Consumer Prices Continue to Soar, Rising 7.5% in January

With prices rising, the Federal Reserve is set to interest rates next month.

By Tim Smart - February 10, 2022

Consumer prices showed no sign of slowing down in January, rising 7.5% on an annual basis, the Labor Department reported on Thursday. Increases in the cost of food, electricity and shelter were the main contributors to the rise. The rise in the core index, which excludes food and energy, was 0.6% for the month, the same as in December.

The level is more than double the Fed's annual goal of a 2% average, clearing the way for the central bank to raise interest rates as early as March. The Fed has already begun cutting its monthly purchases of Treasuries and mortgage-backed securities, a program it began at the start of the coronavirus pandemic in March 2020.

Yields on bonds have risen in anticipation of higher interest rates, as have mortgages. Demand for mortgages fell by 10% last week as the average rate for a 30-year fixed-rate loan rose to 3.83%.

Although the omicron variant of the coronavirus slowed economic activity toward the end of last year, the labor market remains hot with 467,000 jobs created in January and the unemployment rate at 4%. Meanwhile, many restrictions including mask mandates are being lifted, paving the way for a return to normal.

The Fed is facing the highest level of price inflation since the 1980s and is generally considered to be behind the curve in addressing inflation. Analysts are divided on how aggressive it will be in the coming months, as the economy is already slowing down from the breakneck pace of 2021.

"We now project Q1 U.S. real GDP (gross domestic product) expanded at just a 0.7% annualized rate, down from our initial call of 2.9% a month ago," Sam Bullard, managing director and senior economist at Wells Fargo Corporate &

Investment Banking, wrote on Wednesday. “The downward revisions to our Q1 forecast are concentrated in our outlook for personal consumption expenditures, due, in part, to the profile of growth in Q4 that resulted in some tough base comparisons.”

Wells Fargo also trimmed its growth forecasts for the next two years on account of reduced stimulus from Washington, as well as persistent inflation.

“We look for full year GDP growth to increase 3.4% in 2022 and 2.9% in 2023 (down from 3.9% and 3.1%, respectively, in last month’s forecast),” Bullard added.

Other economists say that some of the reasons for the spike in inflation, such as supply chain disruptions and a tight supply of labor, could be reversing.

“Foreign goods entering the U.S. rose in each of the last five months and jumped to a record $259.7 billion in December,” **Bernard Baumohl, chief global economist at The Economic Outlook Group**, wrote on Wednesday. “These imports help replenish depleted stockrooms and back lots. Retail inventories, for example, increased by 4.4% in December to $643.8 billion, the highest since the onset of the pandemic.”

“And more supplies are on the way,” **Baumohl** added. “Wholesalers were filling up shelves with the value of stocks reaching a record $790.8 billion in December, up nearly 20% from a year ago. These items covered a wide spectrum of products – capital goods, consumer products and motor vehicles. This massive rebuild of business inventories contributed more than half to the economy’s 6.9% GDP growth rate the final three months of the year.”

And, he noted, January saw a record 1.55 million people employed in the trucking industry, with another 1.73 million workers in warehousing and storage jobs to move supplies along faster.

“These are deflationary forces at work,” he said. “The Federal Reserve Bank of New York and the Institute for Supply Management have also noted an improvement in supply chain activity. While that’s not the case with every industry, such as semiconductors, there is some measurable relief across many other sectors of the economy.”

The addition of nearly half a million workers to payrolls in January will also dampen the rise in wage inflation, Baumohl said.

“In January alone, the labor force surged by 1.4 million, the biggest one-month increase since June 2020 when it bounced back from the COVID-linked collapse. As a result, the labor force participation rate and the employment-population ratio have moved to their highest level since the onset of the pandemic. As the supply of labor increases, it will also tamp down wage pressures and we should see initial evidence of that by midyear."

Baumohl is calling for a half-point increase in interest rates when the Fed meets in March, a number that has recently gained favor with market strategists and economists who believe the Fed needs to send a signal after saying throughout 2021 that the inflation spike was "transitory." That would be above the more typical 0.25 basis point hikes the Fed has done in the past.

But others believe the stock market's recent sharp sell-off may have done a little of the Fed's work for it, while market interest rates have risen as well.

Fed Chairman Jerome Powell "has said they are going to be very flexible" and watch the data before acting too strongly, says Dan Wantrobski, associate director of research at Janney Montgomery Scott. "Powell doesn't like to pander to the markets but we are in a correction."

While the consumer price index will remain elevated, Wantrobski adds, "our feeling is there is going to be a pull back."

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