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Please Stop Saying That Inflation Is Cooling

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Commentary

For anyone following price trends, there was nothing particularly surprising about this week's report on consumer prices. They came in hotter than expected. This makes sense. The money stock is generally up with velocity on the rise. Real-time prices are rising again. The Fed recently lowered rates. They didn't call it "quantitative easing" but that is what it is.

Clearly, the excesses in money printing over four years have not yet been mopped up, and that is showing itself in price increases some 50 percent above what the Fed claims to be its target.

I like to play a mental game when these data releases come out. I had dug through the spreadsheets to see energy prices down and food and transportation up, and everything else chugging along in ways that keep reducing the U.S. standard of living.

In my mind, I thought: "I bet they will report that inflation is cooling."

How did I know? That's what the major media has said for three years. Cooling is the go-to word because it sounds somehow better but it is imprecise enough to be nearly meaningless. It's a safe term, much safer than the proper headline: "Hot Inflation Higher than Expectations."

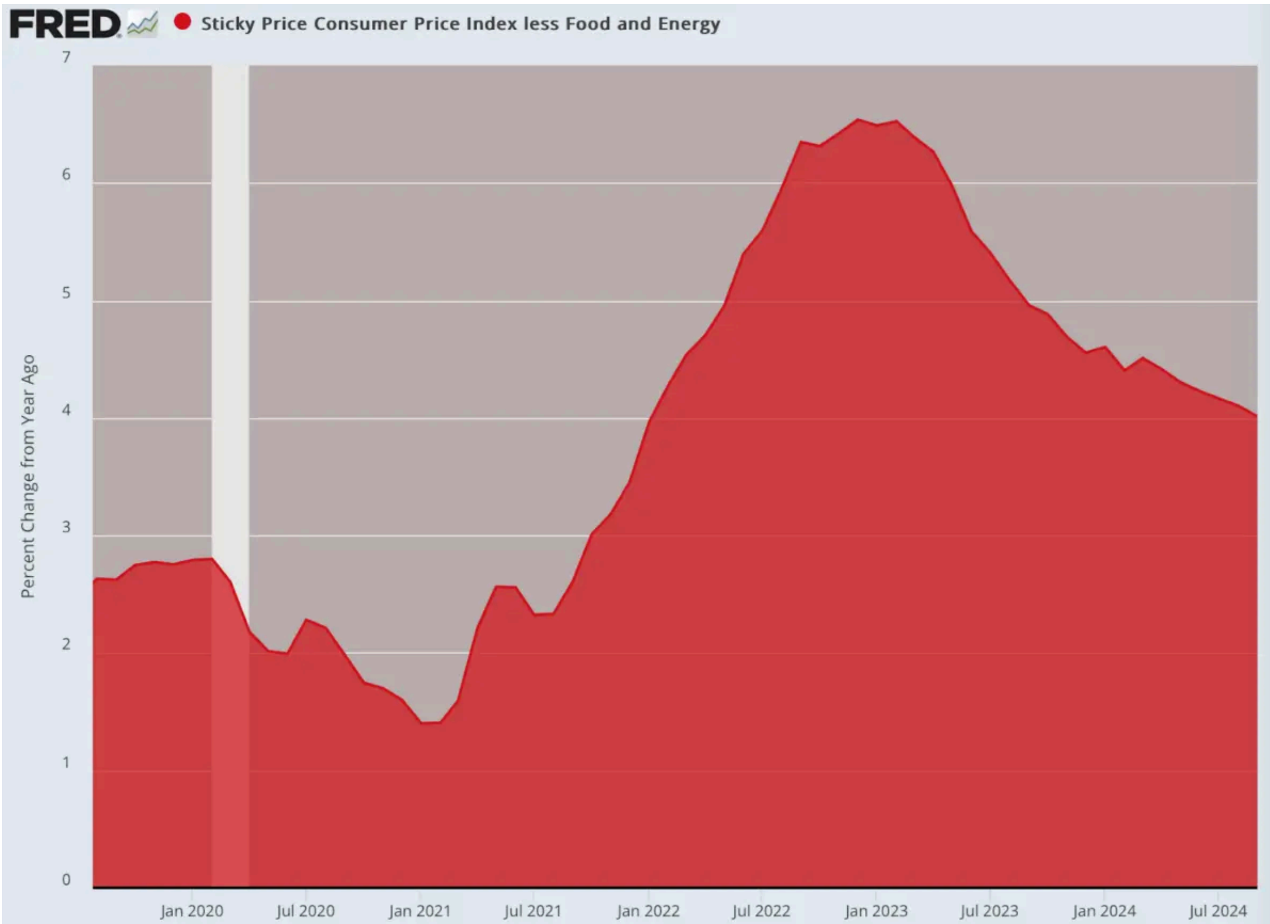
Sure enough, the Wall Street Journal went there; "Inflation Cools in September." So did the New York Times: "Inflation Cools Slightly." An hour later, the *WSJ* rethought and changed its headline to: "U.S. Inflation Is Cooling More Slowly Than Expected." Then they changed it again: "Inflation Continues Its Bumpy Decline With Mixed September Reading."

My favorite of all comes from the Associated Press: "US inflation likely cooled again last month in latest sign of a healthy economy."

It took nearly all day before the journalists themselves realized that they were once again fooled by the press release.

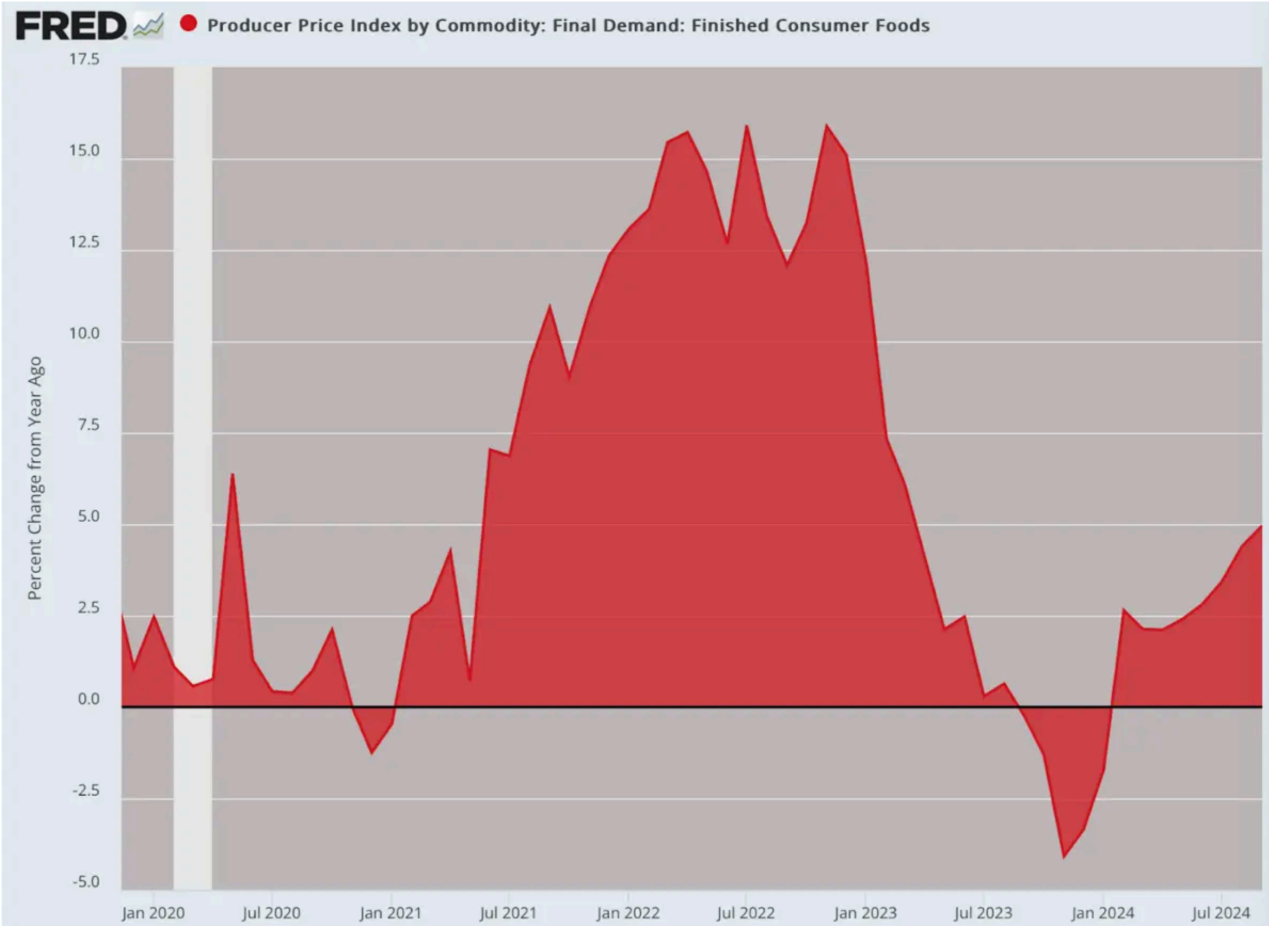
Try to understand this temperature metaphor. It's hot in the room, so you turn on the air conditioner. Someone says, it's still hot. You say it's cooling. They say it's still hot. You say it is cooling more slowly than expected. You might respond: the air conditioner does not work.

Indeed, the anti-inflation campaign of the last three years has not worked.



(Data: Federal Reserve Economic Data (FRED), St. Louis Fed; Chart: Jeffrey A. Tucker)

Producer prices, which reliably predict future trends in consumer prices, are also re-accelerating after having calmed down a bit last year.



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If five years ago, we experienced inflation on this level, there would have been shock and alarm in the air. People would have been screaming about how the one-month rate had tripled and the year-over-year rate doubled. There would have been a frenzy of concern.

But after what we've been through, reporters routinely call inflation on this level "cooling" even though they have said this for three years as the dollar has lost 20 percent and more likely 40 percent of value. This really needs to stop. Surely the headline writers can be more accurate and descriptive rather than propagandistic.

Let's consider more in detail. No one actively involved in the consumer marketplace truly believes that prices are up only 20 percent over four years. Brownstone released a detailed empirical study of actual prices that concludes they are up some 40 percent, by making only three adjustments: using actual housing prices, actual health-insurance prices, and mitigating against "hedonic" adjustments. With just these changes—and many more could have been added—it concludes that all of the output increases since 2022 have been eaten up by inflation.

The reaction was exactly what I might have expected. There is shock on the one hand, but not because of the conclusions. Everyone knows that inflation is far worse than what they have been saying. The shock is that someone finally said what needed to be said.

There are thousands of institutions that might have commissioned this study. There are hundreds of thousands of working economists out there. The trouble is that none of them gain any reward from contradicting falsehoods that come from agencies. All the incentives are the reverse.

As with public health and medicine, the industry of economics as a profession tends to have an internally self-reinforcing story that they like to tell. When an outlier comes along and says otherwise, it is a bit like the boy who says the emperor is not wearing any clothes.

One of the widely believed doctrines in the world of economists is that deflation is always terrible because it indicates economic decline. Economists have generally believed this since the Great Depression. It stems from a basic error over cause and effect: the belief that falling prices are driving lower output rather than attempting to correct it. As a result, economists have long been more sanguine about inflation than they should be.

This puts many mainstream economists in the awkward position of opposing what most people actually want, which is lower prices. This is especially true after four years of unrelenting and grueling inflation that has so dramatically lowered purchasing power. Who wouldn't want to go back to 2019 prices?

Sadly that is not going to happen. Even if inflation falls below zero temporarily, there will be panic at the Fed and among professional economists as if something terrible is happening. This has no basis in fact or in history. The price of software and computer memory experienced declines on the level of 90 percent over several decades even as the industry boomed. In the late 19th century, a general and gentle deflation in all goods and services took place under a strict gold standard regime, and this coincided with the largest rate of economic growth ever seen.

Ruling out the possibility of not going back to prices of five years ago, the least we could ask is that prices stabilize now and in the future, so that at least we can work toward regaining some of the prosperity that has been taken away from us. For that matter, it would at least be nice to have some honesty about how much inflation there has been.

Sadly, all trends are headed for the worse. Real-time inflation measures suggest a reacceleration and money stock levels are rising and at an 18-month high. The Fed is cutting rates in response to demands by Wall Street for looser credit and lax lending standards. All of the trends point in only one direction: we are experiencing higher prices. Indeed we might be headed to wave two, consistent with the experience of the 1970s. No one wants to see what wave three looks like.

If this is true, the next administration is going to have a serious problem on its hands. There will be no way to fix the inflation problem by attacking retail prices directly with anti-gouging laws or price controls. Nor is more drilling going to fix the issue. There will be no choice but to go to the real source of the problem. The money printer itself needs to be unplugged. And, yes, doing so will be rather disruptive of production structures and investor expectations. It could even bring about a deeper recession.

At some point, this economy has to right itself, face the truth, and start standing on its own without the constant infusions of money and credit that are showing themselves in higher prices.

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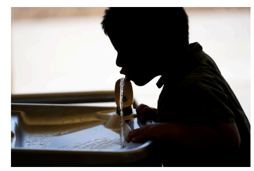

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