# GIS INSIGHTS

WEEKLY PODCAST

LOCAL INSIGHT INVESTORS

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TITLE: **Thinning Shock Absorbers**

TRANSCRIPT:

**Host:**
Eric, investors have had a lot to digest this week: renewed tension in the Middle East, oil above 85 dollars, a sharp technology sell-off and central banks sounding increasingly cautious.
Yet the global economy still appears remarkably resilient.
What is the market really telling us?

**Eric:**
I think the most revealing signal came from the bond market.
US inflation data were softer this week, but the ten-year Treasury yield remained close to its recent highs, at around 4.5%.
Normally, better inflation news should push bond yields meaningfully lower. The fact that it did not tells us investors are looking beyond the latest inflation report.
They are focusing on three things: resilient economic activity, persistent government deficits and the possibility that higher energy prices keep inflation elevated.
So the bond market is effectively saying: inflation may be improving, but the problem has not disappeared.

**Host:**
How important is the rise in oil?
Brent above 85 dollars is uncomfortable, but it is hardly unprecedented.

**Eric:**
That is true. The current oil price, by itself, is unlikely to derail global growth.
The concern is that the energy system has fewer shock absorbers than it did during previous geopolitical crises.
American strategic oil reserves remain unusually low. Russian infrastructure continues to face disruption.
Maintenance in Kazakhstan has reduced some additional supply, and the risks now extend beyond the Strait of Hormuz.
Iran has reportedly encouraged the Houthis to threaten shipping through the Bab el-Mandeb and potentially target Saudi energy facilities. That introduces risk to another major route connecting Europe and Asia.
The important question is therefore not whether oil reaches 100 dollars tomorrow.
It is whether shipping becomes less reliable, insurance becomes more expensive and refined products such as diesel and jet fuel remain elevated.
Those costs gradually spread through the global economy.

**Host:**
Does that mean central banks could raise rates again?

**Eric:**
It is certainly back within the range of possible outcomes.
Only a few months ago, the debate was about when central banks would cut interest rates. The conversation has now shifted from delayed cuts to the possibility of further tightening.
The Federal Reserve has gained some flexibility from softer inflation data, but it does not have complete freedom.
The American consumer is still spending. The labour market has not weakened materially, and estimates of second-quarter economic growth have continued to improve.
If you combine resilient demand with higher energy and transportation costs, inflation can prove more persistent than expected.
That is why bond investors are becoming less convinced that the inflation problem has been solved.

**Host:**

Technology shares also had a difficult week, even though companies continue to report extraordinary demand for artificial intelligence infrastructure.
Is the AI investment story beginning to unravel?
**Eric:**
I would not describe it as an unraveling. I would describe it as a transition.
For the past two years, investors have been rewarded simply for identifying companies exposed to artificial intelligence.
Now they are asking a more demanding question: how much capital is required, how will that spending be financed and what return will shareholders ultimately receive?
TSMC is a good example.
Its quarterly profit rose sharply, it increased its revenue expectations and it announced capital expenditure of between 60 and 64 billion dollars.
Those are exceptional numbers, yet the shares still declined.
That tells us the market is no longer satisfied simply by strong demand. Investors want to know whether even exceptional growth is sufficient to justify current valuations.

**Host:**
So this is more about price and capital efficiency than weakening demand?
**Eric:**
Exactly.
Demand for advanced semiconductors, data centres, memory and power infrastructure remains extremely strong.
But the cost of supporting that demand is also rising.
Large technology companies are committing an increasing proportion of their cash flow to capital expenditure. Some are borrowing more heavily, while electricity, construction and financing costs have all risen.
The easy phase of the AI trade was about multiple expansion.
The next phase will be about cash generation, balance-sheet strength and measurable returns on invested capital.
That will create much greater separation between the winners and losers.

**Host:**
The American consumer, meanwhile, continues to hold up. Is that reassuring?
**Eric:**
It is reassuring, but the details matter.
Headline retail sales remain resilient. However, households are becoming more selective.
In areas such as groceries, consumers are often paying more but buying fewer individual items. For several years, consumer companies were able to grow their revenues by increasing prices.
That strategy is becoming more difficult.
Over the next few quarters, companies will increasingly need genuine volume growth rather than relying on further price increases.
So the consumer has not collapsed, but pressure beneath the headline numbers is gradually building.

**Host:**
We also saw considerable volatility in Asian markets. What should investors take from that?
**Eric:**
It demonstrates how market concentration can become a macroeconomic issue.
South Korea and Japan have unusually high exposure to semiconductor companies within their main equity indices.
When the global chip sector falls sharply, it can make the entire Korean or Japanese market appear as though the domestic economy is deteriorating.
In reality, much of the movement reflects index construction and concentrated exposure to the same global AI investment cycle.
India faces a different challenge because it imports a large proportion of its energy. Higher oil prices affect inflation, the currency and the current account.
China remains mixed. Its advanced manufacturing and export sectors are resilient, but household demand, property and credit growth remain subdued.

Asia should therefore not be viewed as one uniform trade. The differences between countries are becoming increasingly important.

**Host:**
What is the practical conclusion for investors?
**Eric:**
The conclusion is not to abandon risk assets.
The world economy is still growing, corporate earnings remain broadly supportive and the AI investment cycle is still substantial.
But the margin of safety has narrowed.
Investors should favour companies with strong balance sheets, visible cash flows and the ability to demonstrate returns from their capital spending.
They should be more cautious around leveraged growth companies, weak credit and businesses that depend permanently on cheap financing.
Within emerging markets, energy exporters and countries with credible policy buffers should prove more resilient than oil importers with fragile public finances.
And in the bond market, investors should be careful about assuming that softer inflation automatically means sharply lower interest rates.

**Host:**
So what are the key signals to watch next week?
**Eric:**
Watch the bond market as closely as the equity market.
Watch whether Treasury yields remain high despite softer inflation data.
Watch shipping activity and insurance costs around both Hormuz and the Bab el-Mandeb.
Watch whether semiconductor companies maintain their capital-spending plans, and whether investors reward them for doing so.
And watch the consumer: not simply how much households spend, but how many goods they are actually buying.
Markets have remained resilient because the global economy continues to absorb each new shock.
But resilience should not be confused with unlimited capacity.
The shock absorbers are still working.
They are simply becoming progressively thinner.

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