

# Our Inflation North Stars: An Outlook

---

**Troy Ludtka**

Senior US Economist  
SMBC Nikko Securities

(212)-224-5483

Troy.Ludtka@smbcnikko-si.com

November 2024

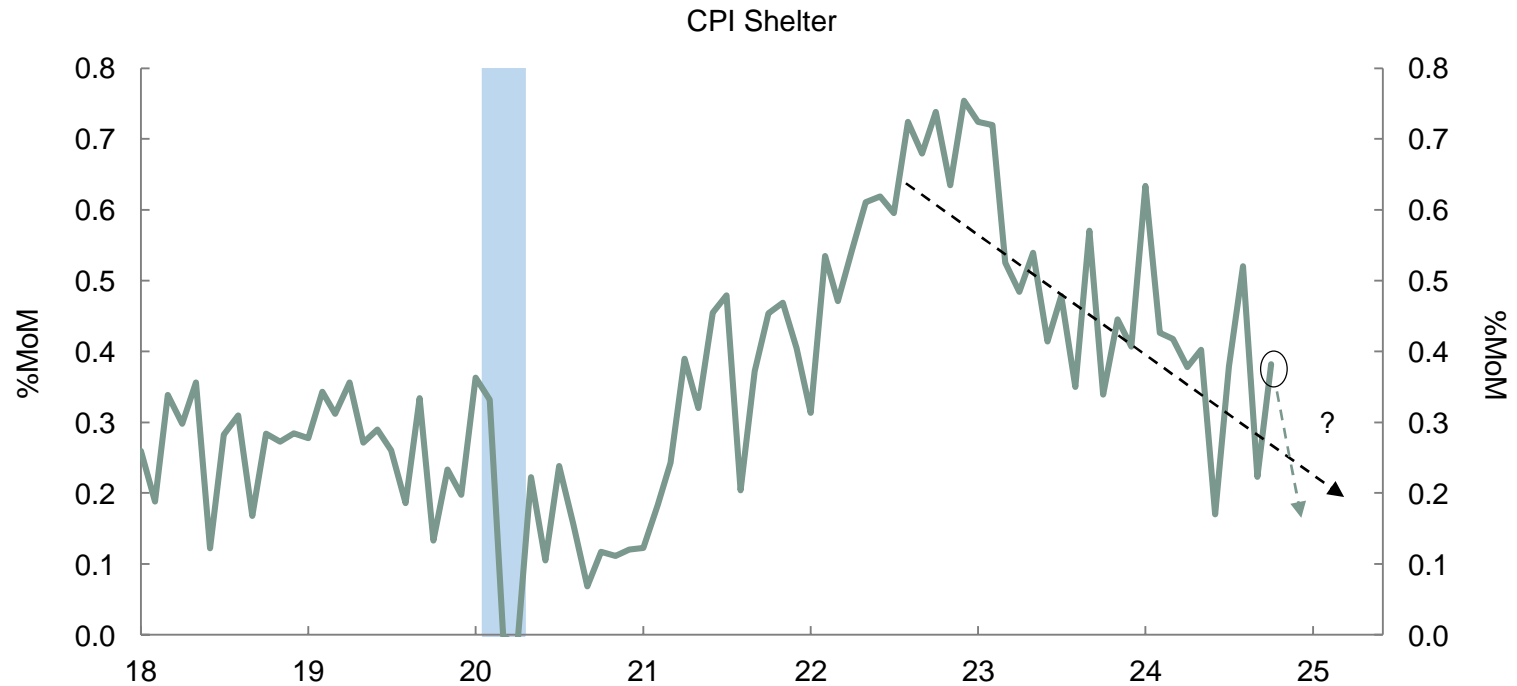
# Summary

---

- Shelter accounts for ~36% of the total CPI index. We forecast shelter will fall to 3.5% YoY by mid-2025 (from 4.8% at present). Shelter is broken up between rent (RPR), weighted at 7.7%, and owners' equivalent rent of residence (OERR) weighted at 27.7%. These components are critical for headline CPI. We remain highly encouraged by the disinflationary forces in housing (discussed in this slide deck).
- Food prices account for 13.5% of the total CPI. Mechanically, food prices will follow land and fertilizer prices lower. The “food” category is comprised of food away from home and food at home, whereas the latter leads the former. Fertilizer and farmland prices statistically imply food prices should slow to 1.7% by Q1 2025 before stabilizing at 2.1% in mid-2025.
- Energy prices account for 6.6% of the CPI. Technological advancements, from “fracking” (and others), in the exploration and production sector has made the US energy dominant on the global stage. The energy complex is well supplied because of US energy production, and oil prices (adjusted for inflation) are low. Then demand appears to be contained. US energy demand off its cyclical high. The path forward for oil is dictated marginally by China and India, with the former seeing cyclical strain.
- With manufacturing supply chain issues now cleared, China is exporting goods deflation.
- We forecast CPI and core CPI at 2.2% and 2.3% by yearend 2025. Core inflation's continued down-move toward the Fed's target will allow official interest rates to fall much further.

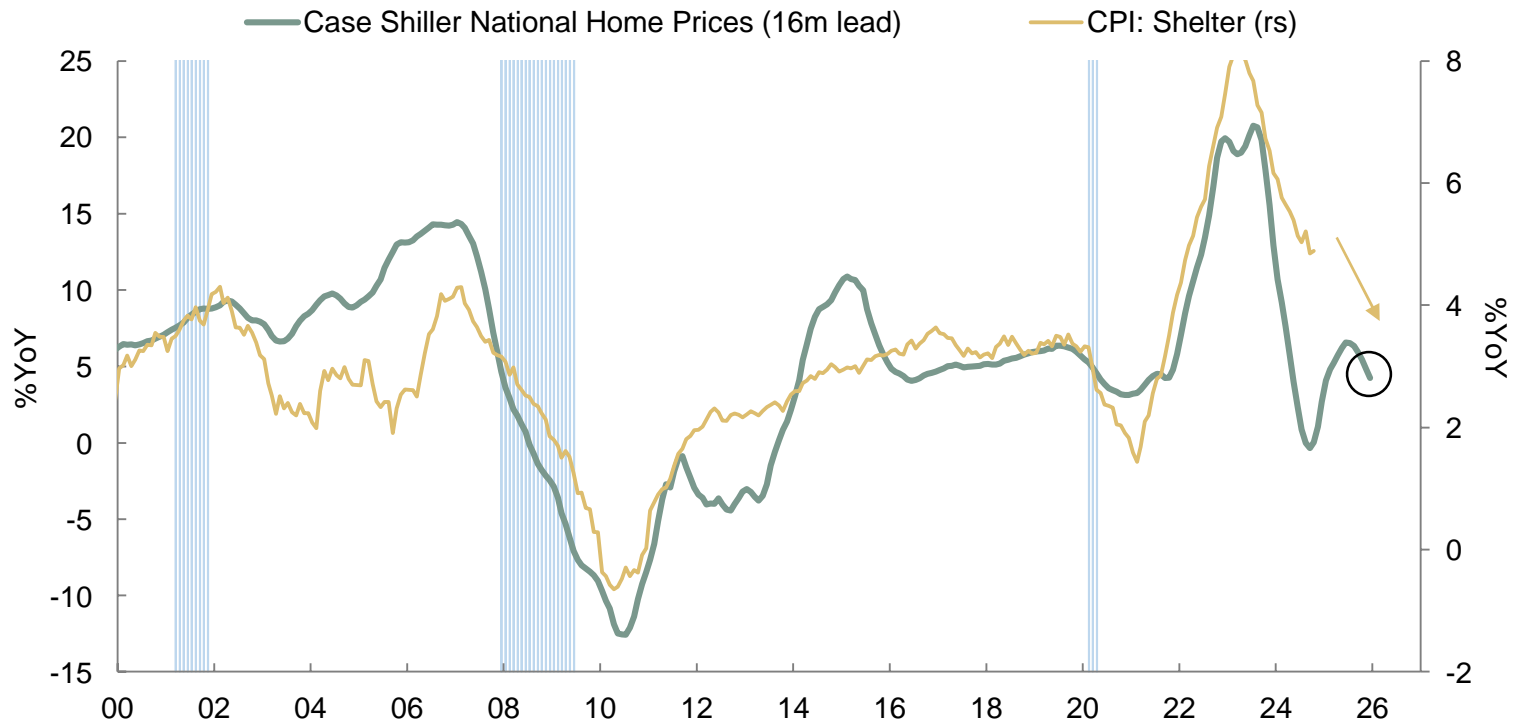
# A Friendly Trend

The monthly variation is noise, it is the trend that is important.



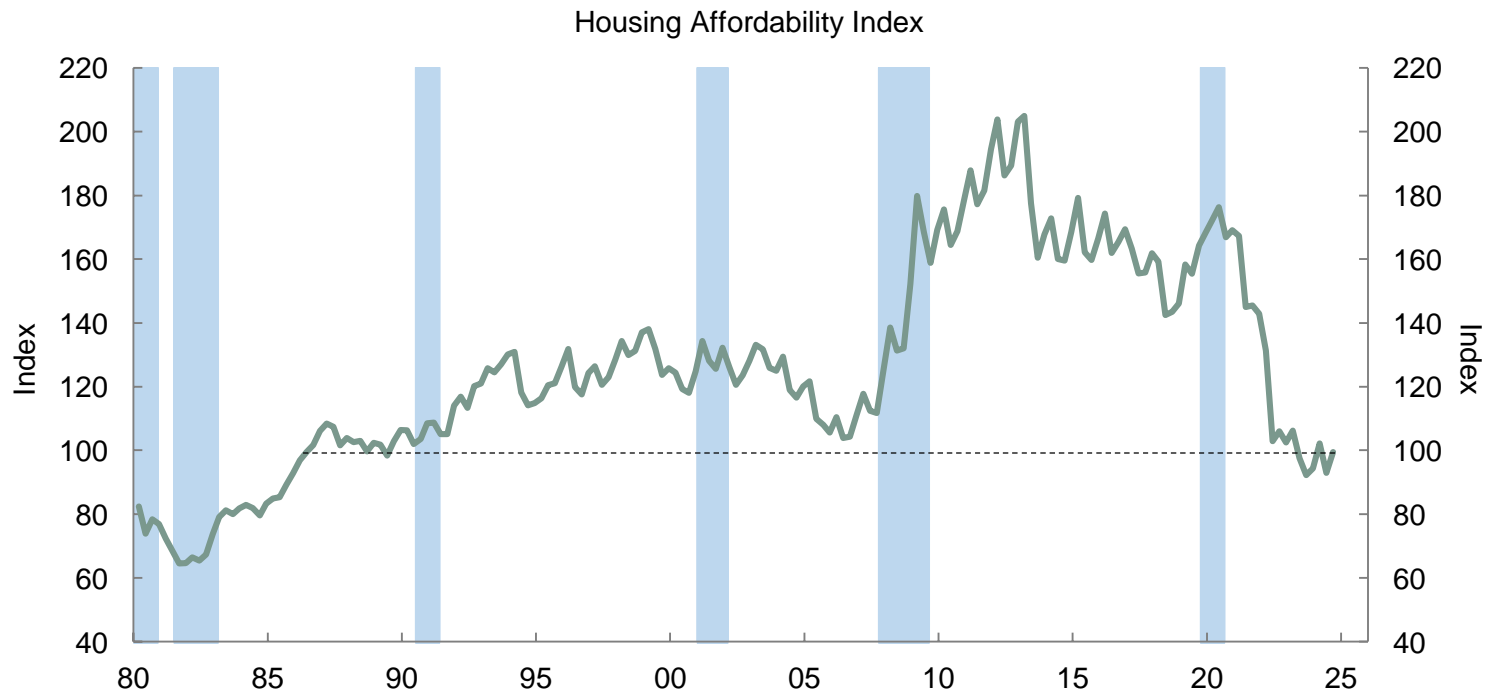
# Home Prices Leading Shelter Lower

Shelter costs as measured by the BLS tend to follow home prices with a 16-month lag.



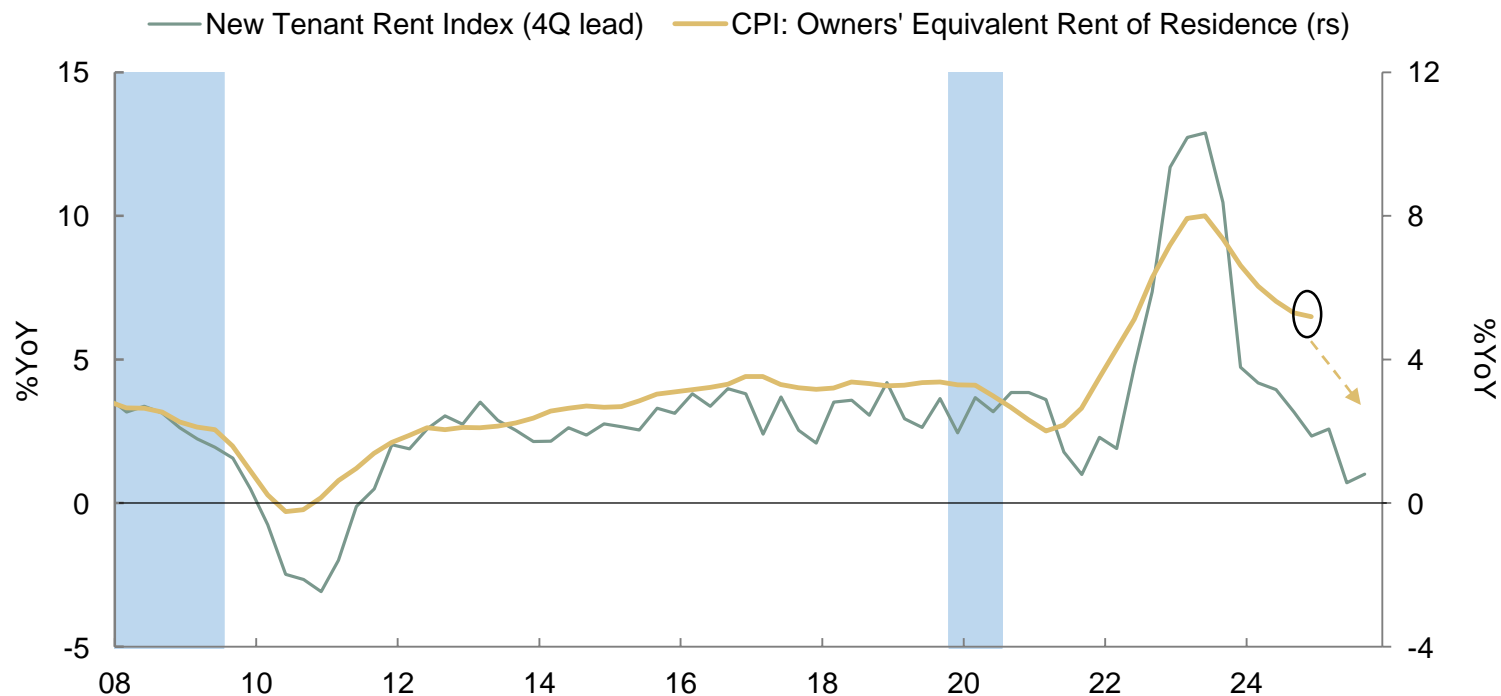
## Home Prices Leading Shelter Lower (2/2)

Home price growth is likely to be restrained because housing affordability — which measures the cost of a median home purchase for a typical household given mortgage rates — is at the lowest since 1989 and appears unlikely to meaningfully change soon.



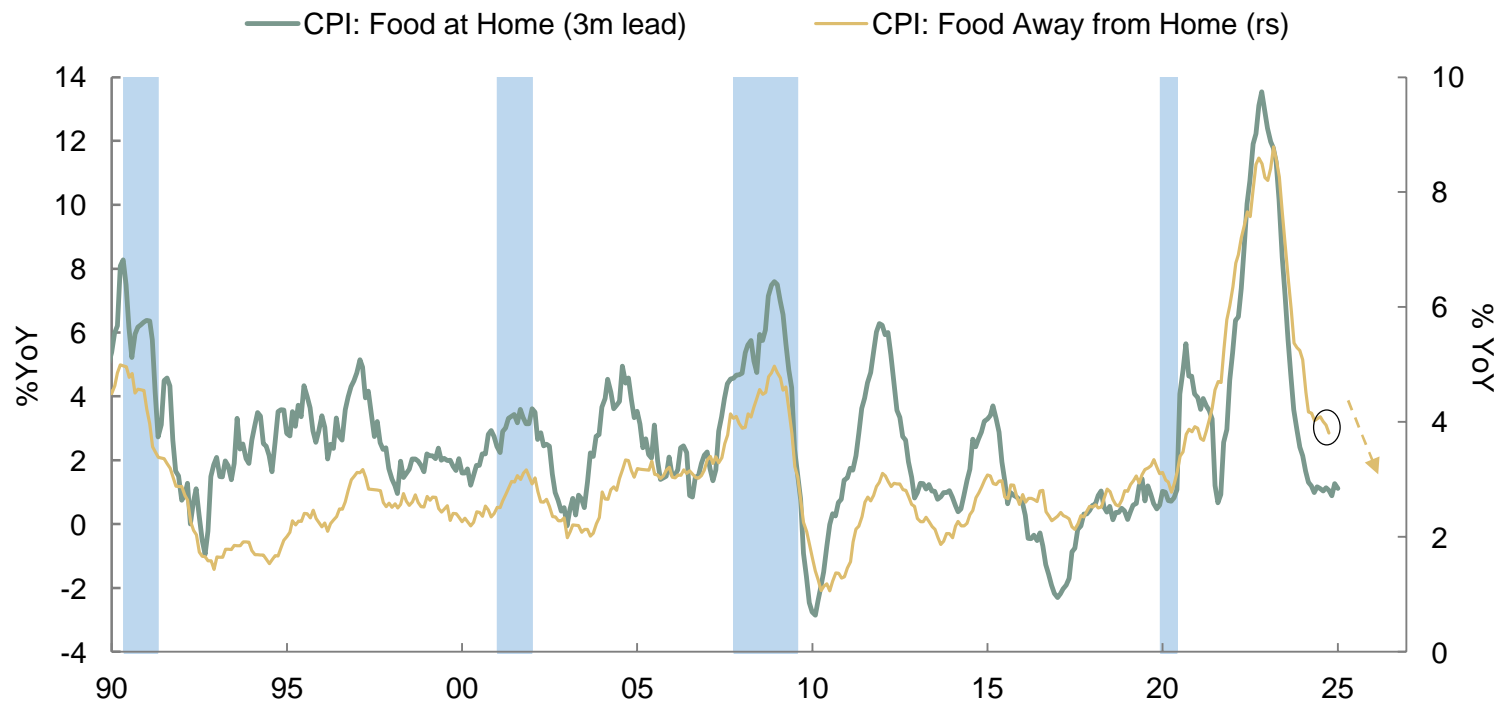
# Rental Reprieve Coming

The prices on newly signed rental agreements lead CPI data by one year and point to even *lower* inflation than pre-pandemic.



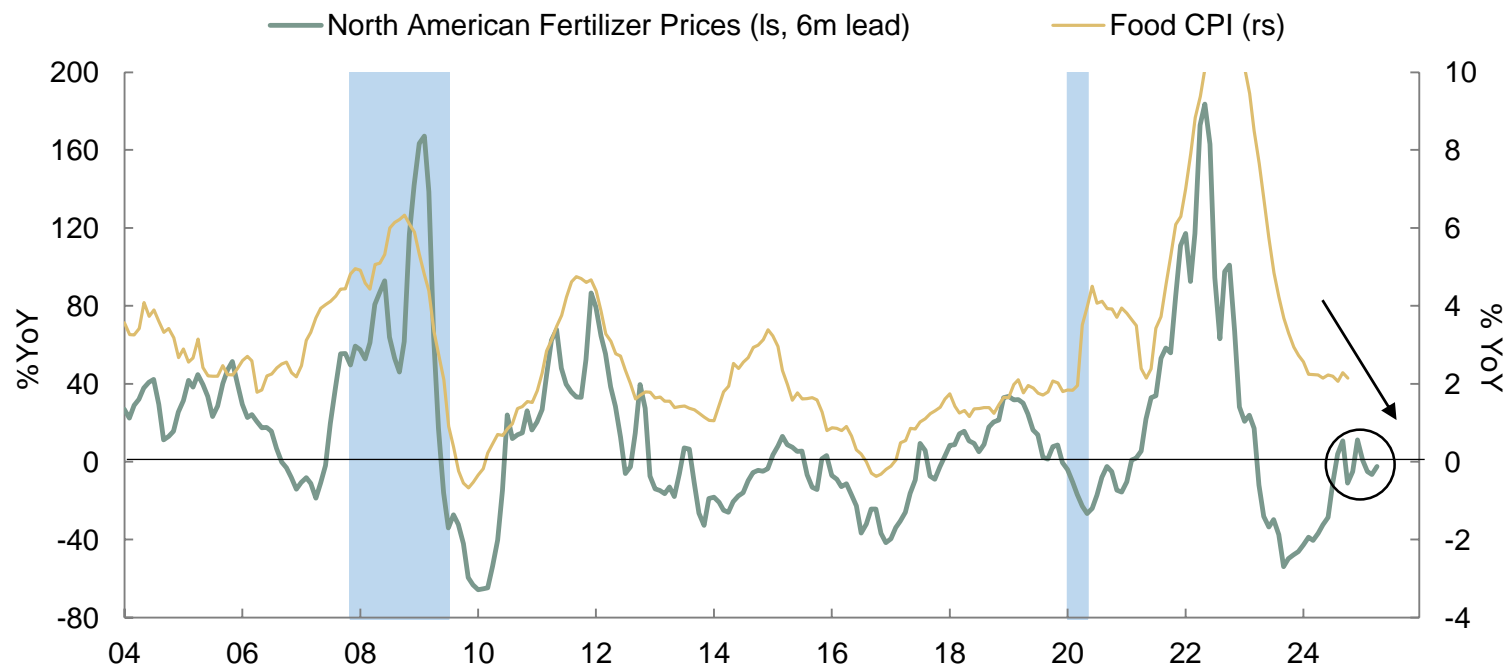
# Competition Begets Lower Prices

Because restaurants compete with grocery stores, food prices *away from home* end up following *at home* prices by three months. Away from home, and thus overall, food prices will decelerate further.



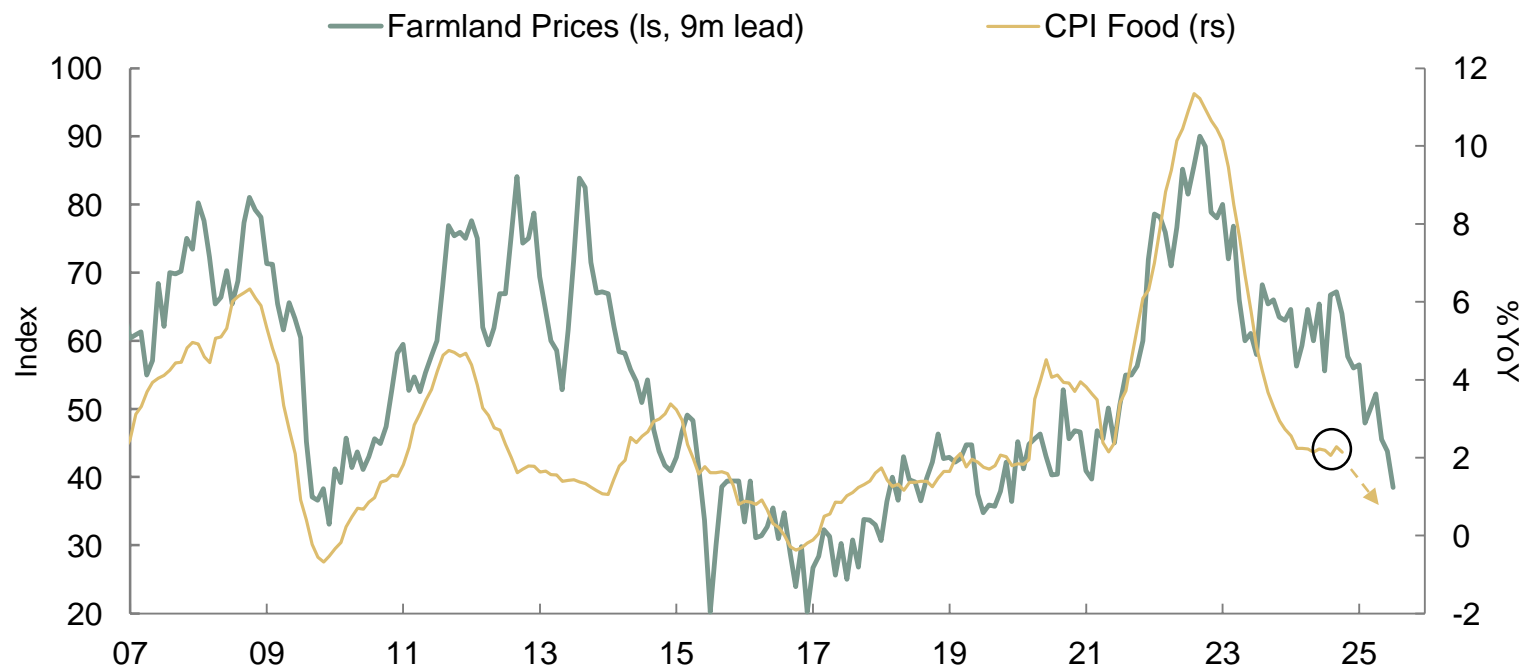
## Lower Input Costs

Fertilizer prices — which are down -2.4% YoY and almost -60% from their cyclical peak — tend to lead food prices by six months.



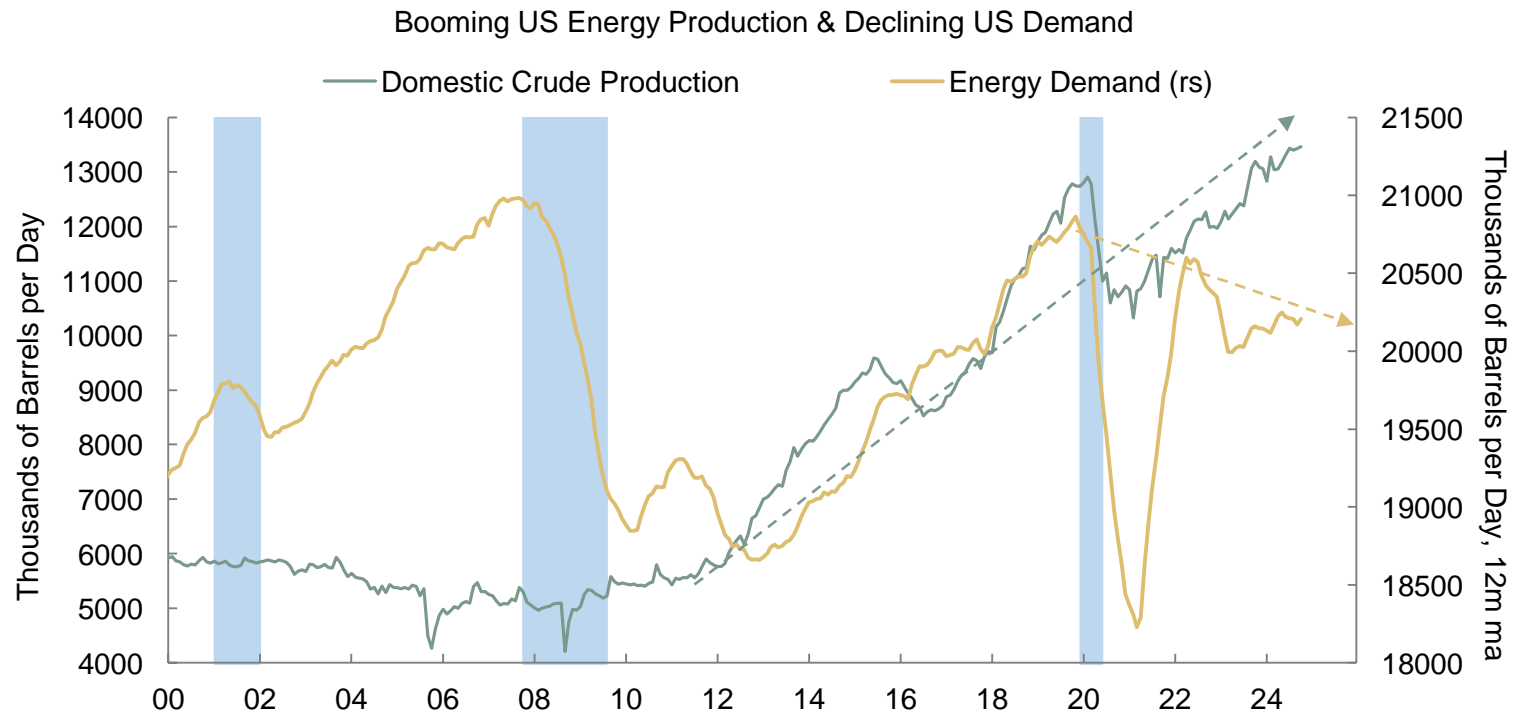
## Lower Input Costs

Farmland prices have declined sharply in recent months, which suggests that food prices should decelerate into the mid 1% range over the coming three quarters.



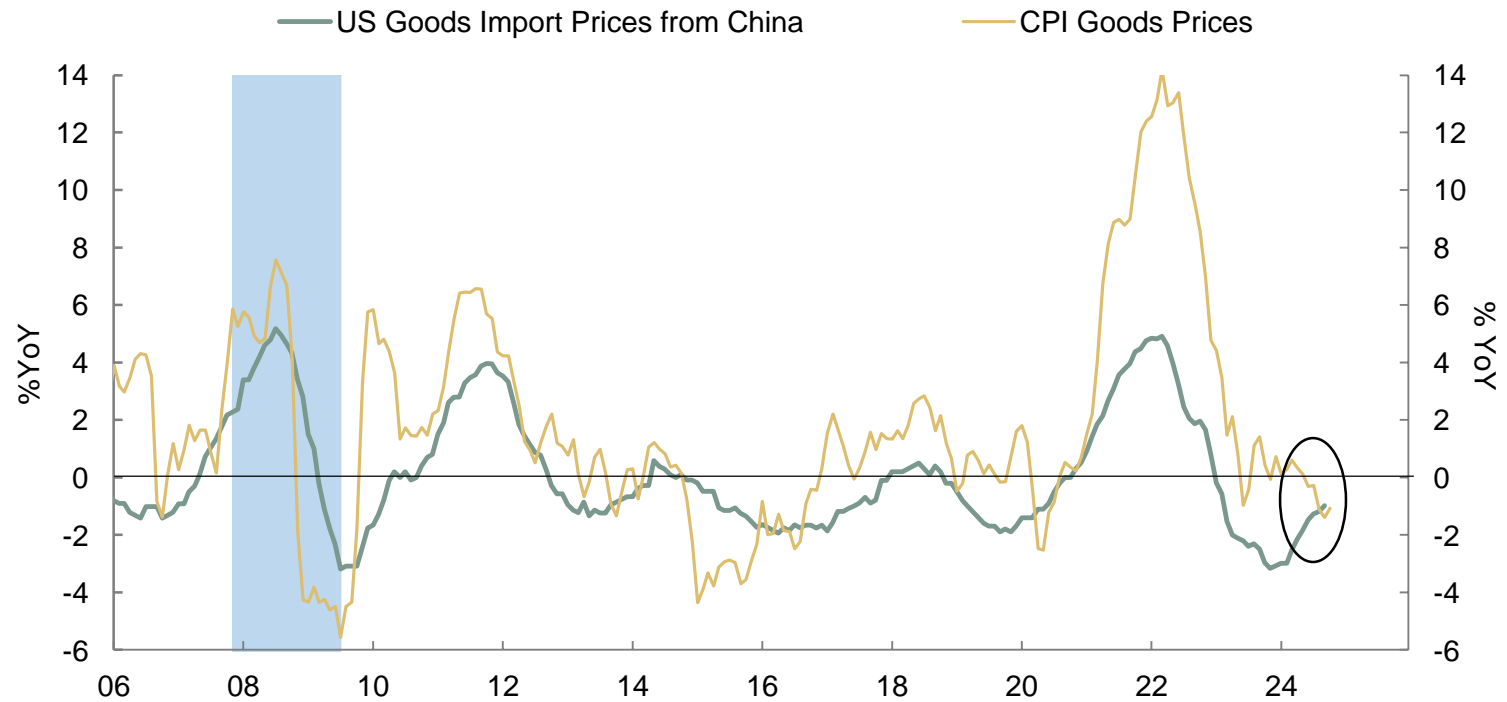
# The Energy Dominant US

Technological advancements in the E&P space (e.g., hydraulic fracturing) have supercharged energy supply, turning the US into the world's foremost energy producer, pressuring prices downward. This does not appear to be changing anytime soon. Meanwhile, demand has been uninspiring.



# With Help From China

China is exporting deflation, with goods imports declining -1% YoY.



# Disclaimers

---

This document is provided by SMBC Group (including, collectively or individually, Sumitomo Mitsui Banking Corporation, SMBC Nikko Securities America, Inc., and their affiliates, as applicable) for informational purposes only. This document was prepared by SMBC Group's economist(s). The views statements, assumptions and forecasts expressed herein are those of the author(s) and do not reflect the judgment of any other person or of SMBC Group. It does not constitute an offer, or solicitation of the sale or purchase, of securities or other investments. The information contained herein is obtained or derived from sources believed to be reliable, but SMBC Group and the author(s) make no representations as to its accuracy or completeness. In some cases, such information may be incomplete or summarized. This document has been prepared based on assumptions and parameters determined by the economist(s) in good faith. The assumptions and parameters used are not the only ones that could have been selected, and therefore no guarantee is given as to the accuracy, completeness, or reasonableness of any such quotations, disclosures, or analyses. Past performance is not a reliable indicator of any future results.

This document has been prepared for and is directed at institutional investors and other market professionals, and is not intended for use by retail customers. It does not take into account any specific investment objective, financial situation, or particular need of any recipient. The information contained herein should, for whatever purpose, be used solely at the discretion and responsibility of the recipient. SMBC Group does not accept any liability or responsibility for any results in connection with the use of such information. Recipients are responsible for making final investment decisions and should do so at their own discretion after conducting a careful examination of all documentation delivered prior to execution, explanatory documents pertaining to listed securities, prospectuses, and other relevant documents, and their own independent analysis and assessment of the merits of any transaction. The financial instruments discussed may be speculative and may involve risks to principal and interest.

## **Conflicts of Interest Disclosures**

The views statements, assumptions and forecasts expressed herein may differ from those expressed in globally branded research produced by SMBC Group. The trading desks of SMBC Group trade or may trade as principal in the financial instruments that are the subject of this material, and the author(s) of this document may have consulted with the trading desks while preparing this document. The proprietary interests of SMBC Group may conflict with those of the recipient. SMBC Group may seek to do business with the companies mentioned in this material and the trading desks may have accumulated, be in the process of accumulating, or accumulate long or short positions in the financial instruments mentioned and may have acquired them at prices no longer available. The trading desks may also have or take positions inconsistent with the views expressed in this document or may have already traded on those views.

This material is not a research report, and neither this material nor its author(s) is subject to policies and procedures that apply to the globally branded research reports and research analysts of SMBC Group or to legal requirements designed to promote the independence of investment research. It is not subject to any prohibition on dealing ahead of the dissemination of investment research. This means that on the date of this document, SMBC Group, and its directors, representatives, or employees, may have a long or short position in any of the instruments mentioned in this document and may make a market or trade in instruments economically related to the securities, derivatives or other underlying assets mentioned herein, in each case either as principal or as agent.

No part of the author(s) compensation was, is, or will be, directly or indirectly related to the specific recommendations or views expressed herein. The personal views of authors may differ from one another.

Distribution, possession or delivery of this document in, to or from certain jurisdictions may be restricted or prohibited by law. Recipients of this document are required to inform themselves of and comply with all such restrictions or prohibitions.

© 2023 SMBC Group. All rights reserved.