UNITED STATES

THE FED ABOUT TO CALM THINGS DOWN

With the inflationary surge in the US showing no signs of stopping, the Federal Reserve is no longer taking an accomodative stance and could accelerate the tapering of quantitative easing. Inflation has also spread to asset prices: real estate and stock prices have climbed to peak levels. Unless the emergence of the Omicron variant radically changes the situation, everything points to a key rate hike in 2022, possibly as early as next summer.

Long seen as only a transitory phenomenon in the United States, inflation has become a veritable source of concern. In October 2021, US inflation surged above 6% for the first time in 31 years. Core inflation, which excludes energy and food prices, also soared to a record high of 4.6%, well above the 2% target set by the Federal Reserve (the Fed), which finally took action.

PRICES PRESSURES

The Fed began by adopting a harsher tone. At the traditional Congressional hearings in late November, Fed chairman Jerome Powell said that the surge in prices could no longer be qualified as "transitory". He also lent credibility to the idea of a more rapid tapering of quantitative easing, raising the option of a key rate increase, possibly as early as summer 2022.

Unless the emergence of the Omicron variant radically changes the situation, everything points to a tightening of US monetary policy. Inflation is not only accelerating, but it is also spreading, and has now spilled over to rent, one of the biggest items on the price index. Rent is already up 3.5% for the year, and this trend is bound to accelerate following the sharp upturn in house prices, which are under pressure from the boom in mortgage loans (chart 2).

The business climate is euphoric, a little less so in industry, where production continues to be hampered by the global shortage of components, but more than ever in services, where business is returning to normal, and growth and job prospects have yet to show any signs of faltering.

The labour market is robust again. More than 6 million jobs were created in 2021, out of the 9.4 million jobs lost in 2020. In November, the unemployment rate dropped to 4.2% of the active population, far below the Fed's expectations. Although the labour market participation rate is still rather low, it is easily explained by the discouragement of workers with the highest exposure to the pandemic, as well as to demographic influences. Unbiased by an aging population, the share of Americans in the 20-64 age group who are active in the job market (employed or actively seeking employment) continues to rise. This figure can be estimated at 77%, and is now just short of the 2019 average of 77.6%.

Following a series of record stock-market highs and the unprecedented compression of yield spreads in 2021, financial stability has finally become a subject of concern. The Fed's financial stability reports regularly point out that stock market valuations and corporate debt have reached historically high levels, which have been fuelled at least in part by very low interest rates. This message not only sounds like an admission of responsibility, it also serves the double purpose of calming things down.

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GROWTH AND INFLATION

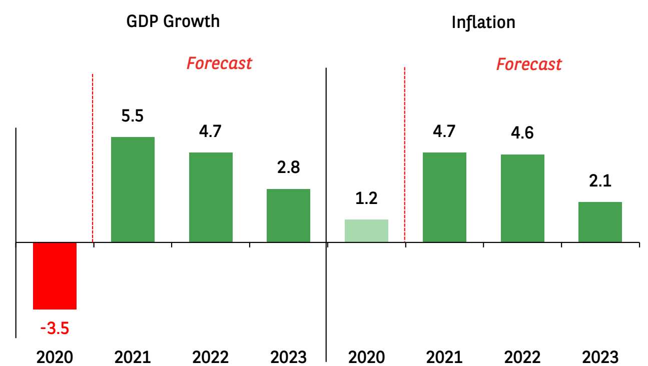

CHART 1 SOURCE: BNP PARIBAS GLOBAL MARKETS

HOUSING MARKET FRENZY

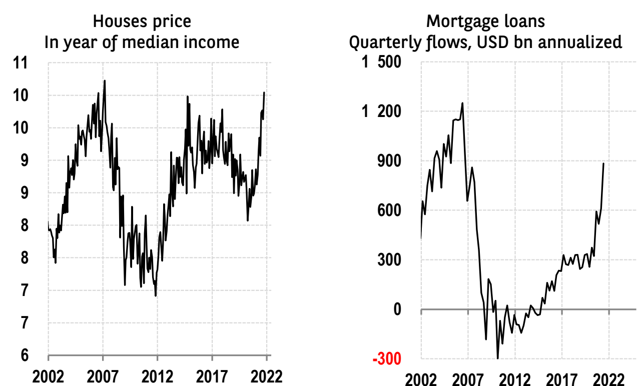

CHART 2 SOURCE: CENSUS BUREAU, FEDERAL RESERVE