

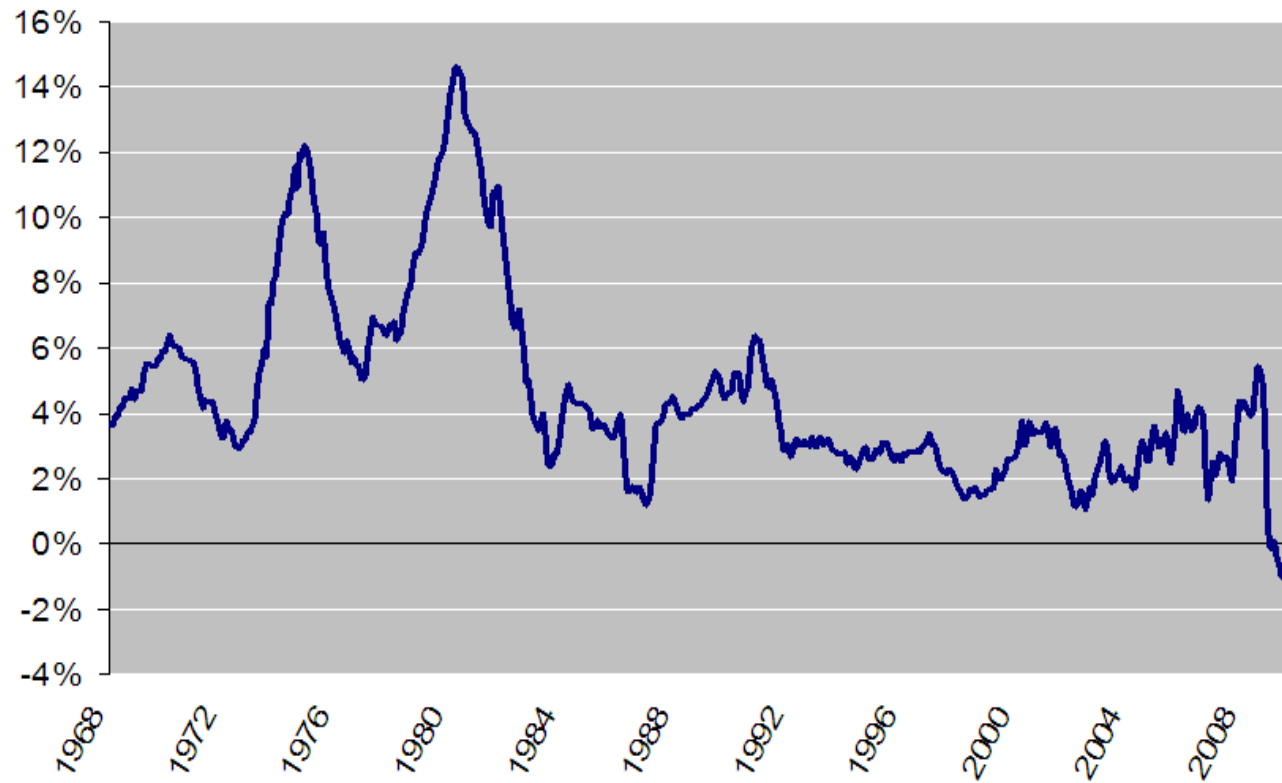
September 10, 2009



Outlook on Inflation

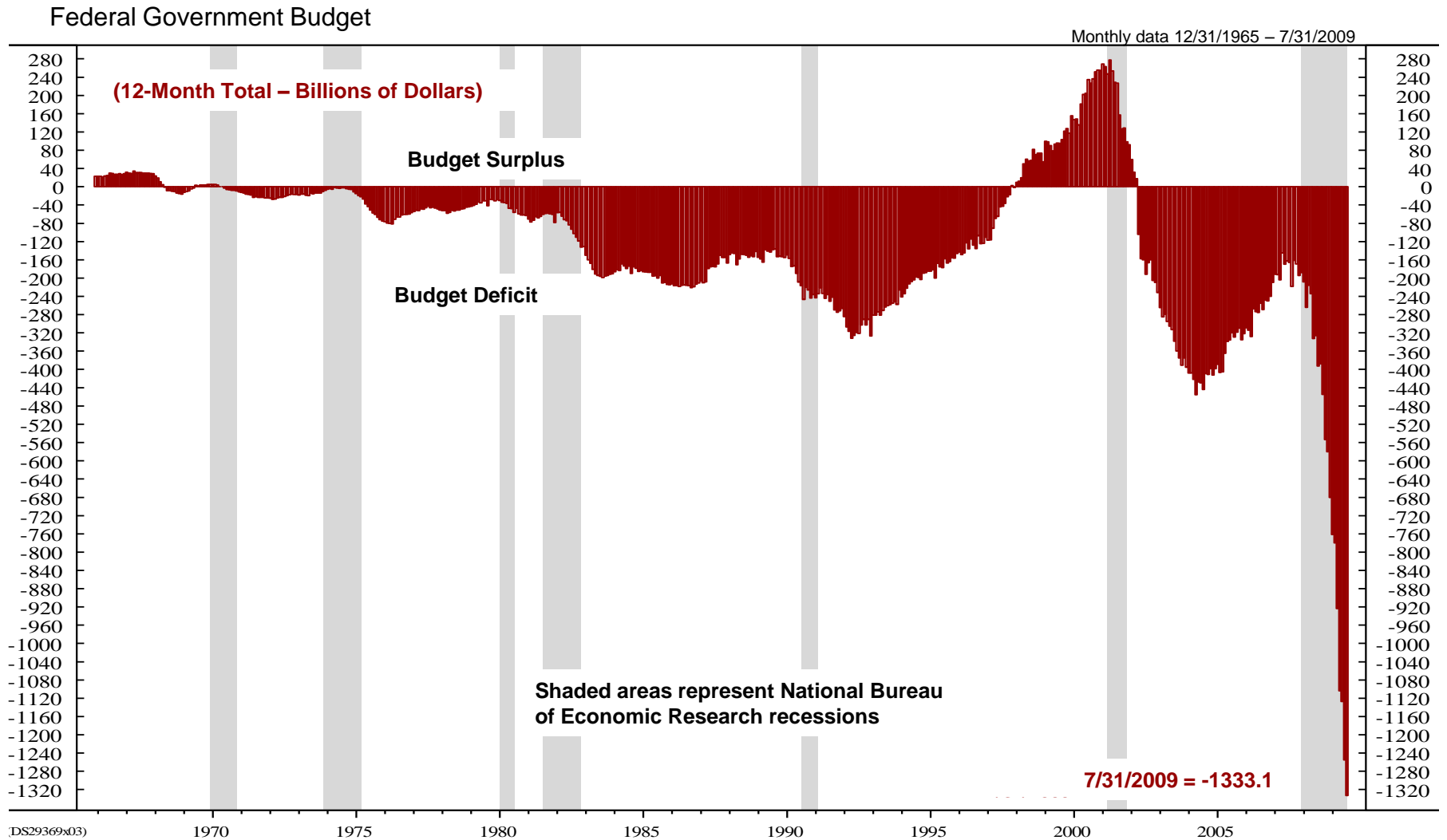
Current inflation levels are very low

Annual Growth in the Consumer Price Index (CPI)



Sources: Bureau of Labor Statistics, SEI

Large deficit spending

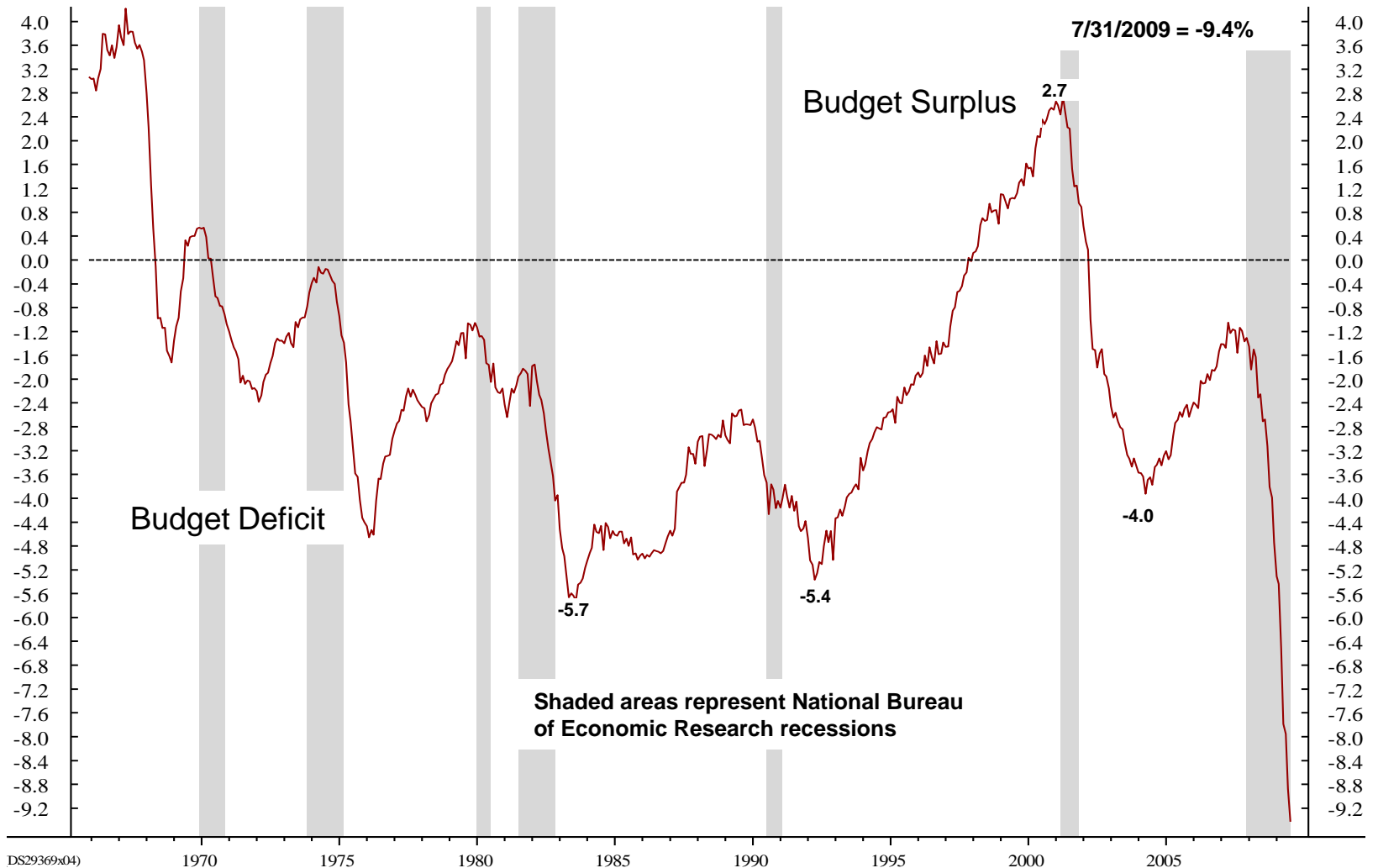


Source: Ned Davis Research

Large deficit spending

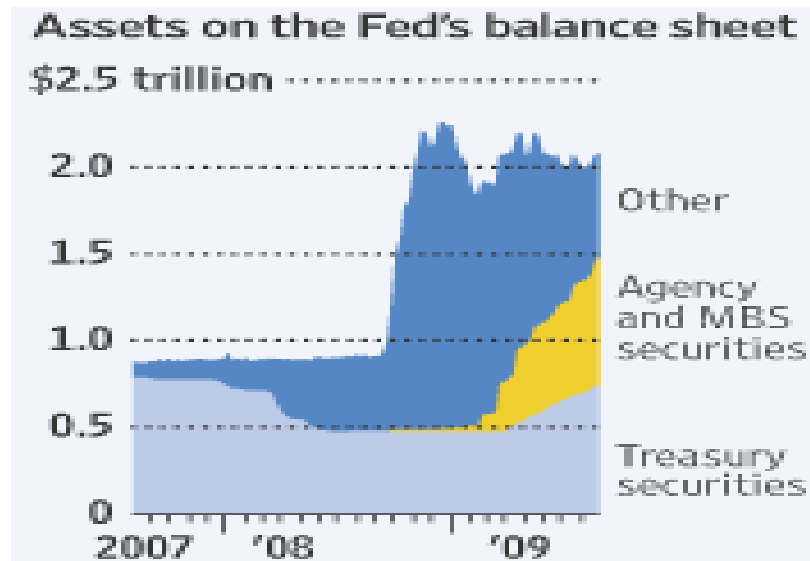
Federal Budget Deficit/Surplus as a % of Nominal GDP

Monthly Data 12/31/1965 – 7/31/2009



Source: Ned Davis Research

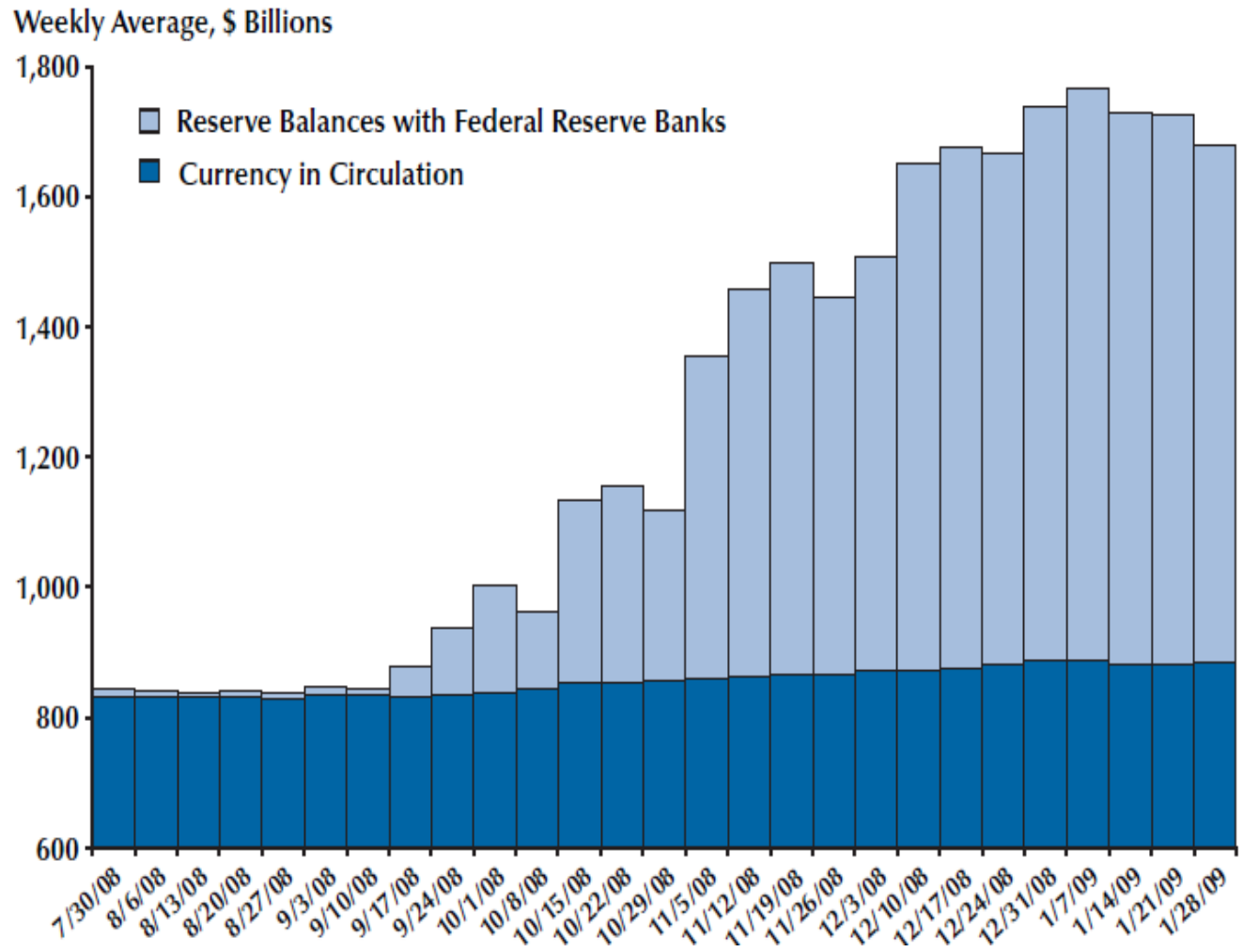
Aggressive monetary stimulus



Source: Federal Reserve

Aggressive monetary stimulus

Monetary Base



Source: Federal Reserve

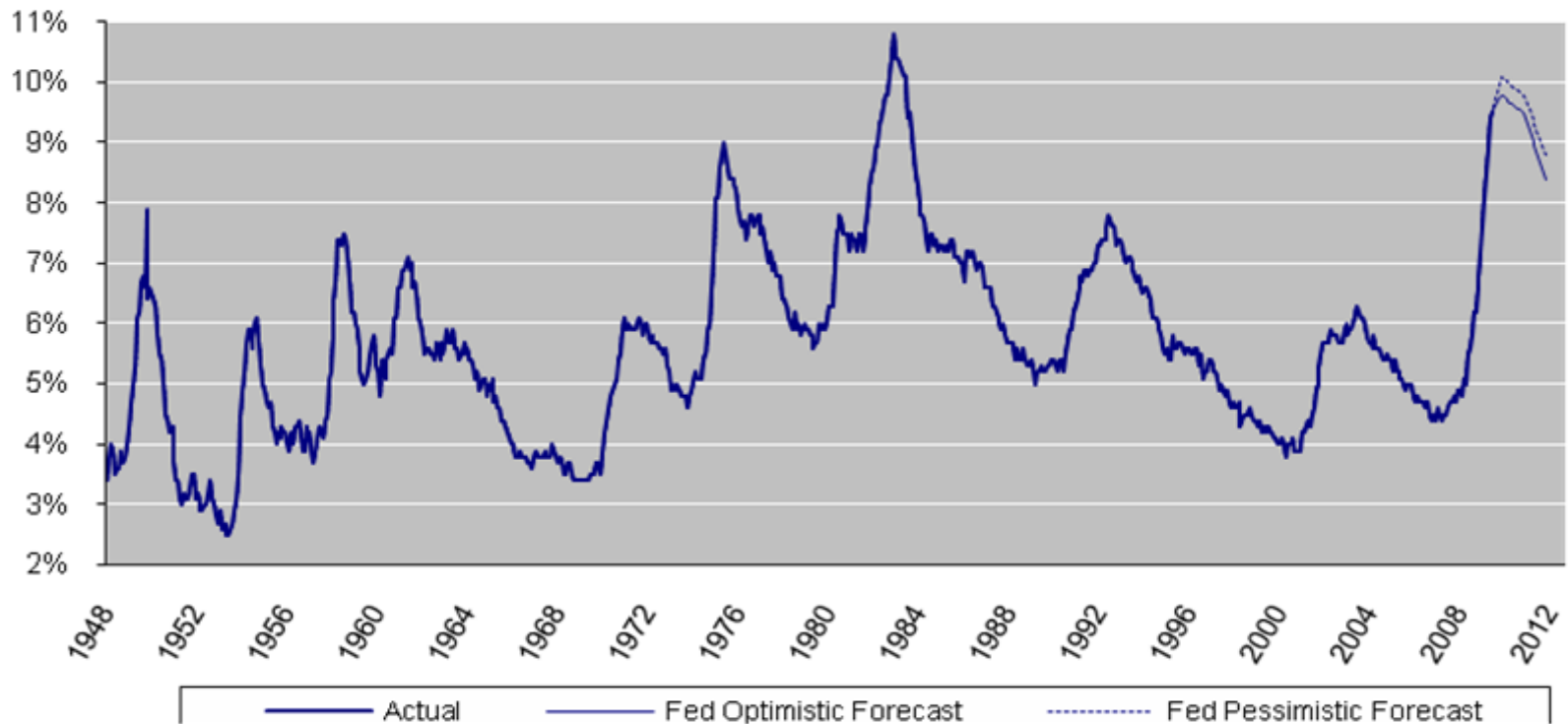
Inflationary pressures with no inflation??

- Inflationary pressure
 - Massive deficit spending
 - Extraordinary injection of money into the financial system
- Our view: Inflation is not a near term threat
 - 3 reasons

Reason #1

Significant slack in the economy

Unemployment Rate

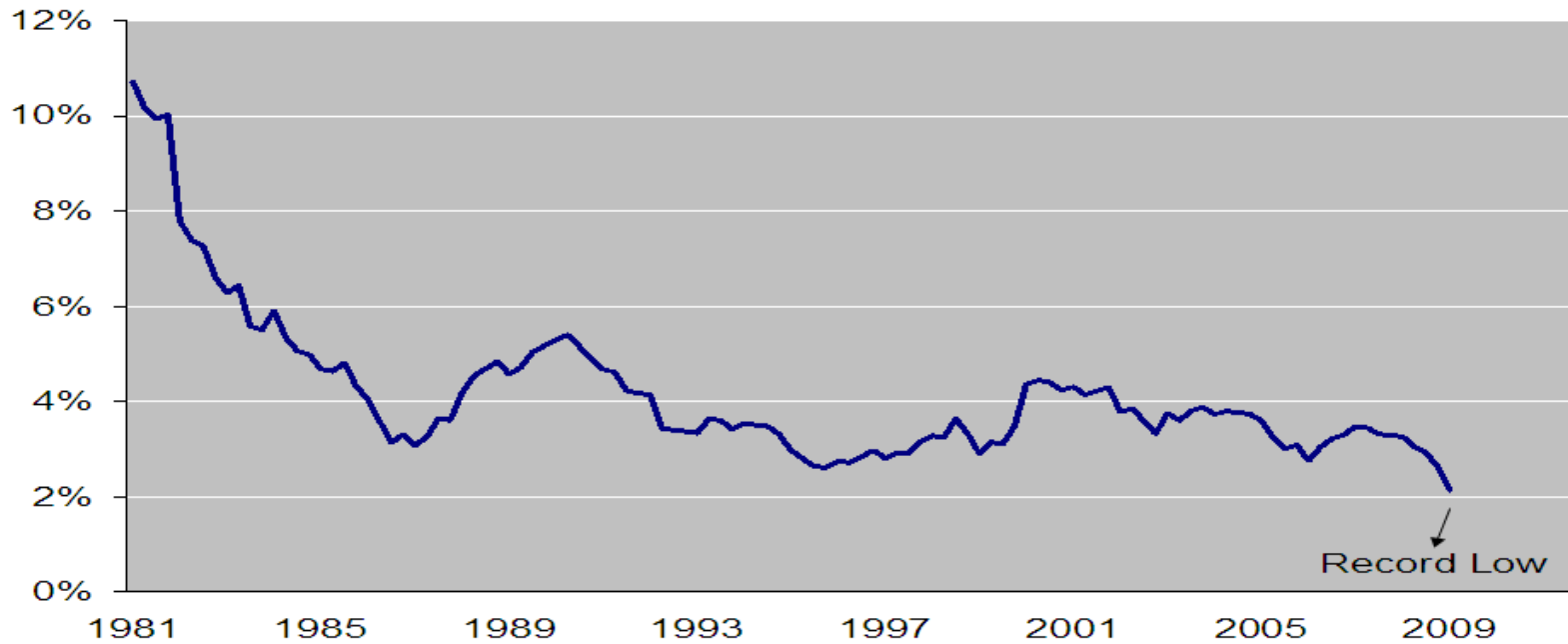


Sources: Bureau of Labor Statistics, Federal Reserve, SEI

Reason #1

Significant slack in the economy

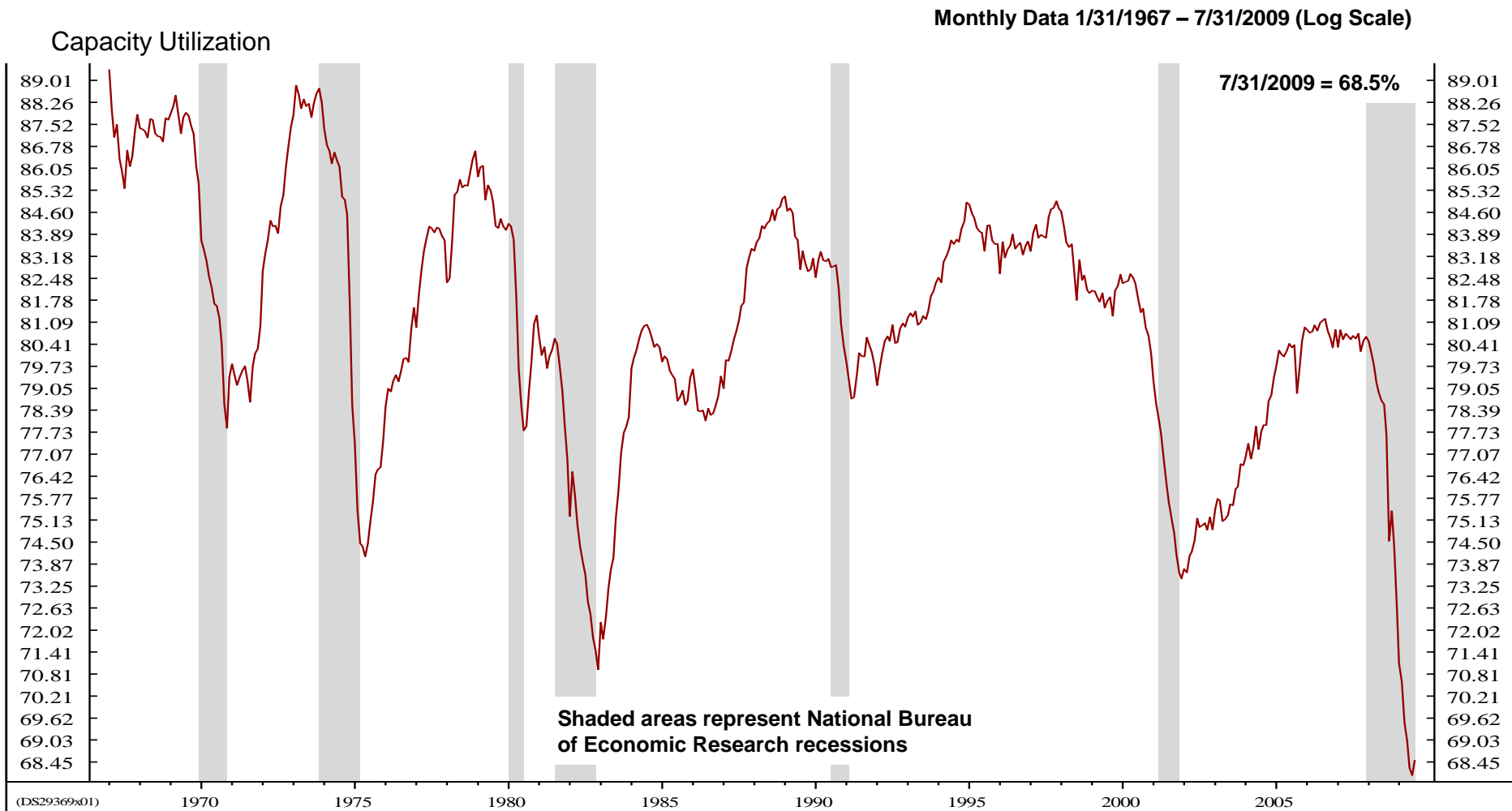
Annual Growth in the Employment Cost Index



Sources: Bureau of Labor Statistics, SEI

Reason #1

Significant slack in the economy



Source: Ned Davis Research

Reason #2

Excess liquidity is not being used to increase economic activity

M2 & M1 Money Supply Velocities --

are important to track because an increase in money supply should make more money available for economic activity, such as lending and borrowing.

Quarterly Data 3/31/1959 – 6/30/2009

M2 Velocity (GDP/M2)

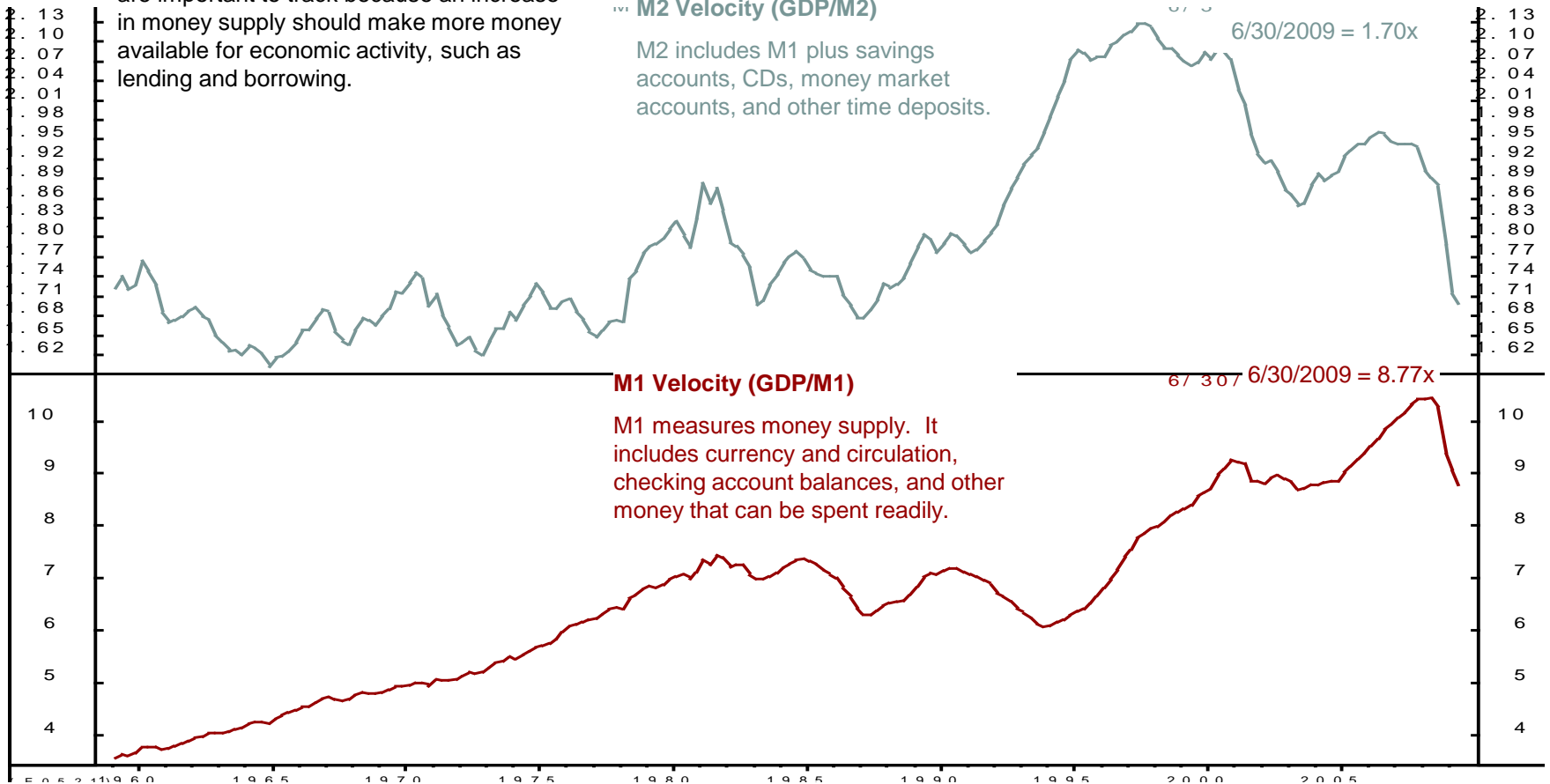
M2 includes M1 plus savings accounts, CDs, money market accounts, and other time deposits.

6/30/2009 = 1.70x

M1 Velocity (GDP/M1)

M1 measures money supply. It includes currency and circulation, checking account balances, and other money that can be spent readily.

6/30/2009 = 8.77x



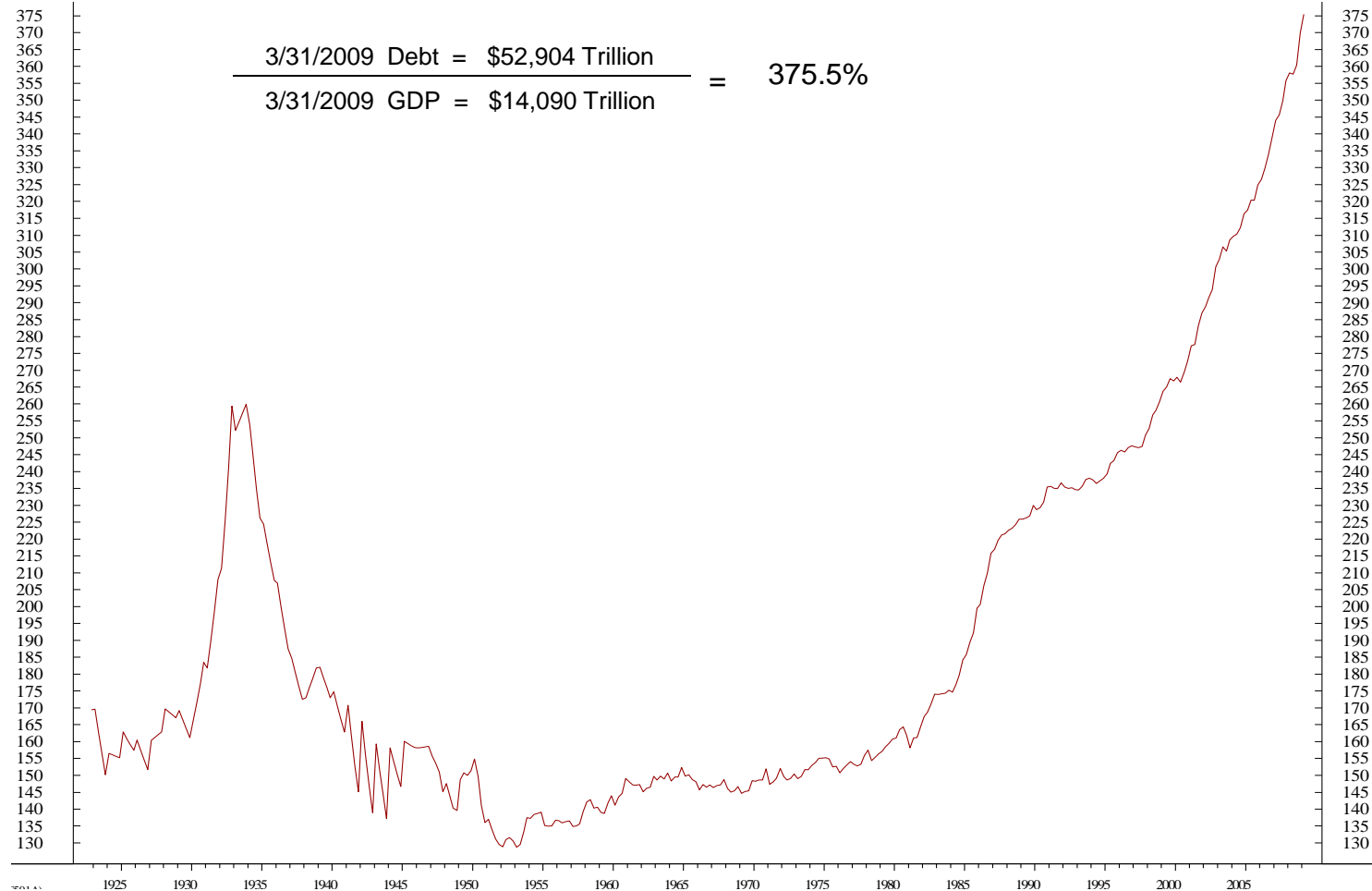
Source: Ned Davis Research

Reason #2

Excess liquidity is not being used to increase economic activity

Total Credit Market Debt as a % of GDP

Quarterly Data 12/31/1922 – 3/31/2009

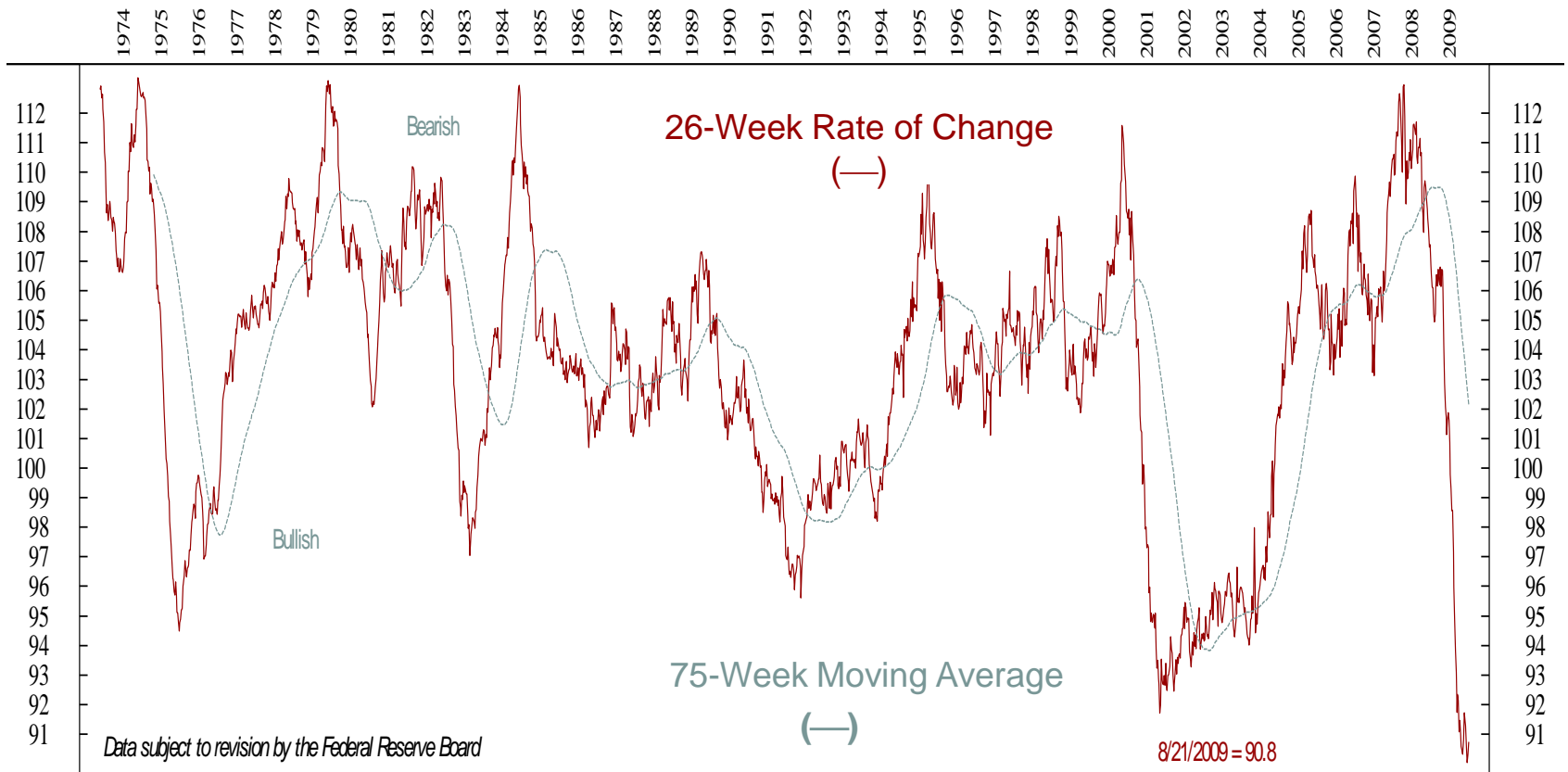


Source: Ned Davis Research

Annual interpolated GDP (including estimates prior to 1929) used prior to 1946. Domestic Nonfinancial Debt used prior to 1946. Domestic Nonfinancial Debt represented 99.4% of Total Credit Market Debt.

Reason #2

Excess liquidity is not being used to increase economic activity



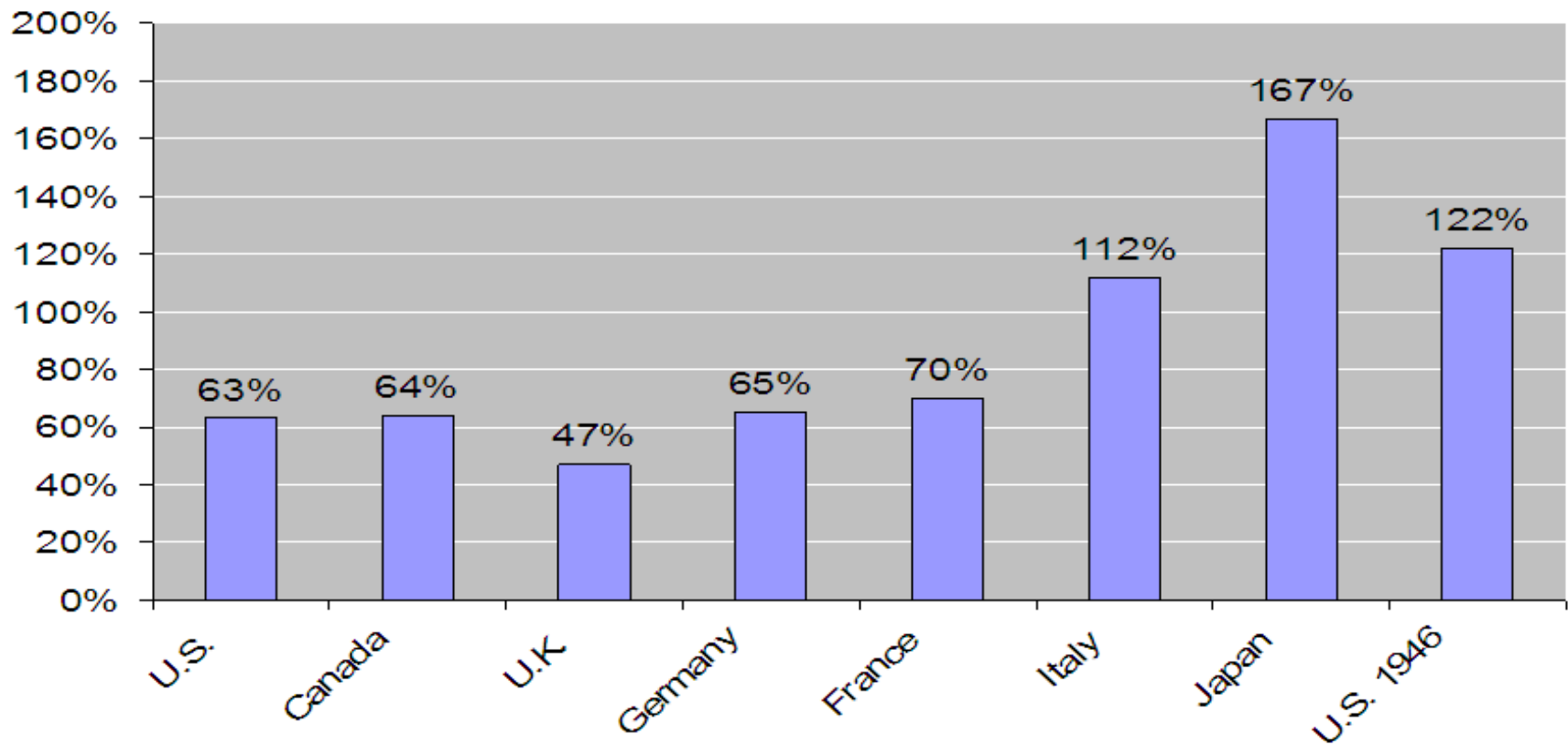
8965) Commercial & Industrial Loans + Non-Financial Commercial Paper

Source: Federal Reserve, Ned Davis Research

Reason #3

Temporary fiscal stimulus should not be inflationary

Gross Financial Liabilities as a % of GDP in 2007



Sources: OECD, SEI

Summary and outlook

- Inflation should not be a near term threat (next 1-2 years)
- High unemployment and record low capacity utilization dampen price pressures in the economy
- Massive fiscal and monetary stimulus is normally inflationary
 - Stimulus is offsetting the deflationary effects of deleveraging as the credit bubble bursts
- Stimulus will have to be withdrawn in a timely manner
 - Too soon and we risk the economy rolling over into recession
 - Too late and inflation becomes a reality

Disclosure

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