

# US Macroeconomics

October 13, 2023

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## Inflation Continues to Follow Historical Script

The September Consumer Price Report showed slightly higher inflation than what investors had been expecting. This caused some handwringing on the possibility that inflation may be stickier from here on out. Despite September results, the downward trend in inflation remains intact. And history suggests further improvement is likely.

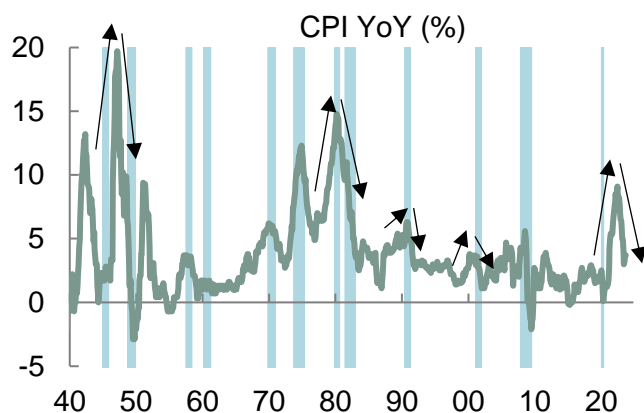
The inflation rate peaked at 9.1% in June 2022. Its growth rate has been slowing ever since. This is normal because as we can see in the left-hand side chart below, **steep runups in inflation are always followed by steep slowdowns in inflation**. Put another way, the increase in the inflation rate is mirrored by the decrease in the inflation. Observe the 1942, 1947, 1951, 1975, 1980, 1990 and 2008 price spikes.

In each of these instances, the inflation rate soared. But when it ultimately made a top, it soon reversed. We continue to see that development happening again in this business cycle. For example, in the right-hand side table below, we measure the slope of previous inflation upswings and downswings. The fact that the slopes in both directions are generally the same reflects this inflation symmetry: 0.44 on the upswing and -0.44 on the downswing. Why will this time be different? It should not be.

The Fed has raised rates aggressively, lifting the overnight cost of money by 525 basis points in just 18 months. This is central to the inflation outlook because **the funds rate is clearly in restrictive territory**, evident by multi-decade highs in private sector interest rates and the fact the funds rate is above the year-over-year growth of gross domestic income. Furthermore, the Fed continues to pledge “higher for longer” which has caused the futures market to remove much of easing it has been expecting next year.

For now, the inflation rate should continue to trend lower, consistent with the historical script. Only if the Fed was to begin aggressively cutting interest rates in response to sudden and unexpected economic weakness should inflation-wary investors become concerned. The economy and the financial markets are not yet at that point.

**Inflation Trending Sharply Lower Just as History Suggests**



Sources: BLS, Haver, SMBC Nikko

| Inflation Upswing        | Slope       | Inflation Downwing       | Slope        |
|--------------------------|-------------|--------------------------|--------------|
| Sep 1940 to May 1942     | 0.35        | May 1942 to May 1944     | -0.47        |
| Feb 1946 - Mar 1947      | 1.61        | Mar 1947 to Apr 1949     | -0.66        |
| Jul 1949 - Feb 1951      | 0.58        | Feb 1951 to Oct 1954     | -0.21        |
| May 1967 - Dec 1969      | 0.12        | Dec 1969 - Jun 1972      | -0.12        |
| Jun 1972 to Dec 1974     | 0.37        | Dec 1974 to Nov 1976     | -0.31        |
| Nov 1976 to Mar 1980     | 0.22        | Mar 1980 to Jun 1983     | -0.31        |
| Jun 1986 to Sep 1990     | 0.07        | Sep 1990 to Jan 1992     | -0.25        |
| Aug 2007 to Jul 2008     | 0.22        | July 2008 to Dec 2008    | -1.19        |
| Mar 2021 to Jun 2022     | 0.37        | Jun 2022 to Sep 2023     | -0.42        |
| <b>Average 1940-2008</b> | <b>0.44</b> | <b>Average 1940-2008</b> | <b>-0.44</b> |

Sources: BLS, Haver, SMBC Nikko

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