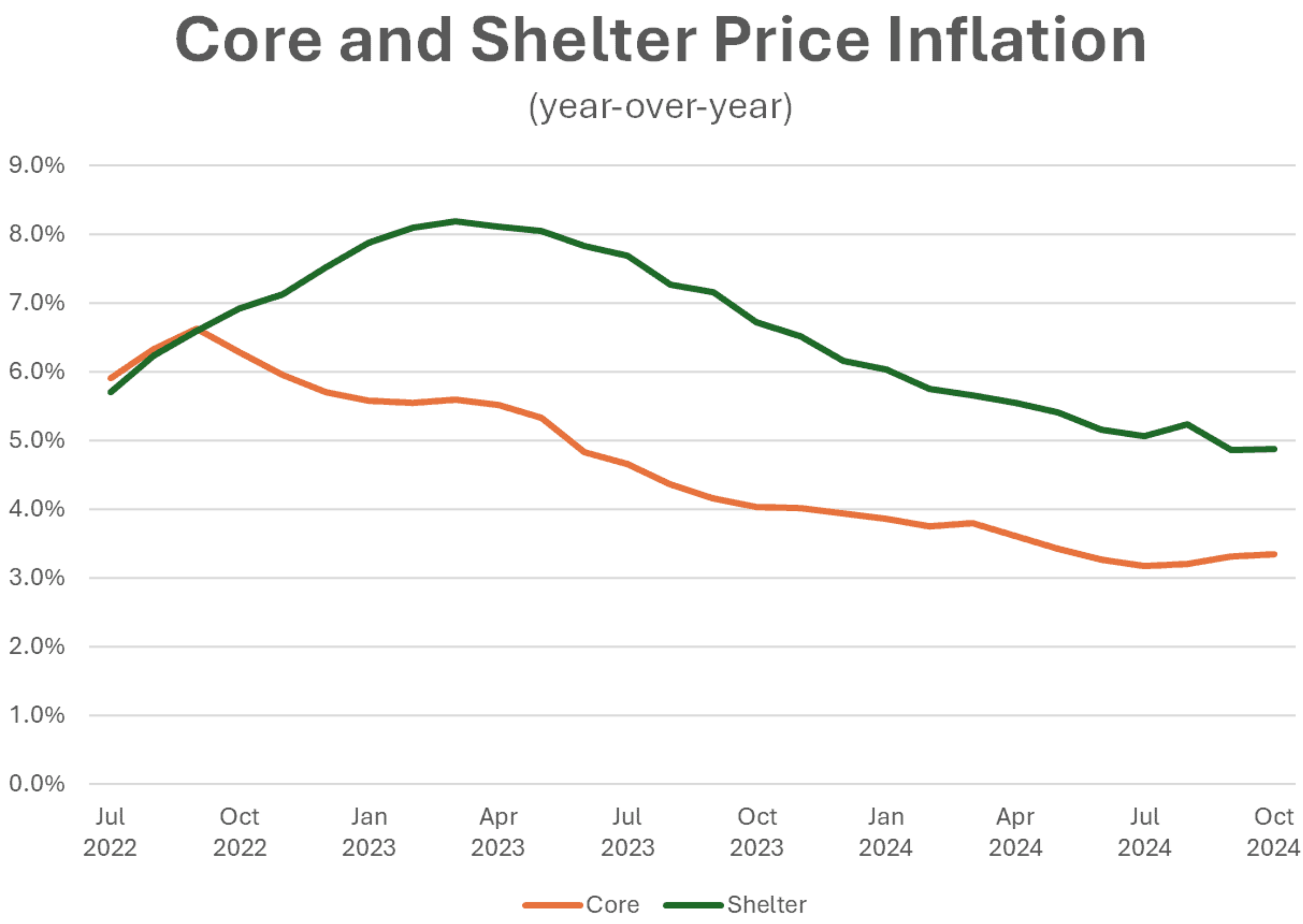
The Daily Dish

The Threat of Sticky Rental Inflation

DOUGLAS HOLTZ-EAKIN | NOVEMBER 19, 2024

Bloomberg is reporting some sobering news on the inflation front, specifically the outlook for rent inflation in the Consumer Price Index (CPI). Recall that shelter inflation is one-third of the CPI and remains quite elevated. (See chart, below.)



So, it is a wake-up call to read:

> *It may take until mid-2026 for rent inflation in the consumer price index to subside toward its pre-pandemic norm, according to research by the Cleveland Fed. While several measures suggest that new rents in particular are coming down, fewer people are moving and signing new leases — so the sample in the CPI doesn't capture as much turnover, the researchers said.*

The problem is twofold. First, it is difficult for the Fed to send the message that inflation is returning to the 2-percent target, and that it is prudent to lower interest rates as a result, when inflation remains elevated because of the lagging measure of shelter inflation.

Worse, the elevated readings may translate to expectations that inflation will continue to be above the 2-percent target. This is especially problematic because inflation expectations are central to actual inflation. As Federal Reserve Chairman Jerome Powell put it in his 2022 monetary policy address at Jackson Hole:

> *If the public expects that inflation will remain low and stable over time, then, absent major shocks, it likely will. Unfortunately, the same is true of expectations of high and volatile inflation. During the 1970s, as inflation climbed, the anticipation of high inflation became entrenched in the economic decisionmaking of households and businesses. The more inflation rose, the more people came to expect it to remain high, and they built that belief into wage and pricing decisions.*

Again, there is some evidence of a small problem on this front right now, as inflation expectations have stalled out in the 3.0-percent range instead of continuing to decline toward the target.

In many ways, the battle against inflation is in the rearview mirror. The Fed has cut rates, the new administration is sucking all the oxygen out of the press with announcements of intentions and nominations, and people have moved on. Let's hope that is right, but the story is a reminder that it is not guaranteed.