



## Zanetti Monday Missive 2022.01.17 Inflation: Where's the Beef?

**“A lie cannot live.”**

~ Dr. Martin Luther King Jr.

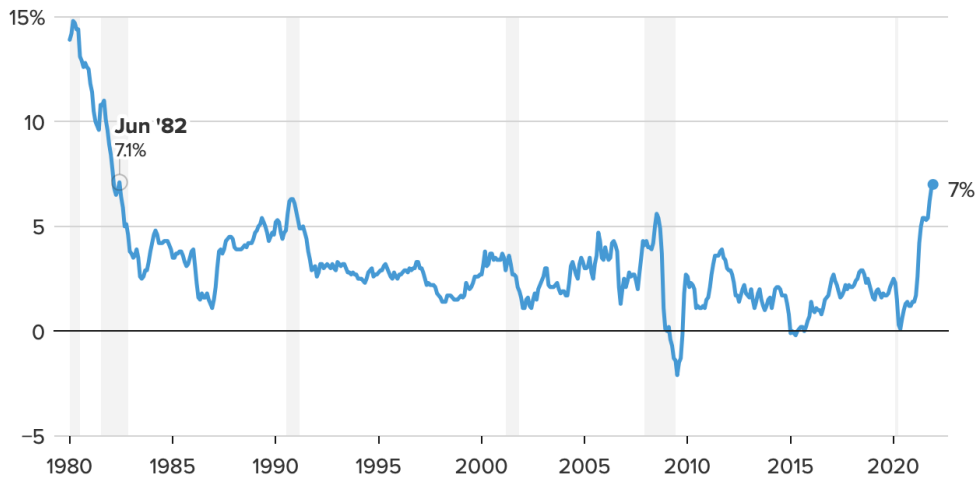
**“Inflation is taxation without legislation.”**

~ Milton Friedman

Last week the Consumer Price Index (CPI – the noted measure of U.S. Inflation) was reported at 7% for December. That’s the biggest jump in annual CPI increase since 1982 and I’ve got a beef with that.

## Consumer price index, percent change from a year ago

All items in U.S. city average



Note: Shaded areas indicate U.S. recessions.

Source: Bureau of Labor Statistics. As of Dec. '21.

You're probably bored and slightly irritated with so much talk about inflation. And now you might be asking yourself, so where's your beef, Walt?

Well, I'm glad you asked! My beef is, how did they come up with 7%? Now let me ask you a question. What costs are you aware of that have risen only 7% in the past year? Not much, right?!?!

- Gasoline UP 50%
- Used Vehicles UP 38%
- Meat and poultry UP 12.5%
- Furniture & Bedding UP 13.8%
- Hotels/Motels UP 27.6%
- Lumber UP 70%
- Rental Cars UP 36%
- Rent for 2 Bedroom house UP 28%
- Average home price UP 19%

So, what's with the 7%? Well, the federal government has to increase Social Security payments based on inflation, and they don't want to increase their expenses unnecessarily, so they calmly correct "emotional" inflation numbers by using a method they lovingly refer to as the "Hedonic Quality Adjustment." To cut through the fog, let's just say this allows the federal government to replace some items on the CPI with others, which brings the "official" inflation number down.

AND EVEN WITH THAT MODIFIED CALCULATION, WE'RE STILL AT 40 YEAR HIGHS! If they went back to using the 1982 formula today, we'd be closer to 15% inflation right now. Which would feel about right for us, wouldn't it?

Let me give you an example of how inflation ripples through an economy and leaves nobody unscathed.

Our current Governor just increased minimum wage from \$10.50/hour to \$11.50/hour on January 1st, 2022. So, just like that, minimum wage employees got a 10% raise across the whole state without having to work harder, increase their skill set, or add to their education. That's a pretty good deal for them, eh?

Well, my family owns a few Baskin Robbins Ice Cream Stores and we hire a lot of highschoolers and young adults at minimum wage to scoop ice cream. We love these employees and are happy to increase their pay (although, left to their own work ethic, some of them normally wouldn't have received a 10% raise).

At the same time, the cost of our ice cream has increased by 15% from the company we are in contract with (We buy our ice cream from DFA based out of Utah). Why is that? Well, part of it is the cost of Nitrogen and Phosphate. Ok, bear with me for a sec.

Nitrogen and phosphate are used in fertilizers. The price of nitrogen increased by 32% in 2021 while phosphate increased by 93%!

When farmers fertilize their crops, they pass that expense increase on in the crops they sell. When dairy farmers buy feed for their cows, their costs go up. Then, when DFA buys milk and sugar to make the ice cream, those costs have risen. Then, DFA has to package their ice cream in 3-gallon cardboard tubs, and cardboard has increased in price. Then, they have to load the ice cream onto a truck by employees that are harder to find and are making higher wages. Then they ship the ice cream to Albuquerque in trucks that have to pay more for their Diesel Gasoline.

We then unload the ice cream into our store with employees that now make 10% higher wages. And we store it in freezers that cost more to run because of the cost of electricity. Then when you come in to buy a scoop of mint chocolate chip, instead of it costing \$3.19, the cost is now \$3.49 (a 10% increase). None of our customers have complained of the price increase, but I'm sure they don't enjoy it any more than we enjoy our operating costs increasing. And the folks making 10% higher wages aren't able to save any more at the end of the month.

That's why as shoppers, we get frustrated when we're at the grocery store and at the local ice cream shop. And that's why inflation is so hard on everybody. But as investors, we're happy because our investments in nitrogen, gasoline, milk, cardboard, and energy have done well. Much better than the 7% inflation that the CPI is reported at.

Your In-2022-Hindsight-Is-2020 Financial Advisor,

Walt

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