THE DAILY CHECK-IN WITH GOLDMAN SACHS

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Liz Bowyer: Hi, Lou.

Louis Miller: Hi, Liz.

Liz Bowyer: Lou, you help our clients in the global markets division invest in key themes across the equity markets. One of the biggest themes on investors' minds right now is the prospect of rising inflation. How are you talking with clients about that?

Louis Miller: So actual inflation over the last 12 months has obviously been quite low coming out of the contraction. But going forward and since March there have definitely been causes for pause. So the trade-weighted dollar, for example, is down 11% since March. Broad commodity indices are up 33%. Ten-year interest rates have doubled, and market measures of future inflation have gone from just over a half of 1% to over 2%. So there are definitely budding signs of reflation from the deflation that we saw ourselves in March of last year.

Liz Bowyer: So what are some of the indicators that you'll be watching in 2021?

Louis Miller: We have two credible efficacious vaccines with one potentially in ten days with Johnson & Johnson. So from a pandemic perspective, as the vaccine gets distributed, there could be pent-up demand which could cause growth to be above expectations.

Just last week, we had the Georgia runoff, and so now we have unified government. So that's going to lead to higher spending and higher inflation than otherwise would have occurred. Early in Biden's administration we could see a $750 billion fiscal package which would equal 3.4% of GDP. So the go forward view on inflation is pretty solid, and so we could definitely see inflation continued to surprise to the up side as the economy normalizes and because of all this fiscal support.

Liz Bowyer: How do you think monetary policy might affect inflation?

Louis Miller: So the Fed has communicated a shift to a flexible average inflation target, which we know that inflation has been below 2%. So that does mean that in the future if inflation is above 2% they should be comfortable with that so that there can be an average of 2% inflation. That should mean that as growth really does recover over the course of this year, they're going to remain dovish for longer than they otherwise would have, which is very supportive of inflation in general.

Liz Bowyer: So how are investors thinking about all of this?

Louis Miller: So I think investors are looking for inflation hedges. And equities is one asset class that tends to do well during periods of rising inflation, especially at low starting levels of inflation. So in the equity market, there's a lot of focus on who and what could potentially benefit from rising inflation expectations. Otherwise, it's, you know, emerging markets, it's commodities. Those are typical inflation safe havens, and there's a lot of ways to play that in the equity market. But broadly speaking, equities is an area of focus.

Liz Bowyer: So with the continued focus on equities, is the equally that clients think about investing in equities staying the same or starting to evolve?

Louis Miller: Yeah, so what investors have bought in equities over the last ten years is going to be very different than what they buy in the next year. So generally speaking, small caps, high beta stocks, stocks levered to commodities, more value-oriented stocks that generate most of their value from today's cash flows as opposed to cash flows ten years from now, companies with real assets, highly levered companies because the real value of their debt will go down as inflation occurs. So it is really cyclical, risky pockets of the equity market that should respond and perform best in this period.

Liz Bowyer: And what about the big tech companies, which have been such a focus for investors?

Louis Miller: So investors are definitely not abandoning tech because there's other things to invest in this year. The largest five tech companies have outperformed the broader market by 354% over the last ten years. So it's hard for investors to walk away from that. And generally speaking, fundamentals are still pretty solid for those companies.

It's just that there's other opportunities now that didn't exist before. The NASDAQ, a popular tech index, is expected to grow 16% in 2021. Most every other index is going to grow at a higher rate than that. For example, the Russell 2000, which is a popular small cap index, is expected to grow eight times faster than that in 2021. So the mega cap tech growth is not as scarce as it used to be over the last decade, and there's just a lot of other opportunities to invest in. And after ten years of investing in tech, many investors find themselves under exposed to that cyclical right tail and are moving into it.

Liz Bowyer: So finally, Lou, beyond inflation, what are the other big themes that you're focused on with clients right now?

Louis Miller: Yeah, there's three themes that I'm focused on right now -- reopening, renewables, and emerging markets. So reopening, many of the companies that are focused on travel and leisure have seen their competition fall to the wayside or they've seen their cost structures dwindle. And now consumers have been stuck at home for over a year, so there's a lot of pent-up potential energy for travel and leisure over the course of the next 12 months. So that's an area we're focused on.

On renewables, Biden's $2 trillion climate package could actually become law, and there's a lot of market opportunity relative to pretty low market caps in the renewable space.

And then on emerging markets, this whole discussion on inflation, on commodities higher, on a patient bed are all very supportive of emerging markets. So we see a number of opportunities there across LatAm, Asia, and CenEA.

Liz Bowyer: Thanks, Lou.