US: Inflation could be a roller coaster ride

US inflation is benign and is likely to remain so over the next couple of months as increased Covid-19 containment measures weigh on activity. Longer term though, capacity constraints coupled with stronger demand could see price pressures mount in key areas

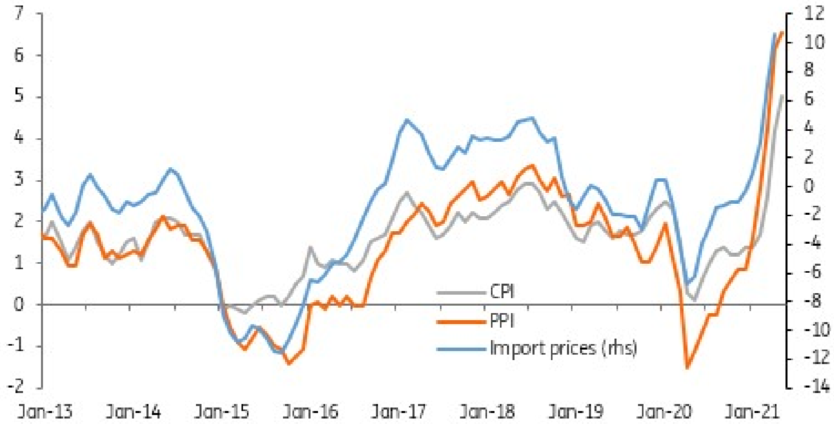
Price pressures kept at bay

US consumer price inflation came in a tenth of a percentage point below expectations for headline and two-tenths below for core (excluding food and energy). Headline CPI and core inflation were unchanged on the month, which leaves the YoY rates down at 1.2% and 1.6% respectably. Both are well short of the Federal Reserve's 2% target – remember too that the Fed is stating it won't consider rates until inflation is "on track to moderately exceed 2 percent for some time".

Currently the Fed's own dot plot chart indicates just four of 17 FOMC members thinks interest rates will need to be increased before the end of 2023 and this is unlikely to change when the new forecasts are published on December 16th.

We believe that near-term price pressures are likely to remain subdued. The rising number of Covid-19 cases across the US means that containment measures are likely to be seen in more and more states over coming weeks. Some could even decide to implement European style lockdowns with bars restaurants and some retail being forced to close. Travel restrictions may also be re-imposed, which aside from having a positive impact on grocery pricing power, is going to be bad news for most other sectors.

US inflation measures



Source: Macrobond, ING

But inflation could rebound strongly in 2021

Looking to next year though we suspect inflation could surprise on the upside, especially in 2H21. The pandemic has led airlines to cut capacity, car hire firms to retrench & hotel capacity to be cut. When looked at together with the fact many bars and restaurants and other entertainment venues have gone out of business the supply side potential of the US economy has been cut back.

In 2021 we expect demand for most of these industries to surge back as a Covid vaccine unleashed pent up demand, with fiscal stimulus and the re-emergence of foreign tourists further boosting activity. The strength of the housing market is also likely to feed through into some of the shelter components so we could see inflation pick up markedly. In our view this could help to bring Federal Reserve interest rate hike expectations earlier than 2024 and lead to a more pronounced steepening of the yield curve.

Job strains persist despite jobless claims fall

Separately, initial jobless claims fell a little more than expected to 709k last week versus 731k consensus. The total number of people claiming unemployment benefits in all programs stands at 21.157mn. The equivalent number for the same point in 2019 was just 1.449mn. Unfortunately, if we see major containment measures kick in again soon after Thanksgiving those jobless claims numbers will climb once more.

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