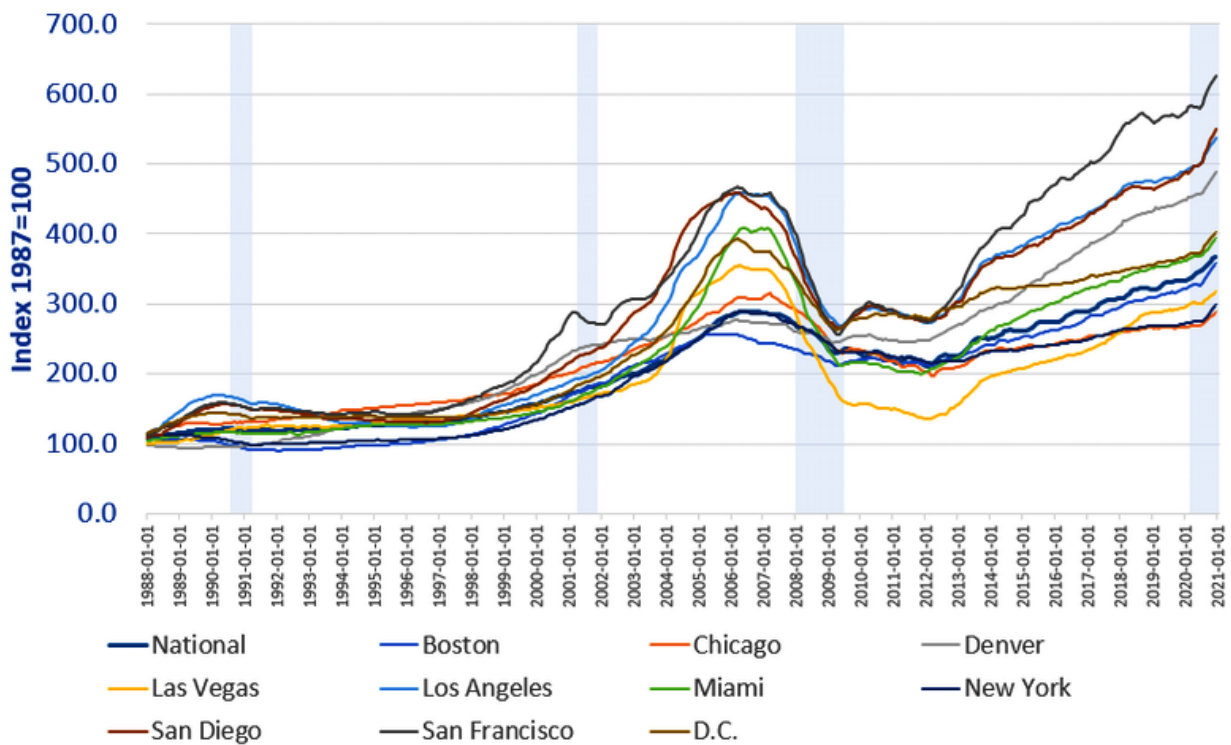



Shedlock: Inflation Is Rampant But Fed Dismisses It

Inflation is rampant but the Fed dismisses it. Year-over-year home prices are up 11.2%, some cities even more. The Fed does not see this, or count it, if they do. Let's discuss why.

Case Shiller Home Price Index - National and Top 10 Metro
Index Level 1987 = 100



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Home Prices Rise at Fastest Pace in 15 Years

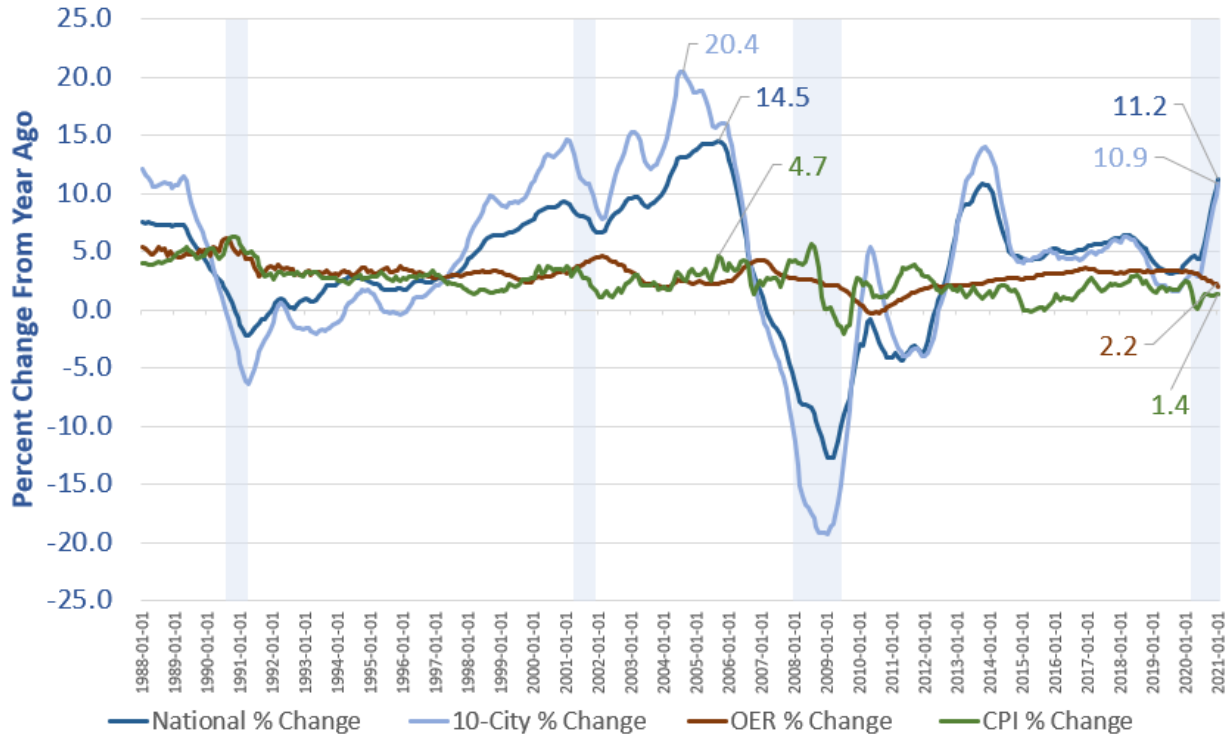
Home prices are running rampant. The national level average year-over-year increase is 11.2%.

Prices have accelerated in the past few months. I discussed the year-over-year acceleration in [Home Prices Rise at Fastest Pace in 15 Years](#)

National and 10-city averages do not tell the full story as the lead chart shows.

Inflation Disconnect

CS National, Top 10 Metro, CPI, Owners' Equivalent Rent
Percent Change From Year Ago



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Owners' Equivalent Rent

OER stands for Owners' Equivalent Rent.

Prior to 2000, home prices, Owners' Equivalent Rent (OER), and the Case Shiller national home price index all moved in sync.

This is important because home prices directly used to be in the CPI. Now they aren't. Only rent is.

Yet, OER is the?Single Largest Component of the CPI?with a weight of 24.07%.

In effect, economists substituted rent for home prices in the CPI. Prior to 2000, this did not matter. Now it seriously distorts measures of inflation.

The rationale is home prices are a capital expense not a consumer expense.

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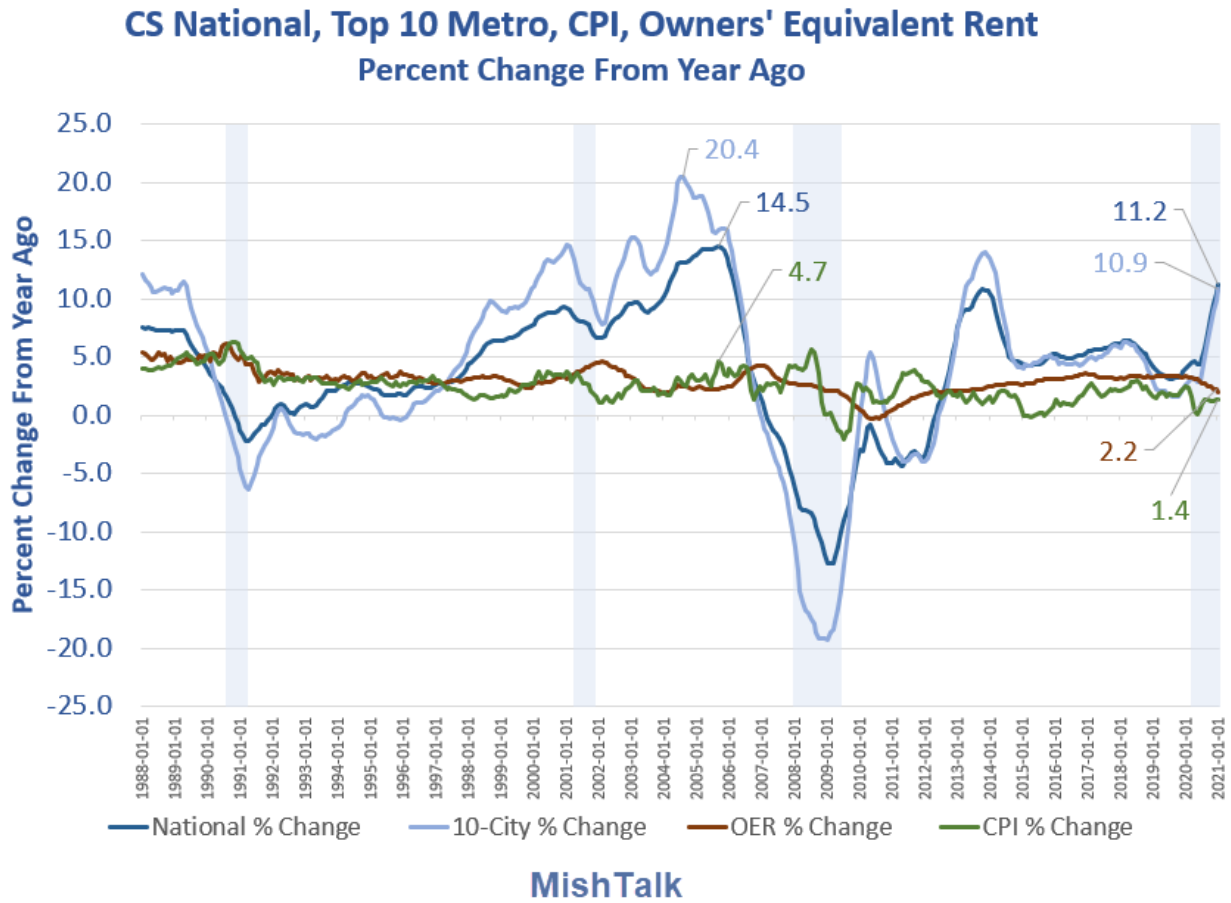
[> Try it now](#)

What Should We Measure?

What is it we are measuring or need to measure?

I suggest we need to measure inflation, not just consumer inflation.

Home Prices, OER, and CPI Percent Change



Year-Over-Year Percent Changes

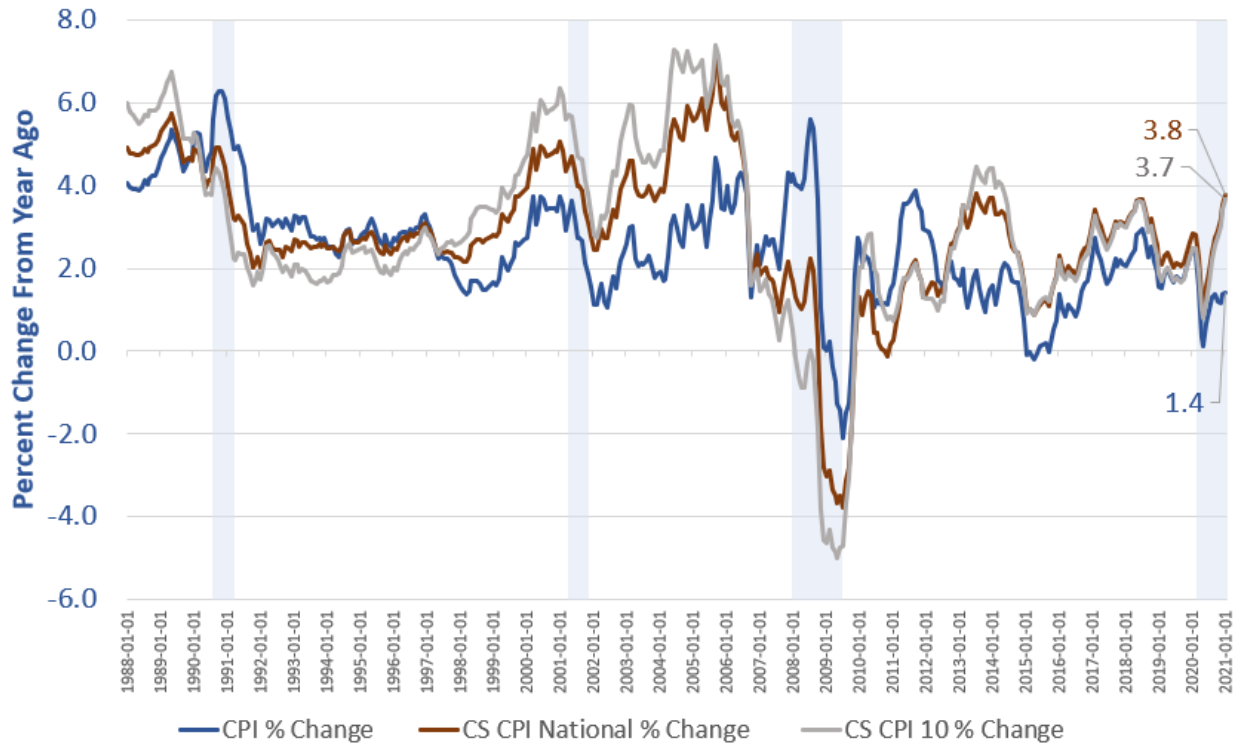
- National Home Prices: 11.2%
- 10-City Average: 10.9%
- OER: 2.2%
- CPI: 1.4%

The CPI allegedly is up a mere 1.4% from a year ago as of January 2021. Let's calculate inflation by substituting home prices for OER in the CPI as it used to be.

I call the result CS-CPI for Case-Shiller-CPI.

CPI, CS-CPI National, CS-CPI Top 10

CPI, CS-CPI National, CS-CPI Top 10 Metro Percent Change From Year Ago



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Economists claim inflation is up a mere 1.4% year-over-year as of January 2021.

If we substitute home prices for OER as it used to be (and is far more accurate as well), inflation is up 3.8% from a year ago.

Having calculated inflation far more accurately than widely believed (yet still understated), we can calculate real interest rates.

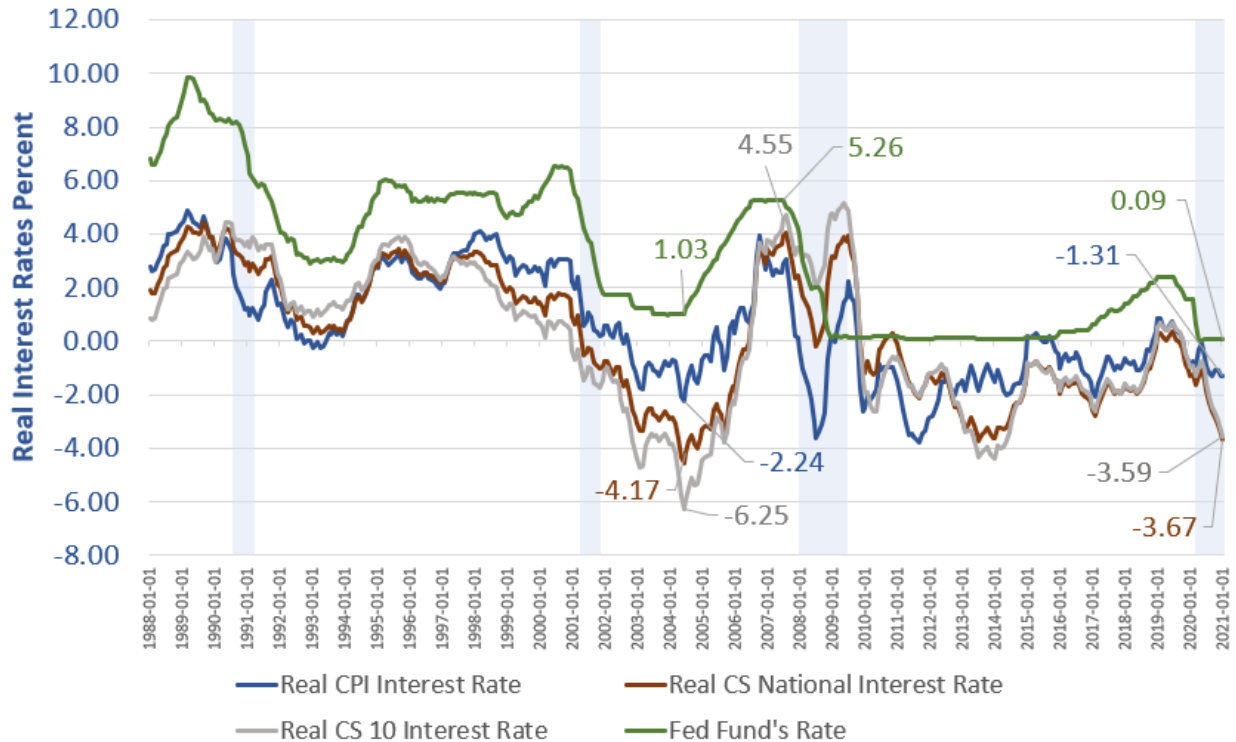
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Real Interest Rates

Real Interest Rates: CPI, CS-CPI National, CS-CPI Top 10 Fed Funds Rate Minus CPI Measures



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To determine "real" interest rates, subtract CPI from the Fed Funds Rate.

- Real Interest Rate as Touted: -1.31%
- CS-CPI 10-City: -3.59%
- CS-CPI National: -3.67%

Q&A

Q: With real interest rates close to -4% is it any wonder asset prices and speculation are booming?

A: No

Q: Why can't the Fed see this?

A: Possibly the Fed can see this. If so it's on purpose.

The Fed wants inflation and numerous Fed members are openly in praise of it.

Easy Money Quote of the Day: Fed "Won't Take the Punch Bowl Away"

On March 25, I noted the Easy Money Quote of the Day: [Fed "Won't Take the Punch Bowl Away"](#)

Numerous Fed presidents made speeches. I awarded gold, silver, and bronze medals for the best "easy money" quotes.

San Francisco Fed President Mary Daly won the gold medal. She said the central bank would show at least ?a healthy dose? of patience. ?**We are not going to take this punch bowl away,**? said Daly.

Does the Fed Understand What They Are Doing?

I don't know. Either the Fed is blindly ignorant of what's going on, or it's on purpose. Take your pick.

The result is a big set of bubbles, whether the Fed sees them or not.



2% Inflation Target

The Fed's 2% inflation target is monetary insanity.

Full speed ahead with the stimulus in search of inflation that would be visible to anyone who was not wearing groupthink blinders.

I have a set of questions for Fed Chair Jerome Powell on inflation. Please read them: [Hello Jerome Powell We Have Questions.](#)

Historical Perspective on CPI Deflations

A BIS study of deflations shows the Fed's fear of deflation is foolish.

"Deflation may actually boost output. Lower prices increase real incomes and wealth. And they may also make export goods more competitive," concluded the study.

For discussion, please see [Historical Perspective on CPI Deflations: How Damaging are They?](#)

Japan has tried what the Fed is doing now for over a decade, with no results.

Yet, Powell hell bent on producing more than 2% inflation until the strategy "works".

I discuss numerous ways Powell is on the Bank of Japan's path in [Is the Fed Blindly Following Failed Policies of the Bank of Japan?](#)

What Would I Do?

For the answer, please see [Reader Question: What Would I do Differently Than the Fed?](#)