GIS INSIGHTS

WEEKLY PODCAST

LOCAL INSIGHT INVESTORS

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TITLE: **Markets caught between weaker employment and persistent inflation**

TRANSCRIPT:

Host: Eric, it has been another eventful week for markets. What should investors be focusing on?

Eric: I think the central issue is that the US economy is sending two quite different signals.

On one side, the labour market is clearly slowing. Today's employment report is expected to show only around 56,000 new jobs in August, which would be a relatively weak number.

But on the other side, the services economy remains surprisingly strong. The latest ISM survey showed services activity accelerating, with business activity and new orders both at very healthy levels. At the same time, the prices companies are paying rose to their highest level in nearly four years.

So the Federal Reserve is caught between weaker employment and inflation that is refusing to disappear. That makes the next interest-rate decision much more complicated than markets might like.

Host: But expectations of another rate increase did fall this week. What changed?

Eric: The main catalyst was a speech from Fed Governor Christopher Waller. He indicated that he would support keeping rates unchanged this month if the August inflation data confirms that price pressures are easing.

That was enough for markets to reduce the probability of a September rate increase from more than 60% to roughly fifty-fifty.

Bond yields fell, and equities responded very positively. The S&P 500 rose just over 1%, the Nasdaq gained 1.4%, and the Dow added more than 600 points.

However, Waller did not take another increase off the table. He made it clear that if inflation begins to accelerate again, the Fed may still need to act. That is why today's employment report is important, but it will not settle the debate on its own.

A weak employment number would normally be positive for bonds because it would point towards lower interest rates. But if services prices are rising and oil remains close to $100 a barrel, the Fed may not have the freedom to respond.

Host: Energy appears to be becoming an important part of the story again.

Eric: Absolutely. Brent crude is trading at around $96 a barrel, while West Texas Intermediate is above $91. Continued conflict involving the United States and Iran, together with disruption around the Strait of Hormuz, has kept a significant risk premium in the oil price.

The important point is that oil is no longer simply a commodity-market story. It is becoming a monetary-policy issue.

Higher energy prices eventually feed into transportation, manufacturing and consumer prices. If Brent moves above $100 and stays there, it becomes much harder for central banks to declare victory over inflation.

Europe is particularly exposed. European gas prices have reached three-year highs, while storage levels are unusually low heading into winter. Euro-area inflation reached 3.3% in August, and the European Central Bank is widely expected to raise interest rates next week.

The uncomfortable part is that Europe’s economy is actually beginning to improve. Germany has raised its growth forecast, helped by government spending and stronger industrial activity. The ECB may therefore be tightening policy just as the recovery is gaining momentum.

Host: What has been happening in Asia?

Eric: Asian equities benefited from the fall in US bond yields, but the picture remains quite differentiated.

One of the most important moves has been in Japan. The yen strengthened sharply, with the dollar falling from around 160 yen earlier in the week to approximately 155. Investors are beginning to take the prospect of tighter monetary policy from the Bank of Japan more seriously.

That matters globally because higher Japanese bond yields make domestic assets more attractive to Japanese investors. They may therefore become less willing to buy US and European government bonds at a time when Western governments need to borrow enormous amounts of money.

India has almost the opposite problem. A special dollar-deposit scheme attracted more than $127 billion and pushed liquidity in the banking system to record levels. That strengthens India’s external position and supports the rupee, but the central bank may now need to absorb some of that excess liquidity to prevent it from adding to inflation.

Host: And what stood out in the equity market?

Eric: Artificial intelligence continues to dominate the corporate story, but the theme is evolving.

Nvidia’s proposed acquisition of Hugging Face would extend its influence beyond semiconductors and into the distribution of open AI models. Meanwhile, Snowflake’s strong results suggest that AI spending is spreading from chips and data centres into software and data consumption.

The next stage may therefore be less about owning every company associated with AI and more about identifying the platforms that can control computing infrastructure, software workloads and developer access.

Host: So, what is the main message for investors?

Eric: The market still wants to believe that weaker economic data will lead to lower interest rates. But central banks cannot focus on employment alone when services inflation and energy prices remain elevated.

Lower bond yields can produce powerful equity rallies, as we saw this week. But unless inflation genuinely begins to moderate, those rallies may remain fragile.

The key question is no longer simply whether the economy is slowing. It is whether central banks can support that slowdown without allowing inflation to return. For now, that question remains unanswered—and it is likely to keep markets volatile.

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