



November 18, 2021
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VIRGINIA'S ECONOMY

BY THE NUMBERS

All About Inflation

- What is inflation, anyway?
- What is causing high inflation rates?
- Why do we care?
- What should we expect in the future?



What is
Inflation?

Inflation

- **Inflation** is a measure of how fast prices are rising
- Measured monthly by the Bureau of Labor Statistics
- Calculated as the year-over-year change in the **Consumer Price Index**

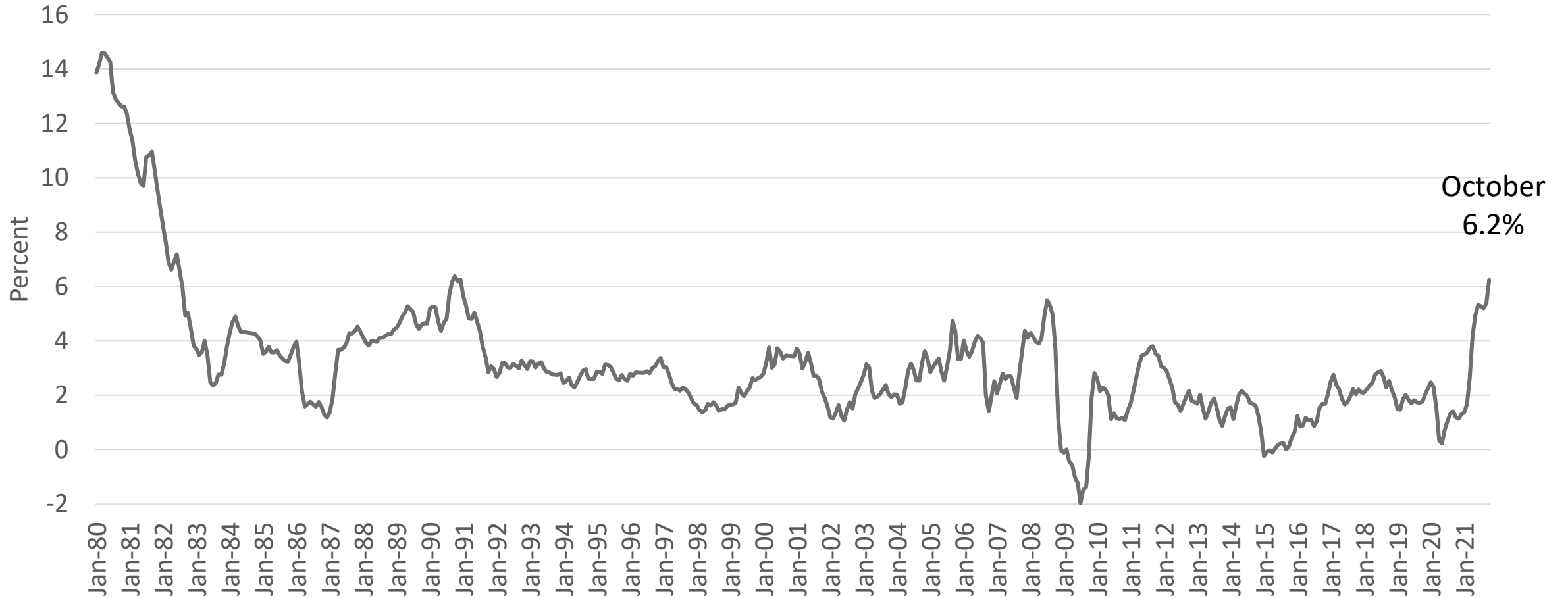
Included in the Consumer Price Index

- Food and beverages
- Utilities
- Clothing and footwear
- Appliances and electronics
- Transportation
- Medical care
- Recreation
- Personal services
- Education
- Shelter

Shelter includes 1) rent for current tenants and 2) homeowners' equivalent rent
Shelter does NOT include 1) rent increases for new tenants and 2) home prices

Inflation Rate

1980-2021



Source: U.S. Bureau of Labor Statistics. Inflation is measured as the year-over-year change in the Consumer Price Index (CPI).

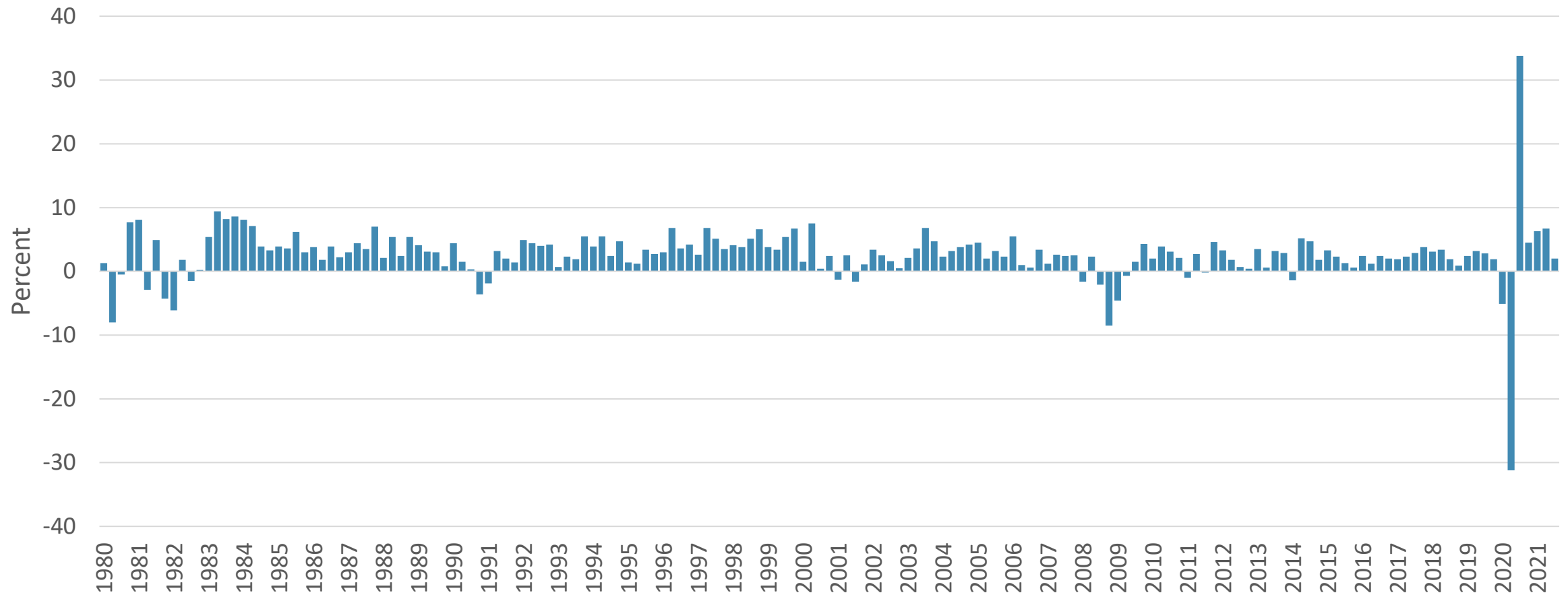
A group of people, including men and women, are standing on a train platform. They are holding various shopping bags, such as a pink one, a grey one, and a brown one. A large white banner with a torn edge is superimposed over the center of the image, containing the text "What is Causing High Inflation?". The background shows a train platform with a metal railing and a blue handrail.

What is Causing High
Inflation?

Higher Demand + Lower Supply = Higher Prices

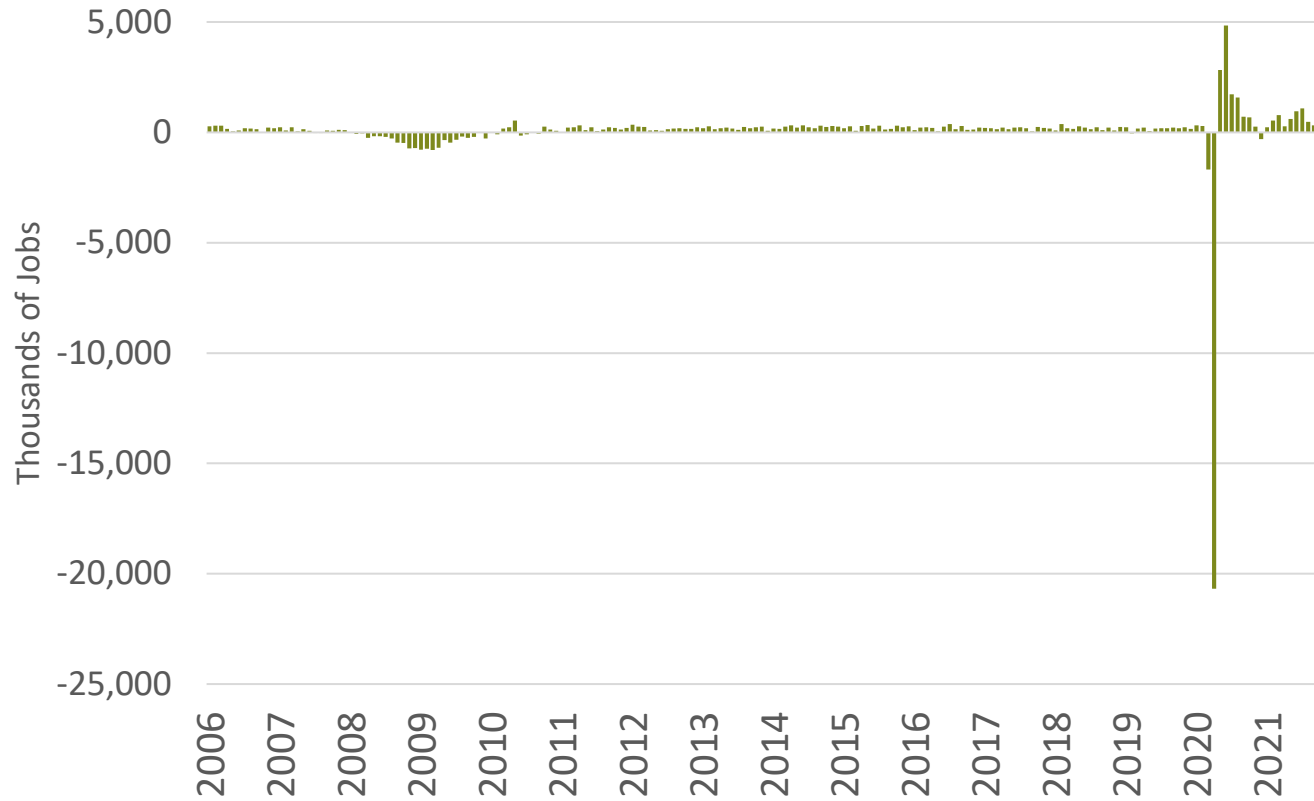
The Economy was Slammed by the COVID-19 Pandemic but is Recovering

Gross Domestic Product, Annualized Percent Change

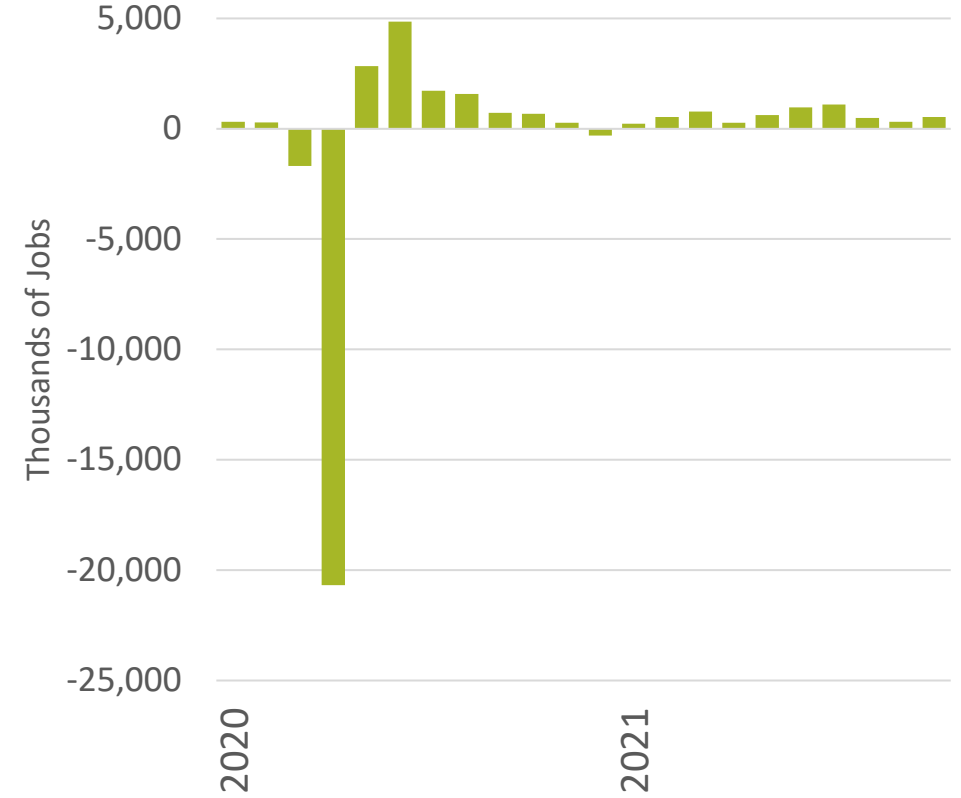


Jobs are Being Added

Monthly Job Change

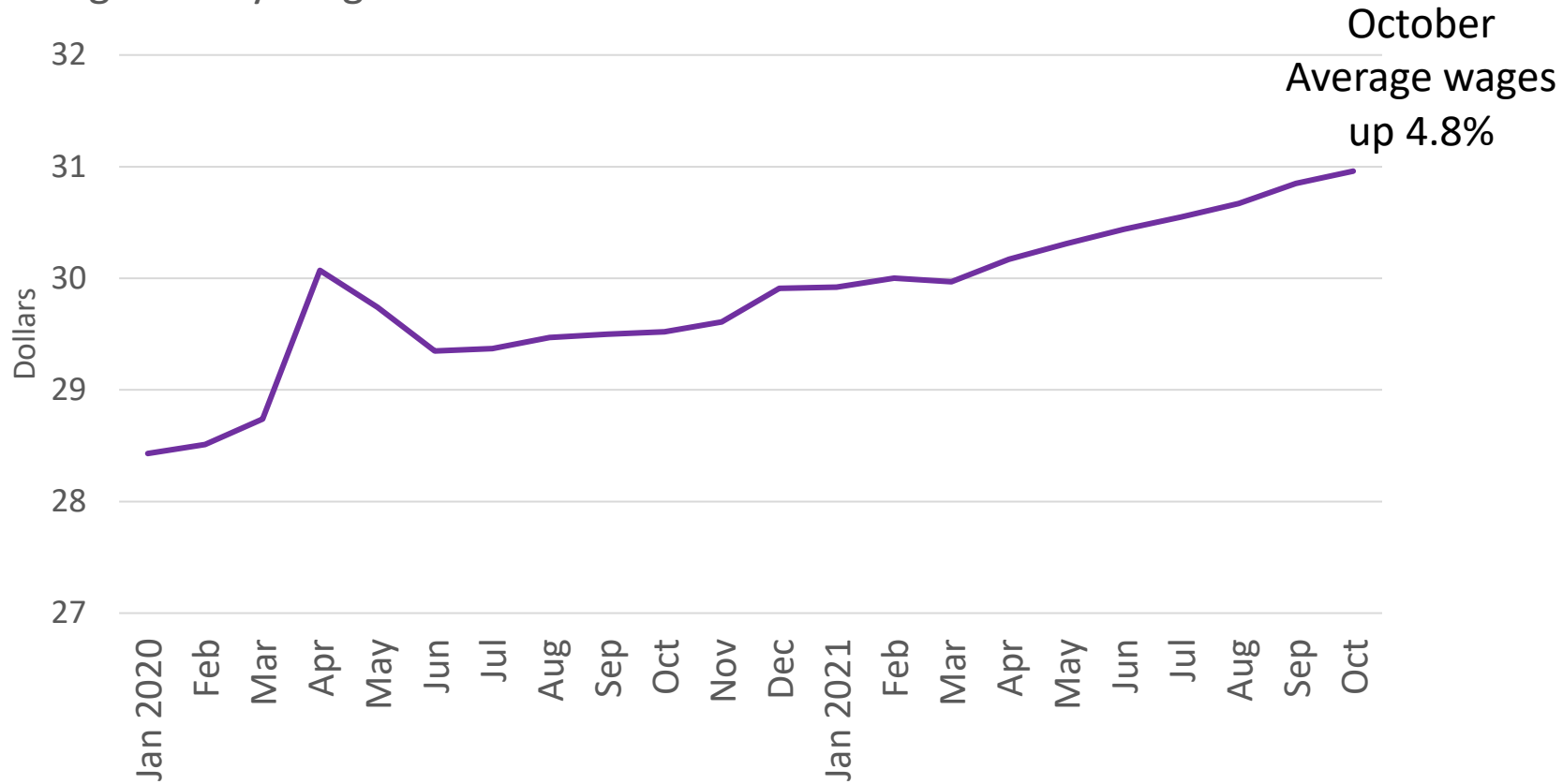


Monthly Job Change

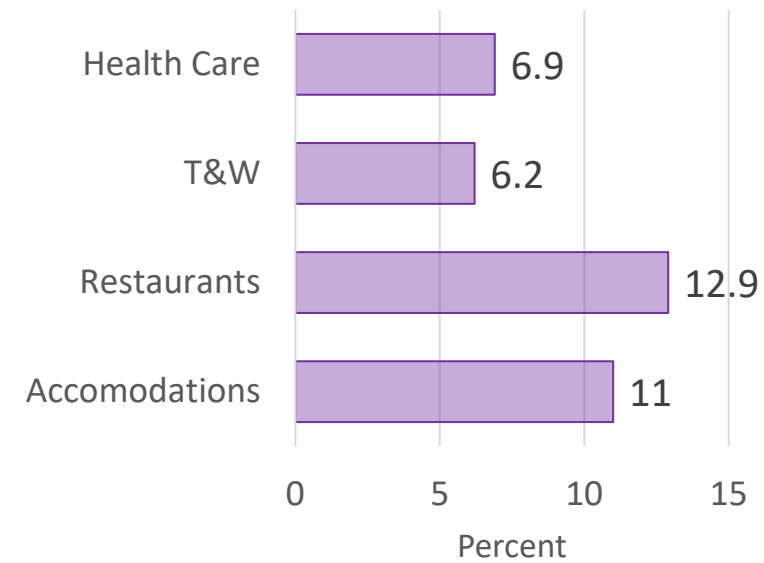


Wages are Rising

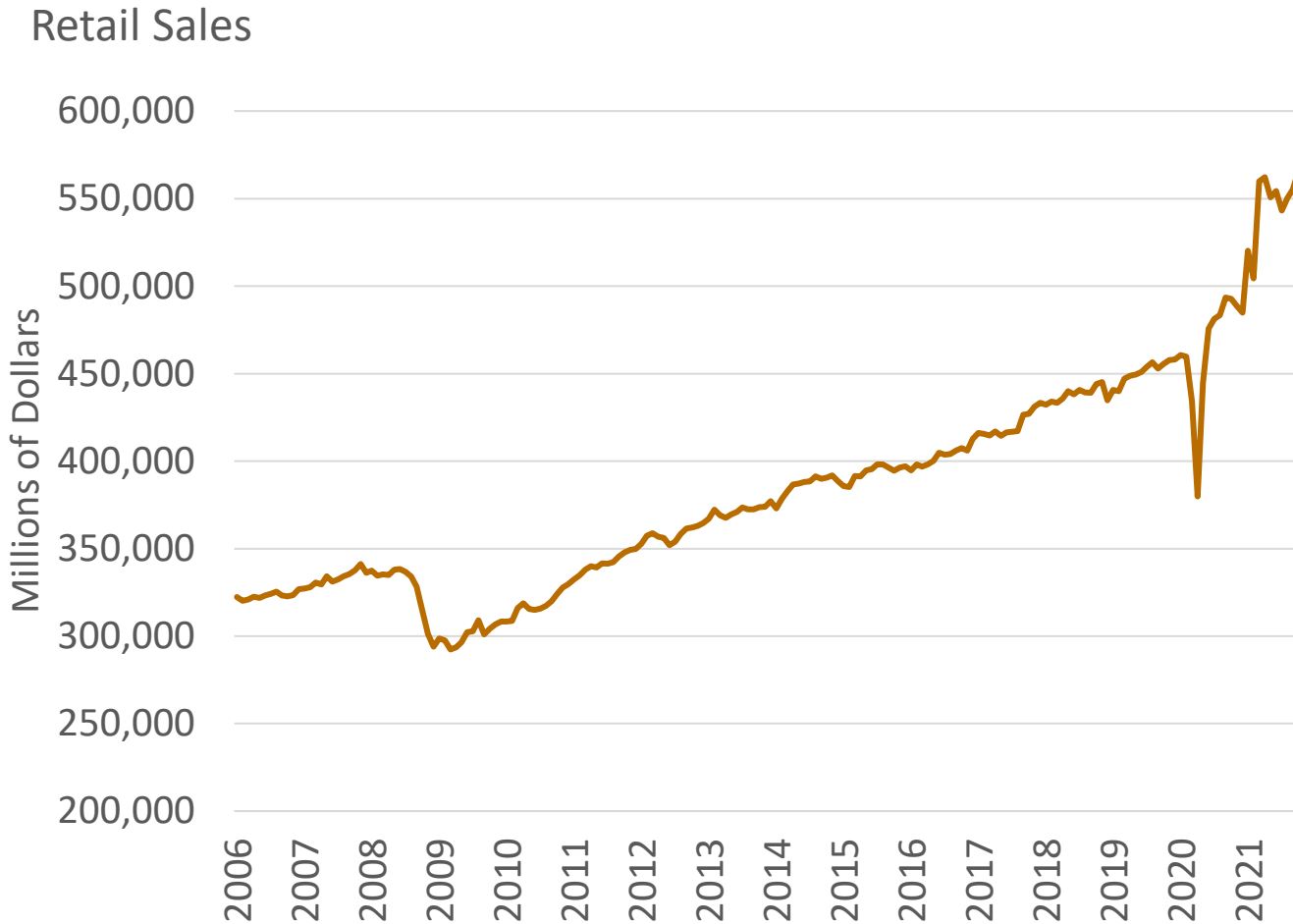
Average Hourly Wage



October Wage Growth

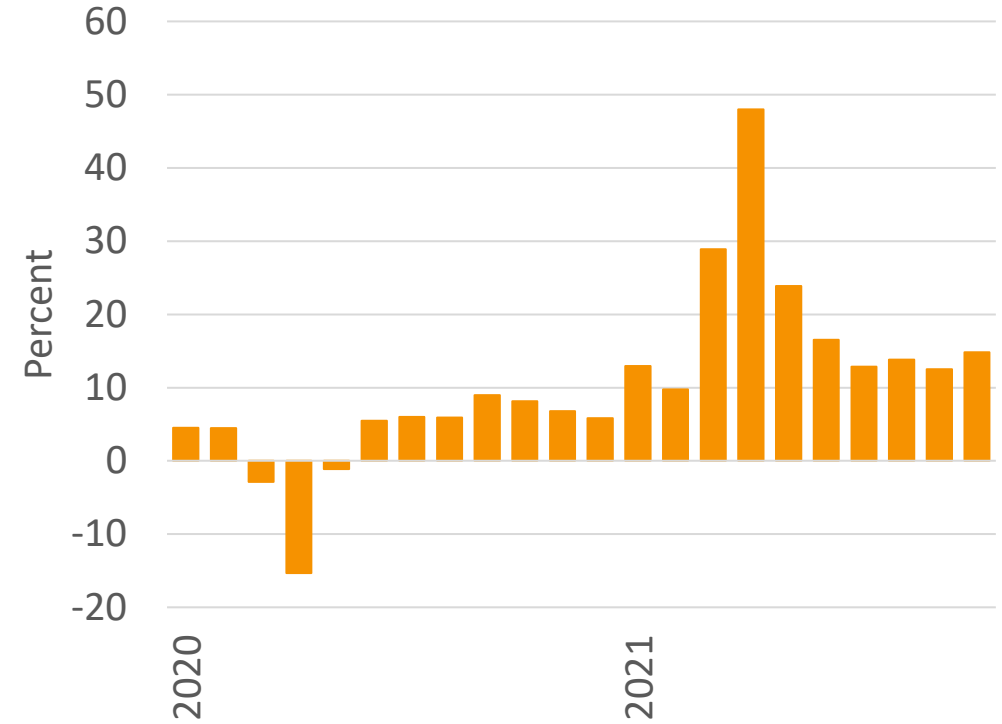


People Are Spending



Source: U.S. Census Bureau. Retail Trade minus food services.

Retail Sales, Annual Change



Category	Increase in \$ Sales from Oct 2020
Gas Stations	+47%
Clothing Stores	+26%
Electronics & Appliance Stores	+18%
Furniture Stores	+12%
Motor Vehicle & Parts Dealers	+12%

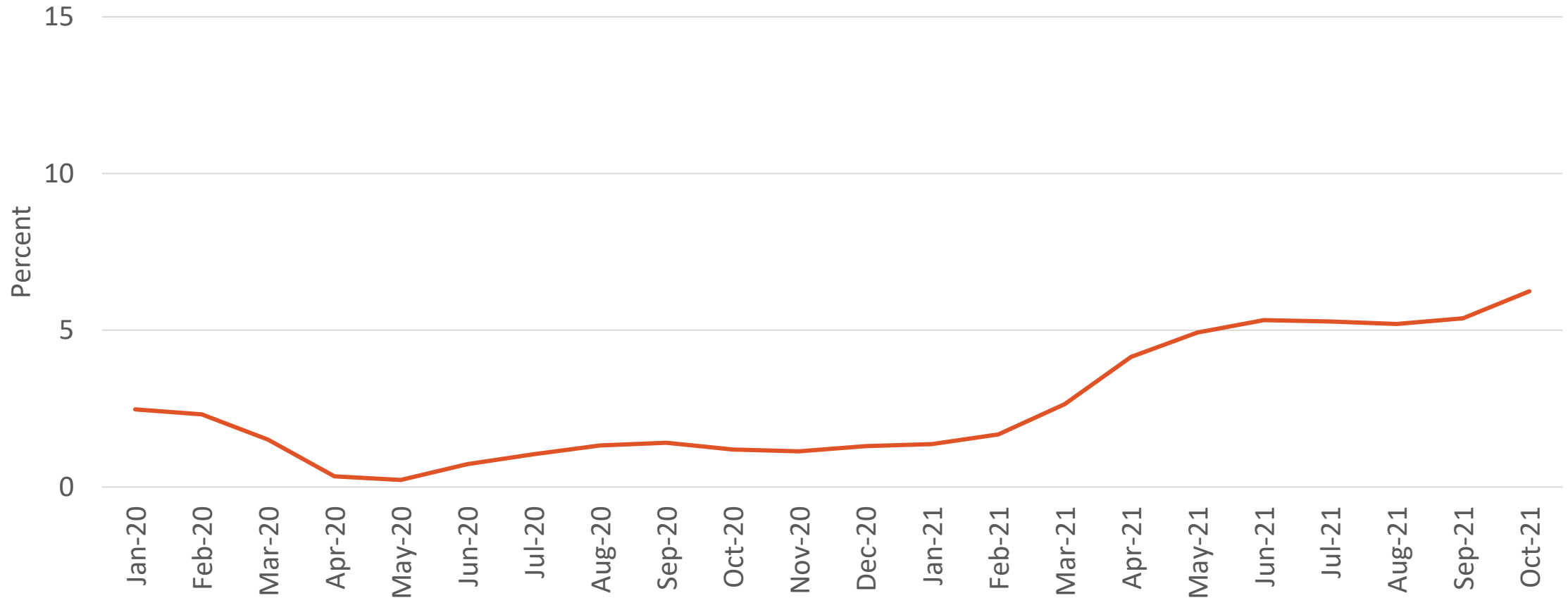
There Are Major Challenges on the Supply Side

- Overseas manufacturing delays
- Labor shortages
- Bottlenecks at major ports

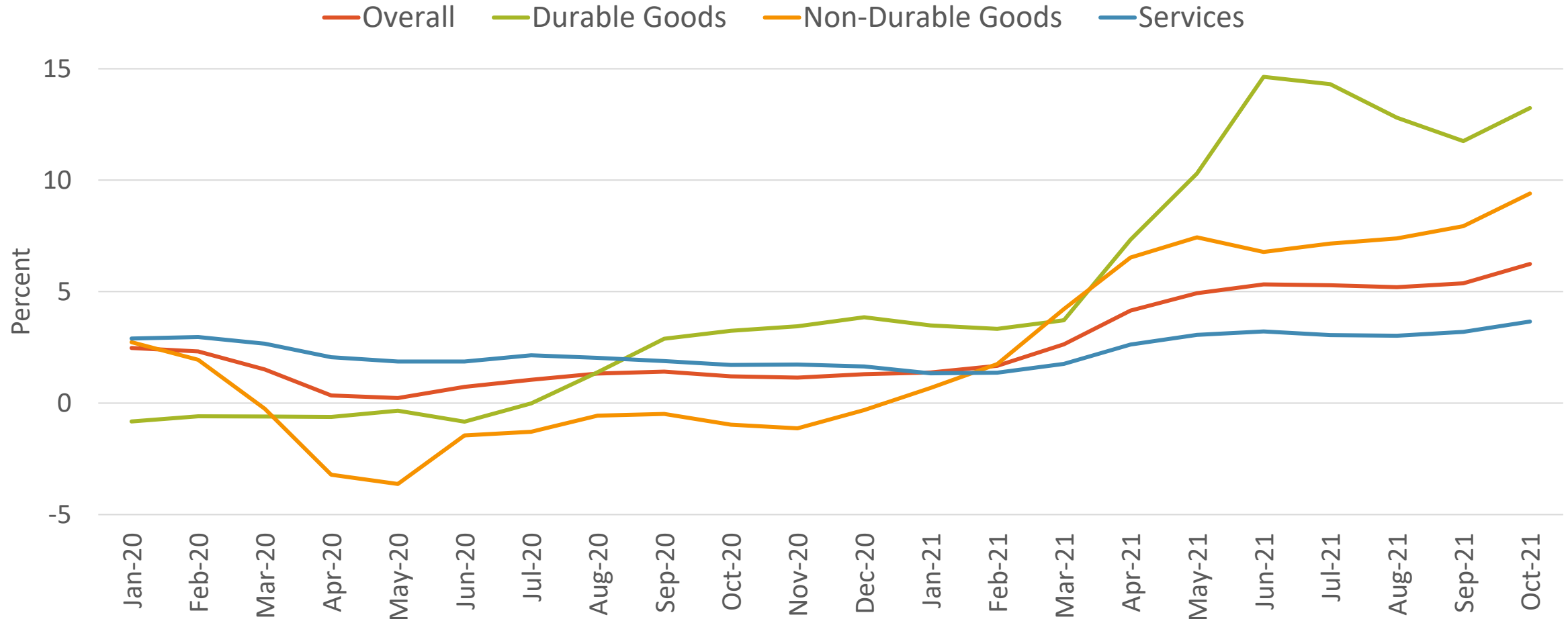


High Demand + Low Supply = Rising Prices (Inflation)

Inflation Rate

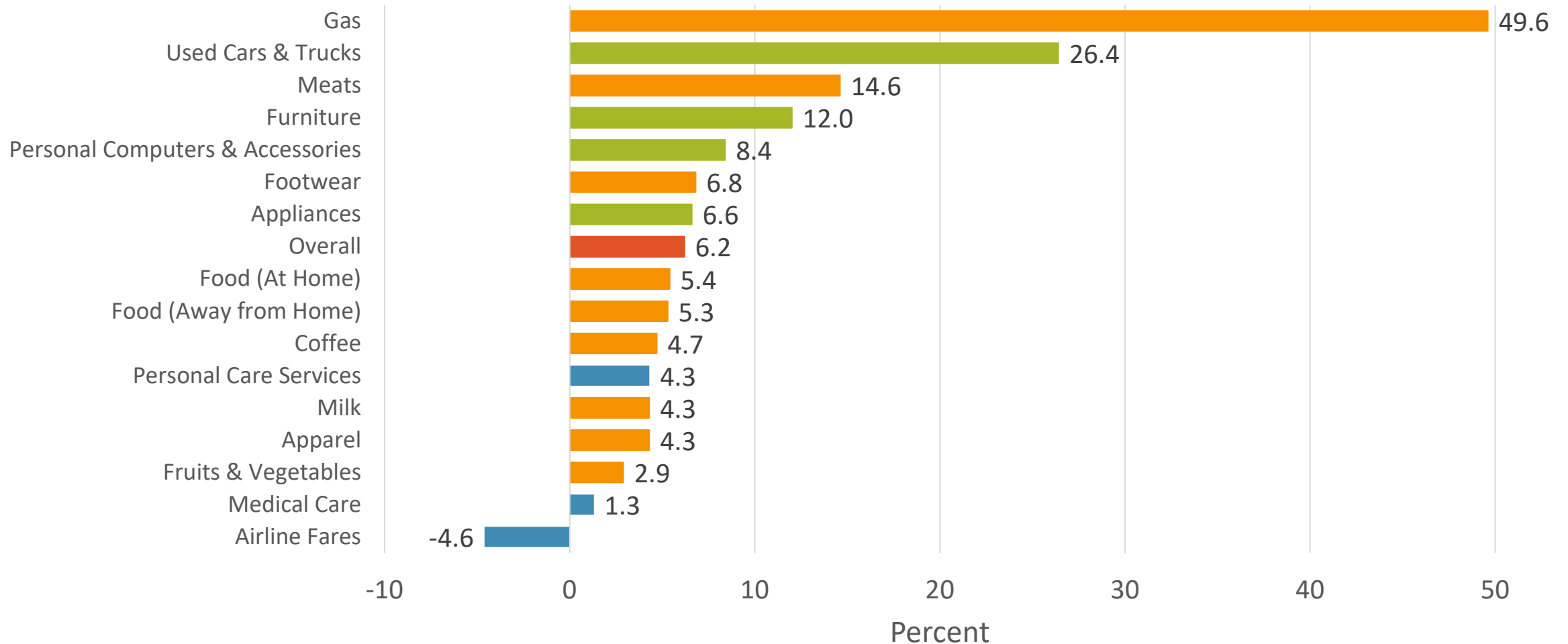


Prices Are Rising Faster for Goods Than for Services



Prices Are Rising for Most—But Not All—Goods and Services

Price Change, October 2020 to October 2021





Why do we
care about
high inflation?

Families Are Having to Watch Their Budgets More Closely

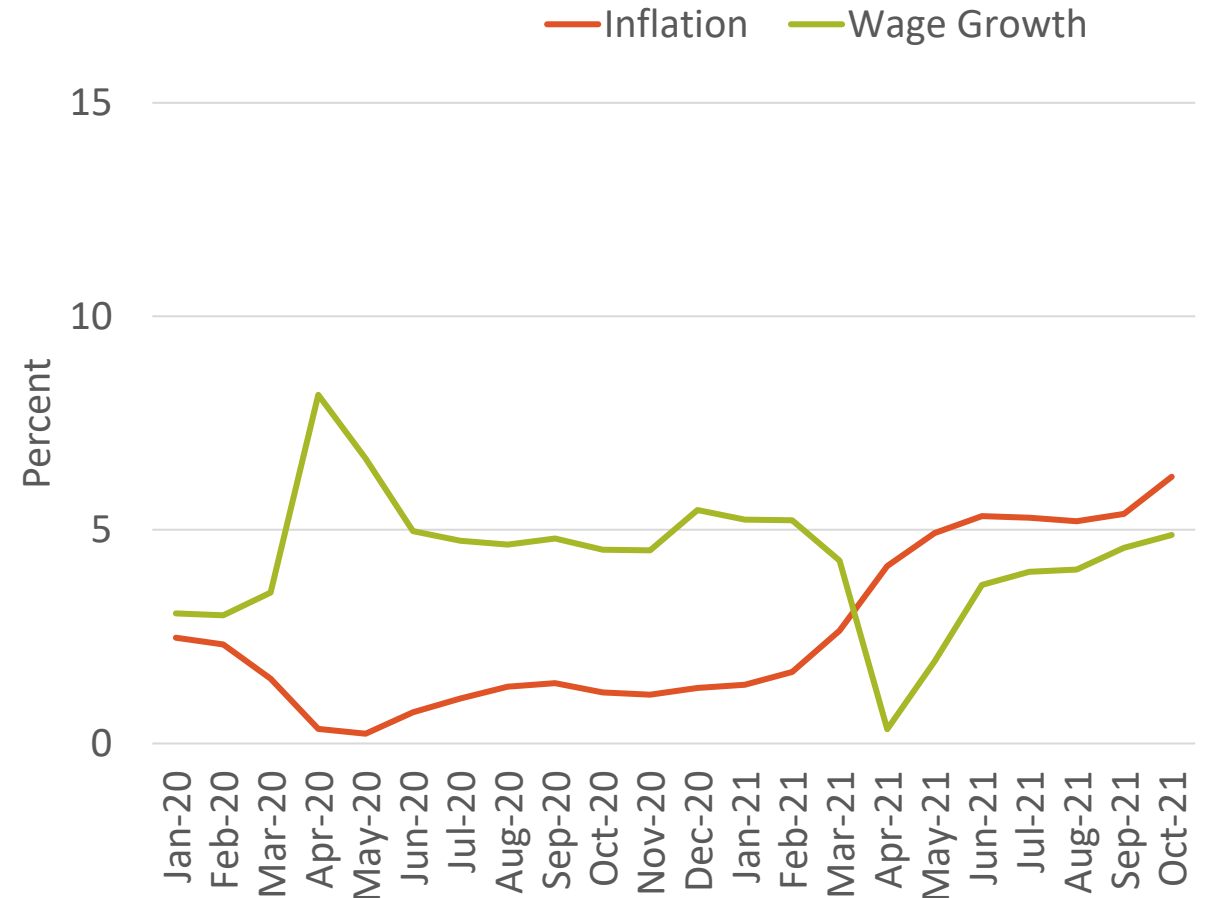
MONTHLY COSTS

2 adults *and* 2 children
Richmond metro area

🏠 HOUSING	\$1,042
🍌 FOOD	\$807
👨‍👩‍👧‍👦 CHILD CARE	\$1,272
🚌 TRANSPORTATION	\$1,156
🏥 HEALTH CARE	\$941
🛒 OTHER NECESSITIES	\$746
🔄 TAXES	\$983
MONTHLY TOTAL	\$6,947
ANNUAL TOTAL	<u>\$83,370</u>

Source: Economic Policy Institute

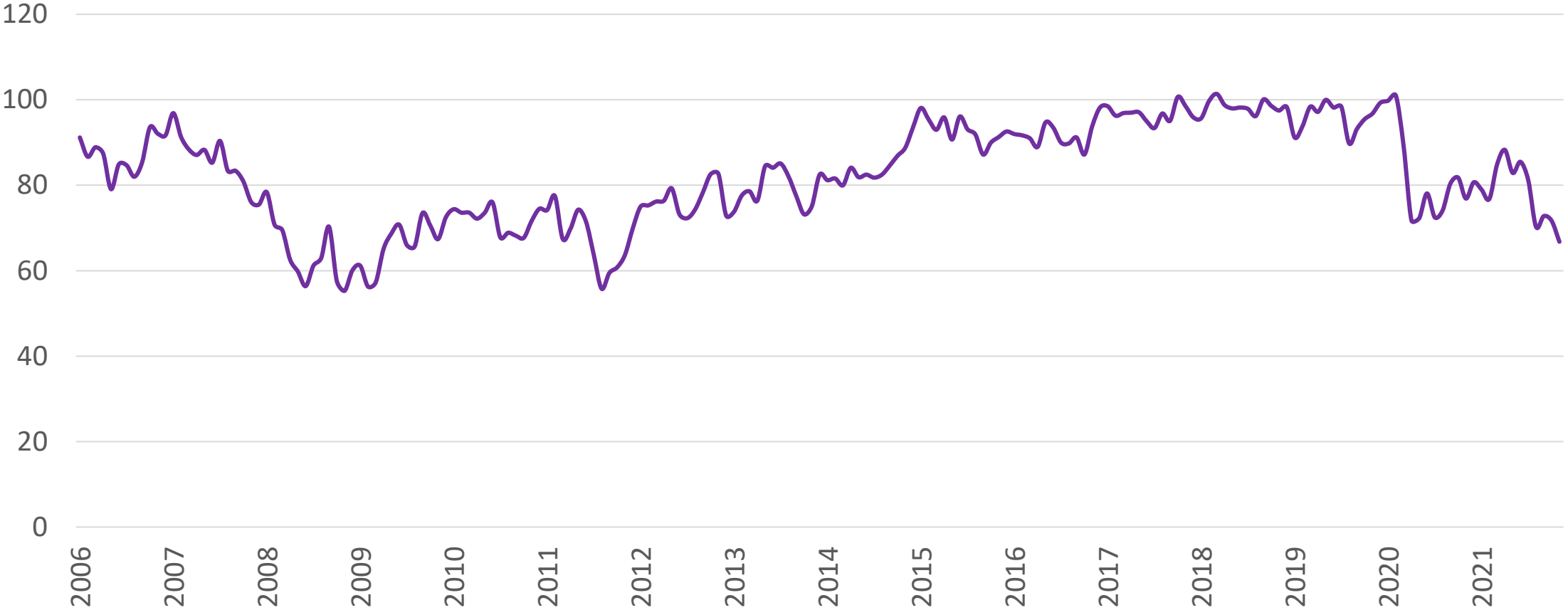
Price and Wage Growth



Source: U.S. Bureau of Labor Statistics

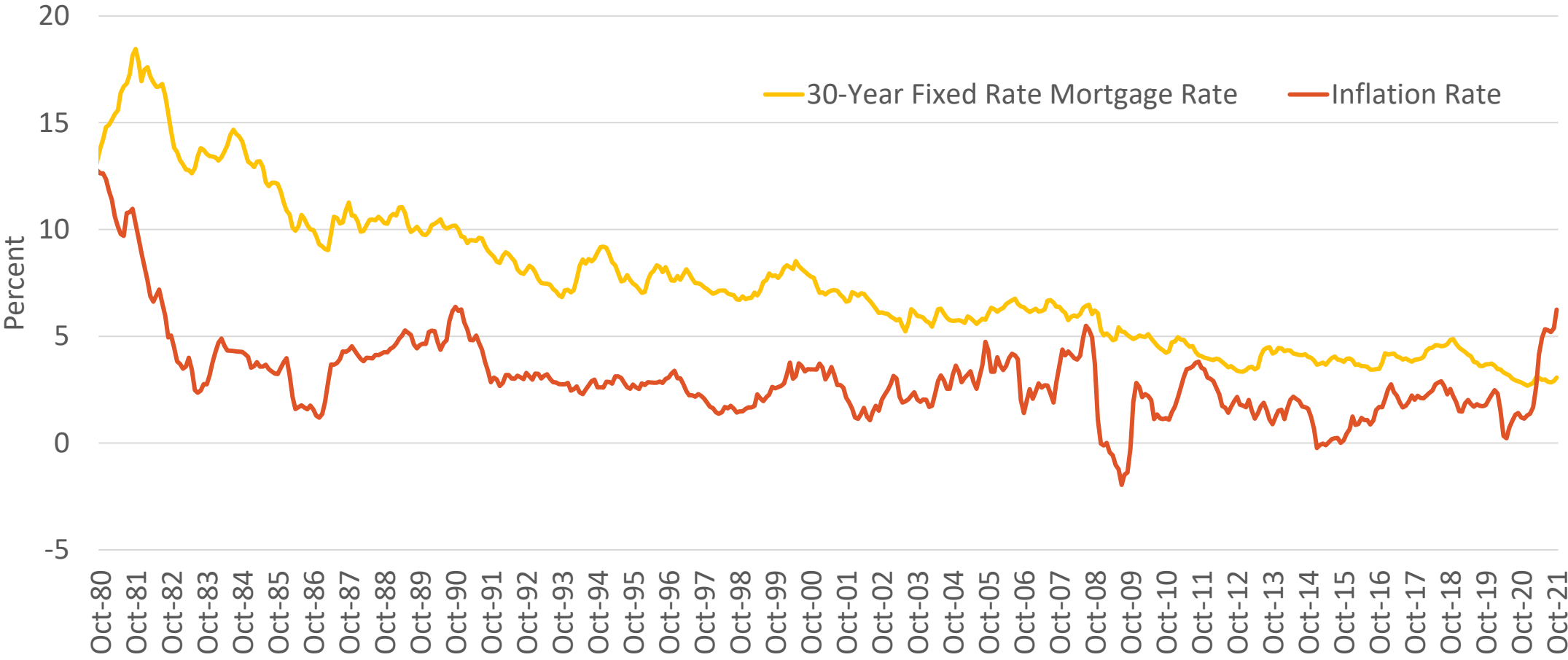
And They are Worried

Consumer Sentiment



Source: University of Michigan

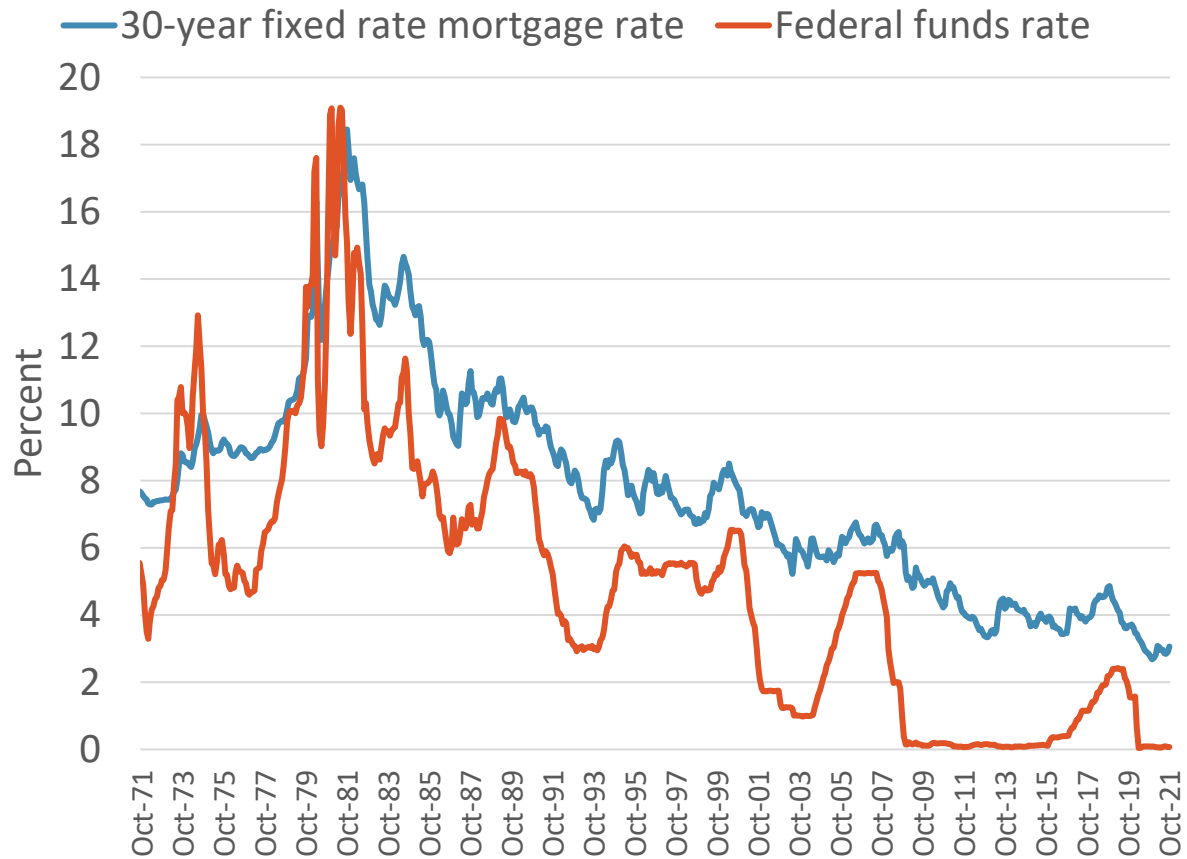
Mortgage Rates Will Likely Rise



Source: Freddie Mac, U.S. Bureau of Labor Statistics

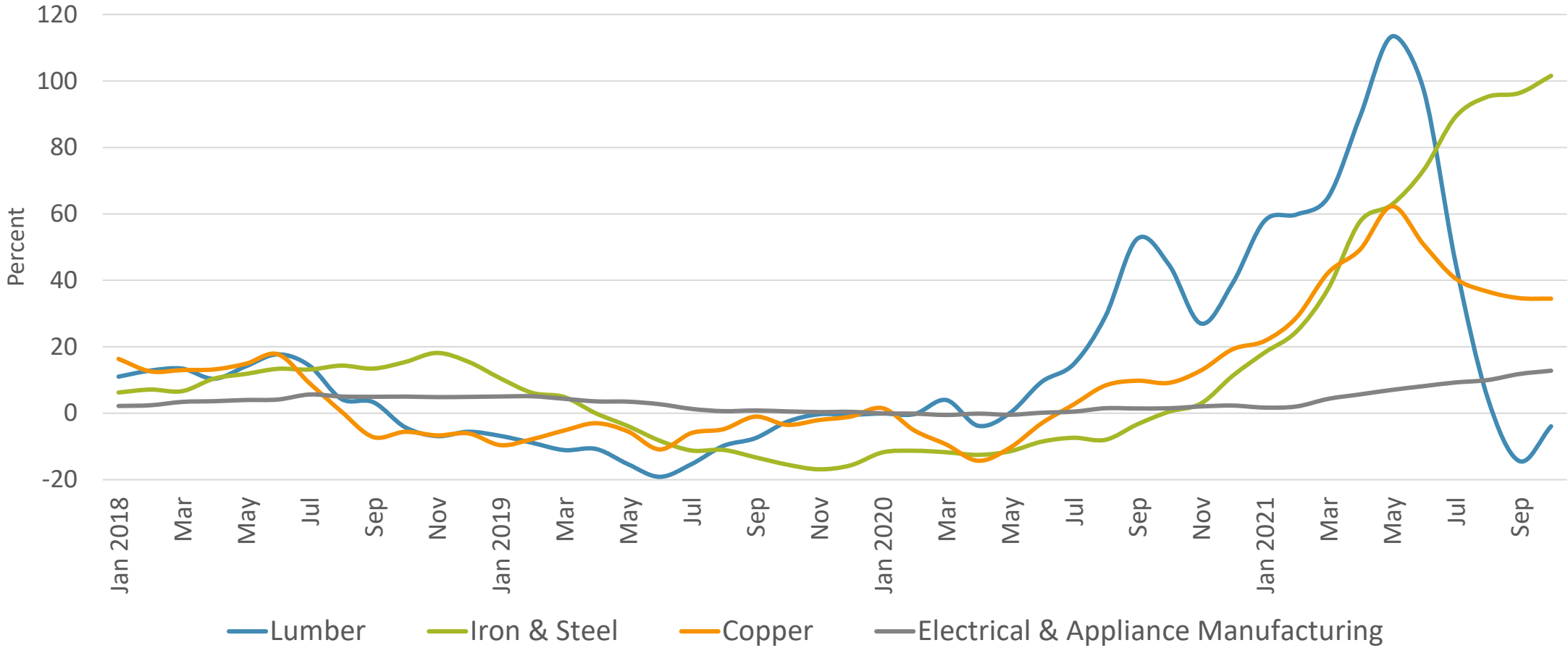
The Fed could increase the federal funds rate

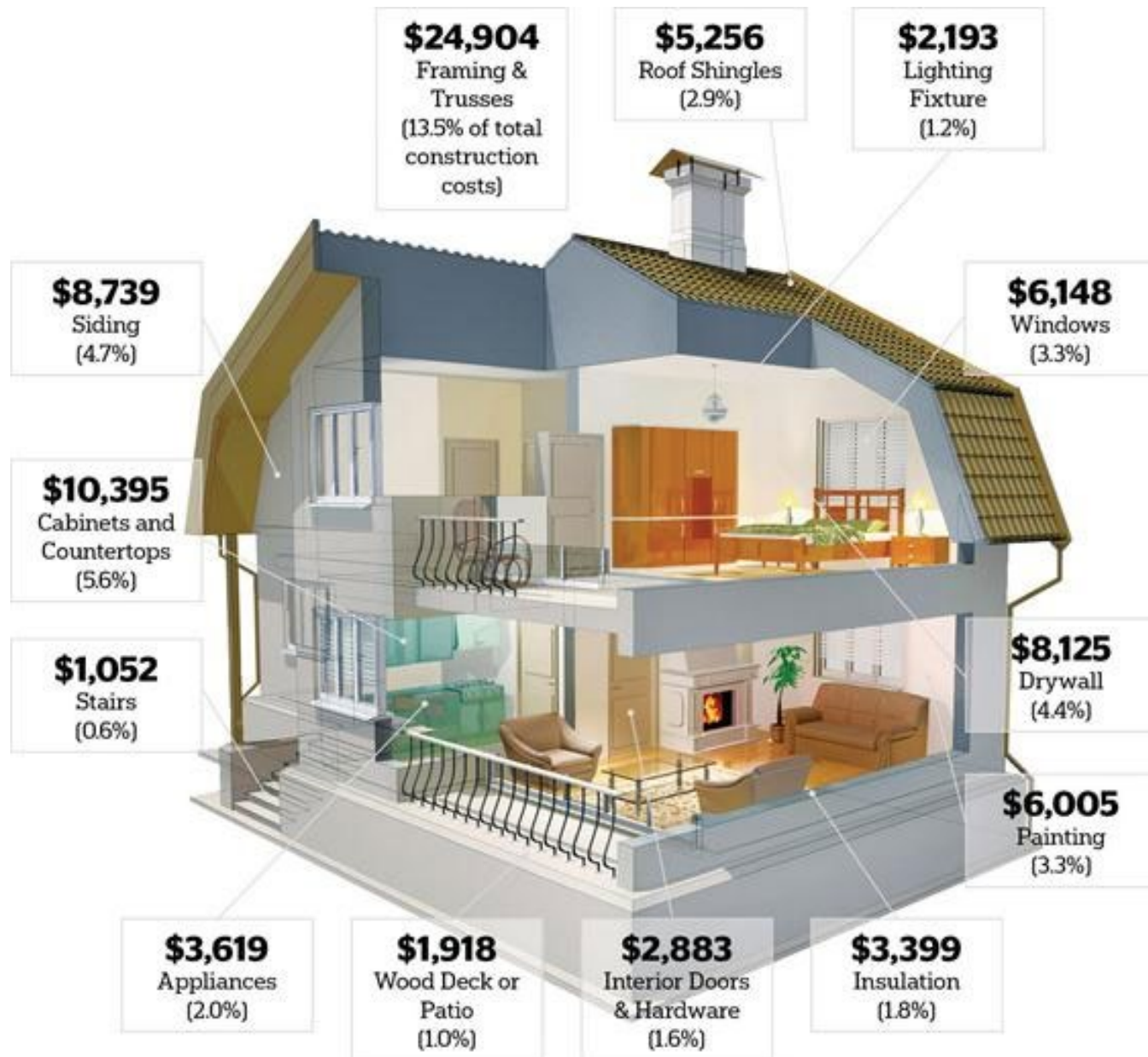
The Fed will slow its bond purchasing



The Cost of Construction is Rising

Change in Producer Price Indices





How Much Does it Cost to Build a New Home?

2,311 square foot home
 Sale price of \$310,619

\$184,125 for construction costs
 \$67,551 for lot
 Remainder for financing, overhead,
 marketing sales commission, and
 profit



What should we
expect in the
future?

Transitory Inflation

- A period of high inflation that is brief or short-lived.
- Prices rise because of pent-up demand and supply chain lags.
- Does not mean prices will fall.

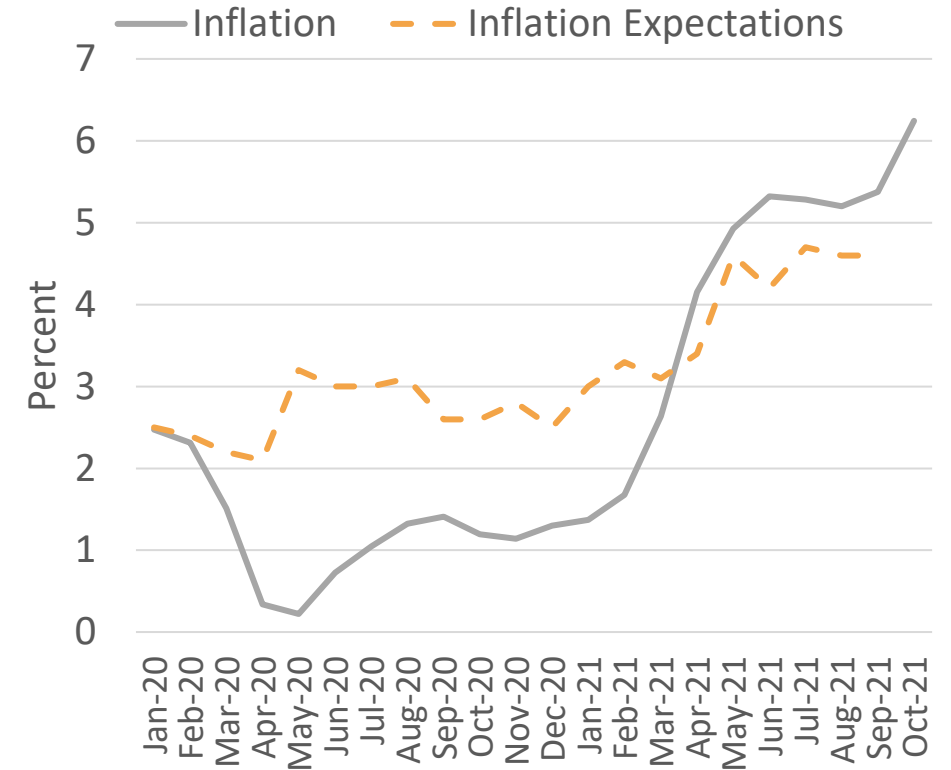
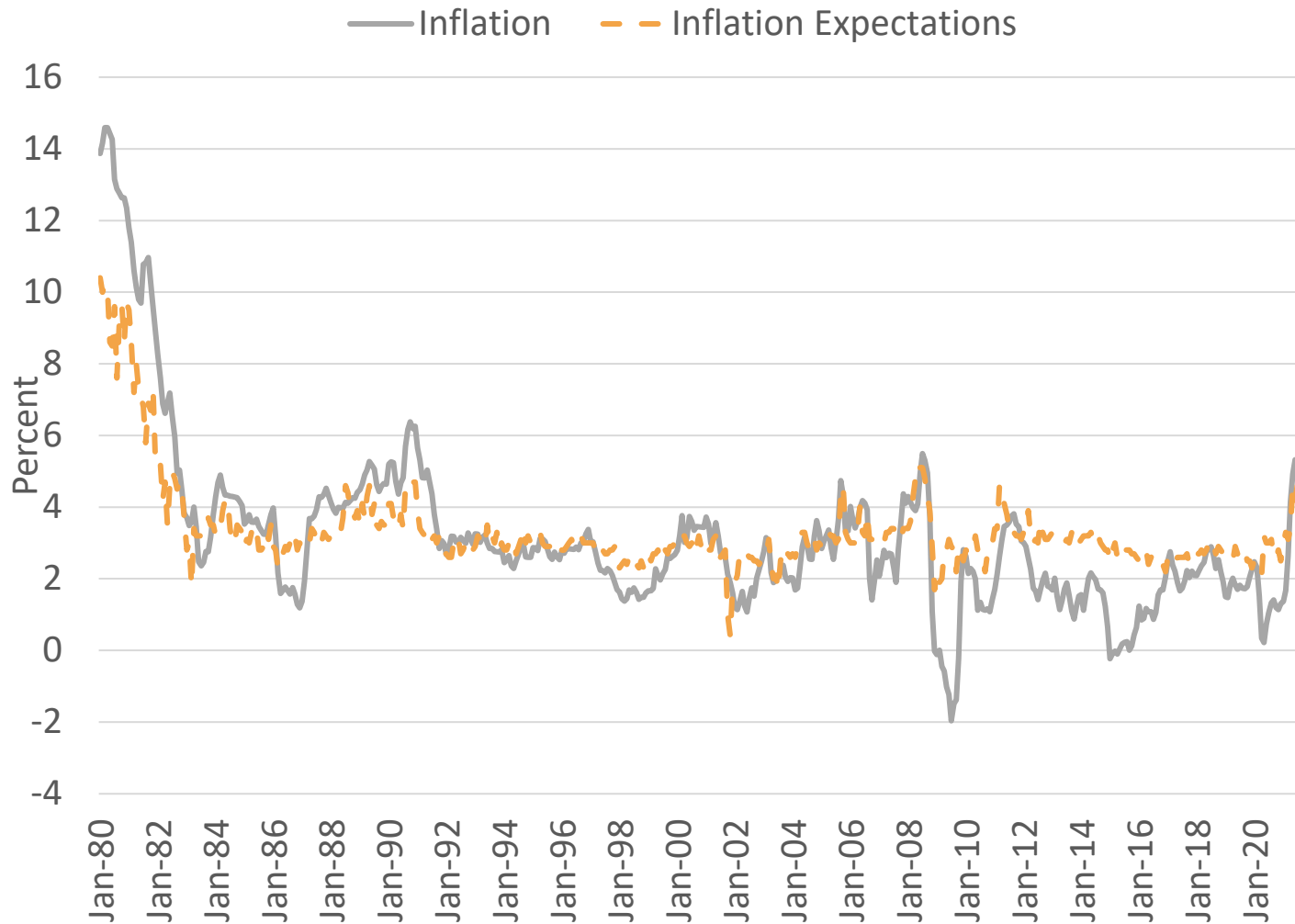
Expected Inflation or the Wage- Price Spiral

- Consumers expect prices to rise, ask for wage hike.
- Producers raise prices in response to wage increases.

Structural Inflation

- Inflation that results from changes in the structure of demand and supply.
- Rigidity in supply side that is unable to keep up with expanded or changing demand.

Inflation Expectations



Inflation Forecasts



Inflation Forecasts

- Today's inflation is caused by a **much more complex** set of factors than during previous inflationary periods.
- Rising employment costs and **labor** challenges are increasing expectations for inflation.
- **Supply chain bottlenecks** will persist until well into 2022.
- Rising prices in the **services sector** could be the next driver of higher inflation.
- **Rising rents and home prices** will ultimately also be working their way into the inflation calculations.
- However, the **end of federal stimulus payments** could dampen the surge in consumer spending.
- Inflation that is not transitory will lead the Federal Reserve to **raise interest rates** to cool price growth.

Inflation May be “Transitory” But Transitory Could be Well into Next Year

High inflation will ease when the pandemic-induced bottlenecks are resolved.

Overall Economic Outlook

- The complexity of the pandemic-fueled recession makes it difficult to forecast how the recovery will play out.
- Risks associated with the coronavirus appear to be easing, as vaccination rates are rising and COVID cases are falling.
- Economic fundamentals remain strong with increases in both employment and wages.
- Demographic trends favor a rebounding of labor force participation rates, as well as home buyer demand.
- The nature of work—including the what, the how, the why, and the where—have changed as a result of the pandemic.

Have Questions or Need More Info?

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