

Going Down The Backside of The Inflation Mountain

Joe Lavorgna

Chief US Economist
SMBC Nikko, Inc.

(212) 893-1528

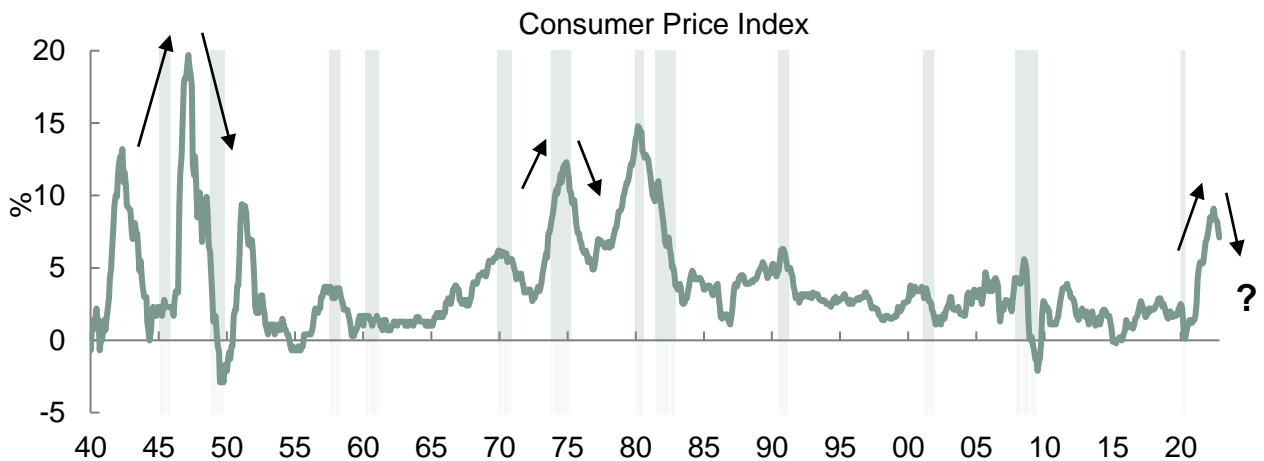
joseph.lavorgna@smbcnikko-si.com

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More Evidence of Peak Prices

For the second month in a row, headline and core inflation each meaningfully surprised to the downside. This provides more evidence **the economy is past peak inflation**. Last month, the consumer price index (CPI) rose just 0.1%, which had the effect of dropping the 12-month change from 7.7% to 7.1%. Meanwhile, the core CPI was up only 0.2%, which had the effect of lowering the 12-month change from 6.3% to 6.0%. We estimate headline and core prices finish 2023 at 2.5% and 3.3%, respectively.

When inflation falls, it tends to do so at the same pace as its acceleration. Visually, this can be seen in the chart below where large gains in the rate of inflation in 1940s, 1950s, 1970s and 1980s were usually followed by large declines in the rate of inflation. These periods are highlighted by arrows. While early in the process, the latest price slowdown looks like past inflation rollovers.



Sources: BLS, Haver, SMBC

What Goes Up Quickly Tends to Come Down Quickly

As our research has demonstrated, when the rate of inflation moderates, it tends to do so at the same rate as the acceleration. This is evident from the chart below, which shows the nine major inflationary episodes of the last 80 years. There is symmetry in the behavior of inflation. For the business cycles between 1940 to 2008, the average slope of the rise in inflation was 0.44 which was mirror image of the average slope of the decline in inflation that followed at -0.44. T

There was one notable exception following the Second World War. From February 1946 to March 1947, the increase in inflation had a slope of 1.61. When it peaked and began falling from March 1947 to April 1949, the deceleration in inflation had a slope of -0.66. But inflation was barely positive on a year-over-year basis in April 1949 (0.4%) and soon the economy experienced deflation! Annualized inflation was negative 3% in July and August. While the risk of deflation is low, the fall in the inflation rates is likely to continue to surprise investors. Stay tuned.

Inflation Upwing	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
May 2020 to Jun 2022	0.38	Jun 2022 to ?	
Average 1940-2008	0.44	Average 1940-2008	-0.44

Sources: BLS, Haver, SMBC

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