



Lakshman Achuthan : Inflation Cycles Amid Regime Change

Erik: Joining me now is [ECRI](#) co-founder Lakshman Achuthan. Lak It's great to get you back on the show. For most of our listeners are familiar with your work, those who are not should just put Lak name into the search box at Macrovoices.com we go fully into the long-term business cycle and cycles analysis work that Lak's firm.

[Economic Cycles Research Institute](#) focuses on in some of those past interviews. I wanna dive into the current situation, though, Lak, because you are Mr. Cycles. You think about the world in cycles. I love your work, but hang on, you told me something off the air about how you guys have this idea of an economic regime change.

It seems to me. Although the cycle's work is very important, and I get it. I respect it, but I think president Trump and Secretary Bessent are intending policy changes that are really literally on the scale of re-architecting the global financial system. Now, I'm not saying that they're going to achieve all of those goals, but.

That's what they seem to be out to do. And it seems to me that potentially puts a real speed bump in reading cycles that are normally based on just, the normal ebb and flow of economics. How should we think about cycles analysis in a world where President Trump and secretary Bessent really are intending changes that are pretty much unprecedented?

Lakshman: That escalated quickly. That was a big question, but I It's great to be back with you. I I I think that's really at the heart. Your question just cuts right to the chase. It's at the heart of decision making in a world where, the rules are changing and and so you have to do a lot, you have to have an interesting framework, I would say.

And I'm very grateful for the cycle framework because it has a tried and true history of navigating what I would call a regime change. You're talking about re-architecting the global economy. I agree. It, it seems like there's some version of that. It's hard to say literally what, but there's some, something's going on.

And cycle work does. Extend back farther than people may realize to the early part of the last century. And there have been a lot of regime change actually changes of kind of the economic lay of the land over that timeframe. I'll rattle off a few, a little trip down memory lane.

You have the panic of 1907 which it was the creation of the Fed. So that's a, it's changing some of the rules of the game, right? You have as World War I ends, you have the end of globalization. And income tax, reduces the reliance on tariffs. That's a huge shift in the way global trade was going on.

In the first half of the thirties, you have Smoot Hawley Tariff Act, the Depression, the end of the Gold standards, the New Deal. There's a lot of huge things going on. More recently. And you could tell I'm a cycle guy when I say this is recent. But you have the Nixon shock in the seventies.

There you have some tariffs. You have the end of the gold dollar link, the Bretton Woods set up and stagflation shows up. That's a new thing relatively new in this century. You've got the housing bubble the financial crisis, the huge bailouts with QE. And then post COVID, you've got that unprecedented is a word that gets used a lot, but unprecedented, massive fiscal stimulus, extreme QE, and all the supply chain stuff that happened.

So these regime changes. Have occurred the cycles continue to happen, right? And if and this is important to remind everyone what we're doing with cycle work is watching for the inflection point, is the cycle going to turn and go the other way? So if we have one job at ECRI, that's our job.

Is it gonna turn and go the other way? The rules can change. The magnitude of the swings can get larger and smaller as the structure of the economy changes over all these decades. But this inflection point monitoring and kind of risk of question actually is pretty darn stable. And all those times I just listed, the cycle indicators didn't break down.

They kept getting the direction correct and more importantly the timing of the direction. And now I'm talking about growth. I'm not talking about markets, but the timing of the direction they were able to get very well. So in the current environment, the reason this is a problem, and this is embedded in your or original question, the reason this is a problem is 'cause when the rules change.

Models break down and nine outta 10 people listening, whether they're explicitly doing it or implicitly taking it in when they take in information, are relying on models. Where there's an estimation of some sort of relationship that has occurred in the recent past, the last five or 10 years, and it's optimized for the next whatever year or something, and you say, oh, 'cause those are the rules that last several years.

It's gonna happen that way in the immediate future during regime change. That's absolutely untrue. However, these cycle indicators continue to get the direction right? So it's in that context that we come into 2025 and you have as you said, this re-architecting perhaps going on of the global economy, and how do the indicators work?

Quite frankly, they work the way they always do. They got the direction right.

Erik: Let's go ahead and talk about how the cycles interpret the last six months or so. Let the amount of time that we've seen these significant policy actions from Secretary Bessent and President Trump starting to affect markets.

How do the cycles interpret those, that period of time when those events occurred, and what do they tell us about what comes next?

Lakshman: I'm gonna refer to a couple of charts that are available that I'll make available that you can make available. Back in basically liberation days, right? It's in April or so. And we had ended 2024 all set up for, there's a slowdown. We're having a slowdown in growth. There's no hard landing. And inflation, while it's still sticky, is gonna stay in check. And in, in April, our indicators were still signaling a slowdown ahead, but there was no recession.

And before Liberation Day that was our view. There was no nothing in our world, nothing too radical. Then you have liberation Day, you have all of the. Headlines and quite a bit of angst about a hard landing or a recession. That was the mood. It, people may or may not remember this, but that's what it was.

So in July, after there's you have a little bit time after after all that news came out. Our forward-looking indicators on growth had turned back up points to growth, firmin not stalling. And that was even as our forward-

looking, separate forward-looking indicators on inflation were showing inflation pressures still fading.

And at the time we called it a setup for a Goldilocks space. And everybody else was still talking about a hard landing, but we just, it didn't show up in the cyclical forward looking directional data and. That's just what, we are very agnostic actually on, on, on most things except what our indicators say.

When the indicators are pointing one way or another. We trust them because of the real time performance and then we try to figure out why afterwards. Now August, by August of this year very interesting because the resilience was giving way to even firmer growth. Our cyclical signals and broader investment data started to really line up and we got into a more, what we would call a balanced brightening.

And it's an unusual situation. I think the last time was quarter, a century ago where you have a cycle. A set of cycle data, which we're tracking moving to the upside directionally at the same time that you've got some sort of structural thing happening. As you say, there was all this re-architecting happening, but there's a separate, the separate issue is the all the tangible and intangible investment drivers.

That surround the ai activity. And so with those pushing to the upside at the same time that the cycle's pushing to the upside doesn't happen like that all the time. And so that's notable, that's happening. We saw that in the summer. In September again, our update is the expansion is totally intact.

Inflation is contained. That's pretty darn unusual. And that brings us to now where it continues to be constructive. There's. There's this I think it's now a little bit more in the headlines. This K shaped stuff, we've been talking about it for, until I'm blue in the face.

But basically the, you have the, a smaller group of consumers at the upper end of the K that are responsible for the bulk of consumption. The top 10% are just spending freely. And they're helped by rising wealth and strong balance sheets. And at the same time, the median household is under a lot of strain.

They, they have slower earnings growth, a lot of credits, stress and. With the job market not adding jobs, right? It's not losing jobs, so it's not

adding jobs. There's more stress. And so you get this, what we've called the kind of plutonomy pattern, a narrow consumption base that props up the overall numbers.

But there's definitely some fragility underneath. And that. Is why things I think are very confusing for people at the moment. And it also explains in a way where one aspect of why inflation can be having trouble like getting a grip of getting some traction here. I'm talking broad inflation not goods, inflation.

And that's because the bottom end of the K just can't stand it. They can't handle higher prices and so it's very difficult for it to start to run. And our forward looking inflation indicators are saying that continues to be the case for now. So right now we're in a Goldilocks phase.

I know that's getting a little tired to say growth firming inflation contain no hard landing, no stagflation. Now eventually that's gonna, the balance will tip. And that's what the leading indicators are designed to do is to give us a heads up on that.

Erik: That's fantastic Lak because that there's so much to unpack there.

I really want to dive into it. I tend to think in macro narratives in my head and I, I really respect the data-driven work that you and others do, that's what I respect technically, but my brain thinks in narration and what I think you just said. Tell me if I got it wrong, is right now we've got an economy that's dependent on rich people being in the mood to spend money like it's going outta style 'cause some of them are new at being rich and they're still celebrating that. But all it takes is one big catalyst, like some of the people that are in the majority who can't afford to go out to dinner watching that conspicuous consumption, getting pissed off and throwing a Molotov cocktail at just the wrong moment that hits a big news story and all of a sudden there's a mood shift and rich people don't wanna show off and go spend money like it's going outta style and everything collapses very quickly because of that one little butterfly flapping its wings at the wrong moment. Trickle down effect.

Am I reading way too much into that? Because it sounds like there's some real risk there.

Lakshman: Here. Here's where our cycle stuff would line up with that story. As I intimated the k-shaped consumption, it's not a new feature. This feature, it, I feel like I've been saying it for decades.

And maybe it's been there forever. I'm not that old. But his, I know that we're not the first ones to struggle with what's going on with the economy and what I do know. Is like relative change, right? And it feels like that gap between the upper end of the K and the lower end of the K has just taken a, good step bigger.

And that would feed into the narrative you just said, right? It's what's the straw that's gonna break the camel's back kind of thing.

Erik: What do your long-term cycles tell us about past times in history when wealth inequality was growing exponentially, which is what seems to be happening here.

Lakshman: Here's what happens, right? It's quite interesting. Imbalance is built. And they're always different, right? If you're a student of these cycles and histories, there's some debt crisis, there's some other boom like the dotcom boom, or there's the housing stuff.

There's weird little ex like imbalances that build, and that in and of itself doesn't tell you when things are going to end, right? We're looking for the inflection point in my world, right? We're looking for the inflection point. So we track the leading indicators, not the coincident ones we're trying to look a little further ahead and when they begin to turn and go down, I don't know exactly what the match is going to be.

That lights the fire, but that's when. The conditions are ripe for something to move the other way, and that's where you generate the cycle. It's the combination of the extreme. In this case, we're identifying tension between the two legs of the K or the two arms of the k and. At some point, something is gonna give, I, I don't know what it is, but I watch the long, what I'm doing every day as much as I can is watch these long leading indicators and I'm trying to see if there's any sign of a growth rate cycle, downturn and reason this is on my mind.

I can't help but remember the dotcom boom. And, roughly speaking, NASDAQ went to 5,000, then it peaked, and then it crashed and fell 50% and took, all the related things around it with it. And there was a whole narrative around tech that it was going to do all of these things.

And it, it's not that. It was untrue, but it was just overdone, right? It got overdone and perhaps that's happening here. I don't know. But what I do know is that in 2000, the year 2000, the long leading indicator index had started to turn down and it was starting to point to growth slowing, which then takes the shine off of the priced for perfection stories.

Erik: But you're saying you're not seeing that now? You're not seeing the topping

Lakshman: today? When I'm talking with you right now, I don't see it. It doesn't mean I'm not aware that it could happen. I'm aware it can happen, but I'm just reporting object is it as I'm trying to be, I'm trying to get rid of my feelings.

And say, I know that booms end in busts because I've read books, right? And I know that the long leading index is just one thing. I don't know. There may be other things that could crack the situation. But the one thing that I know something about is accelerating and decelerating growth.

And I know that decelerating growth would take the shine off of the price for perfection stories. That underpin a lot of what is being said about, you know how people have stories around why, this time is different and right. And you see everybody, I think everybody who's been around for a little while looks at the market and says, whoa, that's pretty high.

And wonders, what might. Topple the apple cart today. I'm saying in the snapshot of what the long leading indicator is saying is it's not growth yet.

Erik: It seems if you look at the market in terms of where all of the upside has been, it would be the risk of an unwind of the AI trade specifically.

And I think there are extreme parallels to the dotcom bust in the sense that they got the call right, that the internet was gonna be a really big deal. They got that exactly right. It's just that. They went and bought a whole bunch of stuff. They didn't understand what it was because it sounded like it was internet related, and that got us into a bust situation that was quickly contagious, even to the cool stuff that really was relevant.

Is there a setup for that to happen again here with AI where Yeah, AI is a really big deal, but it doesn't mean we can't have a bust because it's a big deal.

Lakshman: I, I would say it's virtually certain, right? Because the nature of it is you, as we said earlier, you're priced for perfection, but the misallocation of resources, right?

Because you don't know which one is the right one. So everybody's throwing money at everything and some of them are no good or, maybe I, what is it? I'm not gonna get this right, but I'm sure your listeners know this that in the dotcom boom, they were building certain infrastructure, including lines and capacity for data moving around that just was way beyond anything that could be used.

And it has to be repurposed at some point. It's almost like building, there, there's a whole thing where people built all the malls and stuff like that, and then you don't go to the mall anymore. You buy stuff online, so you gotta repurpose the mall. Here we're building a great deal of dataset or capacity and other things.

I don't know exactly how this works, but if there's some technology change that may not be needed, right? So that's misallocated capital. That's, you gotta be careful what you wish for. Many of us know or understand that these free market economies that we are, we like to think we're in, we're mostly in, for the most part.

Every once in a while they get a kind of crony capitalism, but in these free market oriented economies. If you don't allocate your capital properly, you get, you end up paying for it at some point, and so the boom can turn into a bust. And that's probably gonna happen here, but there's a huge fear of missing out.

If it happens in a month and you pulled out, you're a genius. If it, if you pull out now and it happens in a year, you're an idiot. And so that fear of missing out keeps everybody here. I wanna swing back 'cause you're making me think back to the regime change stuff. Also, if you'll bear with me in the early seventies Nixon the Nixon shock, right?

This is a bit of a regime change. He has a, an America first policy. And unilateral action. In the international trade stage, you get 10% PAC tariffs. You have the inability to exchange dollars for gold to taking off the

gold standard. The upshot of that for everybody looking at it in the moment.

Whoa, this is a really big deal. Which it is. And maybe this is gonna bring us a lot of inflation. What's gonna go on now? There was a whole concern around that. And ultimately they were right. I think in retrospect, people look and they say, oh yeah, seventies had a lot of inflation. It must have been related to that Nixon shock.

And it probably was right. Smarter people than I have made that argument. But what's interesting from a decision making point of view, either for your business or for your portfolio is that after he did this and made the announcement the economy did great and inflation was not a problem.

It was more than a year later that the wheel started to come off. I don't think people really appreciate that. The indicators got the direction right in on both counts. We had been coming out of the 69 70 recession, so the indicators were pointing towards growth and we didn't have an inflation problem at the moment, even though these things were happening.

And it's not that it didn't show up right because they, these were big rule changes. And you have the oil embargo begin also, but the the timing of when it shows up is really critical. And, there might be some rhyming of that now.

Erik: I really want to go deeper on this one, Lak, because, and I'm gonna ask you to hold me to account here 'cause you are a historian and a cycles analyst.

I am not. And if I've got the history wrong, please set me straight. But I think about the Nixon shock and the secular inflation of the 1970s with a different narrative, which is. I think that all the signs of a secular inflation were there in the mid to late 1960s. I think that the first, from what I've read about secular inflations, and please correct this part if I have it wrong, it's very common that the market is misled because for the first few years of a secular inflation, the feedback loops that make inflation bad for the stock market haven't kicked in yet.

So what happens is in the early years of the inflation, it feels like just. Really explosive economic growth, and everything is wonderful,

everybody's happy. But it turns out that it's really just the beginning of an inflation. I think that's what happened. It started in the late sixties, and by the time the Nixon shock occurred, as you said you can get to essentially what we think of in markets is a buy the rumor, sell the news event where the Nixon shock happened.

A lot of people knew that it was going to be inevitable. They were fading. It. That got unwound. It wasn't another year, just like after the bust in the dotcom market. It wasn't until another year before the trade really started to kick in that, the internet is an important thing and that the inflation was very real.

And then you had the stock market bust of the 1970s. It feels to me like we're still in the late 1960s. The Nixon shock hasn't even happened yet. Have I got that all wrong, or what do you think about that view?

Lakshman: So on the secular side I'm like you in the sense of, I, I hear the stories, I try to put them together.

And it's very difficult because the secular stuff or structural stuff very hard to forecast the inflection point extremely hard. You can see it if you're lucky and you're really good in the rear view mirror. Five years after it happened, it's hard to do the to know that stuff.

So that's why it's tricky. I think you need to be a astute, I, in one man's opinion is that history is important, right? And I like to read it. They're great stories. And you learn that, people. Did interesting things and thought, interesting things but you're also reading someone's account of something.

You don't literally know what was happening in the mood in the moment. Like I think you and I and everybody listening know the mood today outside our window. But then you start to re-remember it very quickly and as a decision maker. You're taking in all of this, you have this huge amount of data flow, and nowadays we have more than ever right, of this data flow coming over our washing over our screens and our ears or whatever, and we're trying to figure out is there a structural change? What is the structural change?

What's it doing? And quite frankly, it's very, it's almost impossible, but I think the cyclical stuff, you can start to hang your hat on that. That is reliable information. Even now with the government data, on hold for a

bit we have reliable cyclical inputs. And they're saying that regardless of our understanding of history and of.

The game changes or the rule changes that we think are going on at the moment, growth is not collapsing here and inflation writ large is not running away. The caveat there, how I can reconcile that with the stories that we've been telling about Nixon or the secular changes that, that started in the sixties.

Is that the forward look on the cycle indicators is a couple of quarters, two or three quarters. So it's not saying any of those views are wrong, it's saying not yet.

Erik: Lak. I love that setup because I'll tell you the narrative that's, I think. Driving. This is energy. And if you use that analogy to the internet, they were building a whole bunch of infrastructure.

They weren't thinking about things like social media and, so forth would be the big trends that would be where the money would actually be made in the internet. I think what people are missing now about the AI trade is, yes, it is every bit as important to the future of history as everybody thinks it might be, but.

It's not gonna happen the way everybody thinks or imagines it's gonna happen because there won't be enough energy in order to fuel it. The exponential growth of AI will require an increase in the amount of energy that we consume that simply. Isn't immediately serviceable. It could be long-term with the right nuclear energy strategy, but that takes 10 or 15 years to build out.

There's a really big energy crunch I think that will drive an inflation. So again, I'm thinking in narratives, how does that view align with your cycles work? What do you see in the cycles? That, and by all means, if you contra, if your cycles contradict, tell me

Lakshman: No. Right now the future inflation gauge is not running away.

Okay? And most of the future inflation gauges around the world are pretty benign. We cover, all the major economies, including the major, emerging economies. Actually in China, you want a little inflation, right?

Because they've been flirting with deflation. I'm talking very broadly, not in a commodity or energy inflation.

There are a couple spots where there's a little, UK and Japan had a little inflation stuff, but not, but basically not an issue right here. Does that mean anything that you said was wrong? No, I agree with you. My, I we work with large industrial companies and those who are in the energy production area.

Like the traditional, Hey, I may, I need to have a generator kind of thing. They've sold things for the next five, 10 years already. Because of what you're saying with the demand. What's quite interesting, and I don't know how to fully figure this out, I is just market prices.

I, I was listening to a pitch, this is your basic straight up. Wall Street Bank pitch on how to reallocate your assets, right? And so everything's, all the assets are up year to date across the board. Bonds, equities, whatever, gold stocks except oil, right? Oil's down oh 10%. When I had this report, which is a, in September, end of September.

So that's interesting. Right now, how do I intersect all of that with inflation and cycles and it comes into our work. Now I'm going from structural to cyclical. Looking at the next couple of quarters, it comes into our work in two ways. Industrial materials, prices sensitive ones including oil.

Let's say, let's start there. At the bottom of this very closely linked to global industrial growth cycles. Global industrial growth has been in fits and starts. It was like slowing a little bit and bottomed out and yeah, now it's moving up. Okay, so there's a, there may be a disconnect there on the demand side between a relatively weak oil prices and where the global industrial cycle is headed over the next couple of quarters.

That says nothing about supply. I'm not, I don't have an insight on the supply side. So that's the other side of this equation. And then you switch to the inflation side. What's going on with inflation cycles? So I'm switching from global industrial growth cycles to a completely different cycle.

Inflation cycles in the United States in particular, and sensitive industrial materials, prices, which is much broader than oil. Okay. There's energy, there's metals, there's textiles. There's there's other kind of

miscellaneous materials, building materials, these other things, and they actually are starting to move up as a group.

Some of your longtime listeners may remember the JOC index. The Journal of Commerce Industrial Materials Price Index. That it's actually an ECRI index that we started in the eighties to track sensitive industrial materials. Prices. It's very different than like the Bloomberg one or Goldman Sachs one or whatever.

'cause those tend to be energy heavy. And ours are ore tradable. Our index is specifically designed for inflection points and growth, and I have to tell you that the breadth of that is starting to move to the upside. So it would be unusual, very unusual for oil prices to not eventually participate in that.

One that that, that means that one driver of many. The inflation cycle could start to get a little traction in the coming quarters.

Erik: Lock everything that you're saying very much stands as confirmation of one of my core views, which is I think we are at the beginning of a secular inflation, and I think the bad for the stock market, part of that secular inflation is not happening yet.

It sounds like your data confirms is not likely imminent. It's probably a good year or two off before we get into the kind of inflation cycle that that really starts to affect markets. And there's a lot of good reason to think that this equity market, what everybody thinks of as a very bubblicious maybe it's about to stall out and roll over.

Stock market probably actually has legs to run quite a bit higher before. Eventually I think there will be some serious. Headwinds, but it sounds like it's not time yet. Does that jive with what you're saying?

Lakshman: Yeah, I'd say not yet. I agree. I agree with you. Not yet. I'm, this is an off color joke, but it's, I'm an older guy.

It's the guy who jumps off the Empire State Building. He's and as he's going, passing each floor on the way down, he says, so far so good. It can be fine for a while. And and booms and busts are like that. They're fascinating times. If. You have some awareness as to what's going on and probably some humility on knowing that you're not gonna get it exactly right.

Erik: I wanna turn this conversation upside down now because I think that this secular inflation discussion we're having is gonna be really important. You see this from two sides. One is your cycle work, but you also advise a lot. Of people to the extent that you can talk generally without breaching any confidentiality agreements.

What are your clients asking you about inflation? How are they seeing it? Is any, are other people worried about this? What is your interaction with your client network telling you about this?

Lakshman: What I think the, our, our clients have spent some time thinking about cycles. And once you get into it you're a little more familiar moving between cycles and growth and cycles and inflation.

And it's the latter cycle, the cycle in inflation. I think that is. Interesting to the clients and to me, quite frankly because I think it, it's confusing to, to the general public and therefore has all kinds of risks and opportunities around it. The inflation cycle right now as we've been talking about, is not a problem.

The us cyclical outlook on inflation overall, it's not running away, and that's hard to believe. Because of the things that you see and hear around you, and when you get into it. And we talked about this a little bit at the beginning of the call there are pieces that are moving up and it's related to the headlines.

The tariffs and such are pushing core goods inflation out of deflation where they were in 24 and into inflation, where they are now, and they're running around, they're approaching 2%. And so that's a big change, right? They went from minus 2% to plus 2% on core goods. At the same time. Shelter and services less shelter are all trending down.

And so that's why the overall inflation while sticky is not running up yet. And part of that relates to the bulk of people who, when the median households and who are in the lower end of the K, who can't afford higher prices. And so discretionary. Spending items they can't get a lot of price inflation there for that large cohort of people.

All of this matters because there is this combination of inflation and growth give you interest rates. And interest rates, then price the rest of your portfolio. I'm oversimplifying, it's critical component. And where does this then relate to the interest rate, to the yield curve?

Regardless of whatever the headlines are there's not going to be a strong inflation reason for a hawkish FED. So that's one piece of information. On the other side the continued stickiness and all of the structural and secular concerns, may have the long end hanging out, also sticky.

And so that's the setup for the yield curve going forward. There, there's probably some room on the short end. Certainly not for raising rates, but for being more dovish. And then the other end's sticky for now. And you've got, as I described earlier on a cyclical basis, a Goldilocks kind of outlook, firming growth with overall inflation, not running away.

So you see how the inflation cycle informs so much, and I think the inflation cycle is the most confusing part for most people to figure out.

Erik: Lak. I can't thank you enough for a terrific interview. But before we close, I want to ask the question on a lot of our listeners' mind particularly our institutional audience, which is what if they want to sign up for your service in order not to be left out in the cold and to know when there is a change in what your cycles are telling us is coming next, or when one of those inflection points is upon us.

Lakshman: Look, if you wanna work with us, it's pretty simple. Just call just give us a call. We're old school. Just call Melinda at our office and you can find us at [Businesscycle.com](https://www.businesscycle.com). We're here in New York and we do have some people who are extremely good on, on, on social media and stuff.

So we have a [YouTube channel](#), and that's Economic Research Institute. And we have a [LinkedIn](#) where there's, there's a newsletter and things like that, and that's [Economic Cycle Research Institute](#). Again. So if you just type in the whole name on one of those social channels, you'll get right up to date stuff on what we're doing publicly.

If you wanna work with us, give us a call or send us an email and we'll take care of you. We're nice people and we enjoy talking.

Erik: Patrick Ceresna and I will be back as Macrovoices continues right here at [Macrovoices.com](https://www.macrovoices.com)