

US Macroeconomics

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Troy Ludtka, Senior US Economist | 212.224.5483 | troy.ludtka@smbcnikko-si.com

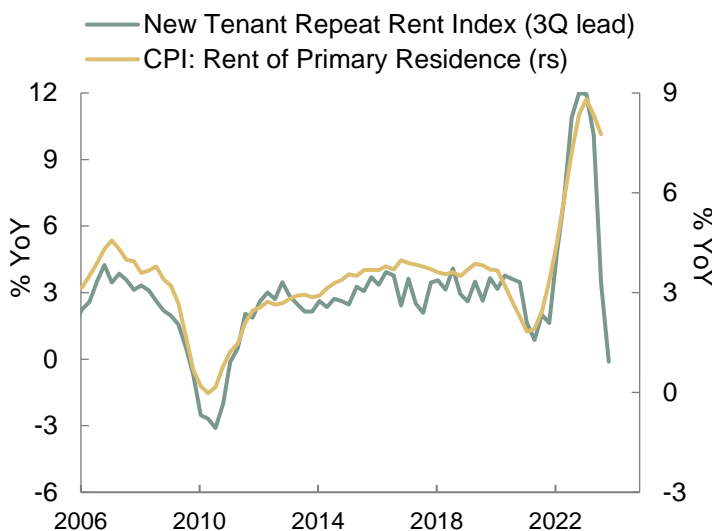
Some Bumps on the Road to 2%

The Fed’s ‘supercore’ measure in the consumer price index (CPI) has accelerated in back-to-back months, while energy prices have risen considerably, best demonstrated by the 31% up-move in WTI since June 27th. These factors are likely to draw the ire of Fed policymakers and encourage near term hawkish posturing. Yet, **we are committed to our view that inflation will decelerate to the Fed’s 2% target. In fact, we are forecasting sub 2% inflation by year end 2024.** Evolving shelter cost dynamics are foundational to this view.

The Federal Reserve Bank of Cleveland’s new tenant repeat rent index shows rental prices actually *declining* 0.1% on a year-over-year basis. This is the lowest rate of change since Q2 2010. This series leads the BLS-measured rents index by approximately nine months and shows more rental disinflation is still in the pipeline (shown below). Further, Case-Shiller home prices, with a 16-month lead, suggest a similar story with shelter costs more broadly. **The trends from home prices and the Cleveland Fed’s new tenant repeat rent index econometrically imply that shelter costs will fall below 3% between now and the fall of 2024 (compare this with August’s 7.8% YoY print).** Considering that shelter holds a 34% weight in the CPI, this is the dominant inflation dynamic.

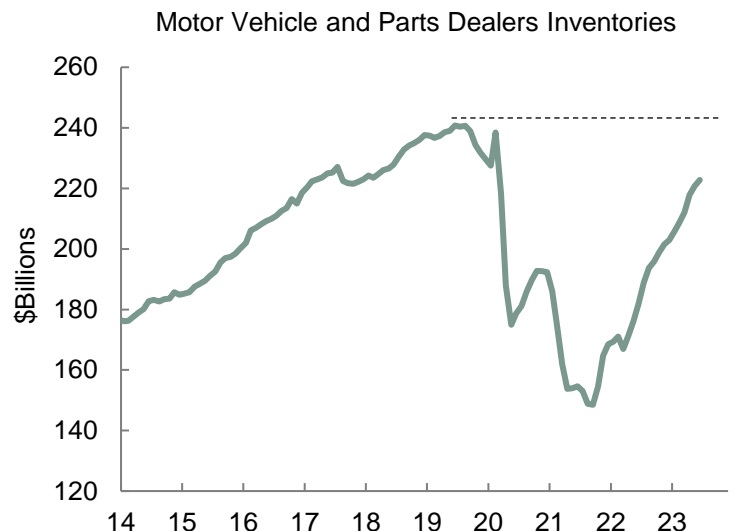
There are near-term bumps in the road, however. **Rising energy costs will ultimately boost both headline and core inflation temporarily.** Additionally, a possible auto workers strike is a stagflationary event at a time when inventories still have not yet fully recovered (below). A dramatic reduction in car production supports prices at a time when auto prices, auto insurance premiums and energy hold a combined 16.9% CPI weight. In sum, look for more disinflation over the next year, but not before hotter near-term pressures and more hawkish Fed rhetoric.

Longer-Term Dynamic



Sources: Cleveland FRB, BLS, Census, Haver, SMBC Nikko

Near-Term Dynamic



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