

# Our Inflation North Stars: An Outlook

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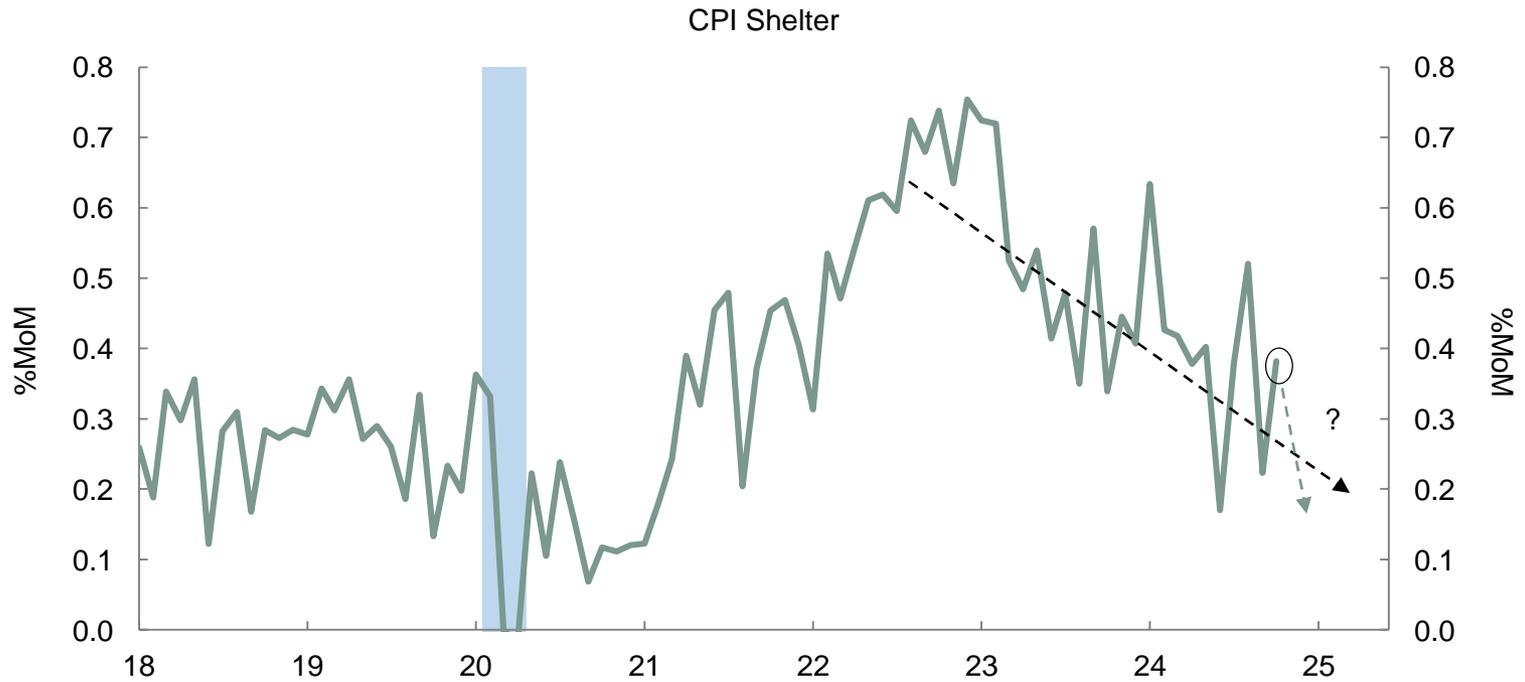
# Summary

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- 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.

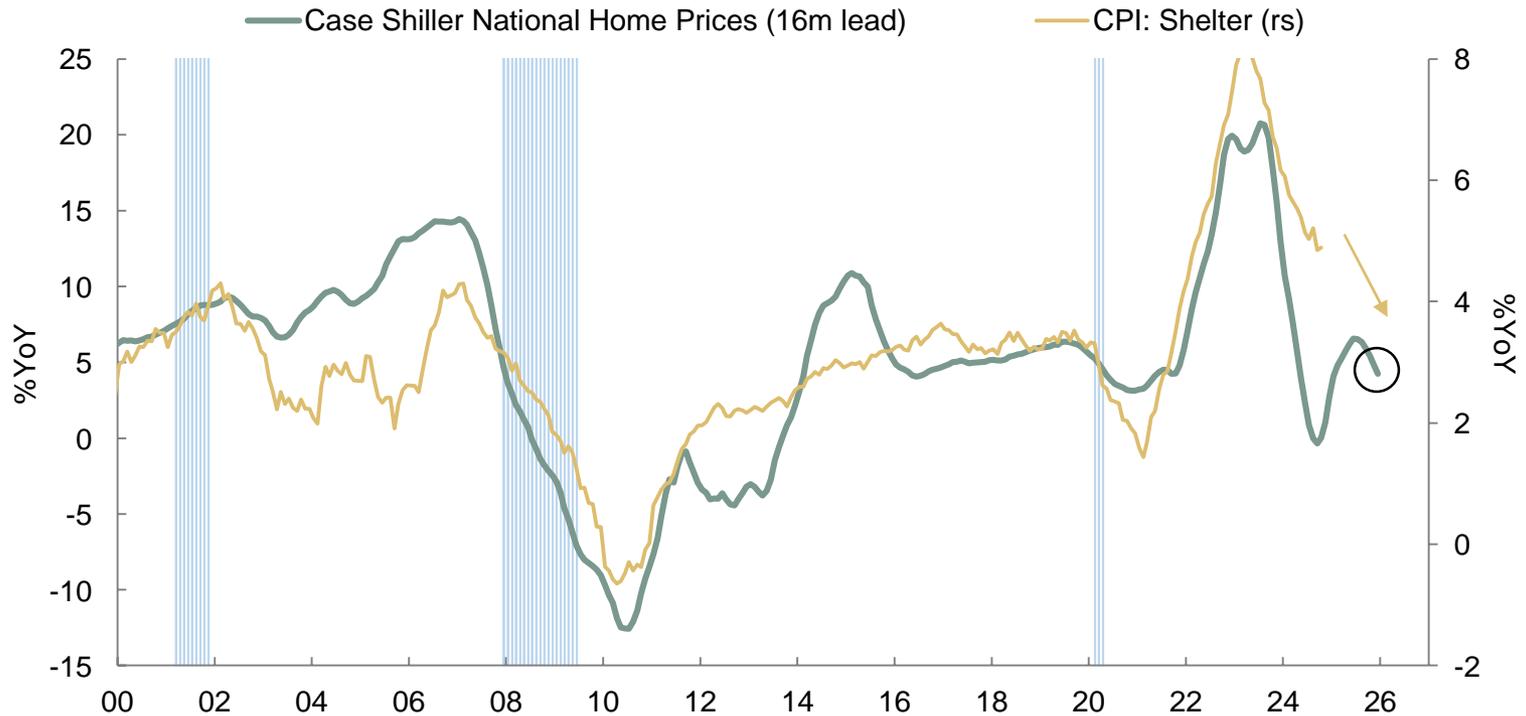
# A Friendly Trend

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



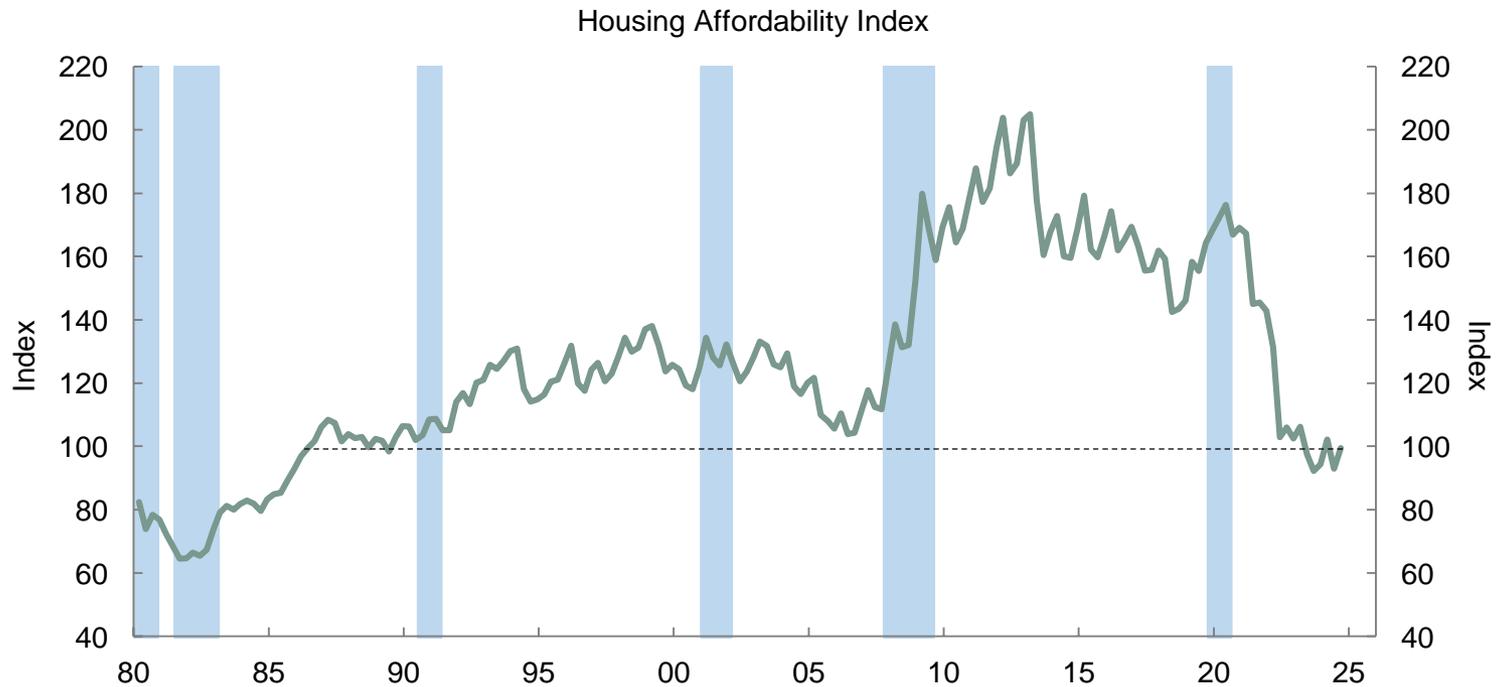
# Home Prices Leading Shelter Lower

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



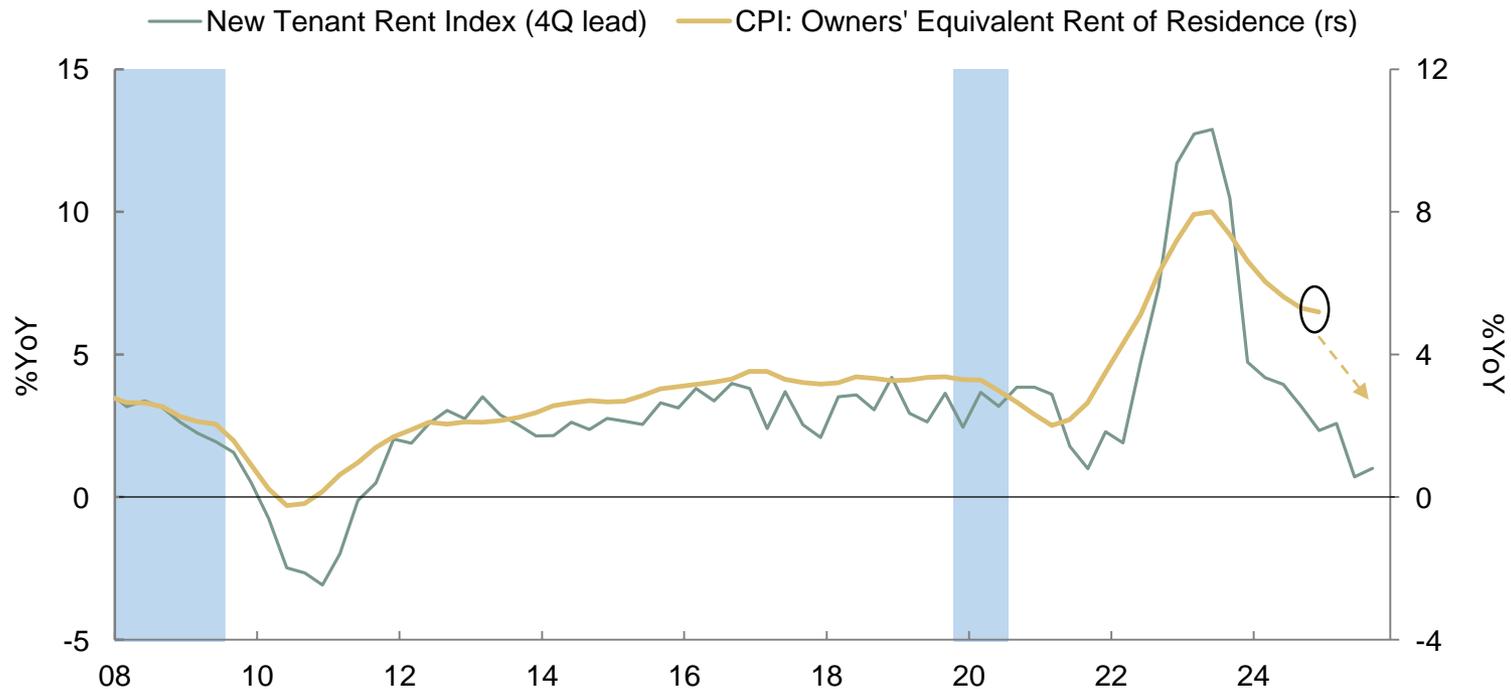
## Home Prices Leading Shelter Lower (2/2)

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.



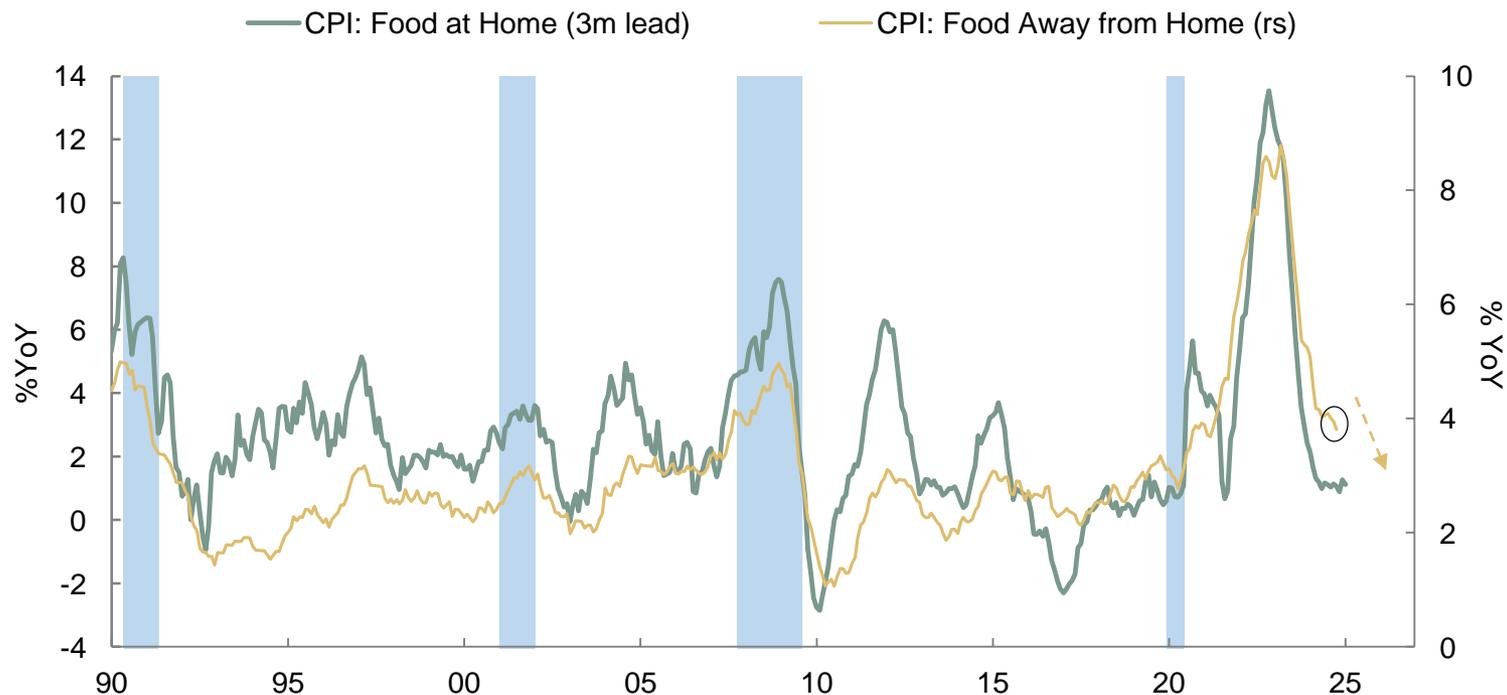
# Rental Reprieve Coming

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



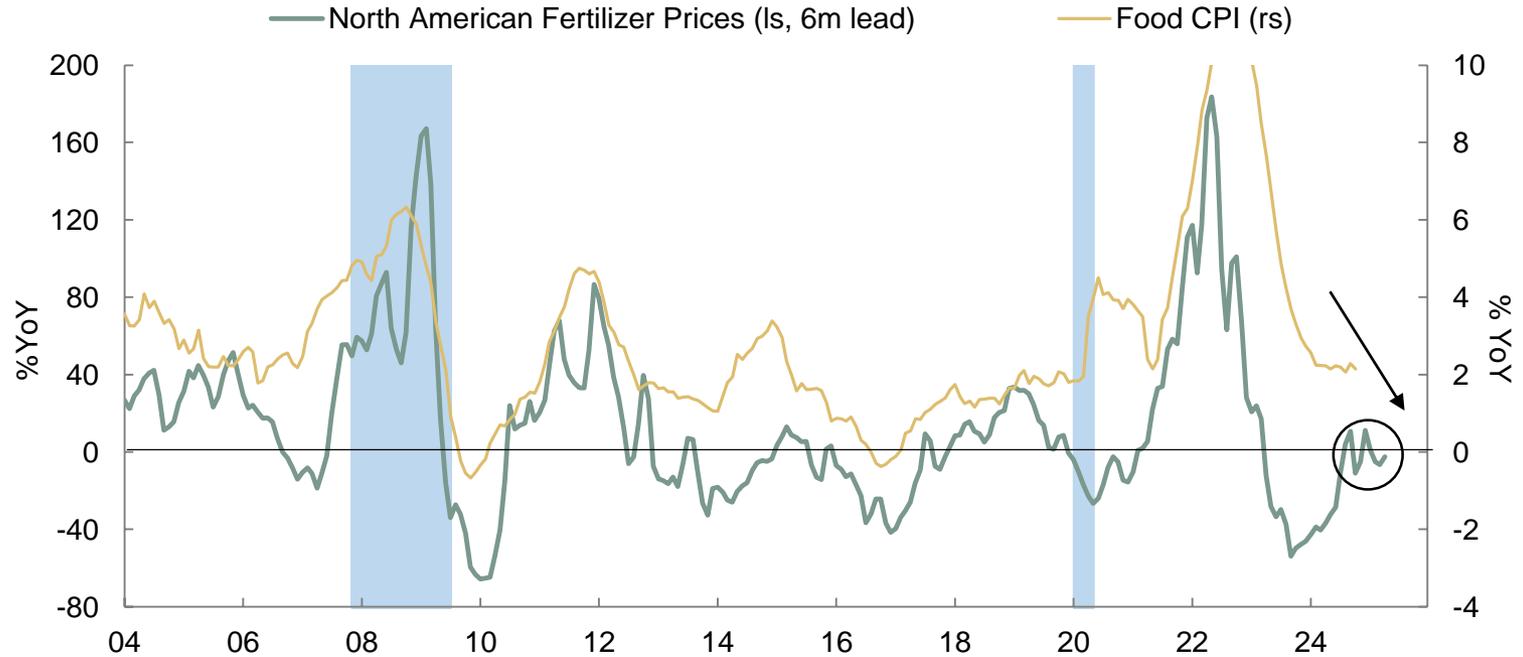
## Competition Begets Lower Prices

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.



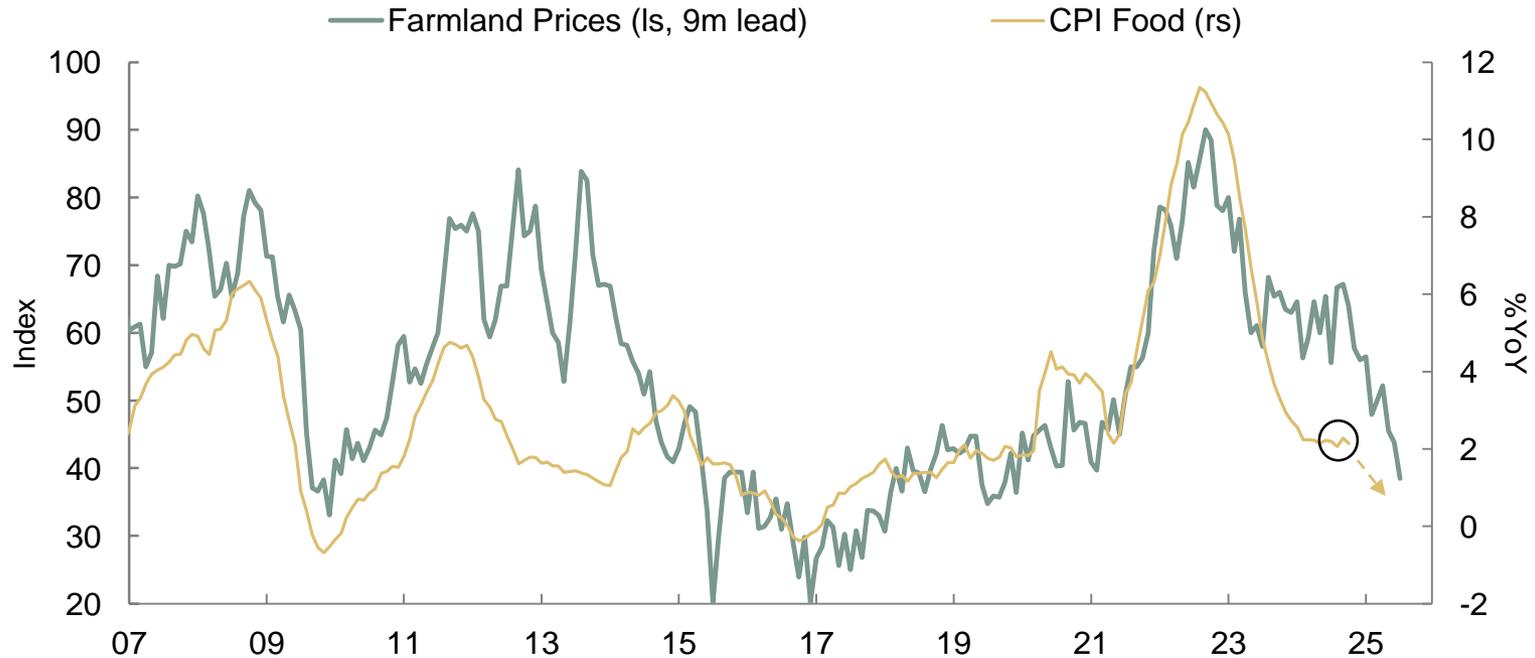
# Lower Input Costs

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



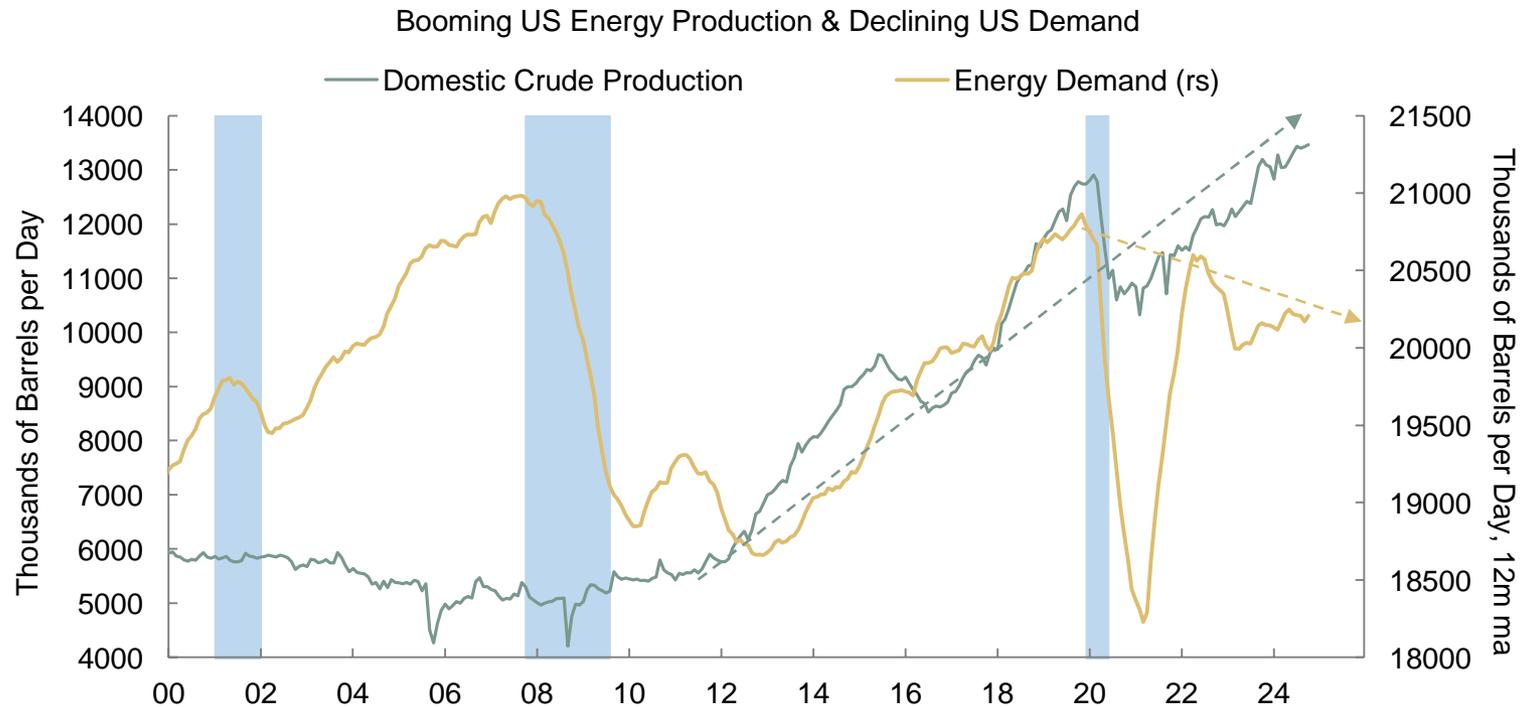
# Lower Input Costs

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.



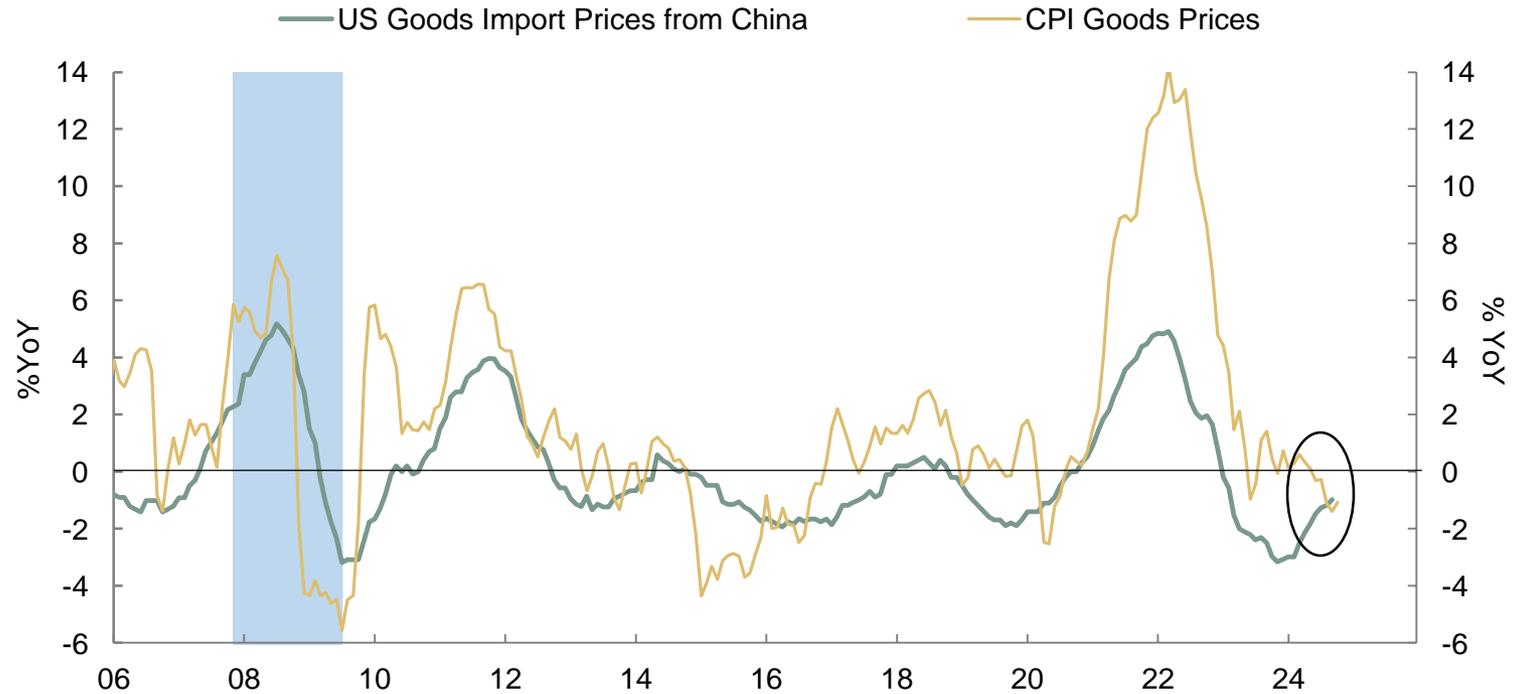
# The Energy Dominant US

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.



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