

# What are equities telling us?

Report for the week ending May 23, 2026

Dylan Smith

## Key Takeaways

- **MONOLOGUE:** We take stock of the macro narrative. Our three scenarios ("Supply Shock Sorted," "Stagflation Nation," and "Rapid Resolution") and their probability weights are unchanged. The wrinkle is that markets aren't pricing the Iran conflict as a pure supply shock, motivating a Memo exploring the role of demand.
- **MACRO:** The data flow is running well ahead of forecasts. Consumers, labor markets, GDP nowcasts, and global PMIs all point to broadening strength.
- **MARKETS:** A risk-on week. Oil fell on Iran talks progress, rates round-tripped, and equities were broadly higher with small-caps shining.
- **MEMO:** Markets aren't following the textbook supply-shock playbook. The negative bond/stock correlation, rising industrial commodities prices, and bets on rate hikes all suggest investors believe demand is strong. That shifts the inflation-hedging toolkit. Front-end bonds now offer shelter, commodities offer diversification, and within equities, it's a sector story. Whether to stay long or get defensive comes down to your read on demand.

## Monologue

Sometimes things move slowly. There has been no major change in the macro narrative this week, unless you count a potential 60-day extension of the US-Iran ceasefire as one (at the time of writing, the parties are "edging closer" to such a deal). It looks more like a preservation of the status quo, enabling both parties to pursue their strategies of economic attrition to see who blinks first.

Against that backdrop, it's worth taking a step back to remind ourselves where we are from a macro standpoint.

*[Note: Shortly after publication, it was reported that President Trump claimed a deal with Iran to reopen the Strait of Hormuz was "largely negotiated." This claim goes beyond the initial ceasefire reports, but remains subject to further negotiations, and has not yet received a response from Iran.]*

**Inflation is rising sharply.** All metrics, whether "hard" or "soft," "quantitative" or "qualitative," "headline" or "core," indicate that an inflation spike is underway and spreading beyond gas prices into general goods prices. The shock is not evenly distributed — countries with more flexible markets and existing inflationary pressures (e.g., the US) or heavy reliance on imported energy (e.g., Australia) are seeing sharper price rises across the board, while others (e.g., Canada) are seeing milder inflation.

**Growth is holding up, though there are still some soft spots.** This week's Macro Monitor highlights just how much stronger activity has been than expected. Artificial intelligence is fueling a boom in technology and energy infrastructure spending and, increasingly, general business investment. Consumption growth is steady in aggregate, but unevenly distributed; lower-income consumers continue to increase spending at a slower rate than higher-income consumers. Labor markets are unambiguously improving, though slowly.

**Financial conditions remain very easy, especially in the US.** This is supporting growth and offsetting concerns regarding the future impact of higher inflation and higher expected interest rates. Businesses are not struggling to raise capital.

**The three medium-term scenarios we introduced in our Quarterly Outlook are unchanged, and the fairly flat probability distribution across them will not shift until there is clarity on the path toward the reopening of the Strait of Hormuz.**

*[Note: Needless to say, an imminent full and unfettered reopening would shift the probability weighting to Scenario 3.]*

- **Scenario 1: Supply Shock Sorted** (*Weight: 40%*): A stalemate in the Iran conflict persists through most of 2026, driving annual headline inflation to 5%. Growth slows but remains positive, driven by AI-related investment and fiscal largesse. The Fed shifts to a hawkish tone mid-year, and a rate hike follows around the turn of the year. This proactive stance means that the Fed can limit the response to two 25bp moves, which transmit through equity prices and credit conditions to cool the economy and contain second-round effects.
- **Scenario 2: Stagflation Nation** (*Weight: 30%*): The Strait of Hormuz blockade is not fully lifted until 2028, with intermittent openings and closures amid a frozen conflict keeping oil prices volatile and global hydrocarbon-linked supply chains severely disrupted. The inflation shock dampens demand. The Fed opts to “look through” the shock initially, allowing price pressures to move beyond volatile headline categories and into slower-moving core prices. A Stagflation regime results, with anemic growth and asset prices driven by their inflation betas.
- **Scenario 3: Rapid Resolution** (*Weight: 30%*): This scenario contemplates a deal to reopen the Strait of Hormuz in the very near term, enabling inflation to peak and begin falling in 2026. Within 12 months, the Fed eases interest rates and delivers another cut in the second year of the scenario to arrive at its judgment of the neutral rate. Meanwhile, growth remains around the long-run average, supported by the AI investment boom and fading economic uncertainty as a Democratic-controlled Congress mitigates executive economic policy risk (but lingering consumer weakness outside the top deciles prevents an overheating).

**The subject of this week's Memo is inflation resilience.** Across our scenarios, and especially in the first and second, inflation is the defining medium-term challenge for markets. We find in the research that markets are *not* trading the Iran conflict as a pure supply-driven inflation shock. To explain pricing, one must also assume robust or improving demand.

**One need not look hard to see that equity markets are sending a positive signal about demand,** especially in AI-exposed sectors (a set that's getting larger by the month). On closer inspection, so are other asset markets. The debate over whether demand would be hit so hard that the Fed might actually *lower* interest rates has all but disappeared from bond markets. And a rise in the industrial metals commodities index suggests productive investment is not about to stall.

**This leaves any investor who is nervous about recent market moves with a straightforward question to answer: "Do I believe that markets are misreading a stagflationary shock as a dual demand and supply shock?"**

In other words, though the economy is being driven by a supply shock, markets must make a judgment on the type of demand environment that shock is hitting. If the shift in supply is a given, taking a view on demand as being either robust or fragile can flip the investment case for a wide swath of assets. Any investment, and especially one in public or private equity, contains an underlying bet on demand.

The challenge is that one can read the real-time data in a way that supports either view. Indeed, this week's Macro Monitor outlines the case for robust demand partly in response to last week's observation that the arcMacro Activity Factor (which weights capacity-based measures heavily) is still putting growth below trend (though that may change as the model updates from April to May).

Luckily for me, I don't have to pin arcMacro to a single dogmatic view. Our assessment of aggregate supply and demand interactions is contained in the subjective adjustments we've made to the probability weightings in the scenarios above. Time will tell whether markets have the right read on demand. Until that debate is settled (retrospectively), there is another heuristic worth thinking about: bets against US growth have been a losing strategy since 2021.

**Dylan Smith**

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## Marginal Movers

### Rising 🙌

- **Supply elasticity:** [Saudi Arabia's Sabic loads urea vessel at Yanbu](#) — "The urea was trucked from the production hub of Jubail to Yanbu for loading, meaning that around 1,250 truckloads of 20t each would have had to be delivered to the port for this cargo alone."
- **Total Portfolios:** [Total Portfolio Approach: A Quant Lens](#) — The total portfolio approach to investing (TPA) has been aptly described as "buzzy but fuzzy [...]" We identify a set of tangible advantages and a countervailing set of possible risks from removing traditional strategic asset allocation constraints."

### Falling 🙋

- **K (more like a wonky Y?):** [K-shaped Economy or Not? Evidence from a Payments Survey](#) — "Rather than the canonical K-shaped recovery—in which lower-income consumer spending declines while higher-income consumer spending expands—our findings point to a bifurcated recovery in which both groups' spending grew but at sharply divergent rates."
  - **The old economy:** [The manufacturing renaissance is real, but only in advanced manufacturing](#). — "Since 2022, four subsectors have accounted for essentially all of the net growth in U.S. manufacturing industrial production. That's more real than the skeptics think."
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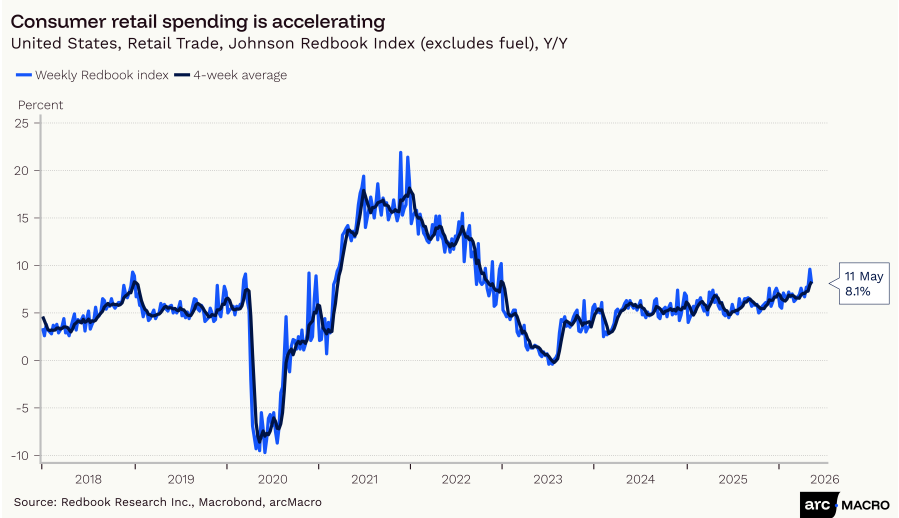
## Macro Monitor

It was a light week for macro data. In the coming week, we'll get important new data on inflation and business activity. In the meantime, the lacuna in new data gives us a chance to summarize the underlying economic strength we're witnessing in the US and global economies.

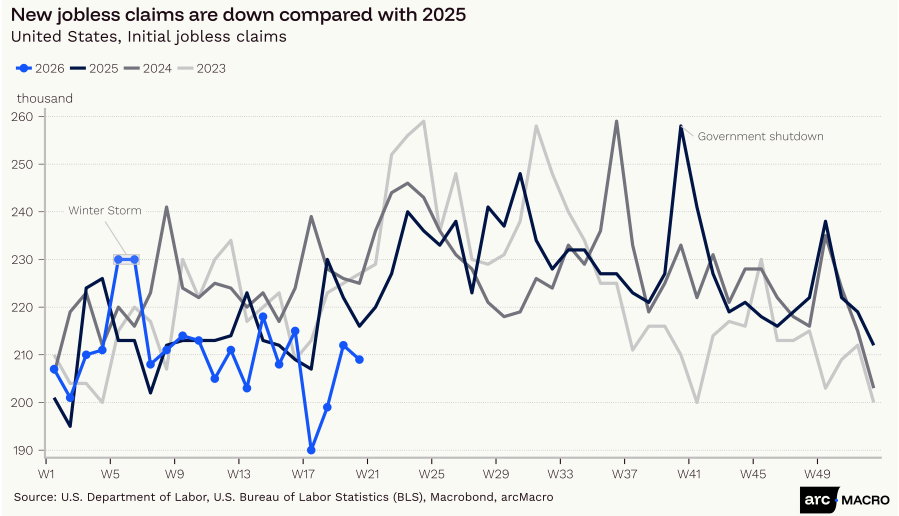
1. The economic data flow is significantly stronger than Wall Street forecasters expect.



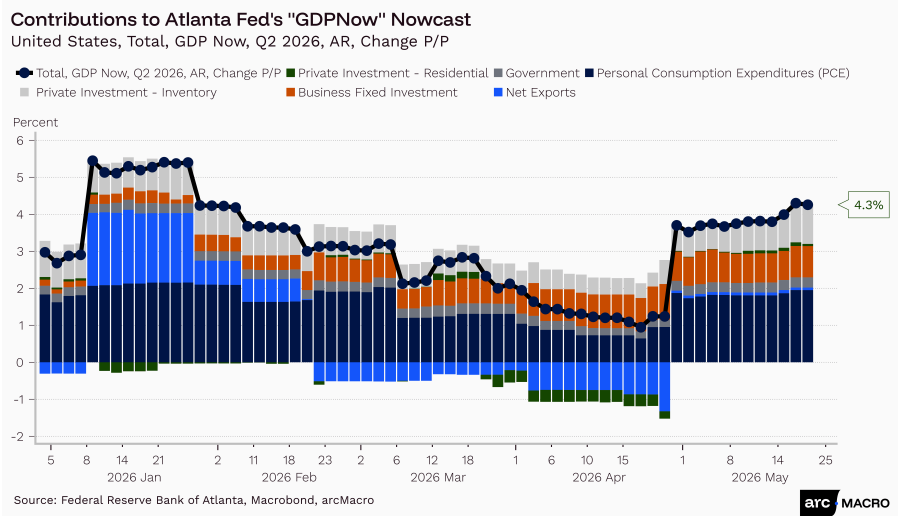
2. Consumers aren't just absorbing higher prices; they're accelerating spending (chart excludes fuel purchases).



3. The US labor market is steadily improving across a range of indicators.

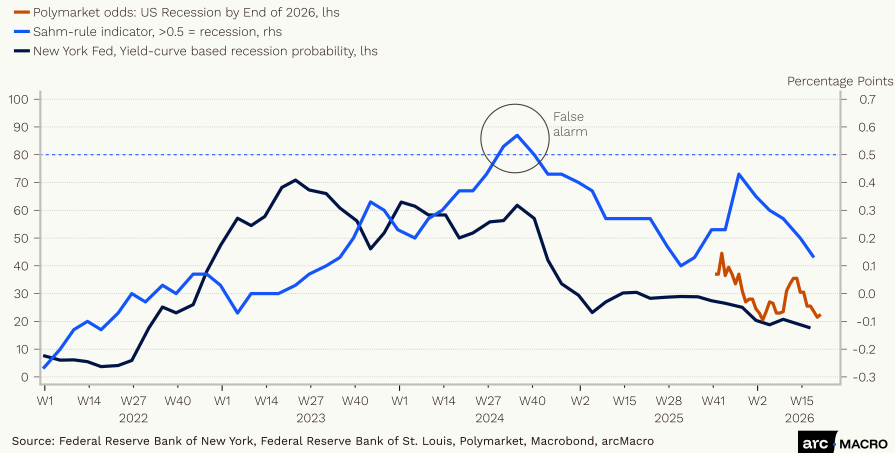


4. The Atlanta Fed's "GDPNow" nowcast is tracking Q2 US GDP growth above 4% annualized.



5. Various measures of recession odds have declined steadily.

**Recession odds are falling**  
US, Recession indicators



6. Global PMIs indicate strengthening cyclical activity in most economies, with momentum carrying through into May in early releases (less so in the Eurozone).

**A Global Greening**

World, S&P Global PMI, >50 signals expansion

	May '25	Jun '25	Jul '25	Aug '25	Sep '25	Oct '25	Nov '25	Dec '25	Jan '26	Feb '26	Mar '26	Apr '26	May '26
<b>World</b>	49.5	50.4	49.7	50.9	50.7	50.8	50.5	50.4	50.9	51.8	51.3	52.6	
World, Developed	50.0	50.5	49.2	50.9	50.3	50.6	50.5	50.5	51.4	51.8	52.0	53.8	
World, Emerging	49.2	50.4	50.1	50.9	51.2	51.1	50.5	50.4	50.6	52.0	50.7	51.6	
<b>Americas</b>													
United States	52.0	52.9	49.8	53.0	52.0	52.5	52.2	51.8	52.4	51.6	52.3	54.5	55.3
Canada	46.1	45.6	46.1	48.3	47.7	49.6	48.4	48.6	50.4	51.0	50.0	53.3	
Brazil	49.4	48.3	48.2	47.7	46.5	48.2	48.8	47.6	47.0	47.3	49.0	52.6	
Mexico	46.7	46.3	49.1	50.2	49.6	49.5	47.3	46.1	46.3	47.1	48.9	47.7	
<b>Europe</b>													
EU	49.2	49.2	49.6	50.4	49.7	49.8	49.5	48.8	49.5	50.5	51.3	52.0	
Euro Area	49.4	49.5	49.8	50.7	49.8	50.0	49.6	48.8	49.5	50.8	51.6	52.2	51.4
Austria	48.4	47.0	48.2	49.1	47.6	48.8	50.4	49.3	47.2	49.4	52.4	51.2	
Czech Republic	48.0	50.2	49.7	49.4	49.2	47.2	48.0	50.4	49.8	50.0	52.8	52.9	
France	49.8	48.1	48.2	50.4	48.2	48.8	47.8	50.7	51.2	50.1	50.0	52.8	48.9
Germany	48.3	49.0	49.1	49.8	49.5	49.6	48.2	47.0	49.1	50.9	52.2	51.4	49.9
Greece	53.2	53.1	51.7	54.5	52.0	53.5	52.7	52.9	54.2	54.4	54.5	52.4	
Ireland	52.6	53.7	53.2	51.6	51.8	50.9	52.8	52.2	52.2	53.1	53.7	54.9	
Italy	49.2	48.4	49.8	50.4	49.0	49.9	50.6	47.9	48.1	50.6	51.3	52.1	
Netherlands	49.0	51.2	51.9	51.9	53.7	51.8	51.8	51.1	50.1	50.8	52.0	54.4	
Poland	47.1	44.8	45.9	46.6	48.0	48.8	49.1	48.5	48.8	47.1	48.7	48.8	
Spain	50.5	51.4	51.9	54.3	51.5	52.1	51.5	49.6	49.2	50.0	48.7	51.7	
Switzerland	42.4	48.7	49.5	48.2	46.1	48.1	49.6	46.4	48.8	47.4	53.3	54.5	
United Kingdom	46.4	47.7	48.0	47.0	46.2	49.7	50.2	50.6	51.8	51.7	51.0	53.7	53.7
<b>Asia &amp; Pacific</b>													
ASEAN	49.2	48.6	50.1	51.0	51.6	52.7	53.0	52.7	52.8	53.8	51.8	50.7	
Australia	51.0	50.6	51.3	53.0	51.4	49.7	51.6	51.6	52.3	51.0	49.8	51.3	50.2
China	48.3	50.4	49.5	50.5	51.2	50.6	49.9	50.1	50.3	52.1	50.8	52.2	
India	57.6	58.4	59.1	59.3	57.7	59.2	56.6	55.0	55.4	56.9	53.9	54.7	54.3
Indonesia	47.4	46.9	49.2	51.5	50.4	51.2	53.3	51.2	52.6	53.8	50.1	49.1	
Japan	49.4	50.1	48.9	49.7	48.5	48.2	48.7	50.0	51.5	53.0	51.6	55.1	54.5
Malaysia	48.8	49.3	49.7	49.9	49.8	49.5	50.1	50.1	50.2	49.3	50.7	51.6	
New Zealand	46.4	49.3	53.0	50.2	50.3	51.7	52.0	56.1	55.0	54.6	52.8	50.5	
Philippines	50.1	50.7	50.9	50.8	49.9	50.1	47.4	50.2	52.9	54.6	51.3	48.3	
Russia	50.2	47.5	47.0	48.7	48.2	48.0	48.3	48.1	49.4	49.5	48.3	48.1	
South Korea	47.7	48.7	48.0	48.3	50.7	49.4	49.4	50.1	51.2	51.1	52.6	53.6	
Taiwan	48.6	47.2	46.2	47.4	46.8	47.7	48.8	50.9	51.7	55.2	53.3	55.3	
Thailand	51.2	51.7	51.9	52.7	54.6	56.6	56.8	57.4	52.7	53.5	54.1	52.7	
Turkey	47.2	46.7	45.9	47.3	46.7	46.5	48.0	48.9	48.1	49.3	47.9	45.7	
Vietnam	49.8	48.9	52.4	50.4	50.4	54.5	53.8	53.0	52.5	54.3	51.2	50.5	

See the appendix for arcMacro proprietary Factors and the Key Macroeconomic Indicators tracking chart.

# Market Monitor

## Public markets

Markets shrugged off a pessimistic period in mid-May to post a broadly strong risk-on week. The WTI crude spot price closed below \$100 per barrel and was \$8.82 per barrel lower over the week, helped by hints of progress in talks with Iran. As an aside, that market management strategy may be running out of room, and another round of false "war is over" rhetoric could disconnect markets from political commentary on the war (at least from the US side).

The sovereign rates complex looked like it would be the big mover, but a sharp rise in interest rates early in the week was gradually unwound to leave benchmarks close to unchanged in the US, and meaningfully lower in Canada (-16 basis point drop in 2- and 10-year GoC bond yields on an encouraging inflation print) and the UK (highly volatile political backdrop, but the UK also got better than expected inflation numbers).

Equities had a relatively strong week across the board. The S&P 500 rose by 0.9%, with Health Care, Utilities, and Real Estate the strongest performers. The small-cap Russell 2000 index rose by 2.7% in a signal that markets are feeling good about economic growth. Robust early PMI releases for May helped extend that strength to global equities. The S&P 500 is still up 8.9% since the start of the Iran conflict, and the Nasdaq Composite index 16.1% higher.

*See the appendix for the market monitor table*

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## Memo

### How to hide from inflation

**Bottom line:** *There is a cross-asset portfolio investing playbook for purely supply-driven inflation. Markets, and especially equities, are not following it. The negative bond/stock correlation, higher prices of non-energy commodities, and increasing bets on higher interest rates, all suggest that investors believe that underlying demand is strong. That shifts the appropriate asset mix for responding to rising inflation.*

**What it means for investors:** *Like it or not, portfolio strategy now involves taking a view on demand. Those who think markets are too sanguine on growth have an opportunity to position for a reversal. The rest are firmly in the consensus, and their views are already priced in with limited upside. For them, the time may be ripe to take profits on equities and shift to a more defensive allocation to short-end rates (now attractively priced) and commodities. In private and public equities, we identify our preferred inflation-resilient industries.*

With the Strait of Hormuz set to enter its fourth month of virtual closure this week, even the most committed inflation dove has to acknowledge that we will not be able to avoid a serious bout of inflation for the rest of the year and likely beyond.

That has clear market strategy implications. In this week's Memo, we're running through the major asset classes and asking how we can hide from inflation.

### **The type of shock matters**

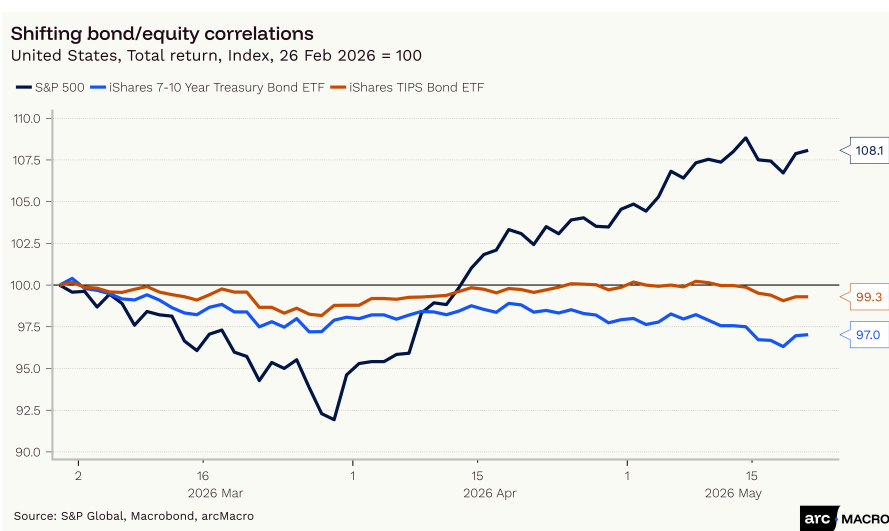
Before we get to asset performance, we need to distinguish between two different types of inflation-generating shock.

**Demand-driven inflation ("good" inflation)** happens when a cyclical upswing in consumption and investment causes temporary bottlenecks and improved pricing power. This type of inflation is easy for central banks to manage, as their job is simply to cool the economy. Interest rates rise (and fixed income returns fall), but stocks are lifted by strong demand and improved margins, so the bond/equity correlation is negative, and the classic 60/40 portfolio provides effective risk management.

**Supply-driven inflation ("bad" inflation)** occurs when a disruption to productive or trading capacity causes unexpected shortages, which in turn drive prices up. Supply shocks also harm growth (both directly and indirectly, as spending must be reduced in some areas to cover higher prices in others). Lower growth and weaker purchasing power are generally bad news for equities, and so a positive correlation between returns on stocks and bonds should emerge. The 60/40 portfolio performs poorly.

**What type of shock are we in now? Common sense says a textbook supply shock.** Supplies from the Gulf have been removed from the economic system, causing the prices of affected final goods to surge. So you would expect to see a positive correlation between stocks and bonds, confirming that interpretation.

**Alas, it's not that simple.** As the chart below shows, markets initially had a textbook reaction to the shock, with stock and bond prices falling in tandem. But since mid-April, this pattern has reversed. Stocks have been on a tear, and bond returns have only worsened as interest rates have soared.



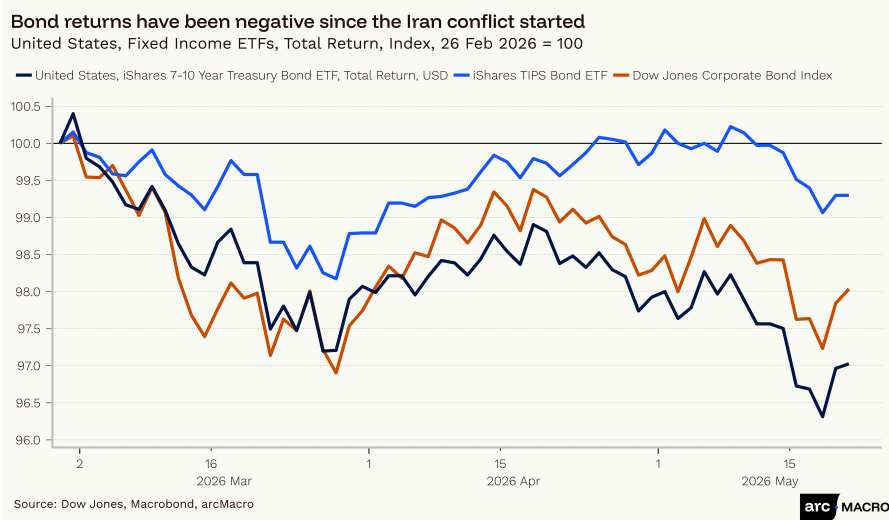
Thus, asset pricing reflects the real-time consensus on a debate between "Stagflation" and "pure inflation." At face value, markets appear uncertain as to whether we're facing a pure supply shock or a combination of supply and demand shifts that are generating inflation without significantly harming growth.

We need to take this into account when thinking about how to position a portfolio or investment decision to be inflation-robust.

### **Bonds have moved enough to provide shelter**

**No matter the type of shock, bonds are no place to hide from unexpected future inflation.** Large supply- or demand-driven inflation shocks both raise interest rates and therefore lower bond prices. The timing and extent may differ – supply shocks require a less forceful interest rate adjustment to contain inflation, as demand does not need to be squashed. Central banks need only do enough to convince economic decision-makers that they are not ignoring inflation risks.

**Global bond markets have behaved predictably, if a tad dramatically.** Recent headlines have fixated on long-dated bonds hitting post-2008 record yields on both sides of the Atlantic. That's because the entire yield curve has shifted up: shorter-dated rates have risen to reflect a now-dominant belief that central banks will need to raise interest rates.



Meanwhile, the forces justifying an upward-sloping yield curve from there on out to 10- and 30-year notes remain in place. These are two negatives – unsustainable public debt trajectories and higher long-term inflation risk – and one positive – the productivity gains of AI delivering higher returns on capital.

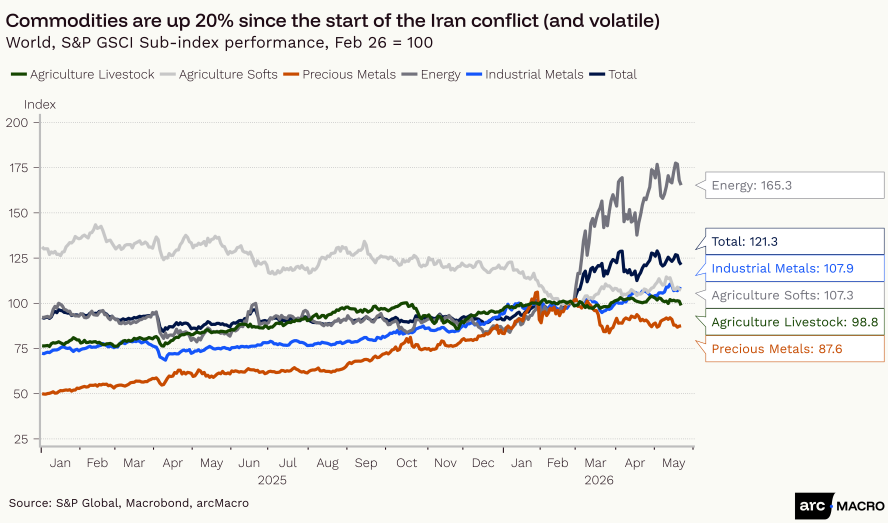
**There is now an advantage to the size and speed of the rise in interest rates: they've been sharp enough to make bonds a place to ride out the storm.** If you buy *and hold* a 2-year Treasury to maturity, you're *guaranteed* a return of 4.13% at annualized rates. That compares with an *uncertain* forward earnings yield of 4.24% for the S&P 500 based on the current ~21x P/E ratio. The 2-year yield corresponds to two 25-basis-point Fed hikes over that period, which would be our base case for a well-managed shock — just enough to anchor expectations without excessively dragging on demand.

**Inflation-protected bonds** (TIPS in the US) are an even better defensive investment. [Research](#) has shown that they're the one asset class guaranteed to deliver positive returns if an unexpected inflation shock hits (as long as they're held to maturity).

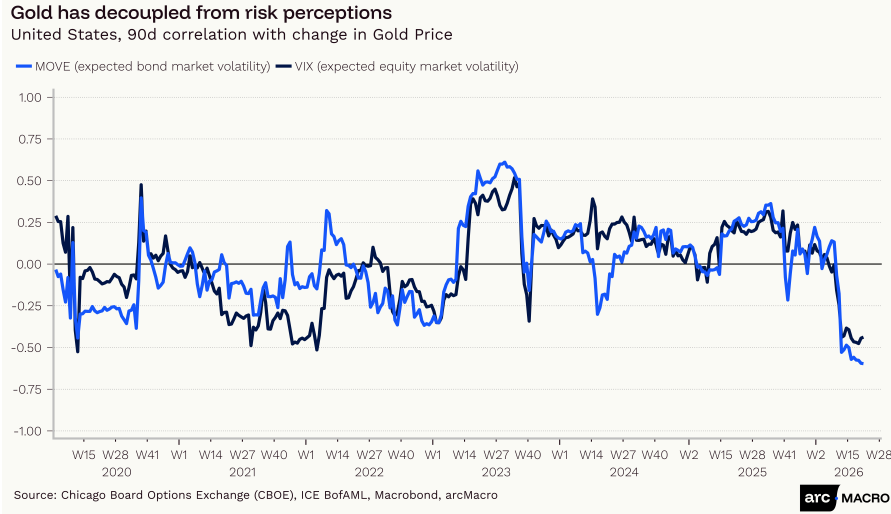
**Commodities are an additional source of cover**

**At the risk of stating the obvious, energy commodity prices rise during oil shocks.** They have easily outperformed other asset classes since the start of the Iran conflict. Gaining some exposure to commodity markets is the easiest way to macro-proof a portfolio at this uncertain juncture.

Even if you're unsure about the outlook for commodities (a reopening of the Strait would surely harm energy commodity prices), exposure is valuable for its weak correlation with other asset classes. If we are in a stagflation episode that hurts both bonds and equities, or if the blockades persist longer than expected, or if the reopening is only partial, the diversification offered by commodities is invaluable.



**A quick word on Gold: it should not be thought of as a direct short-to-medium-term inflation hedge.** Average annual gold price volatility is ~15%, orders of magnitude higher than consumer price inflation (~1%). Gold is an important long-run portfolio diversifier and inflation anchor, but its correlations with macro trends are at best shaky in the short term. In fact, since the start of hostilities in the Gulf, gold has become *negatively* correlated with oil prices and measures of geopolitical risk – the opposite of its supposed USP. Having fallen by around 10% since the start of the Iran war, we see an attractive entry point for a long-term gold hold, but we would not add to existing positions for shorter-run hedging purposes.

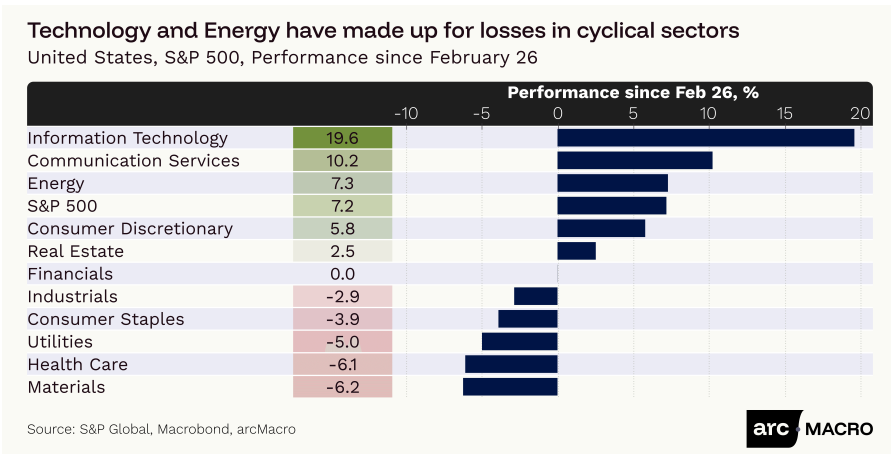


### Equities depend on your priors

Let's return to the question of why equities have not sold off alongside bonds, as one would expect during a classic oil price shock. There is more going on than meets the eye.

First of all, not all stocks are the same. If you drill down to the sector level, equity performance has been a little closer to the theory than the aggregates suggest. The table below shows that, since the day before the first strikes hit Iran, the inter-sectoral spread between S&P 500 sectors is nearly 30 percentage points. Technology and AI-exposed sectors have gone from strength to strength, and the energy sector is up. Everything else is essentially flat or down.

In other words, energy stocks are performing as expected, and AI-exposed industries are seen as immune to cyclical inflation. This has been enough to more than offset the textbook weakness in inflation and rate-sensitive industries.



With that in mind, we should focus on stocks outside the hyperscalers and energy majors. In prior work (see [The Might of Macro](#)), we assembled a long history of data on small- and medium-sized listed companies by market capitalization, divided them into more than 50 industries, and estimated the sensitivity of their growth, earnings, and valuations to our growth and inflation factors ("betas").

We grouped the industries into inflation archetypes, which we present below. It's important to remember that there are industries that benefit from inflation, generating higher revenues and stronger margins. Resource companies are an obvious example, but they're not alone. Utilities, Trucking, and even Durables Wholesaling companies can increase their growth and profitability in inflationary times.

Industries with very little inflation sensitivity – either because they have the pricing power to pass on costs, or because their own cost base is inflation-proof – are also important defensive industries (Finance, many goods producers and distributors, and Telecoms are examples).

Industry class	Price beta of revenue	Price beta of EBITDA margin	Description	Industries
<b>Inflation winners</b>	High	Positive	Costs are fixed or adjustable, and demand is inelastic or correlated with sources of inflation, raising margins. These are the industries that generate inflation for the rest of the economy.	<ul style="list-style-type: none"> <li>•Oil and Gas</li> <li>•Trucking</li> <li>•Mining</li> <li>•Lumber processing</li> <li>•Durables Wholesaling</li> <li>•Specialty Materials Manufacturing</li> <li>•Utilities</li> <li>•Vehicle Retailing</li> <li>•Petroleum products</li> <li>•Primary Metal Manufacturing</li> </ul>
<b>Passers-through</b>	High	-0 (insignificant)	Cost increases are approximately offset by pricing pass-through	<ul style="list-style-type: none"> <li>•Leasing</li> <li>•Chemical Manufacturing</li> <li>•Administrative services</li> <li>•Accommodation</li> <li>•Mining Services</li> <li>•Machinery Manufacturing</li> <li>•Electronics Manufacturing</li> <li>•Appliance Manufacturing</li> <li>•Metal Product Manufacturing</li> <li>•Clothing Retailing</li> <li>•Consumables Wholesaling</li> <li>•Medical Manufacturing</li> <li>•Clothing Manufacturing</li> <li>•Conglomerates &amp; Holding Companies</li> </ul>
<b>Cost-base runaways</b>	High	Negative	Industry structure means high exposure to rising costs (via input costs or a correlated demand decline from consumer switching), which can only be partially offset via pricing adjustments	<ul style="list-style-type: none"> <li>•Food &amp; Beverage Manufacturing</li> <li>•Professional Services</li> <li>•Food Services</li> <li>•Other Transportation</li> <li>•Entertainment</li> <li>•Online Retailing</li> <li>•Air Transportation</li> </ul>
<b>Cycle leaders</b>	Low	Positive	Industry demand and pricing power leads the broader price cycle (e.g., pre-GFC or COVID construction boom), but may be hardest hit in next phase	<ul style="list-style-type: none"> <li>•Building Construction</li> <li>•Other Construction</li> </ul>
<b>Bullet-dodgers</b>	Low	-0 (insignificant)	Not exposed to inflationary forces, or costs can be adjusted to approximately offset inflation	<ul style="list-style-type: none"> <li>•Telecommunications</li> <li>•Investments</li> <li>•Educational services</li> <li>•Banks</li> <li>•Specialty Retailing</li> </ul>
<b>Inflation losers</b>	Low	Negative	Can't claw back cost increases due to fixed contracts or low pricing power	<ul style="list-style-type: none"> <li>•Vehicle Manufacturing</li> <li>•Furniture Manufacturing</li> <li>•General Merchandise Retailing</li> <li>•Healthcare Services</li> <li>•Insurance</li> <li>•Printing and publishing</li> <li>•Textiles Manufacturing</li> <li>•Personal and Social Services</li> <li>•Internet</li> <li>•Funds &amp; Trusts</li> <li>•Real Estate</li> <li>•Software</li> </ul>

Note: Based on median beta  
Source: arcMacro

This analysis did not account for the *type* of inflation shock, instead mixing historical supply and demand shocks. So it's a valuable guide on where to position if you're agnostic on growth and long equities.

To take the analysis a step further, we also examined how companies perform in a stagflationary scenario with spiking inflation and weak or negative growth.

**Industry selection can shield portfolios from the macro storm**  
 Median beta of EBITDA margin to real and price factors



There are two key findings. One is that, aside from oil and gas, no industry sees improving margins under such a scenario. Equities in general are to be avoided in a stagflation episode — a very different view from the inflation-only scenario.

The chart also shows the industries to avoid if strong relative positioning within equities is the goal. These are industries that perform best when growth is very strong and inflation is low: Air Transportation, REITs, and (interestingly) Internet and Software companies among them (likely due to high interest-rate exposure correlated with inflation risk).

**Investing during supply shocks is all about demand**

The implication of the analysis above is that, while the economy may be facing a global supply shock, positioning is about your views on demand.

If, like markets, you think growth will hold up and we're facing an inflation shock without major implications for aggregate demand, then your view is in the price. You would be justified in staying long on equities, but given the still-elevated level of uncertainty in the market, it may be time to seek out some inflation hedges, whether via sector tilts, commodities, or even harvesting high short-term yields.

If you're of the view that a longer blockade will damage growth and cause stagflation, it's open season, especially if you're able to take short positions on equities and industrial commodities.

Our own preference would be to manage risk across potential scenarios by seeking out assets that offer inflation protection and a neutral growth profile.

## Appendix

### Proprietary Factor and Regime Model and Key Indicators

#### The Week in Markets

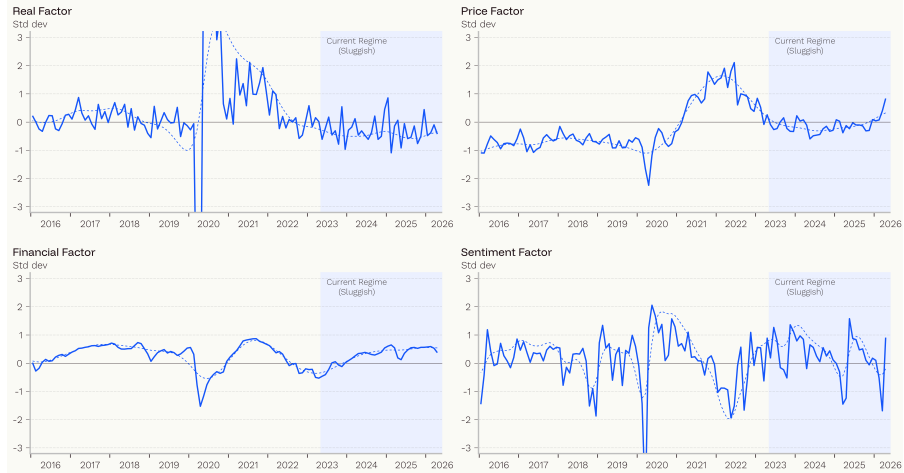
	Latest*	Change since last week (units)	Change since last week (%)	3-month change (units)	3-month change (%)	Year-to-date change (units)	Year-to-date change (%)
<b>US Equities</b>							
S&P 500	7473	65	0.9	612	8.9	628	9.2
Information Technology			1.0		23.2		18.1
Financials			1.6		-0.3		-5.4
Consumer Discretionary			1.9		7.2		2.3
Communication Services			-1.9		12.2		9.0
Health Care			3.3		-4.7		-3.4
Industrials			0.2		-2.7		10.6
Consumer Staples			-1.0		-2.4		10.1
Energy			-0.4		7.1		31.5
Utilities			3.3		-1.7		5.9
Real Estate			3.0		3.2		10.9
Materials			0.0		-5.1		9.9
Nasdaq Composite			0.5		16.1		13.3
Dow Jones Industrial Average			2.1		2.4		5.2
Russell 2000			2.7		7.7		15.6
<b>Global Equities</b>							
DM: MSCI World index			1.3		6.9		10.5
EM: MSCI EM Index			1.1		8.5		20.9
CAN: TSX Composite			1.9		2.6		8.7
EUR: STOXX 600			3.0		0.0		5.6
HK: Hang Seng			-1.4		-4.1		-0.1
JPN: TOPIX			0.7		1.0		14.2
UK: FTSE 100			2.7		-1.5		5.4
<b>Sovereign Fixed Income</b>							
US: 2-year Treasury	4.13	0.04		0.66		0.66	
US: 5-year Treasury	4.27	0.01		0.62		0.54	
US: 10-year Treasury	4.56	-0.03		0.48		0.38	
CAN: 2-year GoC	2.91	-0.16		0.47		0.33	
CAN: 10-year GoC	3.54	-0.16		0.32		0.12	
UK: 10-year Gilt	4.97	-0.27		0.53		0.43	
GER: 10-year Bund	3.06	-0.05		0.31		0.21	
CHN: 10-year CGB	1.75	-0.01		-0.0409		-0.0954	
JPN: 10-year JGB	2.73	0.12		0.6		0.67	
<b>Corporate Bond Spreads</b>							
US: A-rated	60.5	-3.8		-8.5		-9.3	
US: BBB-rated	93.5	-3.4		-10.8		-11.0	
<b>Foreign Exchange Rates</b>							
DXY US Dollar Index	99.2		0.0		1.3		0.9
EUR/USD	1.16		-0.2		-1.3		-1.3
USD/CAD	1.38		0.2		0.6		0.6
USD/CNY	6.8		0.0		-1.5		-2.7
USD/JPY	159		0.2		2.7		1.6
GBP/USD	1.34		0.3		-0.3		-0.2
USD/CHF	0.788		0.5		1.8		-0.6
<b>Commodities</b>							
WTI Crude	96.6	-8.82	-8.4	30.2	45.4	39.2	68.2
Gold	4506	-21.9	-0.5	-499	-10.0	138	3.2
S&P GSCI Commodities			-2.6		22.2		33.4
S&P GSCI Industrial Metals			1.6		11.5		14.1
S&P GSCI Agriculture			0.7		6.3		3.9

\* Weekly closing value. Color indicates positive (green) or negative (red) change since prior week.

Source: S&P Global, Russell Investment Group, Nasdaq, U.S. Department of Treasury, Macrobond Financial AB, Central Bank of Germany (Deutsche Bundesbank), Bank of Canada, Intercontinental Exchange (ICE), International Monetary Fund (IMF), CME Group, LBMA (London Bullion Market Association), Robert Shiller, Chicago Board Options Exchange (CBOE), U.S. Department of Labor, U.S. Bureau of Labor Statistics (BLS), Federal Reserve Bank of Atlanta, Citi, Federal Reserve Bank of St. Louis, Energy Information Administration (EIA), MSCI, STOXX, Tokyo Stock Exchange, Toronto Stock Exchange, FTSE Russell, Hang Seng Indexes Company, Pitchbook | LCD, arcMacro

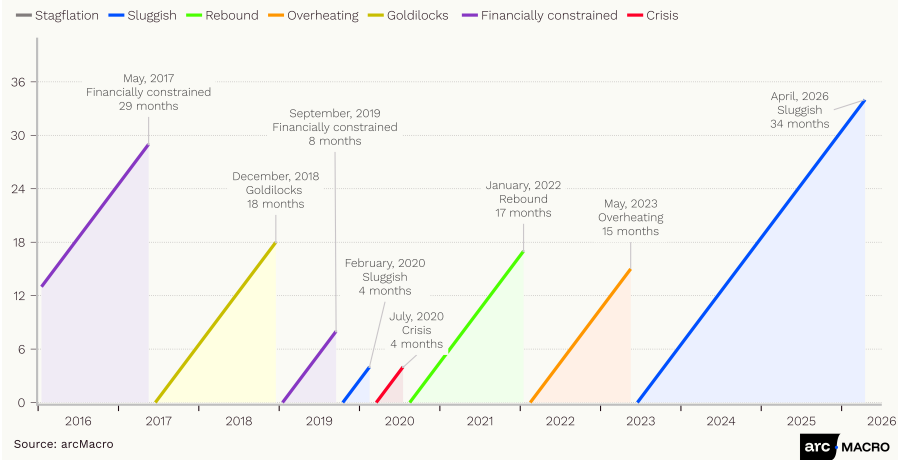
arc MACRO

**arcMacro Real Time Factors**  
United States, z-score



Source: arcMacro

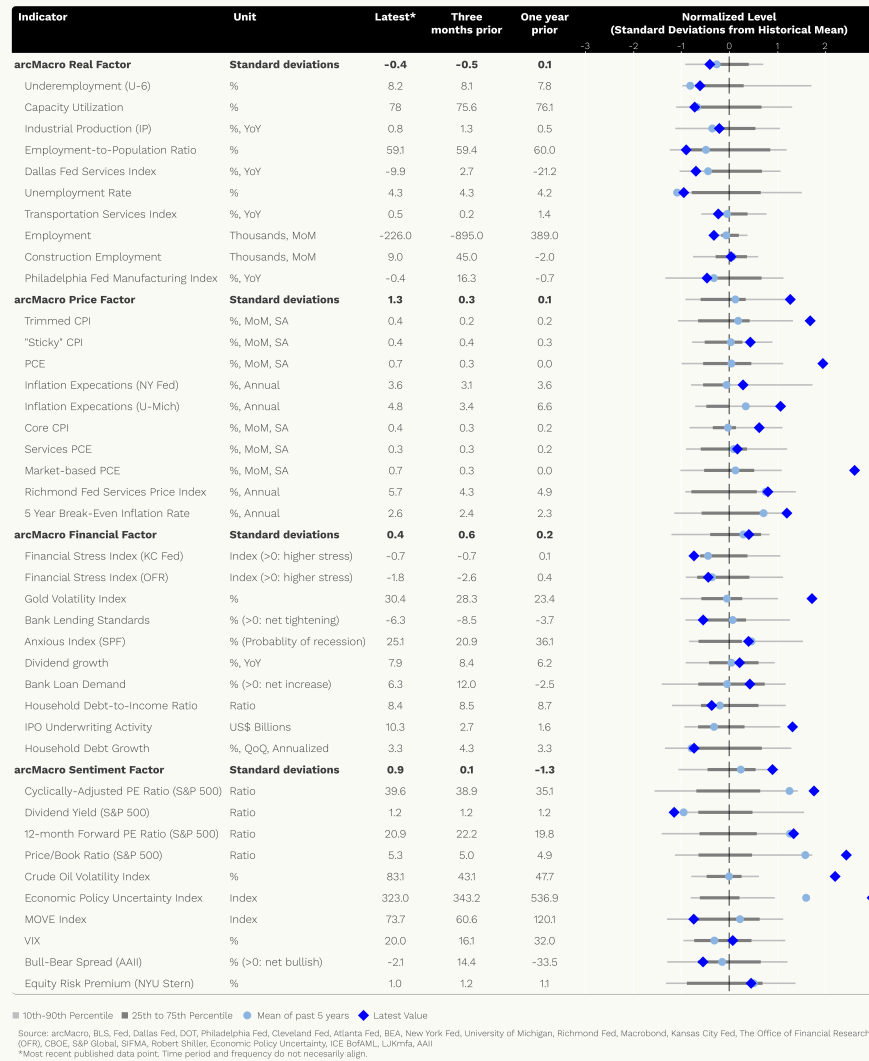
**arcMacro Regime Summary**  
United States, Cumulative Months in Regime



Source: arcMacro



**arcMacro Factor Input Monitor**  
Top 10 inputs by factor loading



## Disclosures

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