THOUGHTS FROM THE FRONTLINE

The Inflationista Illuminati

By John Mauldin | March 15, 2025

Propagating Price Pressure Plotting
Dallas, Palm Beach, Washington, DC, and More

Last week we published a chart of the Atlanta Fed's GDPNow model, which had just dropped sharply to a -2.4% real GDP growth forecast for the first quarter of 2025. This model can be volatile. Its latest big swing was mostly an artifact of spiking gold imports. Economic growth prospects do seem to have dimmed considerably, though.

My friend Danielle DiMartino Booth follows data like a hawk. Many of you are familiar with her. Today I'm sharing her recent essay showing that inflation may be a lot lower than the current headline suggests. I was talking with David Bahnsen last night. We both agreed that the way the BLS calculates inflation, especially the lag in housing reporting, makes inflation appear artificially high. Danielle's work really hits that home.

Danielle's piece is long enough that I will make a two-part series from it, with my comments next week. There is a great deal of data here, but I strongly suggest you read carefully and think about it. Understanding *actual* inflation – instead of what the media's narrative tells you it should be – is critical to your investment planning. It is one thing for a pundit to say this or that, but it is another to look at the actual data for yourself.

And so with that, I will turn this letter over to Danielle's capable hands.

Propagating Price Pressure Plotting *by Danielle DiMartino Booth*

**“Please allow me to introduce myself
I’m a man of wealth and taste
I’ve been around for a long, long year
Stole many a man’s soul and faith”**

—*Sympathy for the Devil*, by The Rolling Stones

Whoever controls the narrative… Such was the unoriginal thinking that drove a professor of law at the University of Ingolstadt, Bavaria, to hatch a secret society he called the Orden der Illuminati. In Adam Weishaupt’s mind, to be among the “Illuminated Ones” raised one above the muck of the monarch’s and especially the church’s brainwashing. And so it began in 1784, in a nearby forest. There, bathed in torchlight, five men crafted the rules of admission with the proviso that all candidates be of the highest societal standing, men of “wealth and taste,” to quote Mick and Keith in what many, myself included, agree is one of the best songs of all time. And like the iconic lyrics, seen to glamorize the darkest of figures, the Illuminati were castigated as atheists and anarchists.

No surprise, because the Orden der Illuminati was forced to disband under the threat of the death penalty, a reverent following has been sustained forever more. The allure of a “world-dominating” cabal was too perfect for those prone to fomenting conspiracy theories. The rise of social media couldn’t help but fuel the romantic idealism inherent in the battle against the evil elite, a war that continues to recruit soldiers enraged by the seemingly unstoppable widening of the inequality gap.

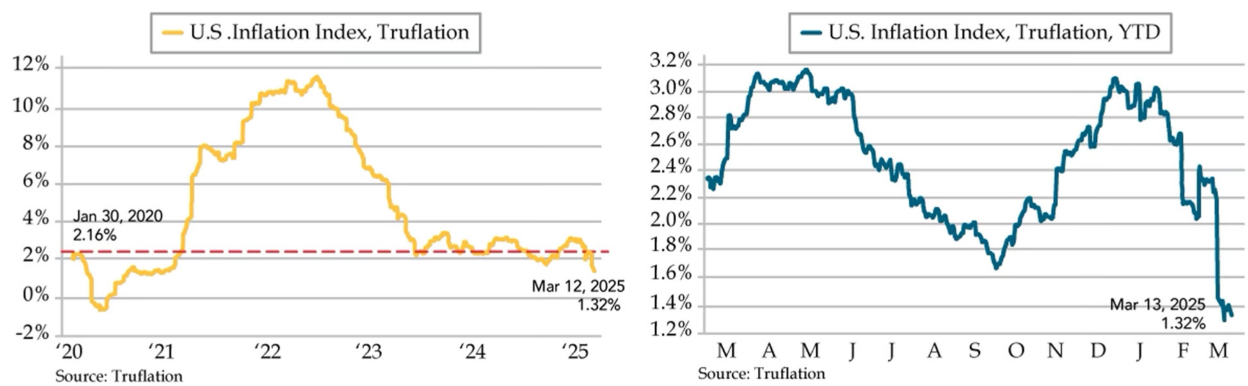
And then came Biden. As reported in *The Week* last November after the US presidential election had been decided, four years ago: “Joe Biden unwittingly fanned the conspiracy theory flames when he referred to a coming ‘new world order’ during a speech. ‘He was referring to the shifting sands of geopolitical relations in response to Vladimir Putin's invasion of Ukraine,’ said *The Independent*. However, for conspiracy theorists, such comments are seen as further evidence that there is a ‘puppet-master overlord, hell-bent on global domination and busy manipulating international events to achieve his villainous ends.’”

And while historic luminaries including David Rockefeller, Henry Kissinger, Jacob Rothschild, and Queen Elizabeth II were among those rumored to be members of the Illuminati, it’s been performers who’ve done the heavy lifting in growing its cultlike status. Those linked to the movement include Madonna, Kim Kardashian, Beyoncé and her husband Jay-Z, Rihanna, and even Taylor Swift. As *The Week* added, “Katy Perry once told *Rolling Stone* the theory was the preserve of ‘weird people on the internet’ but said she was flattered to be named among supposed members: ‘I guess you’ve kind of made it when they think you're in the Illuminati!’”

In our world, those deemed shrewd enough illuminators to "make it" talk their books. As countless can attest, successful trades need not be grounded in fact when accessorized by the financial media and a convincingly credible sell side. If the bonanza wasn't bountiful enough, supported as it is by this cast, an unwitting ally in the Bureau of Labor Statistics further amplifies the narrative's windfall.

But what of the truth about inflation? Last year, the founders of Truflation granted QI access to their full history of real-time daily inflation prints harvested using blockchain technology to collect and analyze 18 million data points from more than 60 data providers. The output was a .97 correlation with the headline US consumer price index (CPI). Per Truflation, on a time continuum, their metric tells you with near-perfect accuracy where the CPI will be 45 days hence. There was thus no irony in TJM Institutional Services' Mark Gomez sharing first thing this morning that Truflation had printed at 1.32%, down from 2.70% when Federal Reserve policymakers last convened on January 31.

The Truth About Inflation Via Truflation



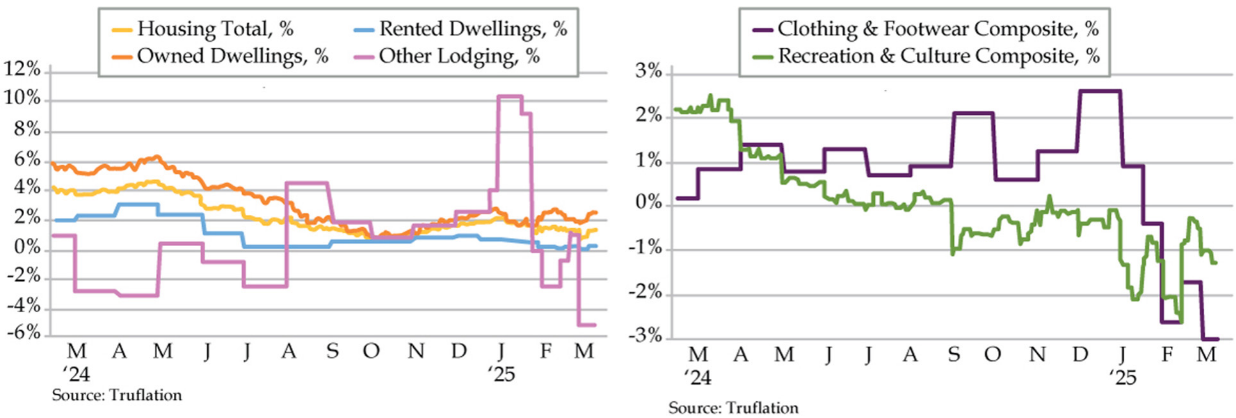
Source: Quill Intelligence

Zoom into the more recent history of Truflation and you can see that as recently as mid-December, the year-over-year (YoY) rate was as high as 3.11% on December 14. Understanding the drivers of both the upward and subsequent downward pressures to land at today's 1.32% YoY is key to appreciating the simplicity of what's played out in the CPI with a lag.

Note the lilac line in the left chart—Other Lodging. The first days of the last six Januarys have been marked by my traveling to Los Angeles to film DoubleLine's Annual Round Table. The difference this year was that the neighborhood of Pacific Palisades was on fire and evacuated when I landed at LAX on January 8. On that day, Truflation hotel inflation peaked at 10.38% YoY. Can a mass evacuation press up hotel inflation nationwide when it occurs in the nation's sixth-largest hotel market? Though that was a rhetorical question, the visible spike and retrenchment in hotel prices as residents found longer-term solutions or, in the case of the lucky ones, were able to move back to their homes is clearly visible. As of today, hotel prices are in outright deflation, at -5.32% YoY. Note also that Rented Dwellings saw their fastest pace of price appreciation of 3.08% YoY last April and are now flirting with deflation, at 0.30% YoY.

In the righthand chart, you see evidence writ large of the decimation of discretionary spending. After a last hurrah to mark the holiday season, when apparel pricing topped at 2.55% YoY on December 27, Clothing & Footwear prices have come tumbling down to today's -3.0%. Recreation & Culture has continued its yearlong decline, from 2.66% YoY last March to the current read of 0.14%.

Small Factors Held Huge Sway Over Recent Rise & Fall in Truflation



Source: Quill Intelligence

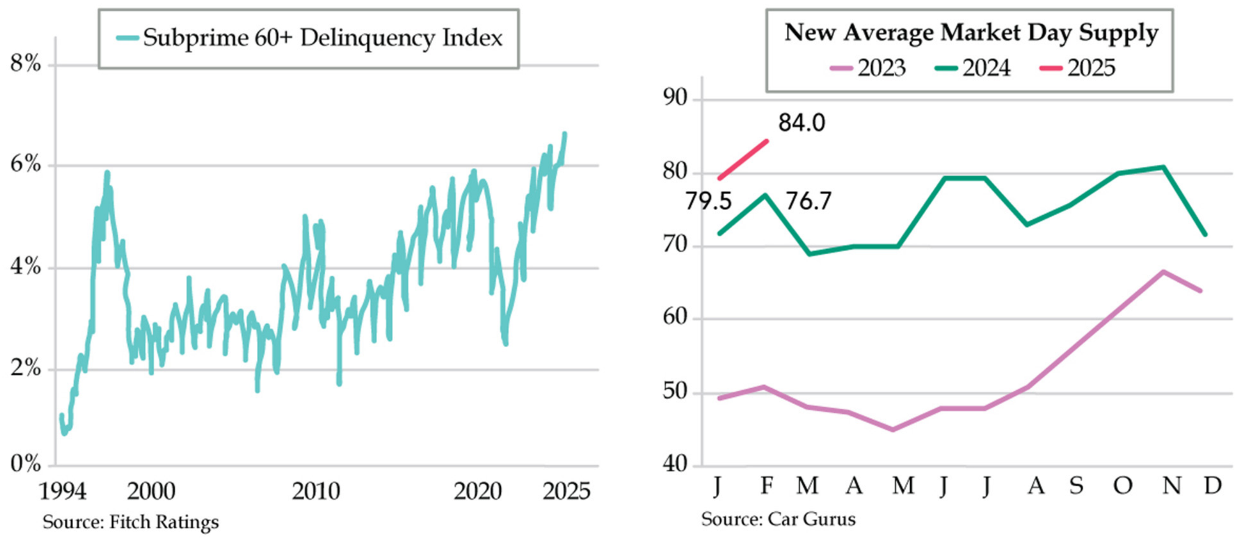
Some of the other big drivers of the hotter-than-forecast CPI were eggs, which spiked by 15.2% in January but "settled" down to 10.5% in February. Still, they're up and are up an eye-watering 58% YoY, which conflicts with February's Food Away from Home's 0.4% rise, which took that discretionary category to 3.7% YoY.

Before settling back to 0.9% in February, used car prices were their own outlier in January, rising 2.2% for the month, the biggest increase since March 2023. Two notes there—Hurricanes Helene and Milton and the Los Angeles fires created a one-time surge in replacement purchases. On top of that, annual seasonal adjustments announced every February amplified the weight of used cars in January, which should continue to fade into the second half after the usual bump catalyzed by income tax refunds.

Those who were able to access auto financing should consider themselves lucky as lenders are increasingly pressed by regulators to tighten standards. The starting point of January's reported 4.0% unemployment rate was sufficient to produce a subprime auto loan delinquency rate of 6.6%, the highest since Fitch Ratings began collecting more than 30 years ago. Not illustrated, but equally notable, are recovery rates on subprime repossessions collapsing to 32% in March, a far cry from the 75% at which recoveries peaked during the pandemic when cars were impossible to source.

The silver lining that should amplify auto disinflation is that auto dealers are sitting on too much inventory. At 84 days' supply, according to CarGurus, the hope is that the threat of tariffs spurs fence-sitters to pounce on the cars gathering dust on packed lots. The risk is that income tax refund season has seen its best days, with the volume of processed returns 2.7% lower year over year. It's human nature to file the minute you can if you know a refund is coming your way. For those taking advantage of the child tax credit, that window opened the week of February 21. If past is precedent, the filers who follow fall into that other category—those who will have to write Uncle Sam a check on Tax Day, a.k.a., "taxpayers."

Spurred by Tightening Lending Standards and Packed New Car Lots (For Now), Auto Disinflation Should Offset Tariffs



Source: Quill Intelligence

Before leaving the subject of revisions behind, most in the media were quick to disregard (or didn't take the time) to properly dissect what hit the wires alongside the "hot, hot, hot!" inflation data for January. Bloomberg's Anna Wong, who has become a friend and is a refreshingly unbiased media economist, did do the legwork. Her takeaways are both cogent and materially alter the narrative:

- Every February, the Bureau of Labor Statistics (BLS) re-estimates seasonal factors to include data from the previous year—this year, the re-estimation covers 2017–2024. This didn't change non-seasonally adjusted values but changed the contour of seasonally adjusted CPI and core CPI.

- The revisions strengthened the disinflation narrative for the second half of 2024. Both the three- and six-month annualized rates of core CPI for December 2024 were revised down to 3.1%, from 3.3% and 3.2% respectively.

- Details of the report help us understand why the print was so strong, and none of them convinces us core CPI is in the midst of reheating. One obvious factor is residual seasonality—the idea that BLS's seasonal factors haven't properly accounted for typical January price gains.

As Wong rightly predicted, the surge in 2025's first month was nearly fully reversed in February. At the headline level, CPI tumbled to 0.216% to the third decimal, less than half January's 0.467% and an appreciable decline from December's 0.365%. Meanwhile, the core rose 0.227%, exactly half of January's 0.446% and lower than December's 0.210%. Finally, the so-called supercore services gauge, on which the inflationistas have been fixated since Fed Chair Jerome Powell conjured the construct out of thin air last year, sank to 0.22% in February from the blistering 0.76% spike the prior month. As Wong noted, "It's clear the disinflationary effect from softening services outweighed the uptick in goods inflation." Bloomberg Economics' proprietary nowcast for CPI pegs March CPI to come in at 2.5% YoY.

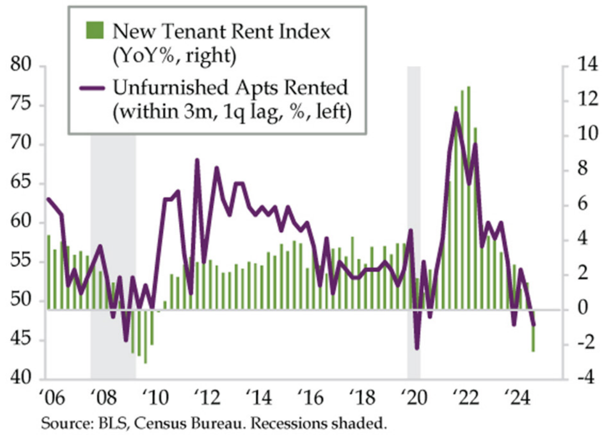
As for the rest of the financial media, the hyperfocus was on market-based inflation expectations, which can obviously be fueled by the narrative that helps traders positioned to profit from short-term bets against Fed rate cuts. Going into the report, five-year breakevens were at the highest since March 2023 and have risen further since. Fearmongering does work if it's persistent and sufficiently alarmist. "It's pretty clear inflation expectations are rising, and not just in the immediate term," Bloomberg's Markets Live declared.

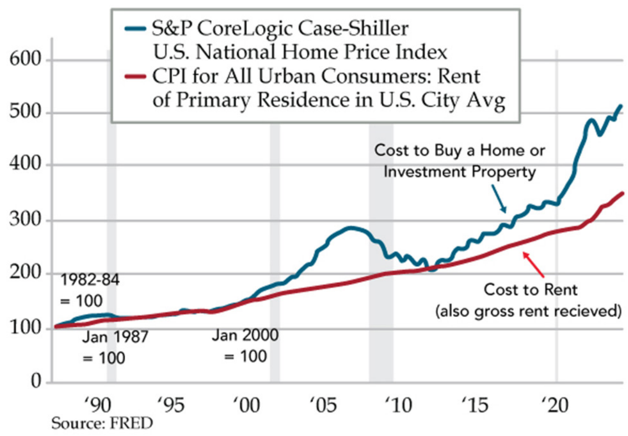
Representing the sell side, Bank of America's economics team chimed in with, "To the extent that residual seasonality is boosting January inflation every year, it would be suppressing inflation in other months. So we think it makes sense to stay focused on year-over-year inflation rates, instead of seeking comfort in three- or six-month rates late in the year, as the Fed has done for the past two years."

The fatal flaw in this thinking is what's materially changed in the last two years. As Zelman & Associates (ZA) pointed out after the CPI hit, "Peak annual rent growth occurred 29 months ago while CPI growth peaked 22 months ago, implying decelerating housing CPI through the summer at least." The marked decline in the Cleveland Fed's New Tenant Rent Index validates ZA's observation as it swung from +1.6% YoY in 2024's third quarter to -2.6% YoY in the last three months of 2024.

To draw parallels to the patterns of the last two years dismisses the downward momentum built into the CPI's biggest weight. And believe it or not, the construction pipeline still matters. As conveyed by Redfin on March 7, "Less than half (47%) of newly built apartments completed in the third quarter of 2024 were rented within three months. That's tied with the fourth quarter of 2023 for the lowest share on record aside from the start of the pandemic. This is according to a Redfin analysis of the US Census Bureau's seasonally adjusted absorption rate data for unfurnished, unsubsidized, privately financed rental apartments in buildings with five or more units, dating back to 2012. The most recent data available covers apartments completed in the third quarter of 2024, and either rented or not rented within three months of then. Apartments are filling up slowly because renters have a lot of options to choose from; **there were 142,900 new apartments completed in the third quarter—the highest number on record**."

Rising Unemployment & Still-Swollen Supply Should Continue to Depress Rents





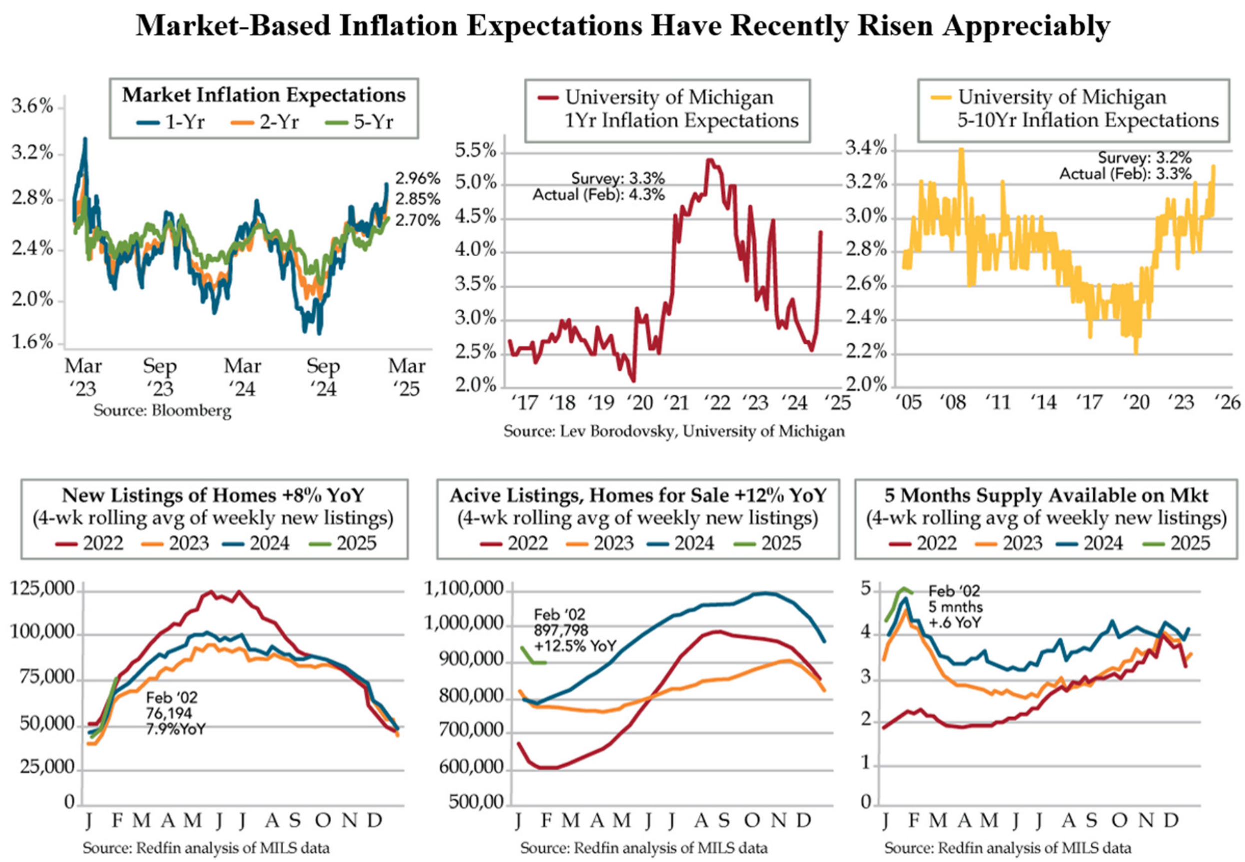
Source: Quill Intelligence

With any luck, home prices will follow that of rents, fueled similarly by a long-awaited swell in existing home listings. That train appeared to finally be pulling into the station. Last month, Redfin noted that, "New listings of US homes for sale rose 7.9% from a year earlier during the four weeks ending February 2, the biggest increase since the end of last year." The upshot is that there is now a five-month supply of homes on the market, up from 4.4 months a year ago and the highest reading in six years. Redfin added that, "The uptick in new listings, along with slow sales, is contributing to a growing pool of supply for homebuyers to choose from. It has also led to the typical home selling for 2% under asking price, the biggest discount in two years—but housing costs are still ultra-high."

Relief, if you can use that term to describe recession, could arrive with spring flowers. As *The Wall Street Journal* recently reported, the number of homes sellers pulled from the market in December hit a nine-year high. The article's conclusion was that this pent-up inventory could combine with the typical wave of homes listed in time for the critical spring selling season to create a tsunami of supply. Two factors work in favor of this hypothesis. Airbnb jocks are rapidly losing access to financing even as US household travel plans hit a 15-year low last month, the pandemic notwithstanding. And natural sellers will soon reject their realtors' vapid reassurances that "prices always rise" as they're barraged with recession headlines. Growing awareness of US taxpayer-funded fraud at the FHA won't help either as the new administration is pressed to rectify the illicit practices associated with a high portion of more than one million FHA mortgages that are in default.

Isolating the new home sales market, in its latest weekly pulse of western markets including Arizona, California, and Nevada, released Wednesday, ZA reported that, "At 0.87 sales per community, Southwest net absorptions were down 9% sequentially and down 3% on a year-over-year basis. California net absorptions were down 17% sequentially to 0.69 sales per community and were down 30% year over year. Last week's absorptions fell roughly 20% short of the typical pace observed during this time of year across our data series dating back to 2000, and fell 21% on a year-over-year basis, marking the fifteenth straight week of declines and the steepest in four weeks. Foot traffic per community declined 4% sequentially for the second consecutive week. On a year-over-year basis, traffic was down 10%—marking the eleventh consecutive decline." You would agree that cold weather has not been a factor in these states. More concerning yet is that California absorptions are down 10 times that of the Southwest, as if the fires had never burned so many homes to the ground in Los Angeles. Still rampant market prices and an unemployment rate of 5.5%, which is 25% north of the 4.1% national rate, apparently trump cooling mortgage rates.

Market-Based Inflation Expectations Have Recently Risen Appreciably



Source: Quill Intelligence

Note that the same inflation expectations hysteria the media is hyping was evident in the University of Michigan's (UMich) one-year and five-10-year expectations. And yet, we've seen scant follow-through in what the New York Fed has tracked via its Survey of Consumer Expectations. Convergence better describes what's taken place in the last year. At work are two very fundamental influences on households. Per the NY Fed this past Monday, mean unemployment expectations "jumped 5.4 percentage points to 39.4%, its highest reading since September 2023. The share of households expecting a worse financial situation in one year from now rose to 27.4%, the highest level since November 2023."

To be continued next week

Dallas, Palm Beach, Washington, DC, and More

If you found Danielle's analysis compelling, I strongly recommend you sign up for her "Daily Feather" Substack here and also the "QI Pro" service here. Use coupon code "QIFrontlinePro" to get 20% off an annual subscription.

I will be in Dallas in the next week or so. I will also have to come back to Palm Beach. I will also be in Washington, DC, for a few days before and after April 21. Unfortunately, there is a lot more travel in my future but maybe I'll get to a city near you.

Today I am a little focused on my daughter Abbi as she is likely receiving a stent put in her heart. Her twin sister had a stroke two years ago. They have asked dad to find some way to understand what their bodies are telling them, as we don't know much about their biological parents. I am on it.

I have been extraordinarily lucky with my own health, but my kids have had very serious issues. Couple that with lots of grandkids, work issues, etc., and their lives can get complicated. But the fascinating thing is they all have such positive attitudes.

It was fabulous seeing Barry Habib and that he is doing better. He is a member at Mar a Lago. We were able to have dinner and I randomly met someone that is on Trump's tax policy committee and spent a great deal of time talking tax policy. Ironically, it helped cement in my mind a significant point for the end of my book. I really am going to finish it in the next few months or less.

Shane and I will fly back to Puerto Rico tonight. You have a great week and enjoy those moments with family and friends.

Your watching things change analyst,

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