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Era of Cheap Goods Was Ending Anyway

THE OUTLOOK |

By Matt Grossman

President Trump's tariffs threaten to amplify a big inflation challenge: Even before the new levies landed, a long run of everyday stuff getting cheaper was coming to a close.

Most prices gradually go up most of the time. But over the 20 years before the pandemic, the basket of physical products that typical shoppers buy didn't get even a cent more expensive.

Prices of core goods in the consumer-price index— that is, excluding food and fuel—fell 1.7% between December 2011 and December 2019. Over the same period, prices of core services like housing, healthcare and education rose 2.7% a year. The combined effect of rising service and falling goods prices was a core inflation rate of 2% a year overall.

Goods prices shot up during the pandemic, peaking in summer 2023 then declining over the following 12 months. But in September, core goods prices started rising again, by an average of 0.1% a month, including 0.2% in February.

"You've got high readings for goods inflation, after a string of readings that average close to zero," Federal Reserve Chair Jerome Powell said during a news conference this month.

Powell said the increase is probably partly because of tariffs and partly because of other factors.

"The recent data are telling us that for goods, you won't have that same deflationary impulse as you did during the 2010s," said Steven Blitz, chief U.S. economist at TSLombard, a research firm.

Blitz thinks goods inflation will help push up overall prices by about 3% this year, above the Fed's 2% target. After falling sharply from its 2022 peak, core inflation using the Fed's preferred metric has stalled between 2.6% and 3%.

Deflation is bad news when it spans the whole economy. But deflation in one sector, such as core goods, which make up about 20% of the CPI, can give shoppers a leg up. It's often a sign that, through productivity and technology, goods are getting better without getting more expensive, as has been the case with computers over the decades.

Now Note

That's one reason goods prices barely budged for 20 years. Trade was another, said Ryan Monarch, a Syracuse University economist. China's entry into the World Trade Organization in 2001 kick-started a flood of exports to the U.S.; they grew more than 500% between 1998 and 2014. As a result, inflation for all imported goods was 0.6 percentage point lower a year than otherwise, a study by Monarch and Colin Hottman of the Federal Reserve found.

It will be harder to find those kinds of gains in the future. "There's no second China waiting to be unleashed on the global economy," Monarch said.

Energy markets brought yet more luck. Global oil prices were cheaper in 2019 than at the start of the 2010s, aided by America's fracking boom. That helped reduce manufacturing and shipping costs for domestic and imported goods alike.

Not only are import prices no longer falling, Trump's tariffs could make them more expensive. He has already imposed 25% steel and aluminum tariffs, an additional 20% tariff on China, plus 25% tariffs on most goods from Canada and Mexico that aren't covered by a previous trade deal, and a 25% tariff on all imported cars starting April 3. He has promised an even broader slew of new tariffs starting April 2, which he says are meant to restore fairness against other countries' trade barriers.

Goldman Sachs economists expect that tariffs will push the Fed's preferred core inflation metric back up to around 3% this year, from 2.8% in February.

A month into new levies against Canada and Mexico, the cost of moving goods across North American borders is ballooning, said Breanna Leininger, vice president of U.S. operations at Canada's PCB Global Trade Management.

"I don't think we've ever seen a trade action elicit the kind of response we have now in terms of anxiety, confusion, and changing business patterns," Leininger said.

A survey of 400 chief financial officers, released this past week by the Richmond Fed, the Atlanta Fed and Duke University, found that companies that don't import from Canada, Mexico and China expect to raise prices 2.9% this year. But companies that rely heavily on these tariffed countries plan to raise prices 5.1%.

Many businesses are still selling inventory that has been warehoused since before tariffs were in place, said Scott Moran, president of **Sutker Moran** , a corporate-treasury outsourcing firm. But now costs are rising, and some of his firm's clients are being forced to consider price increases later this year, Moran said. "You can only wait so long."

In theory, a one-time increase in tariffs will generate a one-time increase in prices. The inflation rate rises temporarily, then falls back once the tariff has been in place for a year or so.

But tariffs can add to inflation pressure in other ways. By reducing competition, trade barriers allow domestic producers to raise prices more. The gap between U.S. and world steel prices has risen sharply since January because of tariffs, for instance. With less foreign competition, domestic producers feel less pressure to adopt the latest technology or boost worker productivity, adding to cost pressures over the long term.