AozoraStep Capital LLP

A UK focused Turnaround Value Investment Partnership

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TODAY'S TOPICS

1. US inflation & the Phillips curve
2. UK Autumn Statement
3. Supply shock over?
4. Credit events in online retail

1. US INFLATION & THE PHILLIPS CURVE

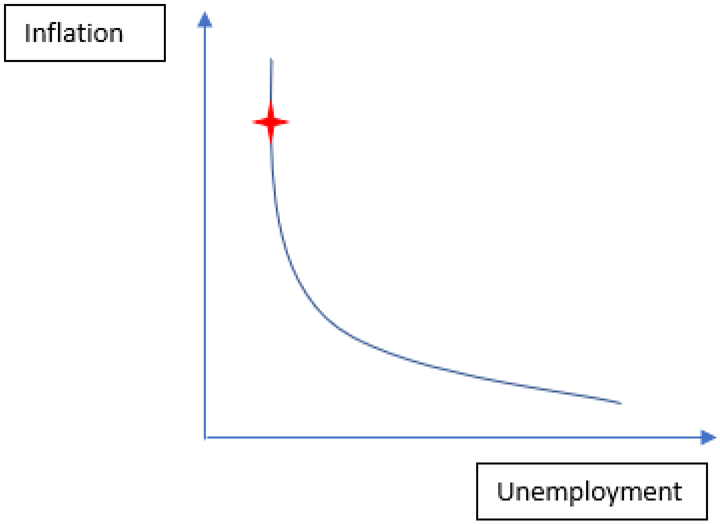
US CPI – OCTOBER CORE PRINT BEAT BY 0.2%

+0.4% September 2022 CPI Print	+0.4% October 2022 CPI Print
Biggest drivers: -1.1% used cars (4.0% weight) +0.7% new vehicles (4.05% weight) +2.5% car and truck rental (0.15% weight)	Biggest drivers: -2.4% used cars (3.8% weight) +0.4% new vehicles (4.05% weight) -0.5% car and truck rental (0.14% weight)
-1.0% lodging away (0.97% weight) +0.8% airline fares (0.62% weight) +0.8% rent of shelter (32.1% weight) +1.9% transportation services (5.9% wgt) -0.3% apparel (2.43% weight) -2.1% energy (8.24% weight)	+4.9% lodging away (0.93% weight) -1.1% airline fares (0.62% weight) +0.8% rent of shelter (32.6% weight) +0.8% transportation services (5.9% wgt) -0.7% apparel (2.48% weight) +1.8% energy (8% weight)
+0.8% Food (13.63% weight)	+0.6% Food (13.7% weight)
+1.0% Medical care services (6.89% wgt)	-0.6% Medical care services (6.9% wgt)

PHILLIPS CURVE – SUPPLY SHOCKS SHIFTS CURVE TO RIGHT

1. High inflation
2. Supply shock/stagflation: Central banks cannot do anything, except raising rates, causing a recession

1.



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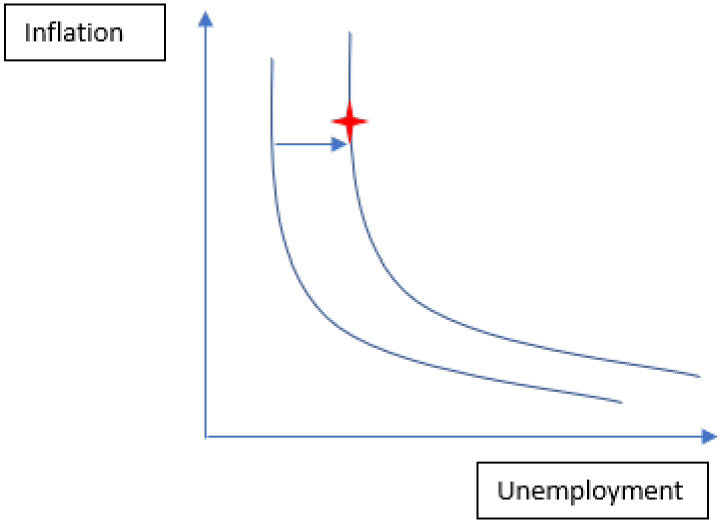
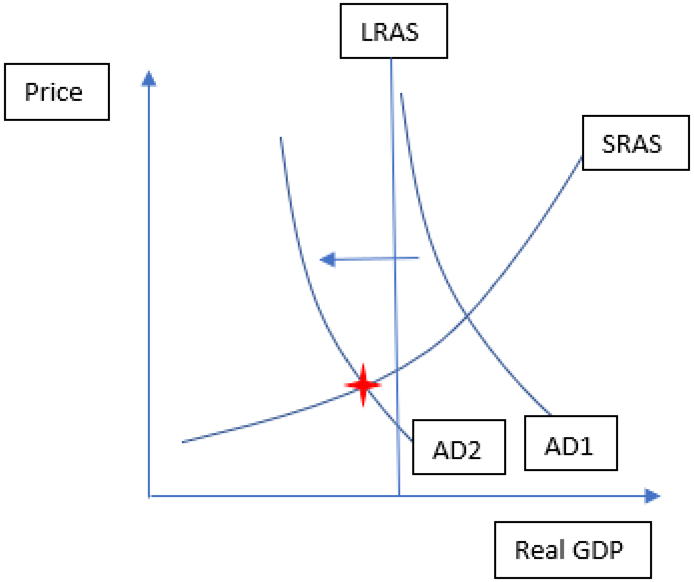


PHILLIPS CURVE – AGGREGATE DEMAND NEEDS TO DECLINE

3. Short term supply cannot move, but government can help with changing aggregate demand: Raise taxes and reduce spending to shift aggregate demand to the left
4. Philips curve will shift back to the left at lower prices

3.



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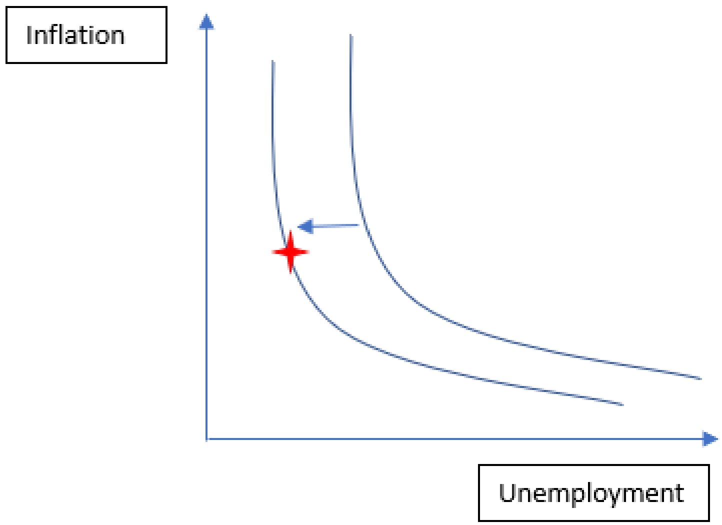
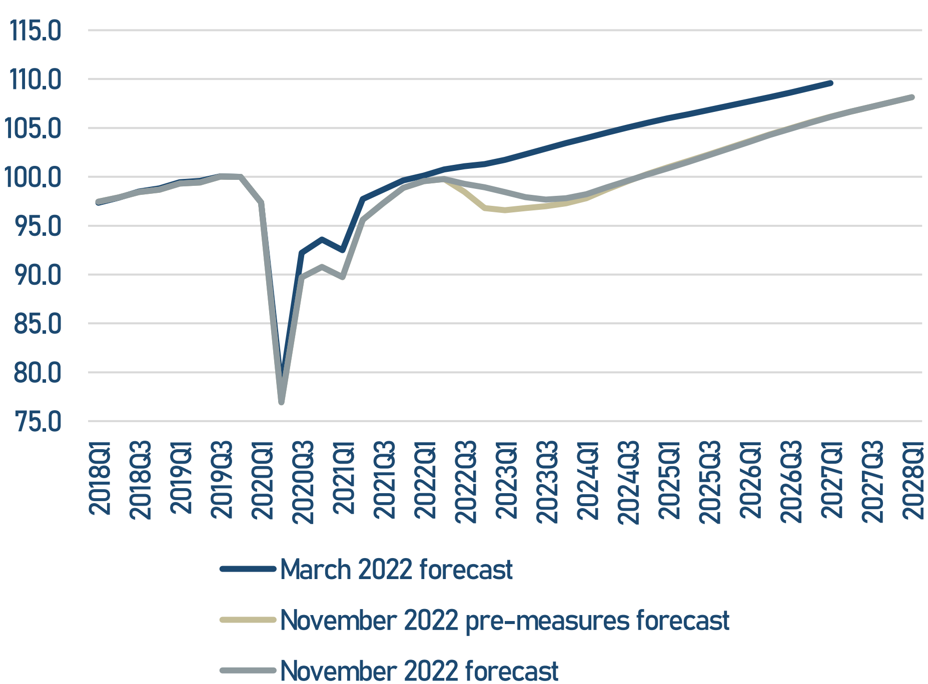


2. UK AUTUMN STATEMENT

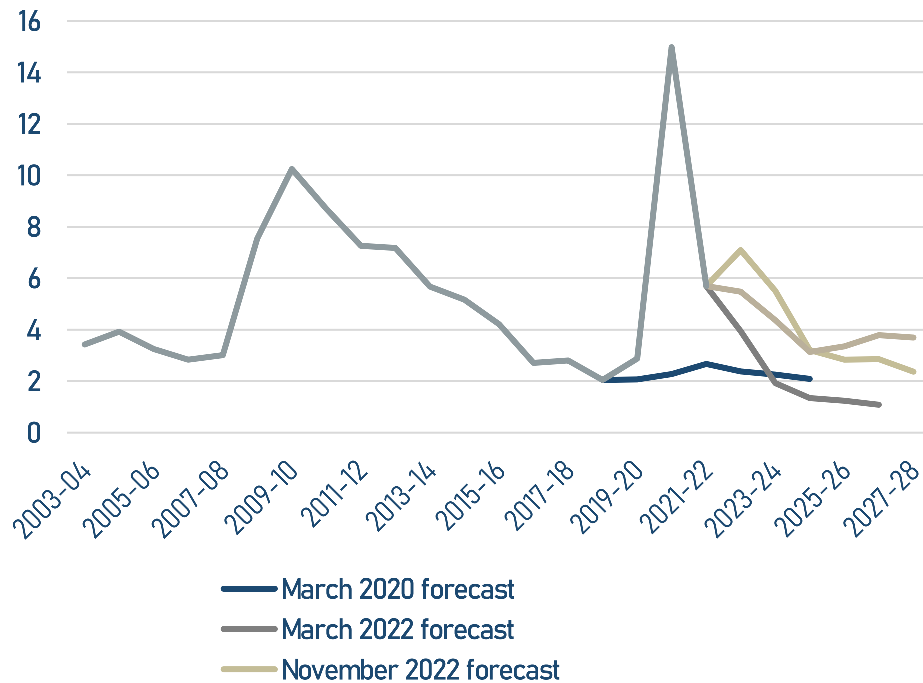
OBR – A VERY PESSIMISTIC OUTLOOK

- Like the BOE, OBR expects a one year long depression
- The forecast is entirely focused on inflation & interest rates

OBR UK GDP forecast could turn out to be too pessimistic for Q4 22



OBR UK Public sector net borrowing as % of GDP has had a wide margin of error



Source: OBR

AUTUMN STATEMENT – ALL ENERGY RELATED

- Without the energy crisis, the UK government would be in a very healthy spot
- If gas prices were to drop to 100p a therm, the UK government would quickly have a fiscal surplus
- Index linked interest payments were £47.8bn Jan-Sep 2022 vs. £27.5bn nominal interest payments

Key Expenditures	in £ bn 22/23	in £ bn 21/22	in £ bn 23/24
Energy support 22/23	40	-	20
Debt Interest	120.4	42.9	?
Bulb Energy takeover	6.5	-	-

Key Expenditures part 2	in £ bn 22/23
Business rates support for 5 years	13.6
NHS support in 24/25	3.3
Adult social care in 24/25	4.7
Public schools in 23/24 and 24/25 each	2.3

Key Tax Revenues	in £ bn 22/23
Additional income tax threshold moved from £150k to 125.14k	0.67
Energy Profits Levy increased from 25% to 35%	14
Capital gains tax allowance reduced to £6k and then to £3k	1.6 (5 yrs)
Dividend allowance reduced to £1k and then to £0.5k	0.8 ?
Corporation tax from 19% to 25%	15

AUTUMN STATEMENT – BIG PLUS FOR THE NHS

- More spending towards the NHS & health care

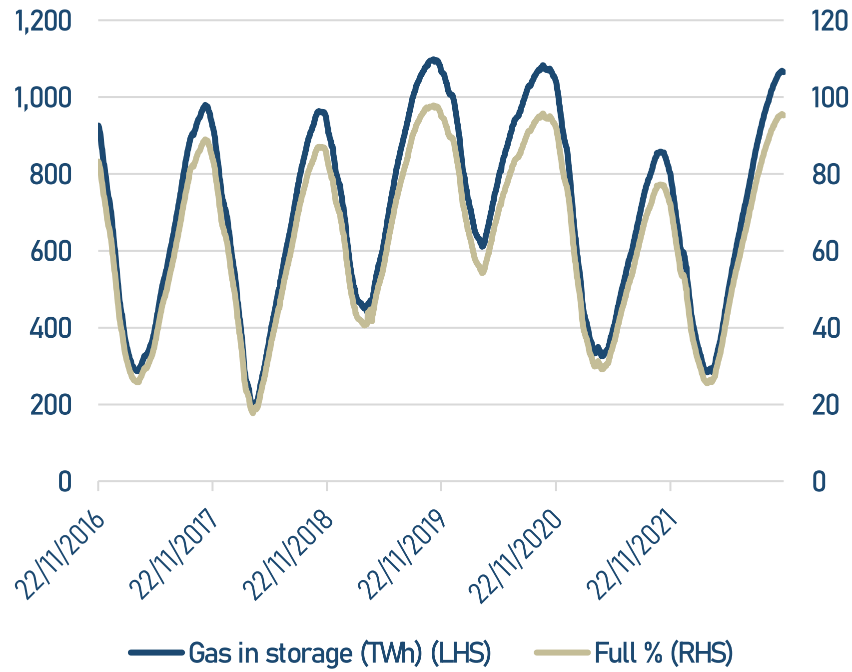
Largest spending items UK government	Current % of total expenditures	2024/25 % of expenditures
Health and Social care	38%	39%
Education	18.5%	18%
Defence	8.5%	7%
Scotland	8.5%	8%

3. SUPPLY SHOCK OVER?

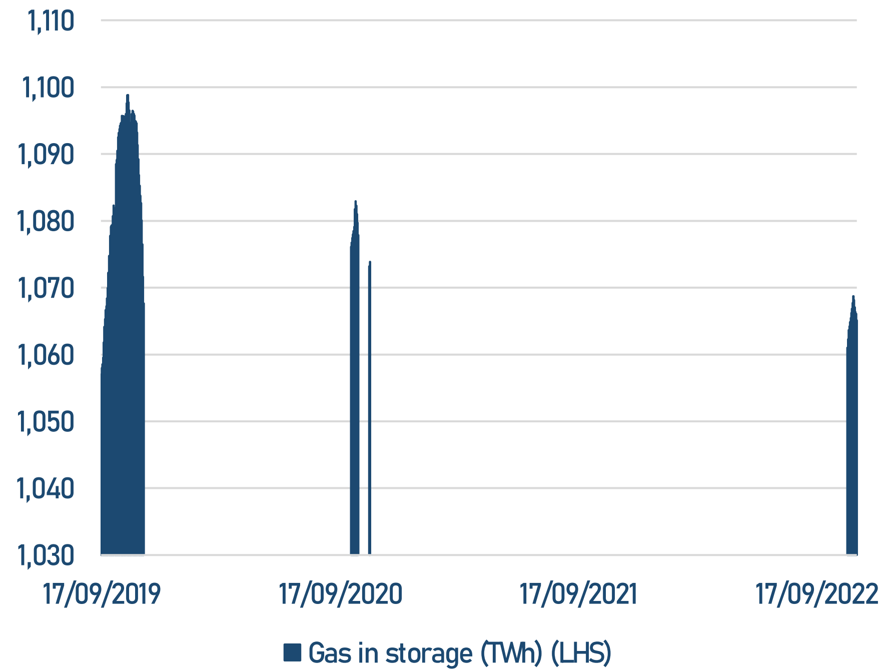
GAS STORAGE NEAR 2019 HIGHS

18th Nov	EU Gas Storage Full % (RHS)
18/11/2017	85
18/11/2018	86
18/11/2019	96
18/11/2020	93
18/11/2021	73
18/11/2022	95

European gas in storage peaked on 13th Nov 2022

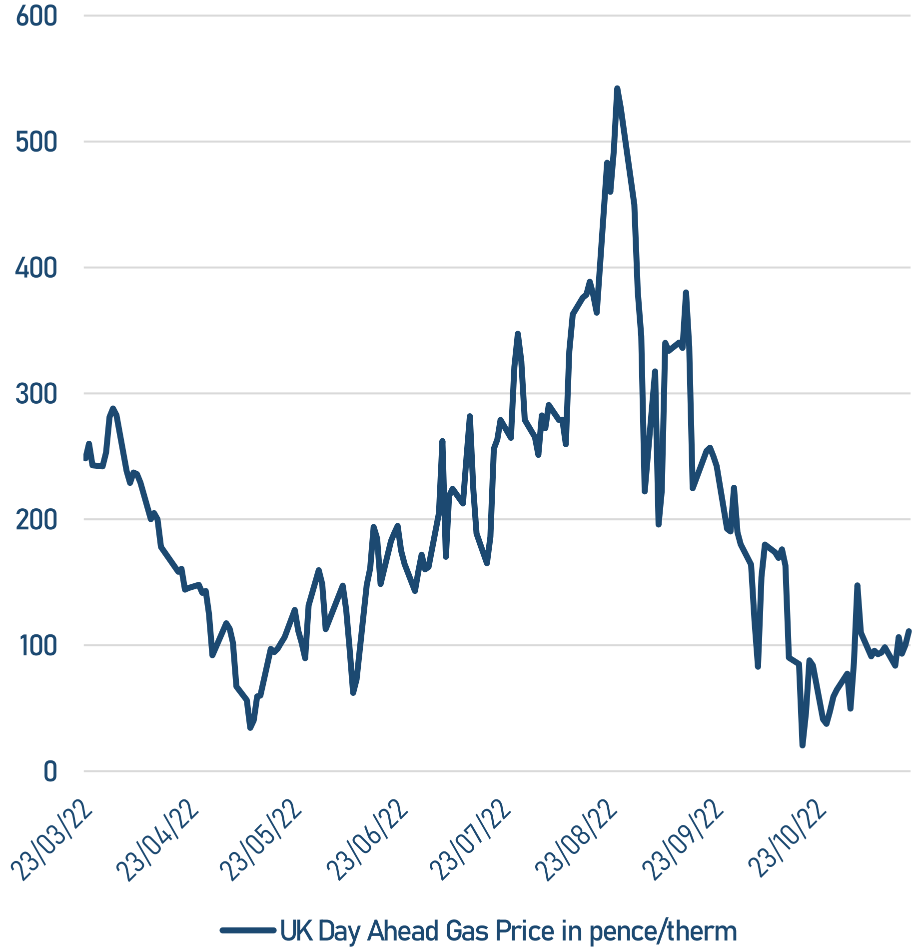


Days when EU gas storage was above 95%

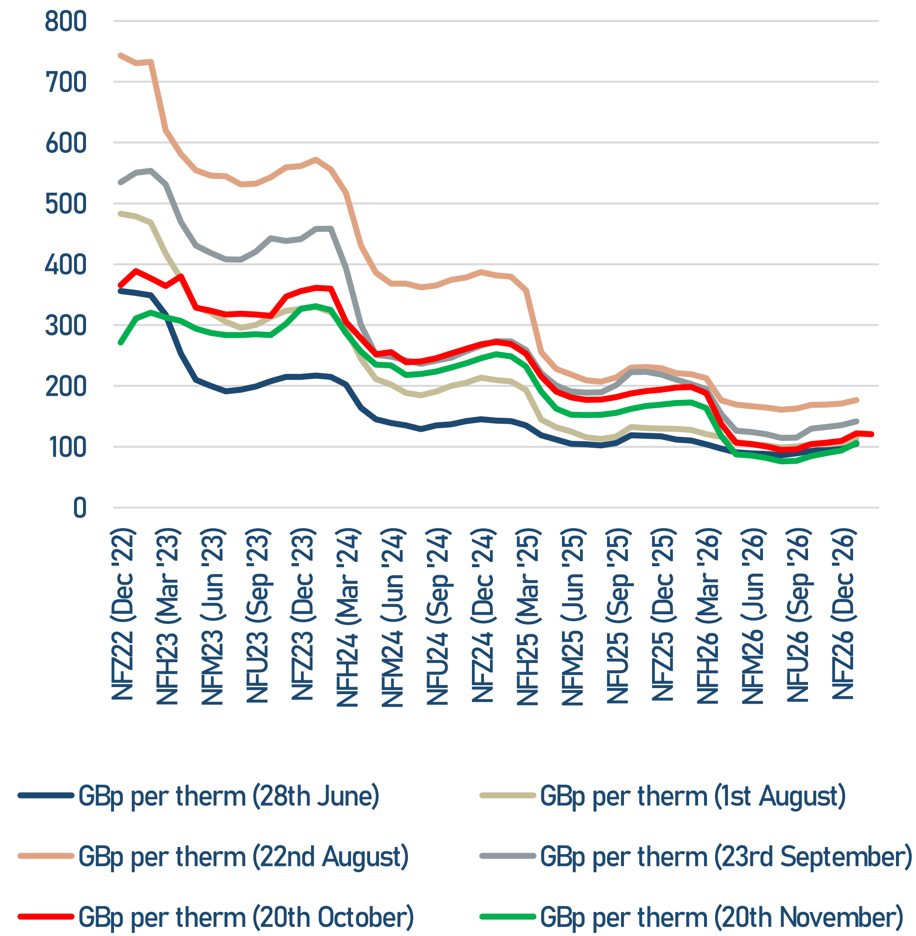


FUTURES GAS PRICES REMAIN ELEVATED

Day-ahead gas prices have cooled amid high storage levels



UK future gas prices remain elevated, but near-term have come down



4. CREDIT EVENTS IN ONLINE RETAIL

MADE.COM AND JOULES BANKRUPTCIES & RETAIL

- Made.com had 7 showrooms, but was selling purely online
- Joules made 61% of its sales from online in 2021
- US based Target sees fewer sales in discretionary items in recent weeks vs. Walmart, which has tried to leave prices low and has a higher share (50%) of sales in groceries sees strong demand

→ Consumer shifts towards cheaper products

→ Consumer moves back to stores and away from online