Once upon a time, there was a tight labor market, inflation and the FED…

Contrary to a widespread belief, the true ultimate driver of long-term inflation is not commodity prices nor supply chain disruption. It is wages. That is because inflation is essentially a redistribution of wealth between owners of financial assets and other creditors on the one hand, to workers, producers of tangible goods or debtors on the other. Such redistribution depends on the balance of power between those stakeholders.

This balance of power was massively in favor of rentiers against workers, from the beginning of the 1980 to the eve of the 2020's, mechanically leading to substantially expanding corporate margins and therefore wealth concentration. However, as is now abundantly clear, this long-term tide has reversed: in other words, ongoing inflationary pressure on a global basis is not transitory in nature. That will remain the case as long as wages demonstrate durable resilience.

In the U.S., wages are clearly displaying such resilience at the moment. According to Vincent Deluard from StoneX, the most up-to-date statistical tool in that field is the Atlanta Fed wage tracker, which shows persisting wage acceleration in many crucial sectors. The data suggests a bifurcated job market where wage growth is moderating for white-collar jobs but keeps increasing for blue-collar positions. The resilience of the labor market is confirmed by non-farm payrolls and job openings: according to the BLS breakdown of job openings, demand for service jobs is still growing.

Taking more perspective, increasing numbers of labor markets worldwide now look STRUCTURALLY tight, notably for demographic reasons and that is quite apparent in the outcome of recent pay negotiation rounds: as an example, German public sector unions obtained an impressive 10.5% pay increase for next year.

Vincent Deluard underscores another interesting trend: the “secular rise of the gig economy”. According to a survey by Prudential Financial, 81% of Gen-Z workers and 77% of millennials in the U.S. are either pursuing or considering side hustle work to get by. It implies that households are increasingly able to maintain, or even increase, their real incomes by working gigs, even if their main income source becomes pressured. That is further altering the traditional wage/growth relationships. Ultimately and quite crucially, we reckon that is one of the main drivers that will lead central banks to revise upwards their inflation targets from the “classical” 2% level to thresholds closer to 3 or 4%.
If that pivot occurs next year, 2023 risks being more of the same in terms of traditional asset classes behavior. Acknowledging a higher inflation target will steepen the yield curve and pressure the equity multiples. The perception of a US monetary debasement may reverse this year's USD strong appreciation and benefit EM, commodities and metals.