

Easing pipeline price pressures boost hopes for lower US inflation

Last week's lower-than-expected core CPI reading raised hopes that the Federal Reserve's tightening cycle was entering the end phase. Today's PPI report has offered further succour to the notion that the Fed will actually be in a position to cut rates if, as we fear, the US enters recession in 2023



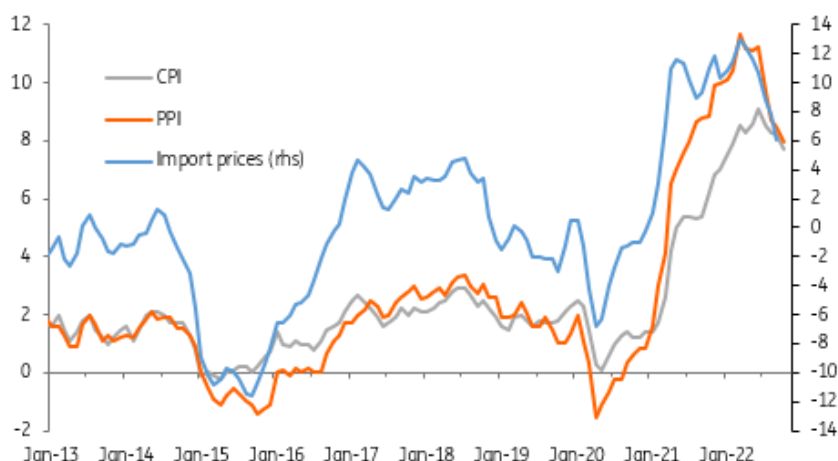
The headline producer price index rose 0.2% month-on-month in October, which was lower than expected

PPI surprises on the downside

With core CPI rising only 0.3% month-on-month last week, rather than the 0.5% expected and the 0.6% MoM prints seen in previous months, the market saw evidence that inflation pressures may finally be abating after the most aggressive Fed tightening cycle since the early 1980s. While it is certainly very helpful to our view that inflation can get back to the Federal Reserve's 2% inflation target next year, we warned that nothing can be taken for granted and that the 0.3% figure was still nearly double the 0.17% MoM figure we need to average over time to be confident that the 2% year-on-year inflation target will be hit.

Today's PPI report has given us confidence that inflation can fall more quickly than the market had been expecting. In turn, this will give the Federal Reserve the flexibility to respond with stimulus should a 2023 recession materialise, as we fear.

Annual inflation rates are slowing



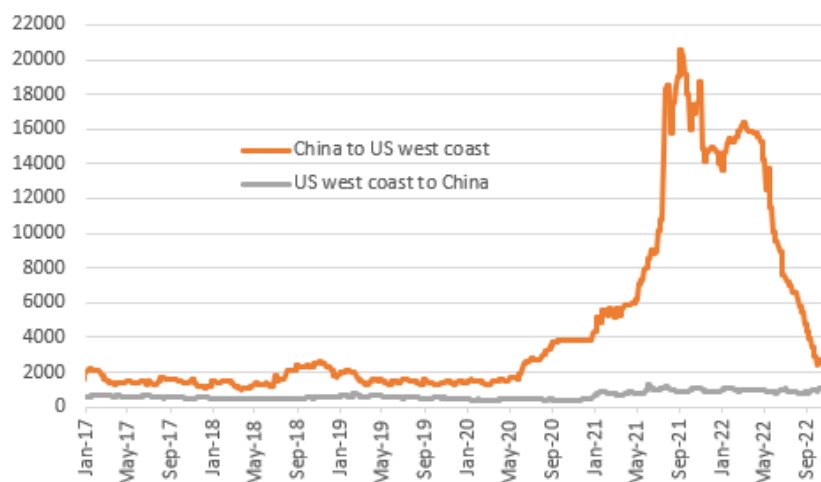
Source: Macrobond, ING

The headline rate rose 0.2% MoM, lower than the 0.4% expected, while September's MoM rate was revised down to 0.2% from 0.4%. The details show that food +0.5% MoM and energy +2.7% MoM continue to run hot, but goods ex food and energy fell 0.1% MoM and services fell 0.1%. Consequently, the more important core figure (ex food and energy) was unchanged on the month versus the 0.3% MoM expected, leading the YoY core PPI rate to slow to 6.7% from 7.1%.

Lower input costs reduce the pressure for consumer price rises

Falling commodity prices and the effects of earlier energy price falls have been very helpful and together with the strong dollar and falling freight costs has meant imported prices are receding quite rapidly now. Indeed, freight costs from China to the US are now pretty much back to pre-Covid levels, suggesting supply chain frictions caused by logistic issues have abated to a large extent. This is all very helpful to reduce corporate input costs, which in turn reduces the pressure for companies to raise prices for consumers. Moreover, in a weakening economic environment it could allow companies greater flexibility on the pricing to respond to weaker demand without such an aggressive squeeze on profit margins.

Freight costs for a 40-foot container



Source: Macrobond, ING

Federal Reserve has greater scope for flexibility

Nonetheless, it is far too early for the Fed to signal the all-clear with Federal Reserve officials continuing to signal that while this is encouraging it is only one month. They will need to see consistent readings for core CPI coming in around 0.1% or 0.2% and we are still some way off from that, while we have to remember that the jobs market remains hot and wages continue to rise at a rapid clip. Consequently, we continue to have a 50bp rate hike in for the December Federal Open Market Committee meeting and look for a further 50bp hike in the first quarter of 2023, but that should mark the top. Recessionary forces are intensifying and lower inflation will give the Fed the scope to reverse course with rate cuts in the second half of 2023.

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 <http://www.ing.com>.