

## Sticky US inflation increases pressure on the Fed

Cost push and demand pull inflation show little sign of fading as cracks form in the Fed's "transitory" narrative. Housing costs, low inventories and rising energy prices will keep inflation higher for longer and with inflation expectations accelerating the case for earlier and swifter Fed corrective policy is growing



**5.4%** Annual US headline CPI

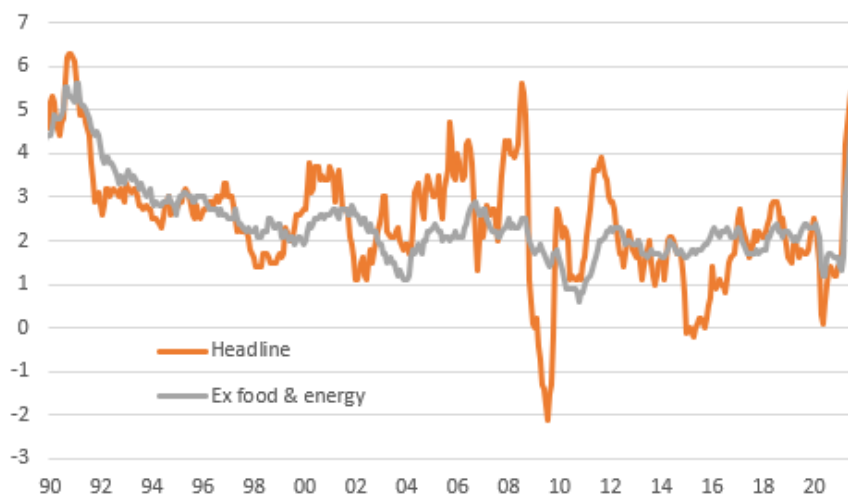
### Stubborn inflation not going away

US CPI rose a tenth more than expected to 0.4% month-on-month/5.4% year-on-year while core came in-line with the consensus prediction at 0.2%/4.0%. The larger headline figure was caused by energy prices rising 1.3% MoM and food gaining 0.9% MoM.

Gasoline prices have accelerated through the first half of October, suggesting more upside from this component next month and it will feed through into higher transportations costs too. We also have to be braced for sharply higher wholesale natural gas prices translating into higher utility bills.

Within core apparel prices fell 1.1% and used cars and trucks fell 0.7% while medical care was flat and airline fares fell sharply again. While these are positive developments we don't see them as being sustainable. Used car auction prices are on the rise again given the lack of new vehicles to buy caused by chip shortages while retail inventories are at all-time lows so the need for seasonal discounts ahead of the key shopping season is simply not there.

## Annual inflation rates



Source: Macrobond, ING

## Housing costs intensify inflation risks

Another key reason why we think inflation will stay higher for longer is housing costs. Primary rents and owners' equivalent rent account for a third of the CPI basket with movements in these components tending to lag 12-18 months below house price changes. The chart below suggests that housing components of inflation are now the story to watch year and could add nearly a full percentage point to annual inflation on their own.

Putting this altogether it means we think headline inflation stays above 5% through 1Q 2022 with core inflation above 3.5% through 2Q 2022. This hardly fits the "transitory" narrative put out by many at the Fed.

## Housing costs and house prices (YoY%)



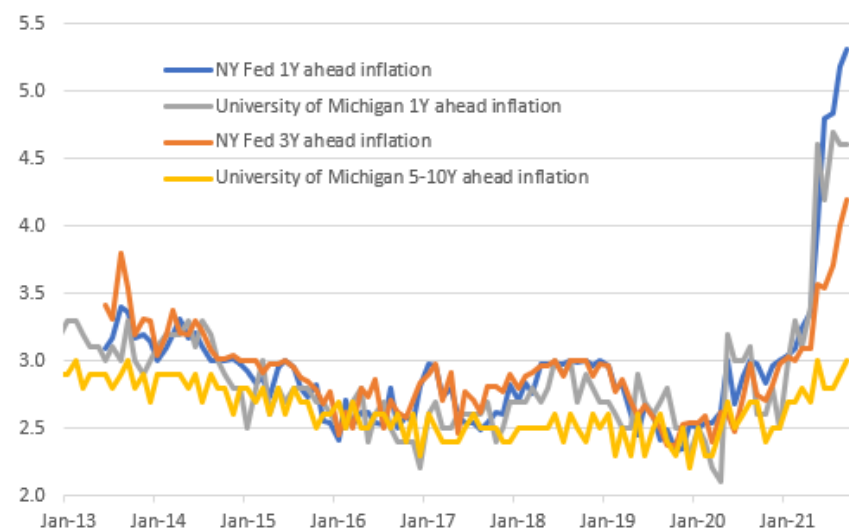
Source: Macrobond, ING

## Not so transitory now

The Federal Reserve continues to assert that "longer term inflation expectations remain well anchored at 2 percent", but there is growing discontent with this assessment – most notably from Atlanta Fed President Raphael Bostic. They can just about get away with it when talking about market inflation expectations. Using Treasury Inflation-Protected Securities, the breakeven rate 5 years out is 2.65% and 10Y it is 2.5%.

However, consumer inflation expectations are looking much less anchored. The Federal Reserve's own survey (conducted nationally by the NY Fed), shows 1Y ahead inflation consumer expectations rising to 5.3% – not really surprising as it tends to track actual inflation. However, the 3Y ahead inflation expectations rose to a new all-time high of 4.2%. We wouldn't be surprised to see the University of Michigan 5-10Y ahead expectations break-up toward 3.5% in the next few months.

## Inflation expectations are surging



Source: Macrobond, ING

We are already predicting earlier and swifter policy action from the Fed than the market – QE taper to end in 2Q 2022 with rate hikes in September and December next year. An acceleration in these inflation expectations would bring that time-line even further forward.

## Author

### James Knightley

Chief International Economist, US

[james.knightley@ing.com](mailto: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 <http://www.ing.com>.