 3%, then very quickly goes straight back down, and 12 months. I think we're looking at 0.8% and spot C, which is basis points higher.

Term break have to five, maybe 20 basis points. The started, but the has five to basis points and I think the memory is kicking back in. Inflation will always go back to target. I think that's I think that's quite complacent and that's why it's helpful to look.

Is perfect. But, the seventies does have an uncanny amount of common commonalities with them today. And also the one thing that doesn't change is human nature. Human nature is immutable and inflation is as much of a psychological thing as it is an actual, financial phenomenon or an economic phenomenon.

So the chart on the left was something I first used 22, so almost four years ago. And it was uncanny because I updated it. And so the blue line shows the CPI in like level, not the growth from the late sixties into the late seventies, early eighties. And the white line is today. And so I updated it on today at the end of Act two.

So the way I thought about it's act one was when inflation first hits new highs. So this time round, that was the pandemic. First climb round in the seventies. It was on the back of we had a lot of fiscal because of the Vietnam War. We had LBJs, great Society, Medicare. We already had quite loose fiscal policy.

Inflation started to creep up much higher than expected. And then we went into act two, which was like the premature all clear.

Inflation, a temporary phenomenon wasn't gonna be much of a problem. Gonna back in fairly quickly, and that feels like where we've been over the last couple of years. But you, inflation not back to target, stayed Target. So remains elevated. And if you look actually where act two ends, match October. The beginning of the yo Kippur war.

And that in itself is a comparison work looking at, there's a lot of differences with that war, but there's actually a lot of commonalities that definitely makes it looking compared to, what we're seeing today. So back then it was a surprise attack. It was the Arab states led by Syria and Egypt on Israel and attacked.

It was a very short war. It was only three weeks, so this war is not yet three weeks. Initially, it was expected to be short, but that's looking less likely now. I think as an end of April ceasefire now down to 40% probability from something like 65% not that long ago. And you had obviously a major oil shock in response to this this war because what happened after the war, after the three week war was that the US state aid to Israel and the Arab states decided to have an embargo on oil.

And that created this huge oil shock. So oil prices managed to quadruple in a matter of months. That's quite a significant oil shock. That led to the Act three, which the comeback, this massive in inflation the end of the decade. And it really didn't end until you got in this exceptionally high interest rate heights, the Saturday night special that really managed to break back inflation.

Look the further commonalities,

the Middle East

also. Next slide. You look at the then, so market, back then, this was the time of the nifty 50. So this was a set of stocks that everybody thought they had to own. They had great earnings, they were great businesses, and pretty much everyone owned them excuse me. And similar to today.

So we had very narrow leadership. In fact, it wasn't until the tiny, the banks and the magnificent seven that we had such narrow leadership again, as what we had back in, in the early seventies. Extremely narrow leadership as well. Before, just after it started, stocks had already sell off maybe 10% the months before the following year, they sold off another 45% and that the largest sell off we've seen since the since the great, so we saw significant stock sell.

Now, that's not to say, that we're gonna get the same thing playing out here. There's a lot of differences obviously today. The US is a major oil producer. This is not the same, exactly the same states that are involved. The choke point here is not an embargo, it's the of hor. And there is still nonetheless, choke point in the supply states.

But I think it's worth bearing in mind that, as a non, just given, we're in a sort of not similar situation and kind of nail the coffin, if you like in some ways for why be. To the, is that even though this massive in market in

and also households compared to financial assets, which much lower back then it's much, much higher back to date. So really it's the number of reasons why. You could see things, we're not see a more deterioration obviously, or to get anything like that, but given some of the commonalities, I think it's worth in, especially when you look at the market today, it just does seem, again, there is some complacency in stock market been to believe.

I think that there is some sort of tackle on the way and therefore, it's not really worth market trading down too much. Even if you look at the food spread. So the V went up initially a lot of that was, first of all it was driven by cold spreads falling, and then it's driven by food spread rising.

So people were putting on insurance, but then they quickly monetized. I think those monetize those edges and that spread start to come off. And so the V has started to come off. So really I think the markets getting to the point where it feels like, you know what, this isn't gonna be a major issue.

We don't have too much to worry about here. Not ready to obviously rally and making your highs again. So get overly knickers. I'd argue along with inflation, that's something that is beginning to look a little bit complacent.

**Erik:** Simon, let's go a little bit deeper on some of the both differences and similarities between the Yom Kippur war and the present conflict.

The Yom Kippur War was really a war of solidarity. As you said, the US had sided with Israel. Basically all of the Arab states together went in on the Arab oil embargo. You have a very different situation today where the US has once again sided with Israel in a conflict with Iran, but now Iran. Does not have solidarity of the other Gulf States.

In fact, it's attacking the other Gulf states that are allied with the United States. It seems to me there are still similarities, but there are some almost diametric opposites in some aspects of this. How do we sort that out and make sense of, what extent the economic outcome might be the same or different?

**Simon:** Yeah, I think as hundred percent, I alluded to that there is a number of differences. And so that puts you in a point where, no analog is gonna be perfect. But I think when you combine it, as I say with the overall inflationary backdrop, where we're in terms of this free in the seventies, you could argue that what happened in the seventies were a series of kind of quote unquote bad luck that inflation rising.

Inflation, as I mentioned, we had already the war, we had the fiscal expansion on the back of the society. And then you had, 1971 was Nixon closing the gold window. Then you had the Arab oil embargo, the war. You had the end of the decade, you had the Iranian revolution. You could argue all these things were bad luck, but they're also hitting a situation where inflation was already in a different regime.

So I think that's the thing to, to note the differences of when you're an inflationary regime, lots of things can happen, right? Things will always happen. But if they hit when you're already an inflationary regime, they're much more likely to have bigger inflationary impact. You know that's where we are today.

It's very uncanny if we happen to look, compare the two analogies that almost to the month when you get this sort of premature all clear ending. When the yo war started as when the attacks on Iran started. Yeah I wouldn't wanna over the point in terms of the analysis, the there's so many precedent that makes it worthwhile looking a little bit deeper into, for instance, another one that's very interesting is an underappreciated fact that in the seventies the food shop was actually much bigger than the energy shop.

Effect on C. So if you look at the weighted contribution from food and from energy in the 1970s, it much bigger for than it was for energy. In fact, food inflation was already rising before energy. This time around we have the

disruption to the straight of our moves. That obviously doesn't just affect energy prices, it affects energy products.

Lot stuff that goes re produced in that region or has travel through that region. So Iran itself produces a lot of, there's a huge amount of sulfur flows through the, all these things go into and in fact further into presentation, if we go to lemme just find this slide. If we go to slide eight.

We can, there actually, you can see the two shots. So the Blue line chose the good shot after OPEC one the shot. And you can see again after OPEC two, the Iranian revolution, both times the, and today already we have, if you look at the contribution to CPI, the US CPI, that is from food. It's it's higher than ER energy already.

So if you have this effect getting into, fertilizer prices, and that's what I to show on the chart on the right, on slide eight, you can see this fertilizer include some of these I mentioned along with things like bot, when that starts to, it's a very reliable by the six months that CPI will start to rise.

So I don't think that. And especially I think if you take account have very unlikely you're not gonna get some second. Feed into core inflation. And you get the sticky inflation that we saw in the 1970s, and that's a lot more troublesome for the Fed. In one sense, it should make it easier because the Fed can then go, if we see inflation, that's something we think we can do something about. We'll high, but with the. Mute, muted. Sorry. Next, Kevin coming in, whether he's gonna lean towards the do the spectrum I certainly think he's more likely to be more like an Arthur Burns who was in the, in seventies times.

He's likely be

I 19. So I think that further complicates the matter in terms of what the best reaction functions gonna be.

**Erik:** It seems like the analogy that's most relevant is the Yom Kippur War only lasted a few days, but the Arab oil embargo lasted quite a lot longer than that. So the question is, once the direct kinetic conflict is over, how long can Iran continue to disrupt the flow of traffic through the straight of four?

Is that the right thing to focus on? And if so, what's the answer?

**Simon:** Yeah.

Key message, I think from that period was the war itself was very short. Say it was about a few weeks, but the impact was felt way through all through the decade. And I had a number of consequences. So again, no analog perfect, but the human side of things, it doesn't change how humans respond. Human nature responds.

It doesn't really, in fact, I can see that this two nature of the two different shocks, if we go to slide then six. So we've got two more charts there. And this brings me to another point, which I think needs to be made is that I don't think the yield curve is pricing in what's looking to be much larger inflationary shock than for instance has been picked up in the breakeven market.

So the left chart we can see there is what's did. OPEC two. Both cases they ended up, did rise quite considerably, but they long after, if you liked CPI, already started rising kind late. But both times they did rise. And if you look at the chart on the right there, you can see the two, the nature, the different nature of the two shocks.

So OPEC one was definitely more of a permanent shock to oil prices. So really oil prices never really revisited. Pre OPEC one or pre-war, pre war levels, again they just kept rallying through until OPEC two hit the Iranian revolution in 1979, they sharp again, but nowhere near as much in percentage terms as they did O one, and then they gradually start to fairly soon after.

OPEC two was more transient, the more transient, but in both cases, if you look at the bottom, you can see core and in the interim, OPEC both made a higher. Early eighties, and again, it wasn't until Paul Volker got his hands on monetary policy that he was really able to put an end to this this huge inflation that it had through that decades.

**Erik:** One of the theories of secular inflation is that it's a self-reinforcing vicious cycles. So as you begin to see inflation, it changes consumer behavior. People start stocking up on things because they wanna buy it while the price is still cheap before the price goes up more, that causes more consumption than.

Is inflationary and it all feeds on itself. And you, it's like a fire that once you've started it, you can't put it out. Are we already at that point in terms of this coming inflation cycle where the fire has been started and can't be put out? Or are we still in the need to look at this and see what happens?

Stage

**Simon:** We're in, we're already in that my quite clear that what began in 2020 with the pandemic large spike in inflation was the beginning. That, that cycle starting and really what's happening underneath is that why 2% inflation for whatever reason, an but 2%, around 2% inflation overall, like over the whole economy tends to be fairly stable.

And I think that's because all the different actors that are taking price signaled off one another when inflation is not moving around that much. They tend not to go out sync. Once the cat outta the bag, like once you have this large rise in inflation, which we saw in the early 2020s, they get all, it'll sink and it takes a huge amount for them to get back.

And and you end up with inflation remaining elevated. So you can split CPI up, for instance, into, components. So you can look at essentially non components and what you noticed in 2020 is structural start to fall, but the structural one remained more by the time the structural fall, because you can tell by his name cyclical has started to rise again and start to reinforce.

Structural inflation was already elevated and we're right in that period again, now where structural had stopped to fall at a higher low, but the cyclical part of it is already rising again, and this war is just gonna make it worse because obviously the immediate effect is on headline inflation.

And so straight away you're gonna see that feed through into the cyclical side of things. Once again what was 0.4% we're now C 3% and pce, they're gonna look like again, equivalent to what we saw in the mid seventies after the, this is the point where we start to see a rise again. I know how far it goes.

Again, the U US is much more insulated and than it was back then. But I think you do see a re-acceleration. And the real kind of, if you like, the real kind of tinder in this is that as I say, going back to Kevin War, you've got someone that's coming in that nobody's really sure is gonna be an inflation fighter.

In fact, quite the opposite, quite possibly. Which is actually a bit odd, just the slight deviation. But connected is, it's strained. If you look at real yields have been rising. So real yields have been rising since the war, and that's been driven by higher rate expectations.

So that's part of the rise in nominal yield. So evens have moved a bit, as I mentioned, but really the bulk of the, so far have been real. And that's on the back of as say, expectations are gonna higher seems a little bit, given, and the conditions that, not conditions, but the circumstances under his nomination.

And a president who still makes no bones about being absolutely determined to get lower rates immediately. He was saying so only a couple of days ago yesterday. So I feel that is also adding to the structural kind of impediment for inflation to, to keep rising. Go back to the yield point I was mentioned.

So I think yields as say, are not priced for an shock. And I think one, one thing we'll see, the yield curve will steepen. So if we go to slide seven on the look, basically how greys and real yields behaved in the seventies. Now, there was no real yields in the seventies because didn't start trading until 1997.

But you can synthesize real. So you basically look at how reals have traded laterally versus a whole bunch of different economic market indicators. And then you can back it out and look at how and build basically a series of in the seventies. So far there we can see again the dip, OPEC and OPEC two and how the yields behave.

So in both cases breakevens rose. Pec what happened is that you put shock to greats, but then we had equal opposite shock to, that's textbook sta what happened in pec pec two even but stayed largely static. And I think that was basically for two main reasons. One, the US response to OPEC one.

So the US became less energy intensive and more energy efficient. And a lot of non OPEC production came on street completed, like Alaska and the North Sea. And on top of that, you had, or very soon after the Iranian revolution, you had Paul Volker at the Fed and that kind of cushion under how far uhs could fall.

So in OPEC one, the maybe didn't amount.

Steep. And he as mentioned earlier for not believing that central bank much, let shock inflation was of the view that by and large most inflation shock couldn't be solved by a central buyer. And in fact, he was the guy when he was at the bed he got staffers working on some of the first measures of core inflation.

And then to the decades he kept on taking out more and more core inflation and a frantic hope that something would be going down which he discovered wasn't the case. We, we have this very banker who doesn't really believe central banker, who doesn't really believe that inflation is something he can do much about.

So short yields fell. So steepened, OPEC one and OPEC two. Little bit, but had Paul Volker who massively curve flat. But this time I think in some ways be

rise. So I think that move, thus that we see this muted move, I don't think that'll last. And that this should rise more from, the relative status.

You're gonna see lower weight. So I think I would lean curve seating.

OPEC one is as similar to what's happening today. There are, as we covered to some similarities, but there's a lot of differences as well.

**Erik:** If this was 1973 all over again, and clearly you've said that it's not exactly a perfect analogy, but to the extent that there's a lot of overlaps, 1973 was not a good time to have a long-term bullish outlook on buying and holding stocks for the long haul.

What does this mean for equity markets for the rest of the decade?

**Simon:** I it's interesting now. It depends who you speak to. So I've got a lot of stuff, some friends and people I know that speak to commodity people. And they're overall a lot more bearish than rates.

People you seem to be overall less pessimistic. I think, again, going back to what I said earlier, I think that there's still this sort of belief that there's some sort of an attack on. Even more than that. I think the big difference is that ultimately there's atop and if things get really bad the Fed can step in.

I'm not saying that's what's gonna happen right now, but you're always gonna have that tail covered. So the commodity markets can really price in extremely kind of negative outcomes. They don't have a less lender of last resort, right? So there's nowhere to go. If your commodity market sees for whatever reason, there's nothing really can be done.

There's no backstop in the way that you have for financial assets. And so I think that sort of explains why we have that today. And, 1973, I don't think we, we had that to the same extent. It wasn't this belief that the Fed was always gonna protect efficacy returns. So that's why you probably had that situation where you had this huge shock, much bigger than the energy shock we've got today.

Combined with a that was yes, it was overall more dubbish, but this is the decade monetary policy where, policy came back, then you tightened it, and then you're like, oh, listen policy again. Back and forth, back and forward. There's huge amount of volatility underlying there obviously.

Makes it more likely or yeah. Increases the chance that you can have deeper falls in the market. And so you don't really have some of that today. But it does seem, as I earlier, that feels the market overall being more complacent. Even with that in mind, that there is a backstop, that there is still a potential for some sort of still seems to be some sort of complacency.

What especially.

Initially there was the response to let's hedge some downside, but very quickly that reversed. It was almost as if like the market went, oh, maybe I don't need such outta money here. Maybe the market's not gonna sell off that. In which case I don't need this insurance right now. So again, that, that sort of me, just because distribution are still very right there still a lot of moving parts.

Most unpredictable. Back in the seventies we had a lot of volatility, political volatility. Again, I don't think he had anyone quite as volatile and he was able to obviously voice his volatility in such a realtime manner than we've gotta, that puts a lot of people in a sort of frozen moment, like move money.

They're fearful that they can't really put much risk on because so much could change.

**Erik:** Simon, on page 11, you say gold is a hedge against both tails. Elaborate on that please. But also I think it's relevant to point out if we're looking at the analog as being the 1970s. Private ownership of gold wasn't re legalized until 1974.

So there was a very big transition catalyst there where it became legal once again to own gold bullion, which probably disrupts the data. How should we think about this in the 2020s?

**Simon:** Yeah, that, that's a good point. I think. I think there's also another disruption at the yellow side as well because the data on this chart goes back to the late twenties.

Thirties was essentially the USSC gold ownerships gold, I think 20 so quite possibly could up in that period. I think. I think that's why gold misunderstood though, was that it's to some extent an inflation hedge. It's not a perfect inflation hedge. It's not dependent. Inflation goes very high. You're in that sort of environment. It does a good job because you've got the things and the general kind insurance against system.

It's appreciated that it's also a downside tail as well. And I think what has been driving a lot of the rally recently in is this is the lack of alternatives. If start thinking about, I dunno what's gonna happen, I, whether we're gonna basement world where there's a lot inflation, I dunno whether there's gonna be a massive credit event.

And that's gonna be deflation rate. These are potential threats to the financial system. What can I own? You record of protecting a portfolio in such an environment and there's really not much else other than gold. I think people ran through all the options. They're like that would work.

That work Bitcoin that hasn't been tested and they landed upon gold. And a lot of people that. Generally openly admitted. They've never, ever really tapered gold. They've never been a fan of gold. They never understood it, are never nevertheless starting to add or have started to add some exposure to their portfolio.

So I think as an uni of collateral really is what's driving it. And although struggled a little bit over the last few weeks. I think it's premature to say that's the end of the primary trend because a lot of the main reasons that driving it are still valid today. There's still a need for diversification from the system.

I still think there's obviously geopolitical volatility. Hasn't. Central banks I don't think are suddenly like market central banks. They were the ones that initially kicked off the rally a few years ago. I don't think they're gonna turn and start selling in any great size. They, they bought some and they may stop buying it, but I don't see why they were suddenly turned tail start selling on mass.

And there was a story that Poland was mooting selling. Some of its foldings. There were, the reason why they were thinking of selling them was for defense. And that doesn't really strike me as a great sort of a gold bearish kind of reason for selling gold overall. So I think, yeah, the general environment still very conducive to gold still generally keeping to its primary.

And it's struggling right now, perhaps because we've seen some marking up of short-term rates and the dollars had a little bit of a rally, things like that. Overall I don't see why, it would take a big seller to come around to really force into a massive bear market. I just don't see where that's gonna come from.

**Erik:** As you said, unfortunately, what has not gone away is geopolitical excitement, for lack of a better word. The thing that's I've noticed just in the last few weeks is there was a very strong, positive correlation. The next time a bomb

drops gold spikes upward. And what we've seen just in the last few weeks is a breakdown where, when oil is up hard because of geopolitical, bombs are dropping, gold's actually moving down.

What's going on there?

**Simon:** Yeah, I say I think potentially it's because of, the real has risen. That could be partly the little bit of the rally in the, it should also be in times of if there's any capital repatriation going on, maybe in the Middle East. I know for sure, but, gold can often get hit in the shorter term people need to liquidate.

That's unfortunately. Asset. Asset is it's

narrative.

Anything more than just, obviously we've gotta remember the market has rallied extraordinarily much in recent months. So there's partly respectable for it to have. The kind of pause that it's having right now, like it can't continue in that sort of trend indefinitely, but I don't think that means that the trend is over.

Yeah, I mean I think silver is a far more obviously volatile, but a far more questionable kind of response to that kind of overall idea on trade. But gold to me seems certainly more, more secure just because, as I say, the reasons underpinning it rally all seem to be mostly intact still.

Now,

**Erik:** Simon, we've been jumping around in the slide deck. Let's go back to page four because you've basically said you're rewriting the Risk Off Playbook. It seems like an important book to read. Tell us more about it.

**Simon:** I'm certainly not gonna rewrite it myself, but my point here is really know.

We analog guide, I think you have to keep in mind as rules change. So I think standard, playbook, can the dollar rally and risk assets sell off? And that might not be the case to the same extent as, so for instance, take so quintessential. Risk really was the gsc. And then the gsc, the dollar rally.

So I think that's a lot of people's you know what, that the one therefore safe. But really if you look at what drove that and then necessarily say in position to rally

quite as hard as it did back then. So the chart on left there, you can see that the blue line shows the bond flows inflows from foreigners.

They slowed. Equities were tiny back then. Equities much today as far are concerned. What actually drove the dollar, the rally repatriation. So the US basically funds and banks had led to various European entities. And it was these guys repatriating that led to the dollar rallies. It wasn't the case of foreigners channeling money in or meeting dollars to cover like structural shocks.

It was really just US entities repatriating, and that led to the dollar rally. Now this time around the cash flows are the structure of this is different. And so bonds are much smaller now because we've had, because the US has now not seen, is not seeing as much a safe haven and equity falls are massive and the US Outfalls are not as large as they were back in net impact.

Exposed to equity. So in a sort of risk off environment that we're in right now, it's conceivable that more capital repatriation and some of that is equities in the end be is a dollar negative, and you don't have the same cushion of dollar repatriation. Yeah you wouldn't expect to see the dollar necessarily rallying as much, and that could be seen even more if you look at the chart on the right.

So after the Marla Accord all the talk of the dollar disruption, the tariff, that didn't lead to sell America trade, but I certainly think it made people think twice about their exposure to, and that can be seen. Say this chart, just the bark. So the white line shows the dollar reverse.

And what you tend to see is the blue line, which is a reserve in denominating dollars. So when the dollar weakens, I see the white lines rise. Manager

and time

yet in attitude to global demand for dollars. So I don't necessarily see, and I think it's all a rally will be as big as time and thus far, the DXYI think is up about one half, 2% since the war started. Slide at say commodities. So as asset of seen as well recession, general interpretation that isn't always the case either if you have a commodity in recession and if we gonna get recession chance that at the next few months.

But that could change if the war continues. And the negative effects spiral. Happens then is that commodities start to sell off before the slump and growth. But the, that, that sort of sell up and commodity prices eases the growth. And actually that allows commodities to rally through the rest of the recession.

So that might, may well happen again. We get a commodity induced recession, say later, this is your next year. That's not a prediction. But if we were to get one. I wouldn't automatically assume that commodities are gonna sell off through that.

**Erik:** Simon, let's move on to page nine. The title of that slide is it takes a war to bring down an economy This Strong, let's start with how strong the economy is.

But then later you say it would take a protracted war. So I guess the question is, how protracted does it need to be in order to take down the strength of economy that we already have and where is this thing headed?

**Simon:** Economy is actually remarkably strong. Given I think the length of time of the and that really surprised me when I was looking at this.

And it's also a little bit ironic I guess that, coming into this war, the US was fing in all cylinders. And as mentioned, I mentioned war is perhaps just take to derail it. You have number cycles for the US economy that everyone knows about the business cycle.

There's also the liquidity cycle. There's the housing cycle, there's the inventory cycle, and all of them are actually in pretty good shape. And so the business cycle, if you look at leading indicators, has been turning up the liquidity cycle. So that's the chart on the left there. And I look at excess liquidity, which is between real money growth and economic growth.

This liquidity gonna have on markets. So the bigger gap between liquidity and economic growth means the economy needs less, but that more to go into risk assets that has been vacillating around, as you can see the chart, but turned back up again. And even taking into account, we've seen some tightening in financial conditions since the war, but overall they've not been massive.

As I di alluded earlier that the dollars rally hasn't been huge either. Thus, so the s in pretty good shape and the, the general business cycle is in pretty good shape. Even taking into account the job market slow down, it's possible to have a job as, and some of the things that I would look at to see if it was a slow down in growth coming, such that temporary help is actually rising, not falling.

Hours worked kind static. You would expect to see that fall as people cut, start people. I think it's, you've remember that we have companies still very strong.

The balance are generally in good shape and you've got this massive amount of government money still filtering through the system.

And so there's maybe not the same acute needs in the shorter term, at least. Lay and that global, the global economy is also in good shape. As that's the chart on the right there, you can see that we're in the midst. Global cyclical upswing. If leading indicators around world almost all are turning up on six basis.

And then if look at inventory, that looks to be turning up as well. Leading indicators are putting in it to continue to rise. Sales inventory ratios have started to rise. Housing cycle is not as in good shape, it's okay. Okay. Housing growth sales growth has slowed down and things like that, but one of the best indicators for housing is building permits.

Building permits are doing okay. And they're actually led by mortgage spreads. We'll see quite significant compression in mortgage press spreads for bears, such as falling bond volatility, and so you can't see that the housing cycle in particularly bad shape. We have credit, we go to slide 10 the listed credit market.

From a fundamental perspective, my leading indicator there on the chart on the shows that on fundamental are to tighter spread. So things like lending conditions are particularly tightening in a particularly rapid way right now. Personal savings is still quite low, which means there's more money to be spent, which goes into back to corporates their, to their profits.

So you've got this general kind of listed credit markets. The weakest though is private credit. And private credit I think is the one you do probably have to be most aware of. Obviously it's very ap, unlike the listed markets. I've seen a number of cockroaches. To be popping up with a little bit more frequency that probably most people would like.

We had redemptions redemptions in waters funds JP Morgan loans, and was limiting the amount of lending it was doing to, to private and really what kind of triggered this latest little bout or weakness. Concentration of software companies that private credit companies probably have exposure to.

And that was on the back of this massive kind of like content leap in the performance of AI coding agents, which leads lot software companies, business models maybe of them are, it's not existential for a lot of them, but it certainly means that they may not be able to charge as high or get as high margins on their businesses.

Then they have before. So we're seeing this mark down valuations in their stocks, and obviously that's reflected in the loans as well. And we're getting this visible. We can't see the loans themselves obviously, because they're okay. That's a selling point, the USP of the market, but we can see the shares of BDCs.

Business develop companies and they've obviously been B because the market is obviously what they have underneath loans they have aren't good shape. And because used to be, I remember something bad happens that be contained, these guys are kind, insulate the rest of the financial system. That's case. If you look at the banks have been lending to private funds and if you look at lending to non financial institutions that has mushroom in over the last couple years, you're really number of loans been know, extended from banking, a lot of private credit.

So there's your kind of vector of risk right there. And if there is something well happens in private credit, it. The credit markets, and then it's feasible, of course that, that's bad for the rest of the economy. We've obviously been here before, credit markets are big enough that they can do a lot of damage and if they turn down very rapidly.

So that's where we are in terms of the overall economy is strong. Credit market, again, fundamentals look okay, but the weakest link is private credit. And that's obviously the one to watch or watch as much as you can because of its opacity. It's typical, other than just watching red banner headlines coming up telling you which fund is doing what with redemptions.

Otherwise, it's very difficult to really get a proper handle unless you're in that particular space yourself of really what's going on. But certain that's. As the US economy's in a pretty good spot. And the one thing I think that could really derail it would be a protracted war. You asked how long it's protracted.

I, I dunno. But the longer that we have straight or moves blocked, the more the longer it takes to switch things back on. So the longer things are all streamed, the longer it takes to switch back on. So whether that's, if you power down refineries or refineries of damage. M them off six months to bring them back on.

And so there's many of these effects that will start to kick in. I think that's also one of the reasons why a lot of people in space are more bearish because they're kind seeing this and they, they can't see any upside. They're looking at

disruptions going way out, probably well into next year and that's when the basis of, even if the war stopped in quite short term.

So I think that does up to color your view and a protracted war would definitely.

**Erik:** Simon, as you talked about, private credit, it was concerning to me because frankly it, it echoes in my mind to about 19 years ago, the summer of 2007, when we were also talking about an opaque, not well understood in the broader finance community.

Small little piece of the credit market that couldn't possibly disturb anything else. And the reassurance at the time was. Don't worry, it's contained to subprime. There's nothing to worry about. Is this another setup like that?

**Simon:** It looks very much like it. I think that was Bernan himself who said contained.

Look, I go back to my axiom that the one thing that doesn't change is human nature. I think we're seeing that even within the private credit space in terms of when people have opportunities to make money. Off grid. They're away from regulation. The standard kind of emotions of greed and fear will kick in greed initially.

And people will start to take inflated risks to essentially earn money. Now, what are risks later? Hopefully they can not be around when the proverbial hits the fan. So I don't see why it wouldn't be any different. There was even a story today. One of the credit funds, if you look in the private credit fund is yet, it's a black box, but within it, there's even more black boxes.

That straight away reminded me of CDO Square. So here we had CDOs, which are already niche deriv products, but people started making up these CDOs or CDOs themselves. And I'm sure a lot of people at cyber are thinking this probably can't end well. And, here we're again, there's nothing new in finance.

**Erik:** Simon, I can't thank you enough for a terrific interview. Before I let you go, I'm sure a lot of listeners are gonna want to follow your work. You have to be somebody special and have a Bloomberg terminal in order to access most of it. Tell 'em for those who are lucky enough to have that access where they can find your writings.

**Simon:** Sure. And thanks again for having me on the show, Eric. So on the terminals, I have a column called Microscope. Tuesday and Thursday. I also

write for the blog, which is four hour, five days. Follow all the latest market developments.

**Erik:** Patrick and I will be back as Macro Voices continues right here [macrovoices.com](http://macrovoices.com).