# 36 South Views

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**"Understand: the future belongs to groups that are fluid, fast and nonlinear."[1]**

Robert Greene

At the time of writing, Powell has talked the bond market off the ledge and taken some of the froth off the equity markets, not by blinking (see my last blog post) but by talking about the possibility of blinking, i.e. tapering quicker than expected and raising interest rates faster than expected.

I imagine that Biden is now putting pressure on Powell to address inflation more head on, as it is cited as the biggest reason for his drop in popularity in the polls.

Job done for now; the government can fund for lower and longer and the Fed can be seen to be addressing the situation.

But in reality nothing has happened yet and inflation, like the virus, will march to its own drum.

The next inflation print will be very interesting.

The Fed could be damned either way… they have dual mandate goals of price stability and unemployment. For the longest time, you could achieve both by expanding the Fed's balance sheet every time there was a crisis, but more and more they are becoming diametrically opposed… you can have one but not the other.

In fact it could get even worse than that… Stagflation. You get neither stable prices nor low unemployment. In fact, the more the Fed expands the balance sheet in response to higher unemployment, the more inflation you get - which in turn causes more economic dysfunction, which in turn leads to more unemployment.

Alternatively, the higher the Fed raises interest rates in response to persistent inflation, the more the economy tanks and unemployment rises.

So how does one safely deploy assets in this environment?

Where to safely put one's saved resources has concerned humans for millennia and will continue to do so. It is more of a conundrum now, given not only the potential of rapidly shifting sand beneath our feet due to inflation, but also the extremely rapid pace of change due to technology and "what is valuable" disruption.

Most of the big cap technology stocks are now seemingly priced to perfection making it even more difficult.

The dilemma is how to stay in the game to reap the big rewards that are out there, given the rapid pace of change in how we work, live and interact, whilst acknowledging that the more complex a system becomes the more fragile it becomes at the same time.

The answer to me as always (to a man armed with hammer, every problem is a nail) is convexity.

We are living more and more in a 'power law world', where life no longer seems to follow a simple (and fairly predictable) cyclicality, like that of our forefathers. We are now in a world subject to power laws, which amplify butterfly wings into tornados, both beneficial and harmful. The most resilient portfolios will be those exposed to the upside in a non-linear fashion whilst at the same time being exposed to the downside in a non-linear fashion.

[1] Robert Greene, Mastery

It's like holding two opposing thoughts in your head at the same time, whilst difficult to conceptualise… it is not impossible.

We believe we are aligned with this future, as we have made convexity our business and so I look forward to the challenges of next year, not with trepidation, but with excitement.

It only remains to wish all our clients a  wonderful, safe, happy holidays and New Year.

At the time of writing, it looks like a good year all around for the traditional asset managers, so I raise a glass to you and your performance and hope our firm continues to be of service in good times and bad (especially then!)

**"We have minds that are equipped for certainty, linearity and short term decisions, that must instead make long-term decisions in a non-linear probabilistic world."[2]**

Paul Gibbons

**Disclosure**

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[2] Paul Gibbons, The Science of Successful Organizational Change: How Leaders Set Strategy, Change Behavior, and Create an Agile Culture