

Hello Everyone

I saw a headline that read:

### ***How Costco Is Masking A 14% Price Jump With Shrinkflation***

The point of the story was Costco Paper Towel Rolls have only 140 sheets per roll vs. 160 sheets last month.

The price for the roll was the same; but you received 14% less product.

Now when the Bureau of Labor and Statistics computes the inflation rate, it will use just the price of the paper towel roll. It will not adjust the price for the diminished quantity. This is one reason why the current CPI (Consumer Price Index) shows a 2.6% inflation rate, when most of us are saying, *"It feels a lot higher than that to me."*

So why would the government want to understate inflation?

Oh, maybe because many government expenditures such as social security, government employee pay, and military retirements are adjusted annually based on the CPI. What if the CPI showed a 7%-9% annual increase? (Which by the way, many independent inflation calculations show.) Our budget (which is already bad) would be blown to smithereens.

That is a long introduction to this week's missive about the Federal Reserve and inflation. I hope it helps you see the Fed's predicament.

Signed, Your If-Caitlyn-Jenner-And-Randy-Quaid-Both-Run-For-Governor....Californians-Might-Decide-To-Stay-Just-To-See-The-Show Financial Advisor,

Greg

## **KKOB 05.03.2021 For The Fed What Is Next?**

**Bob:** So, Greg, I saw a business headline last week that read, ***"Bank of America Says, "Inflation Is Here"***. My first reaction was Greg has been telling us this was coming for over a year.

**Greg:** Thanks. But you don't have to be an economic genius to know if you print trillions, eventually your currency will be devalued and prices will rise. And since our goal here is to attempt to see what's next, let's view things from the Federal Reserve's perspective.

Fed Chair, Jerome Powell, spoke last week and said the current inflation situation was **“transitory”**. Meaning, he thinks they can stop inflation anytime they want.

My take is he had to say that. Here’s why.

Bob, currently the official inflation rate is 2.6%. Meanwhile, the 10-year Treasury Note is paying around 1.6% interest. So, if you think of it in CD terms, this would be like you committing to a 10-year CD at 1.6%----while the inflation rate is over 2 ½%.

So, Bob, would you commit to that?

**Bob:** No. I may not lose money, but I know I’m losing buying power. And that is assuming inflation stays tame for the next 10 years. I’m not sure I want to make that bet. I mean---every year for the next 10 years--- I risk my money being worth less depending on how bad inflation gets. Plus, I can’t get out without a penalty because I locked in for 10 years.

**Greg:** Right. And since Bob and Greg in Albuquerque know this, the market knows it, too. And so does Fed Chair Powell. But, remember, he still needs someone to buy those billions of 10-year notes every month. That’s how we fund the government. We borrow trillions. *But we need someone to loan it!*

Thus, Mr. Powell is using the prestige of his position to jawbone the market into believing the rising inflation rate is just a blip on the radar screen. Basically, he’s saying, **“Don’t worry. It will all be back to normal soon.”**

**Bob:** But from your tone, I don’t think you believe it.

**Greg:** I don’t. Where we are seeing inflation is in base products. Think copper, lumber, corn, sugar, soy beans, pork, aluminum, and so on. Oh, and watch chicken prices...those are next.

Anyway, all are up 50%-200% over the past year. And the pace is accelerating.

So, Bob, now put yourself in a manufacturer (or food processor's) shoes. All those materials are input costs. You must account for those in the price of your end product. So prices rise.

Oh, and last week, President Biden, gave his pitch for raising corporate taxes. And I get it. He needs some revenue to pay for all his programs. *But for a corporation, taxes are just another input cost.* So, in most cases, they will just add *their* tax into the cost of the end product.

So while the politicians will campaign on "*sticking it to the man,*" in reality it's the consumers who will eat the bulk of those taxes at the register.

**Bob:** So...before you go on...what you are saying is we are looking at a double whammy inflation-wise. Raw material prices are going up and we'll pay for that. Plus, the tax part will be added on.

**Greg:** Right. That's why I don't see inflation as a *transitory* phenomenon like Mr. Powell says. It takes time for inflation to work its way through an economy. It's not like you print money and the next day prices rise. The inflation you see today was baked in a year ago.

The same with rising copper, aluminum, or corn prices. It takes time for rising raw material (or food) prices to percolate to the store shelves. The same will hold true for taxes. Tax increases won't show in higher prices until later. Therefore, voters don't usually make the connection.

The point is, I believe there are structural elements in place that will keep inflation pressure on for longer than the Federal Reserve hopes.

**Bob:** It'll be interesting to see what the Fed does if you're right. How do people reach you?

**Greg:** I have theories on that...but that is for another day. My number is 250-3754. Or go to my website at [zanettifinancial.com](http://zanettifinancial.com).

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