

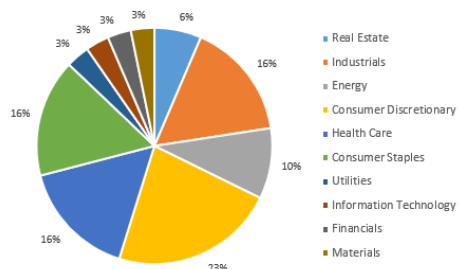
10.06.2022

Hedging inflation

- US CPI day. Until recently, the consensus was the May CPI report would support the idea we'd hit peak inflation. However, the relentless rally in crude oil has rekindled inflation fears.
- [*"Nowhere to hide"*](#) showcased Qi's best-in-class optimiser & its ability to produce out-of-sample baskets that didn't rely on backfitting - it uses only the information available at the time, yet still produced great tracking.
- That basket was a 50:50 long/short & client feedback queried whether we could produce such good results with a long only. The basket below is 100% long & total period correlation with inflation expectations (as measured by 5y USD inflation swaps) is 83%.



- As a reminder the Qi optimizer is a machine learning process based on asset prices & whatever target variable is chosen. There is no bottom-up analysis or subjective opinion. This is not a case where sector analysts opine on which stocks have relative pricing power.
- In that regard, it is interesting to see the mix of stocks the optimiser chooses & the weights it assign. Looking by sector, two intuitive picks – energy & real estate – feature but their weights are probably modest relative to typical preconceived notions. Even more surprising is the large weight of Consumer Discretionary. But a 83% correlation stat doesn't lie. Science or opinion?



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