

US inflation no barrier to Fed rate hikes

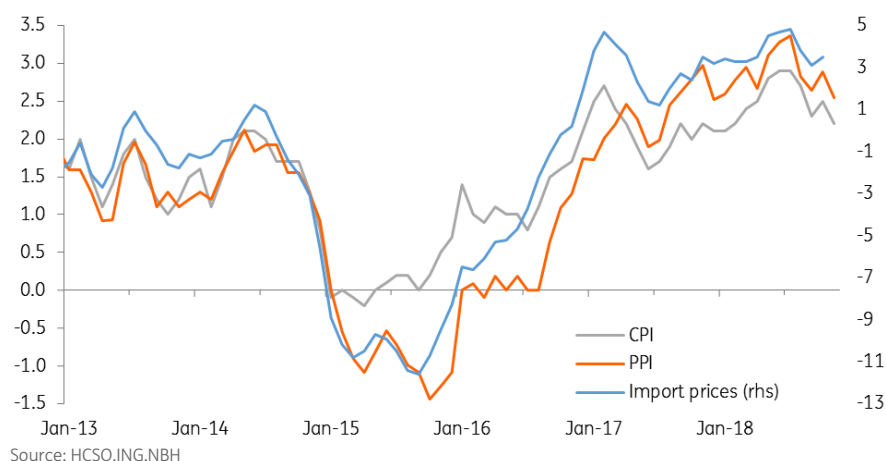
Headline inflation in the US has slowed to 2.2% YoY, but this reflects a \$25/bbl plunge in oil prices since October. Strip this out and “core” inflation is up and will continue grinding higher as spare capacity in the economy shrinks.



Latest inflation figures

US inflation was flat on the month (as expected) meaning that the annual inflation rate slowed to 2.2% in November, down from 2.5% in October. The main drag was energy because of the \$25/bbl drop in the price of oil seen over the past two months with gasoline prices falling from a national average of \$2.92/gallon at the beginning of October to \$2.41 currently. There was also weakness in apparel, transport fares and personal computers.

US headline inflation measures



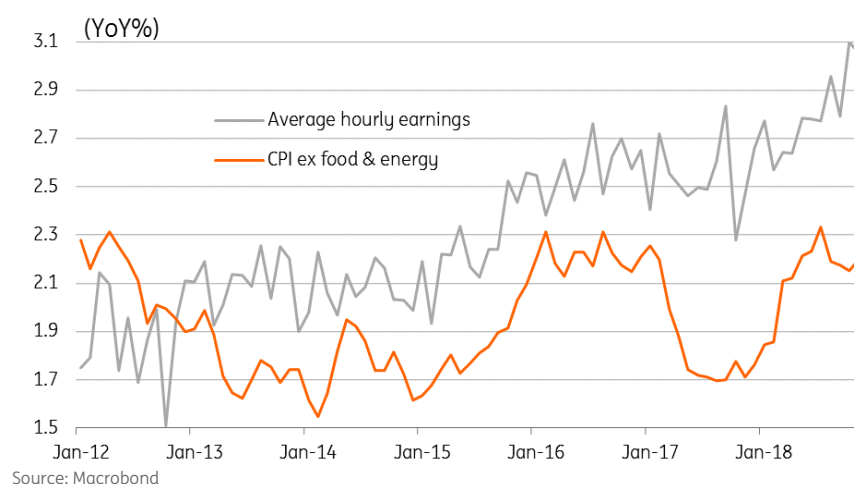
Core inflation should grind higher

So-called “core” inflation, which strips out the volatile food and energy components rose 0.2% MoM, which leaves the annual rate of this inflation measure at 2.2% - as expected. Once again, housing made a strong contribution, rising 0.3%MoM with medical care and recreation both rising 0.4%MoM.

We suspect that this core measure will continue grinding higher through the first half of 2019. The US is largely a service sector economy and the biggest cost input is labour. Average earnings are rising with the Federal Reserve also noting a pick-up in non-wage benefit costs such as paid vacation days, signing bonuses and healthcare packages so in an environment of decent growth there is a good chance firms will look to pass these costs onto consumers. At the same time, producer price inflation is moving higher, suggesting pipeline pressures are building more broadly in an economy which has rapidly been eating into its spare capacity.

With core inflation set to break above 2.5% YoY next year and the economy likely to experience solid, if somewhat slower growth than in 2018, the arguments for interest rate increases from the Federal Reserve will remain strong. President Trump will not like it, but we fully expect a 25bp rate hike at the 19 December FOMC meeting. We are currently forecasting three further 25bp rate hikes next year, but this is subject to downside risks given escalating trade fears.

Wages & core inflation



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.