THE HILL

Economists say inflation fears overblown

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By Peter Schroeder - 07/08/14 06:00 AM EDT

Economists see little risk of a surge in inflation, despite mounting evidence that the American economy is rumbling to life.

Recent economic data have shown the employment picture improving more quickly than expected, with jobs being added at a pace of nearly 300,000 a month — the magic number that economists say would be needed to bring down the nation's stubbornly high unemployment rate.

Along with the quickening job growth, consumer prices have been rising at a rate not seen in months.

That combination could indicate the U.S. is nearing an era of higher inflation — an outcome critics of the Fed say is bound to arrive sooner or later.

"The question isn't if inflation occurs, it's when," said Rep. Kevin Brady (R-Texas), chairman of the Joint Economic Committee.

But economists say that beneath the headline numbers, there is little to suggest the country is at risk of seeing the kind of runaway inflation that helped drive former President Jimmy Carter out of office.

"Inflation has picked up slightly over the past few months, but it still remains very low, still remains below the Fed's target," said Gus Faucher, senior economist at PNC Bank. "I don't see any indication it's going to get above that target in the next year or two."

In June, the Labor Department reported its Consumer Price Index was up 0.4 percent in May, the largest one-month increase since February 2013. And in the past year, prices were up 2.1 percent — just a hair above the Fed's 2 percent target.

Core inflation, which removes more volatile food and energy prices from the equation, was up 2 percent in the last year.

However, the Fed's preferred way to measure inflation, the Commerce Department's Personal Consumption Index, was up 1.8 percent in the last year — an increase from previous numbers but below the central bank's target for the 25th straight month.

The quickening pace of the price increases comes at a time when employment data is raising hopes of a lasting recovery in the economy.

The Labor Department reported on Thursday that the government added 288,000 new jobs, the fifth straight month of gains exceeding 200,000 jobs. The jobless rate has fallen half a percentage point in the first six months of the year, to 6.1 percent, faster than most analysts had expected.

Persistently high unemployment has long been a major concern for the Fed, while inflation has presented less of an issue; it has lingered below the Fed's ideal level since the financial crisis. Bank officials were more concerned with deflation during the recovery because price growth was so stagnant.

Fed Chairwoman Janet Yellen said at her most recent press conference that the Fed could act to raise rates sooner if the economy was growing faster than it predicted. But she downplayed the recent increase in inflation data as more of a fluke than a trend.

"The data that we're seeing is noisy. I think it's important to remember that, broadly speaking, inflation is evolving in line with the committee's expectations," she said.

Economists say there is little risk of the Fed creating runaway inflation because the major drivers of spiking prices are not there. Specifically, experts say rapid inflation usually is driven by strong wage growth, because employers have to increase the prices of their goods and services to continue paying a competitive wage.

Wage growth has been relatively flat, and many believe the labor market would have to improve substantially before prices would start to rise.

"When inflation creeps in, it's usually due to the demand for goods and services being increased because employers are having to pay more wages," said Jay Morelock, an economist at FTN Financial. "That is just absolutely not in the data. ... We see that nowhere."

Critics of Fed policy are still pushing for the central bank to act as quickly as possible to wind down its stimulus. The bank is gradually shrinking the size of its monthly bond purchases that make up "quantitative easing," but has emphasized it might not raise rates for some time after those purchases wrap up.

Brady and other GOP lawmakers say the Fed needs to act more aggressively to exit stimulus and hike rates.

"I'm convinced the sooner the Fed refocuses on inflation, the stronger foundation we have for our economy," Brady said. "We don't have anything to fear from normalizing our interest rates."

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