

US: Fed inflation fears keeps the pressure on for rate hikes

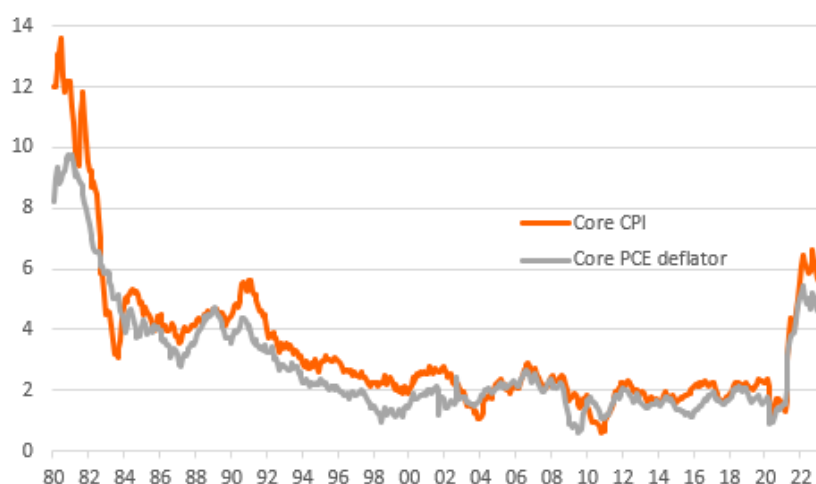
The Fed's favoured measure of inflation accelerated in January with markets now fully pricing 25bp moves in March, May and June. We agree that this is the most likely path ahead, but it will be painful for the household sector, coming at a time when real incomes are squeezed by inflation, borrowing costs continue to rise and lending conditions are tightening



Inflation shows little sign of slowing

The acceleration in the Federal Reserve's favoured measure of inflation, the core personal consumer expenditure deflator, is a big story. It rose 0.6% month-on-month versus expectations of a 0.4% print and is also above the 0.4% increase reported by the core CPI report. There were upside revisions too, which means the year-on-year rate has ticked up to 4.7% from 4.6%, above the 4.3% rate expected. This will ensure the Federal Reserve mantra of ongoing hikes continues with 25bp moves in March, May and June fully priced by markets. Talk of a potential 50bp move at the March Federal Open Market Committee meeting can't be completely discounted, although we don't think they will carry through with it.

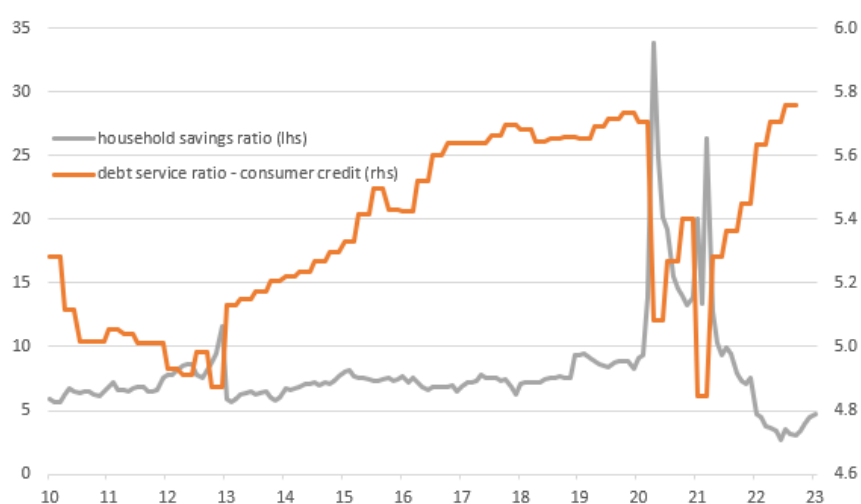
US inflation measures (ex food and energy (YoY%))



Source: Macrobond, ING

Meanwhile, personal incomes didn't rise quite as much as expected, up 0.6% month-on-month. The consensus was for a 1% gain because of the annual uprating of social security benefits by 9%, but there was a 2.7% MoM drop in farm income while "other benefits" fell 15.5%. Real personal spending rose 1.1% MoM as expected. We will see weaker prints in February and March, but consumer spending is still likely to grow in the 3.5-4% annualised range in the first quarter of this year.

Household savings ratio and debt service ratio (% of household disposable income)



Source: Macrobond, ING

Household finances are under pressure though

The combination of decent income growth, rising spending and robust inflation means March and May rate hikes are very likely and we have to accept that a further move in June is more likely

than not. Our caution centres on the combination of squeezed real incomes, rising interest rates and tightening lending conditions all happening at the same time. Household saving ratios are now well below pre-pandemic levels while the proportion of income spent on servicing the debts on consumer loans is at the highest since 2009 (the chart above measures them as a percentage of household disposable income).

This hints at financial pressures on the household sector and this will increasingly bite as we go through the year. It will only get worse if those lay-off announcements keep coming, which could lead to the economy slowing sharply in coming quarters, opening the door for a path to lower interest rates from the fourth quarter.

Author

James Knightley

Chief International Economist, US

james.knightley@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.