



Summary

- August CPI rose due to a double-digit increase in gasoline prices. Core inflation fell further, with falling rent prices aiding the disinflation in core services
- Rising oil prices drove up producer prices, with continued upside risk here. The core readings however remain soft
- Import prices in August also jumped due to rising oil prices, but non-fuel import prices remained steady
- Hourly earnings growth slowed in August following two consecutive strong monthly gains. JOLTS numbers point to a better balance between labor demand and supply
- M2 growth returned to negative territory in August after temporary boosts in prior months due to the debt ceiling standoff
- Consumer credit saw a sharp fall, driven by pre-freeze student loan repayments in the non-revolving credit component

About this document

US Inflation Watch presents 18 charts comprising key inflation indicators grouped into five categories including consumer/producer price inflation, commodity prices, wage inflation, inflation expectations and monetary indicators.

Contents

Price Inflation

Consumer Price Inflation.....	2
Producer and Import Price Inflation.....	2-3

Commodity Prices

CRB Index.....	3
----------------	---

Wage Inflation

Employment Cost Index.....	4
Hourly earnings.....	4

Inflation Expectations

Consumer inflation expectations.....	4
Market inflation expectations.....	4

Monetary Indicators

Money Supply.....	5
Consumer Credit.....	6

Appendix

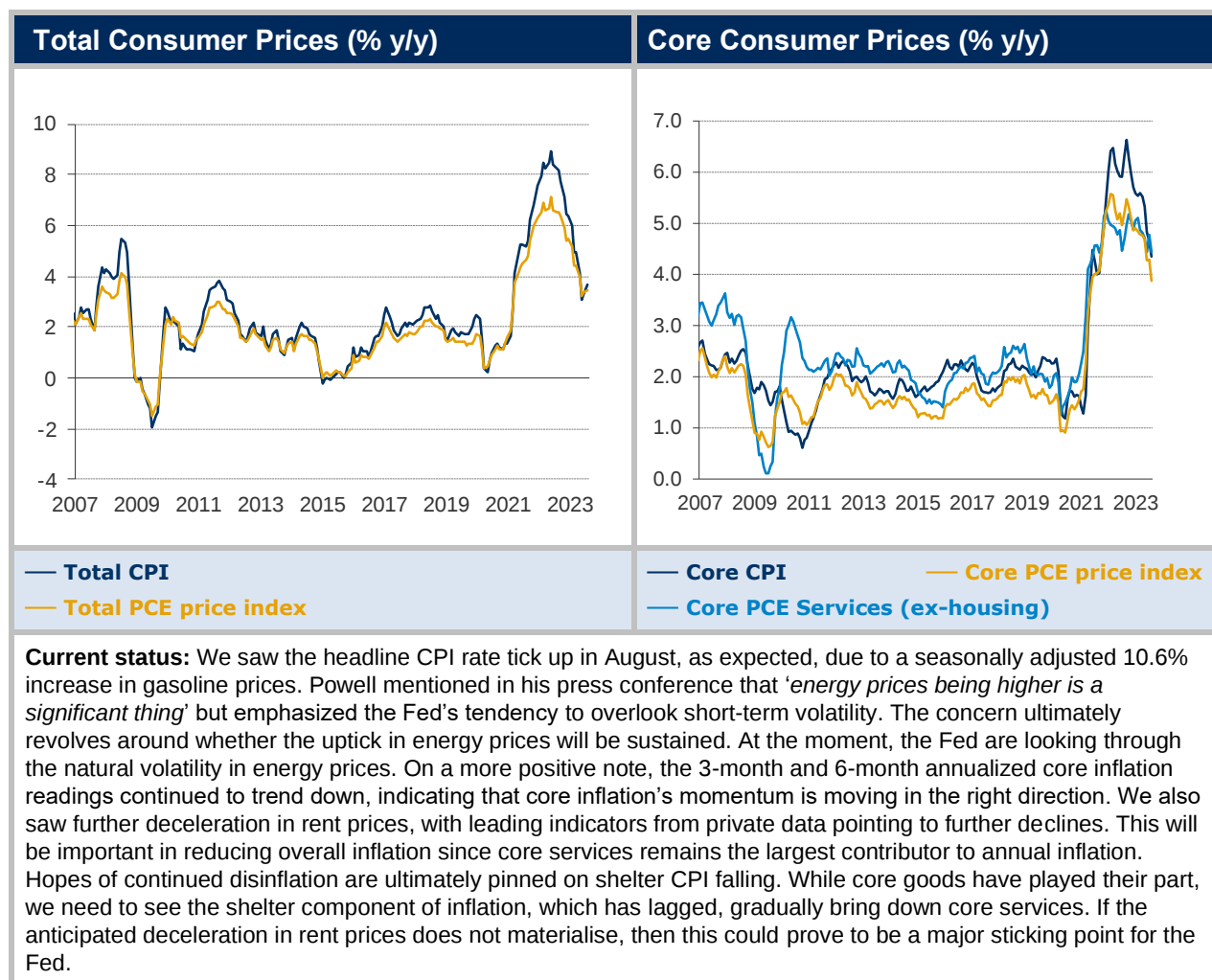
An explanation of money and the monetary framework.....	7-8
---	-----

The Importance of Inflation

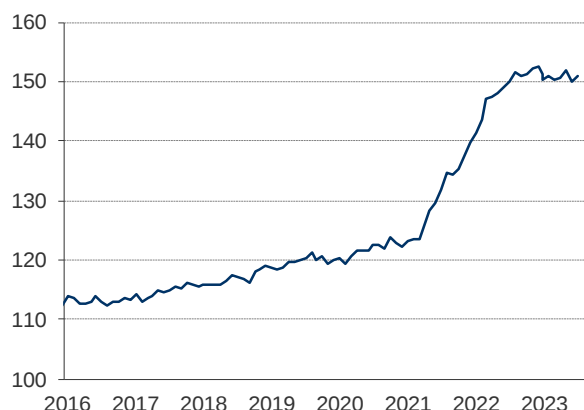
Inflation is the single most important indicator when measuring real wealth as it determines what wealth can buy i.e. purchasing power. If 'nominal' wealth doubles over 25 years but the level of prices also doubles, there is no net gain in 'real' wealth. It only takes annual inflation of 2.8% to cause a doubling in prices over 25 years.

About Altana Wealth

Altana Wealth is a specialist fund manager focused on delivering alpha where we have a competitive edge from niche strategies. As co-investors in all our funds, our interests are aligned with those of our investors. Altana was set-up by Lee Robinson, co-founder of highly successful Trafalgar Asset Managers in 2010. Our funds have won seven performance awards over the past three years.

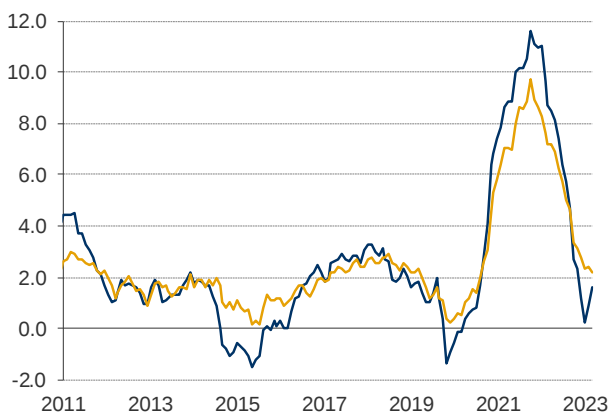


Producer prices (index)



— **PPI Trade Services**
(the margins of retailers & wholesalers)

Producer prices (% y/y)



— **PPI final demand**
— **Core PPI final demand (ex-food and energy)**

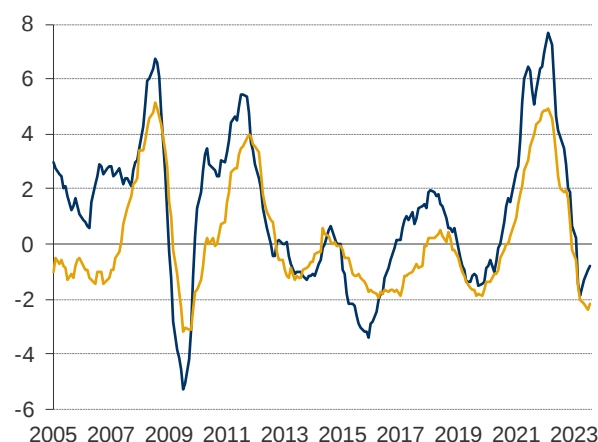
Current status: The August headline PPI rose 0.7%, exceeding the consensus estimate of 0.4%, helped by higher fuel prices. However, the core PPI reading on a y/y basis dipped to 2.1%, the lowest reading since January 2021, and down 5% since the start of the year. Significant progress has been made in bringing down producer price inflation, but it's likely this deceleration will come to a halt over the coming months due to the surge in oil prices. As for food prices, they fell 0.5% m/m in August and have only risen twice this year. This bodes well for consumers, as this tends to lag three months behind falls in producer prices.

Import Prices (% y/y)



— **Import prices**

Import Prices – core and China (% y/y)



— **Core import prices (ex-fuels)**
— **Import prices of Chinese goods**

What is this data? Producer price indices refer to prices set by domestic producers only, so Import Prices are also monitored to gauge price pressures entering the system from abroad. Import price data excludes tariffs.

Current status: Import prices rose more than anticipated in August, with the increase primarily driven by rising oil prices. We should expect the rise in headline import prices to be sustained over the coming months. Import prices excluding petroleum remained flat for the second consecutive month following five monthly declines. We've now seen this measure either decline or move sideways in every month since May 2022, which is encouraging. Despite the challenges posed by rising oil prices, improving supply conditions and slowing goods demand have helped limit price increases in non-fuel categories, indicating that disinflation continues elsewhere. On the goods front, the expectation is for falling goods demand to continue exerting downward pressure on non-fuel import inflation.

CRB-TR/J Commodity Price Index



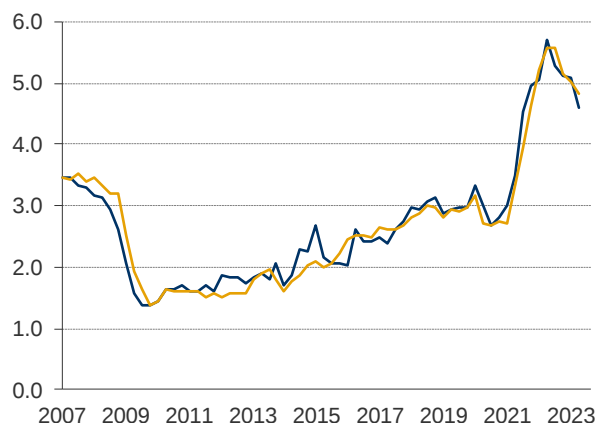
CRB-TR/J Commodity Prices (% y/y)



What is this data? CRB Index is a basket of commodity prices - a timelier indication of Crude PPI.

Current status: Commodity prices remained largely unchanged in August, with oil trading flat for the month and copper experiencing only a slight decline. Despite the dour outlook for the Chinese economy, commodity prices don't seem to reflect the same level of pessimism. If the Chinese economy were struggling as much as many suggest, we would expect commodities such as oil to show weakness, despite a tighter supply backdrop. As for industrial metals, demand appears to be holding up much better than expected, especially considering the downturn in China's property market. One contributing factor could be China's commitment to infrastructure spending, which has facilitated increased construction activity in the renewables sector.

Employment Cost Indices (% y/y)



— **Wage & Salaries** (private sector)
— **Wage & Salaries-ex incentives** (private sector)

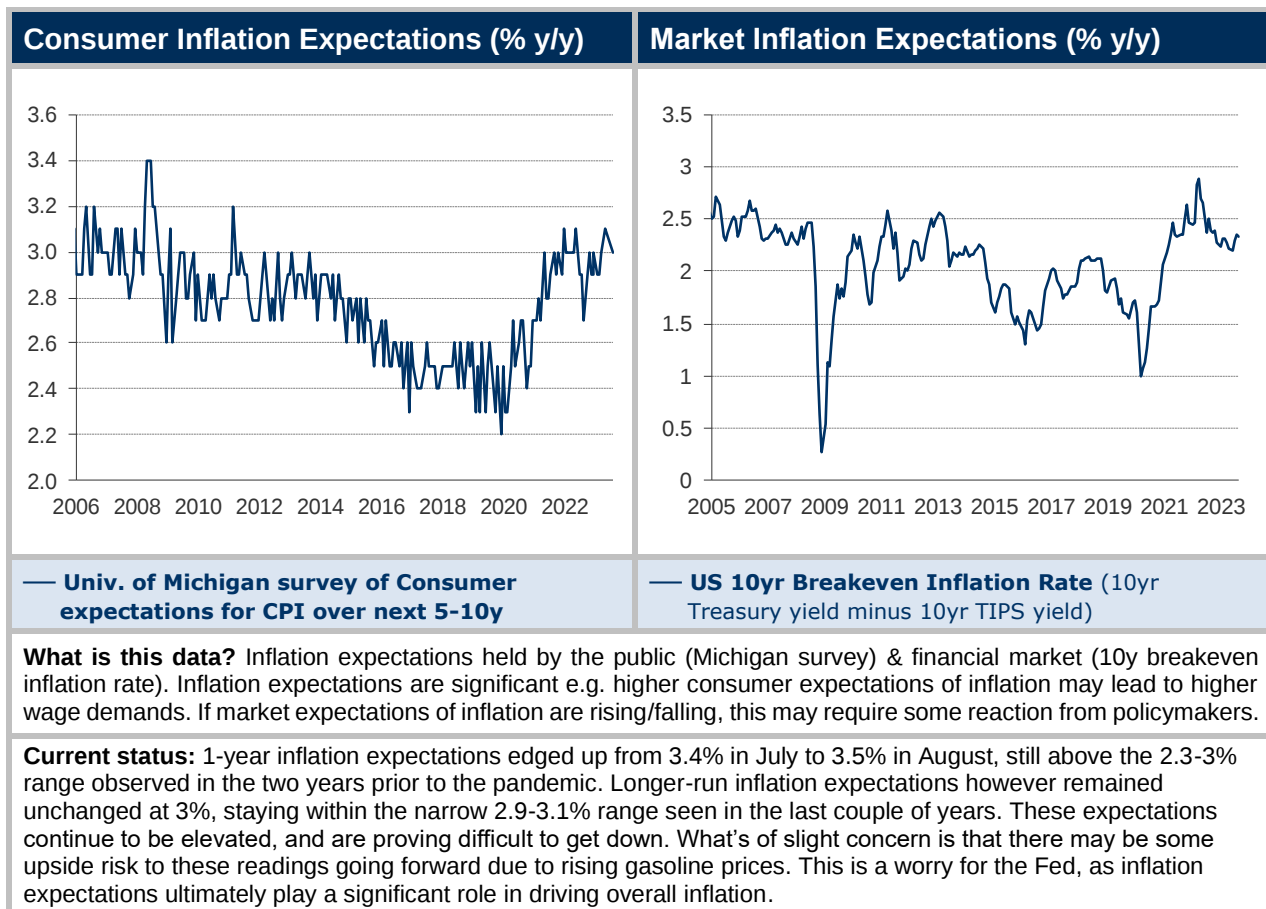
Hourly Earnings (% y/y)



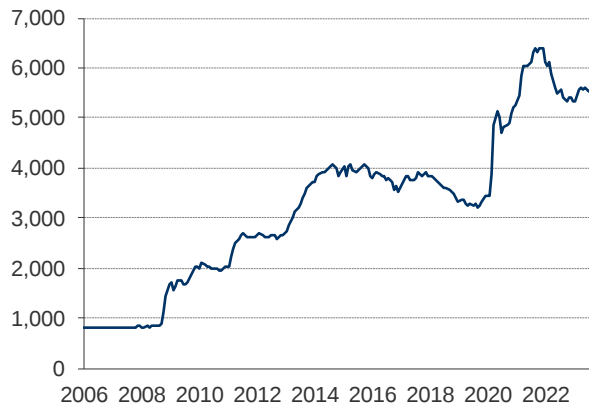
— **Hourly Earnings** (private sector)

What is this data? The Employment Cost Index (ECI) is the total cost of employing workers (wages, salaries, benefits) and is quarterly – just wages and salaries components are shown above; 'hourly earnings' is monthly.

Current status: Average hourly earnings rose 0.2% in August, a pleasant surprise for the Fed, following consecutive monthly gains of 0.4%. The y/y rate dipped to 4.3% from 4.4% in July but remains above the Fed's 3.5% target. We're also seeing a declining trend in job openings, which will help bring a better balance between labor demand and supply, helping slow down wage growth. The fall in the quits rate from the JOLTS report indicates a reduced willingness by workers to move for better jobs, playing a key role in lowering wage bargaining power. As always, we'd need to see sustained softening in these reports to be assured wage inflation is moderating.

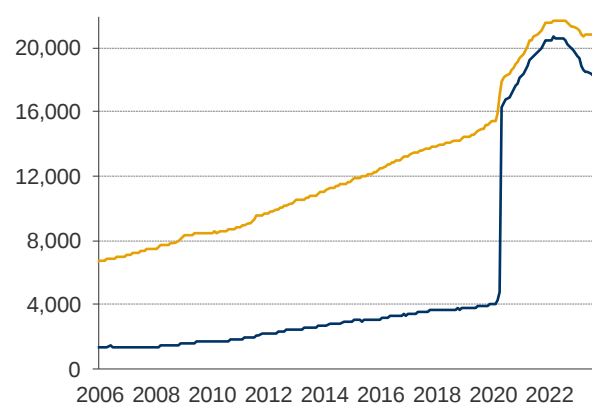


Monetary Base



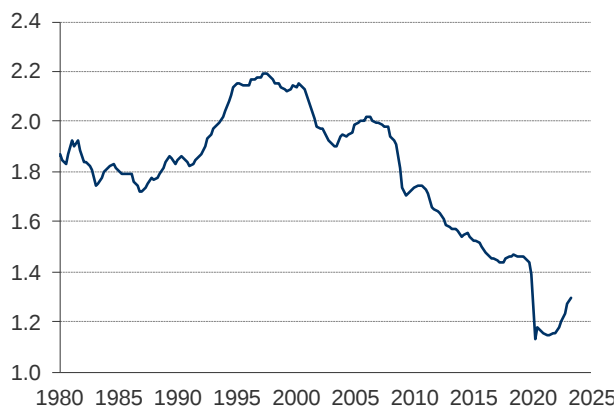
— **Monetary Base** (level outstanding \$bns)

M1 & M2



— **M1** (level outstanding \$bns)
— **M2** (level outstanding \$bns)

M2 Velocity



M2 (% y/y)



About the data

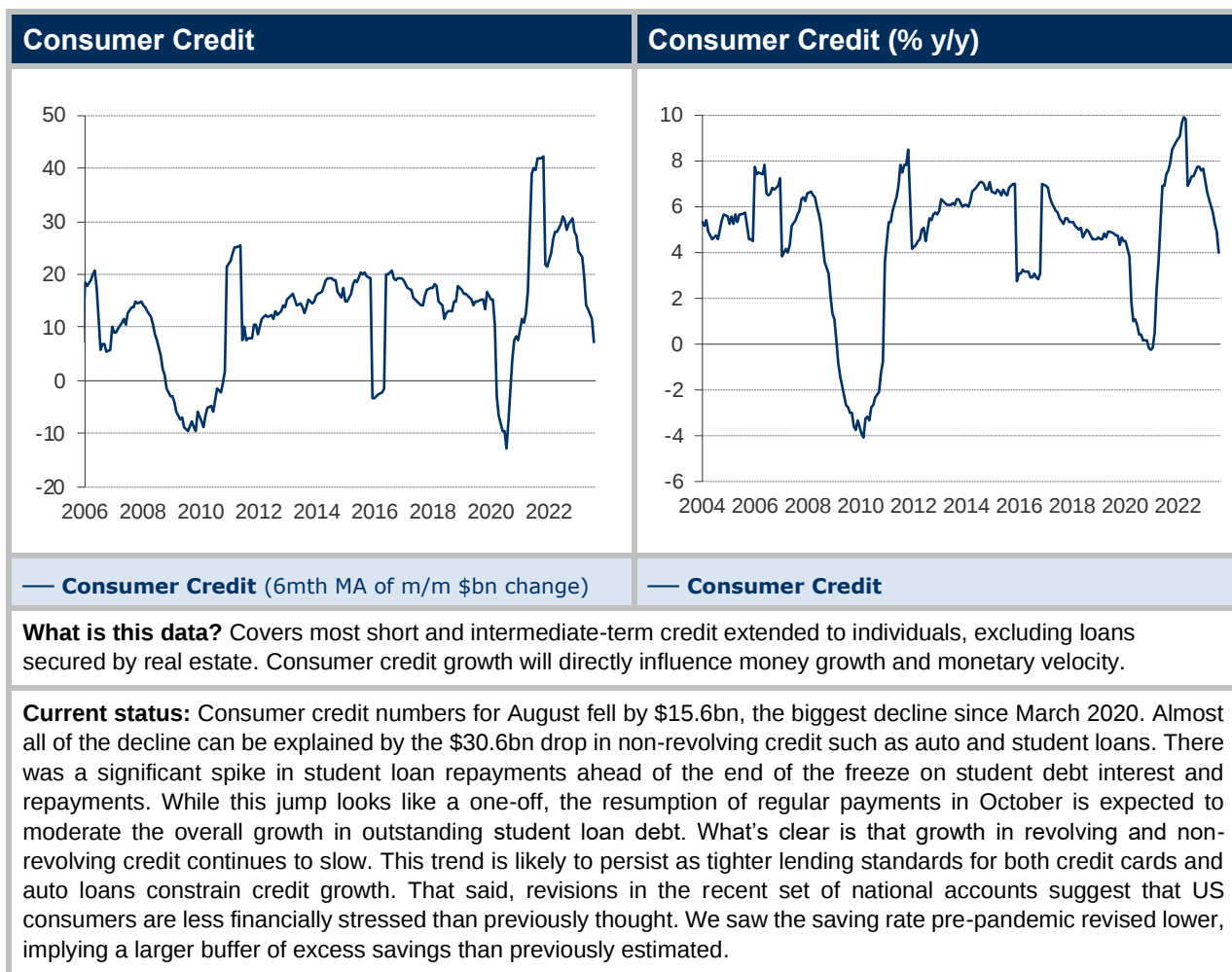
Monetary base = M0 (or notes & coins in circulation) + notes & coins held by banks and the central bank + bank reserves held by the banking system at the central bank. **Note:** the last two items are *not in circulation*

M1 = M0 + demand deposits + other checkable deposits (inc savings deposits previously in M2 – recently revised)

M2 = M1 + time deposits < \$100k + retail money funds.

M2 Velocity = Nominal GDP/M2 shows how often the money stock is used for spending on goods & services and is inversely related to the 'demand for money' i.e. holding that money rather than exchanging it for goods and services.

Current status: M2 growth in August fell 0.2% m/m following consecutive positive prints in the three months prior. Having rebounded in recent months largely thanks to the temporary effect of the debt ceiling stand-off, this boost now appears over, with falling bank lending and continued QT pushing M2 back down again. Bank lending remains the primary driver of broad money supply growth as every new loan creates a deposit, and M2 is comprised mostly of these deposits. With lending continuing to contract, we can't expect M2 growth to start turning more favourably. That said, the trend upwards in money market flows continues and accelerated in August, increasing by 1.8% compared with 1% in July. As for M1, this fell by 0.7% in August, the biggest decline since April. This isn't a surprise given the increase in flows to higher-yielding vehicles such as MMFs. The sharper fall in M1 can also be seen as an indicator that consumers are depleting their savings at a quicker pace. Despite the resilience displayed by the US consumer this year, we should anticipate this drawdown in excess savings to continue and potentially accelerate in the coming quarters.



Appendix A – Monetary Indicators

The monetary backdrop is somewhat profound in terms of its potential influence on inflation and is the subject of considerable debate. Below is a simple monetary framework that helps to explain the role of Money in the economy and how it can affect inflation.

A Monetary Framework

The amount of money circulating in the economy will have implications for inflation in the medium-long term. This is best expressed via the **Quantity Theory Identity**

$$M.V \equiv P.Y$$

Where M is the amount of money in the economy, V is the velocity of money (how many times the amount of money is used), P is prices and Y is real output (GDP). Together, P.Y is money or nominal GDP.

As a basic identity this is not controversial. If M (\$500) is used 5 times (V) then \$2,500 will have been spent and will be equal to the value (P.Y) of all goods sold in the economy - e.g. 2,500 items of real output (Y) at \$1 each (P) or 1,000 of (Y) at \$2.50 each (P) etc.

Where the identity becomes more interesting is in the assumptions made about its components. Traditional Monetarists contend that V is fairly stable and predictable, and Y is constrained by the capacity of the economy. So, Monetarists argue that if M is rising faster than Y and V is stable, it follows that P will also rise. In other words, money growth creates inflation.

Others contend that V is not stable and that Y can occasionally deviate substantially away from full capacity, so the relationship between M and P is less obvious. For example, since the Global Financial Crisis the Federal Reserve has made great efforts to increase the supply of money (M), but this has not led to proportionate increases in P.Y. This is due to two things. First, a reduction in velocity - any extra money balances are merely accumulating in the system (higher demand for money) rather than being spent and second, a lower money-multiplier. The money-multiplier represents the rate at which central bank created money (the monetary base) generates additional increases in the total money stock, primarily via the lending of commercial banks – more on money creation below.

In sum, this basic Quantity Theory Identity is a useful framework for analysing the potential interaction between the monetary and real sectors of the economy and the data followed in this document will seek to shed light on what is happening to the various components of this identity.

What is Money?

Another issue is how 'money' or M is defined. Definitions of money include M0, MB (the Monetary Base), M1, M2, M3 and MZM (maturity zero money) and the basic difference between them is primarily related to liquidity. The further we move along the spectrum towards M3 the less liquid 'money' becomes. For example, a large time deposit cannot be spent immediately whereas a checking deposit can. Note that M3 and MZM are no longer used in the US by the Fed.

Definitions

M0 = notes and coins *in circulation* with the non-bank public.

Monetary base = M0 + notes and coins held by banks and the central bank + bank reserves held by the banking system at the central bank (bank reserves) **Note:** the last two items are *not in circulation*.

M1 = M0 + demand deposits and other checkable deposits (including savings deposits after Fed methodological revision – they were previously in M2). **Note:** bank reserves are not included in M1 – important when looking at how Fed QE affects M1 and M2 etc.

M2 = M1 + time deposits less than \$100k + retail money funds. **Note:** institutional money market funds are not included in M2.

M3 = M2 + large time deposits + institutional money market funds + short-term repos and other large liquid assets.

MZM (Money Zero Maturity) = M2 + all money market funds less time deposits **Note:** MZM aimed to identify all forms of 'liquid' money and was a hybrid of M2 and M3.

Who creates Money?

A useful way to think about money – again relevant when considering Fed QE – is who creates it? The short answer is that both the central bank and the commercial banking system create money.

The Monetary Base is created and influenced by the Central Bank and is so-called because it is the base from which all other forms of money (non-M0, M1, M2 etc.) are created by the commercial banking system via bank lending.

For example, using QE as an example, the Fed buys T-Bonds from a bank and credits that bank's account at the Fed with the proceeds. These funds are now reserves. At this point, no money has entered circulation, so no other measure of money apart from the Monetary Base has been affected.

As the Monetary Base has increased, commercial banks are more *able* to create other money by issuing new loans and if they were to do this it would lead to a corresponding rise in deposits. Bank lending is the main driver of 'money creation'. This is because a loan, when advanced to the borrower, will be deposited in the borrowers account i.e. an immediate rise in deposits (higher M1). Or, if the 'loan' is via a credit card, the borrowers account will not be affected, but the recipient of the credit card spending will deposit the revenue in their own bank account, so deposits somewhere in the system will have increased because of the 'loan' (higher M1).

In sum, boosting the Monetary Base (via e.g. Fed QE) increases the ability of banks to create other money such as M1. But the rate at which this happens (the money-multiplier) will come down to a commercial judgement by the banks as to whether or not they would like to advance extra loans.

Disclaimer

This report is prepared by Altana Wealth Ltd ("Altana") authorised and regulated by the Financial Conduct Authority in the United Kingdom (FRN: 532912). The investment products and services of Altana are only available to persons who are professional clients and eligible counterparties as defined in FCA's rules. They are not available to retail clients. The distribution of this report may be restricted in certain jurisdictions and it is the responsibility of any person or persons in possession of this document to inform themselves of, and to observe, all applicable laws and regulations of any relevant jurisdiction.

This report is based upon information that Altana believes to be reliable. Altana does not represent that this report is accurate or complete and it should not be relied upon as such. Nothing in this report shall constitute tax, financial, or legal advice given by Altana to any party. Performance information for the month of the report is preliminary estimated data net of all fees and expenses and is subject to change. The estimate and other performance data disclosed is not audited. Stock or other indexes are included for comparison purposes only. Where information provided in this report contains "forward-looking" information including estimates, projections and subjective judgment and analysis, no representation is made as to the accuracy of such estimates or projections or that such projections will be realised. Certain assumptions used in formulating such "forward looking" information may differ materially from actual events or conditions. The funds referred to in this report are registered as Regulated Mutual Funds pursuant to Cayman law but otherwise have not been registered under the securities laws, or authorized or approved by any regulatory authority, of any other jurisdiction. This report shall not constitute an offer to sell or a solicitation of an offer to buy shares or interests in any of the funds described in this report. No such offer or solicitation will be made prior to the delivery of an offering memorandum for the relevant fund. Before making an investment in any of the funds referred to in this report, potential investors should read carefully the private offering memorandum for the relevant fund, including the description of the risks, fees, expenses, liquidity restrictions, and other terms of investing in the funds, and consult with their own tax, financial, legal and other professional advisors. Hedge funds are speculative and involve risk of loss. This report is confidential and may not be reproduced in whole or in part, or delivered to any other person, without the prior written consent of Altana. Past performance is not a guarantee of future results. Issued by Altana Wealth September 2023.