

US inflation not as bad as feared, but still too hot

Quarterly inflation data surprised to the upside and led the market to brace for a very unpleasant MoM print today. Thankfully it was due to upward revisions, primarily to January, with the March figure coming in line with initial expectations. Nonetheless, inflation remains too hot and September remains the earliest opportunity for an interest rate cut



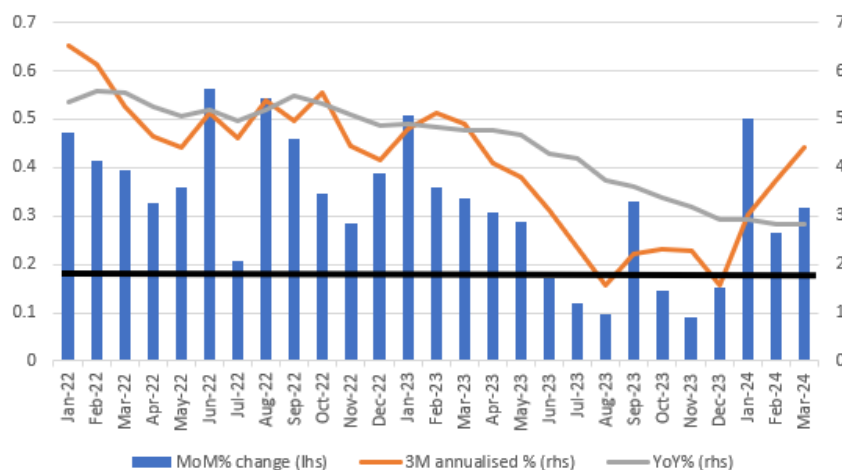
US inflation remains hot, but not as hot as feared

So the core PCE deflator has indeed come in at 0.3% month-on-month, with upward revisions to January and February, rather than the 0.48% MoM implied by the quarterly PCE deflator from yesterday, assuming no revisions. In the great scheme of things, inflation was still far too hot in the first quarter, but the monthly profile doesn't look as concerning as it could have done so we are seeing a little bit of a relief rally in Treasuries.

January has been revised from 0.45 to 0.50 and February is now 0.27 rather than 0.26 with March at 0.32. This remains well above the 0.17% MoM we need to average over time to bring the annual rate of inflation back to 2% - basically we need to see the blue bars in the chart below come in

below the black line, not above them.

Core personal consumer expenditure deflator - MoM%, 3M annualised% & YoY%



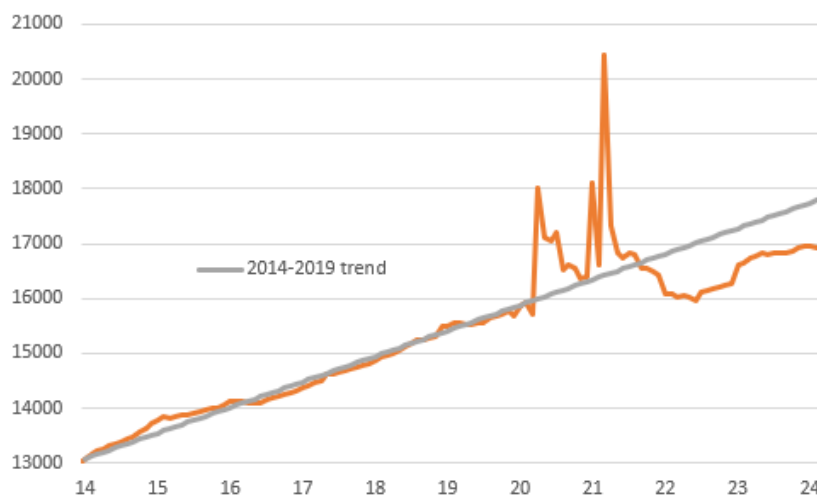
Source: Macrobond, ING

We are of the view that we will see the core PCE deflator average somewhere between 0.2 and 0.3% MoM through 2Q, but there are some economists out there effectively arguing for 0.1-0.2% MoM as an average through the second quarter. Their argument is that inflation is largely down to housing, insurance and medical services - the latter two due to annual price hikes that have a tendency to bump up the numbers in 1Q - so-called residual seasonality - and this will fade in 2Q, which was what we saw happen in 2023. We are a little more wary about making such a call just yet, but we believe that housing should increasingly reflect what is happening in private rents and that will contribute to more modest monthly inflation prints.

Spending fuelled by savings and borrowing, not income

Elsewhere in the report, we see that spending held up well (0.8% MoM versus the 0.6% MoM consensus) so this provides a solid base for 2Q annualised consumer spending growth. However, the savings rate continues to fall - it was at 4.1% in January and is now 3.2%. The average over the past 20 years is 5.9%. Real household disposable income is still effectively flatlining so growth is being driven by lower savings and more borrowing.

Real household disposable income levels \$mn



Source: Macrobond, ING

Remember that the top 20% of US households by income spend the same amount of money as the bottom 60% of households by income. The top 20% are doing very well with good, high-paying jobs, tending to own their own home (largely with low long-term mortgage rates) and can make 4% in money market funds while feeling the benefits of higher stock and home prices. The bottom 60% are feeling more stress with far less wealth exposure. They are more likely to rent and are more likely to have exhausted pandemic-era-accrued savings. The key question for the spending and growth in general is how long that top 20% can keep offsetting intensifying stresses faced by the bottom 60%. We see the story moving in the direction of weaker spending as we head through the rest of the year.

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.