

Economic Indicator — October 10, 2024

September CPI: Minor Turbulence

Summary

The September CPI report came in slightly hotter than expected, but not enough to meaningfully change the outlook for U.S. inflation. Headline CPI rose 0.2% in the month, while excluding food and energy prices consumer price inflation was a tenth stronger at 0.3%. A 4.1% drop in gasoline prices helped restrain overall inflation, although a 0.4% rise in grocery store prices served as a partial offset to the respite at the pump. Core goods prices rose 0.2%, ending a six-month streak of goods deflation. Higher prices for new and used vehicles as well as apparel were the culprits for the increase in core goods prices. On the services side, slower inflation for shelter costs in September was offset by a jump in prices for airfares, motor vehicle insurance and medical care.

Today's data bring the year-ago change in the core CPI to 3.3%, with prices over the past three months increasing at a 3.1% annualized rate. For context, core CPI inflation averaged 2.2% in 2019, suggesting that the underlying pace of inflation at present is about one percentage point above what prevailed before the pandemic. Looking ahead, we expect the disinflation trend to continue, albeit gradually rather than sharply. The ongoing cooling in the labor market and lagging service sector components should help reduce core inflation a bit further in the months ahead. As a result, we expect the FOMC to continue normalizing monetary policy. We still anticipate two 25 bps rate cuts from the Federal Reserve at the two remaining FOMC meetings of the year.

Economist(s)

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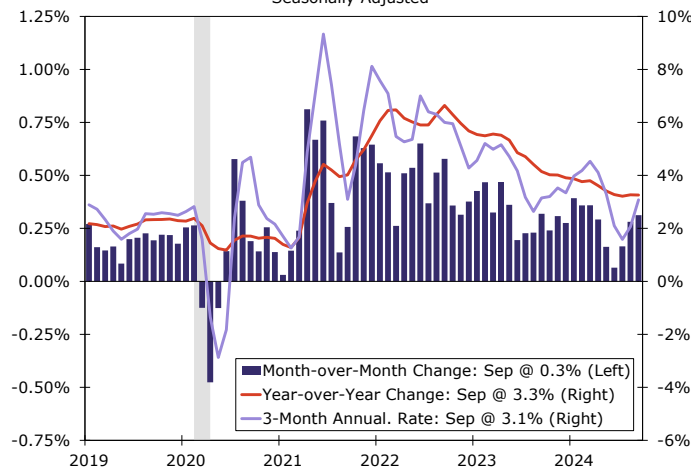
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U.S. Core Consumer Price Index

Seasonally Adjusted

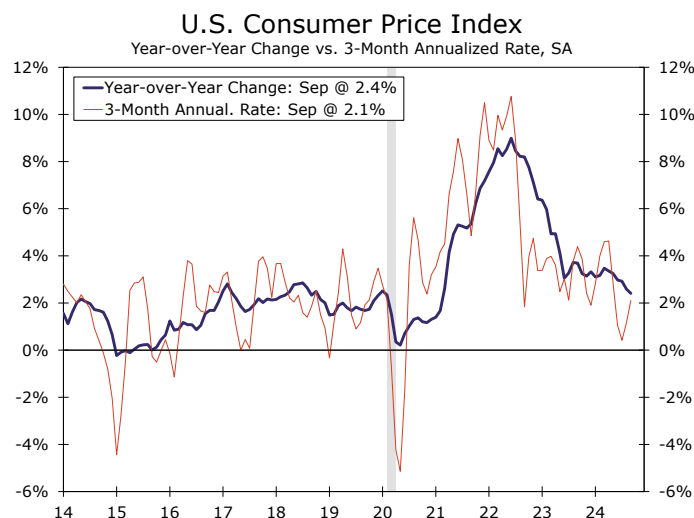


Source: U.S. Department of Labor and Wells Fargo Economics

Inflation Still Cooling on Trend

The bumpy ride to slower inflation continued in September. Overall consumer prices rose 0.2%, which was a tick higher than the Bloomberg consensus. Despite the somewhat larger-than-expected outturn, prices over the past year are up 2.4%, which marks the lowest one-year change in consumer prices since February 2021.

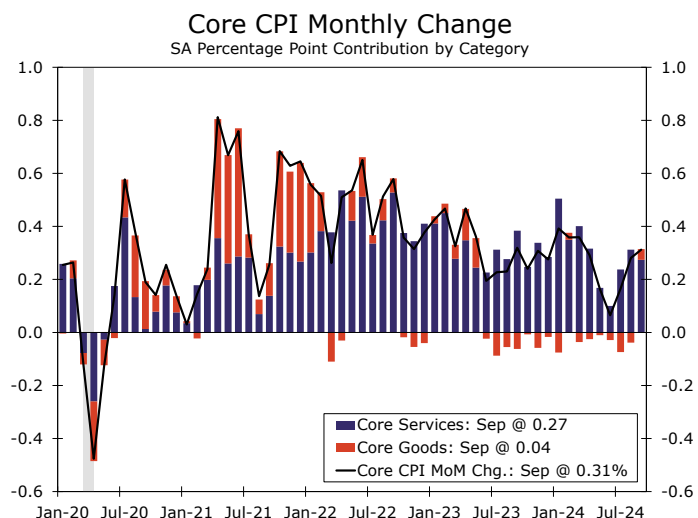
Consumers received some respite at the pump in September, with gasoline prices falling 4.1% last month. However, grocery store prices picked up sharply, increasing 0.4%. This was the largest monthly gain in nearly two years and was driven by a jump in egg prices (+8.4%) and the relatively volatile food component of fruits & vegetables (+0.9%). Even with September's jump, prices for food at home have risen 1.3% over the past year, down from a 12-month pace of 2.4% this time last year and a recent peak of 14% in the summer of 2022.



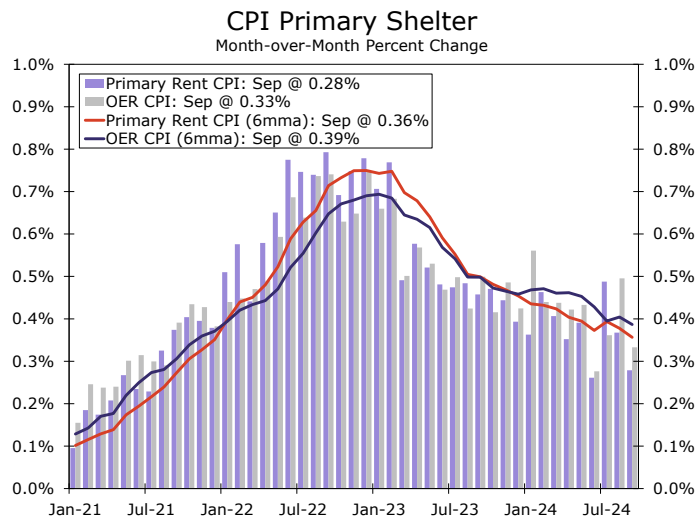
Source: U.S. Department of Labor and Wells Fargo Economics

Excluding food and energy prices, core CPI came in at 0.3% (0.31% unrounded). This was modestly higher than we expected. Core goods prices rose 0.2% in the month, halting a six-month streak of deflation for prices in the goods sector. Small increases for prices of new and used vehicles contributed to the move higher, as did a 1.1% increase in apparel prices. Lower prices for medical care goods and recreation goods helped keep the increase in core goods prices in check.

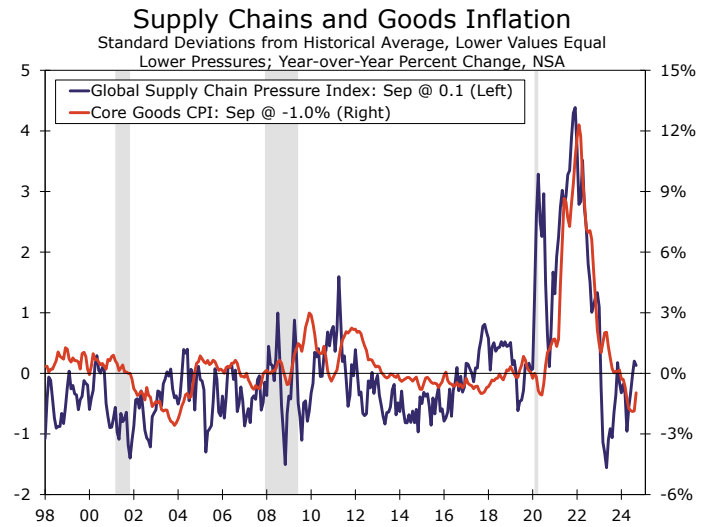
Core services inflation was 0.4% in September (0.36% unrounded), a modest cooldown from the 0.41% pace registered in August. The drivers of services inflation in September were much different from what took place the prior month. Owners' equivalent rent came in at 0.3% in September, reversing the puzzlingly-strong 0.5% reading in August. Rents rose 0.3%, a tenth slower than September. However, outside primary shelter, services inflation jumped on the back of higher prices for airfares (+3.2%), motor vehicle insurance (+1.2%) and medical care services (+0.7%). Looking through the month-to-month noise, the underlying trend in core services inflation in recent months seems to have been between 0.3% and 0.4%, about a tenth or so stronger than the monthly pace that prevailed before the pandemic. Overall core CPI inflation has risen at a 3.1% annualized pace over the past three months, slightly below the year-ago pace (+3.3%) and about a percentage point faster than core CPI inflation in 2019.



Source: U.S. Department of Labor and Wells Fargo Economics



Source: U.S. Department of Labor and Wells Fargo Economics



Source: Federal Reserve Bank of New York, U.S. Department of Labor and Wells Fargo Economics

The September CPI report is consistent with our view that, while the overall trend in core inflation remains lower, further improvement is likely to be slower-going. The deflationary impulse to goods prices has waned with supply chain pressures no longer receding and inventories largely replenished. The downdraft to overall inflation from food and energy also has weakened, with the risks to energy costs for the time-being seeming to lie to the upside. However, we look for services inflation to continue to slow as housing inflation eases further and service providers benefit from tamer input cost growth for goods and labor.

While the next leg lower in inflation may take more time, the good news is that with the jobs market remaining in good shape and solid growth in productivity, average hourly earnings growth, up 4.0% over the past year, continues to outpace inflation. Thus, we do not see slower improvement on the inflation front as an impediment to real spending and output.

While today's inflation report may make some of the more hawkish members of the FOMC somewhat more reluctant to ease monetary policy further at the Committee's next meeting on November 7, we do not believe it is strong enough to warrant a pause. With inflation continuing to slow on trend and upward pressure on prices dissipating amid a cooler labor market and encouraging trends in productivity, there is still likely scope in the near term for policy to "recalibrate" further.

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