Special Commentary — January 10, 2025

December CPI Preview: Concerns About Sticky Inflation to Linger

Economist(s)

Sarah House
Senior Economist | Wells Fargo Economics
Sarah.House@wellsfargo.com | 704-410-3282

Aubrey Woessner
Economic Analyst | Wells Fargo Economics
Aubrey.B.Woessner@wellsfargo.com | 704-410-2911

Summary

The December CPI report should indicate that the underlying trend in inflation is not re-accelerating, but it is unlikely to allay the FOMC's increased concerns that inflation has become stuck uncomfortably above its target. We look for the headline CPI to rise 0.4% on the back of a strong gain in energy prices, which would push the year-over-year rate up to a five-month high of 2.9%. Excluding food and energy, price growth looks to have been more moderate in December. After advancing 0.3% for four consecutive months, we look for the core index to increase 0.2%. If realized, that would leave the year-over-year rate at 3.3% for a fourth straight month. While we do not believe progress in the fight against inflation is going into reverse, we do see it stalling this year as earlier tailwinds to disinflation from supply chain improvements and lower commodity prices have faded and as fresh headwinds from trade policy are likely to emerge.

December 2024 Forecast

	Wells Fargo Economics			Consensus	
	MoM (%)	3-M Ann. (%)	YoY (%)	MoM (%)	YoY (%)
CPI	0.36	3.7	2.9	0.3	2.9
Food	0.34	3.6	2.5	-	-
Energy	2.08	9.4	-0.9	-	-
Core CPI	0.22	3.3	3.3	0.2	3.3
Goods	0.04	1.6	-0.6	-	-
Services	0.28	3.7	4.5	-	-
Primary Shelter	0.31	3.7	4.7	-	-
"Super Core"*	0.23	3.6	4.2	-	-
Not Seasonally Adjusted	**Index**	**MoM (%)**	**YoY (%)**	**Index**	**MoM (%)**
CPI	315.599	0.0	2.9	315.591	0.1

Forecast as of: January 10, 2025; Bloomberg Consensus
*Core services CPI excluding rent of primary residence and owners' equivalent rent (i.e., excluding "Primary Shelter")

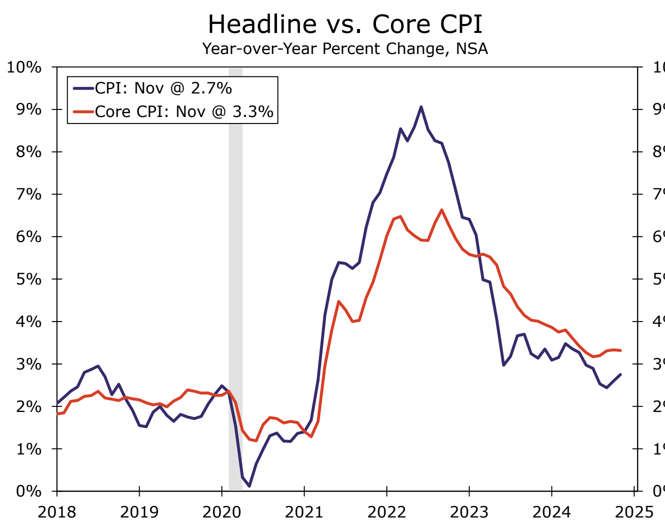
Source: U.S. Department of Labor, Bloomberg Finance L.P. and Wells Fargo Economics

Headline Inflation Firming as Energy Prices Rebound

The lack of additional progress recently in the fight against inflation has tilted the Fed's focus back toward the price stability side of its mandate. The core Consumer Price Index has increased an average of 0.30% the past three months, or at an annualized rate of 3.7%. The Fed's preferred measure of inflation has fared a little better; over the past three months, the core PCE price index has increased an average of 0.21%, or an annualized rate of 2.5%. But that still leaves price growth running above the Fed's 2% target, with the more limited pace of improvement in 2024 evident in the year-over-year rate ticking up to 2.8% in November from 2.6% in June.

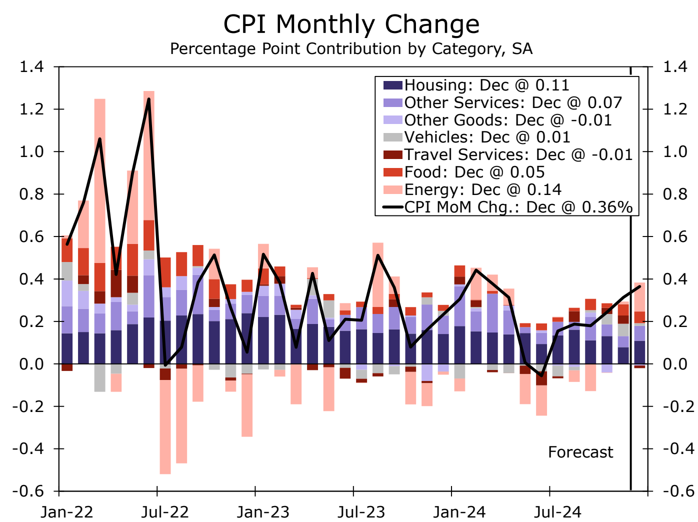
With the jobs market looking steadier since late last summer, we believe the FOMC will need to see progress on inflation resume as soon as this month in order to keep another rate cut in Q1 on the table. The December CPI report is likely to provide a half-hearted step to that end. We look for the core CPI to advance a more palatable 0.2% in November (0.22% unrounded). That said, with the increase in headline CPI looking likely to round up to 0.4% (0.36% unrounded), concerns about inflation becoming stuck above target are likely to linger. We estimate the 12-month change in CPI to rise to a five-month high of 2.9% in December.

Figure 1



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

Figure 2



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

Solid increases in energy and food prices in December look set to bolster the headline's gain. Gasoline prices fell less than usual this December and point to energy goods rising 3.7% over the month on a seasonally adjusted basis. Energy services inflation also looks likely to have firmed, with a further pickup in store in early 2025 after the recent spike in natural gas prices.

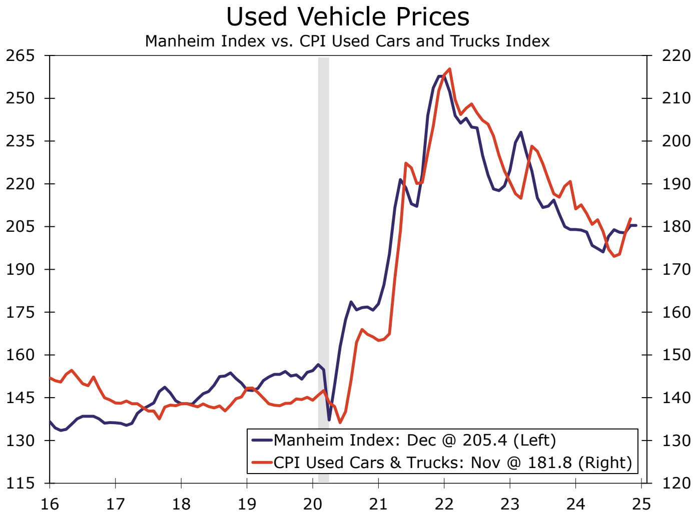
We suspect the late timing of Thanksgiving and the typical discounting that goes on at grocers around the holiday contributed to November's pop in prices for food at home. However, payback in December is likely to be minimal, with promotional activity at supermarkets down relative to last December and food-related commodity prices moving up since the fall.

Softer Core Unlikely to Be a Game-changer for Sticky Outlook

While the December CPI report is likely to show a more challenging price environment for necessities such as food and energy, a more tepid gain in the core index should suggest that the underlying trend in inflation is at least not re-accelerating. We look for the easing in monthly core CPI inflation to 0.2% from 0.3% in November to keep the year-over-year rate at 3.3% and within the narrow range of 3.2%-3.3% for a seventh straight month.

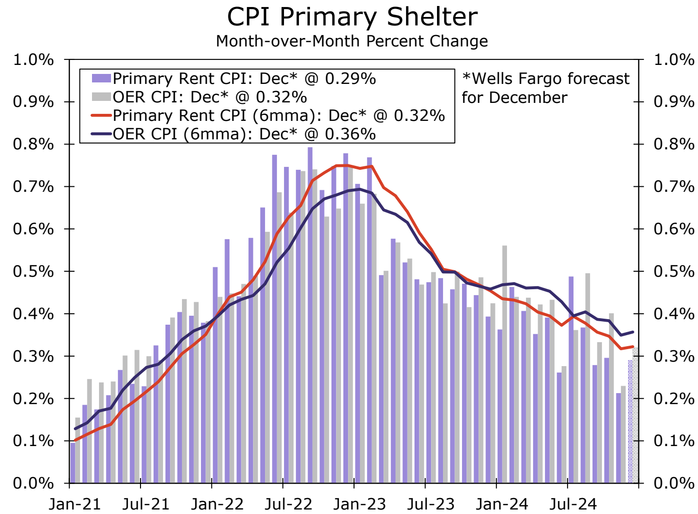
The moderation in the monthly pace of core CPI increases in December is likely to be primarily driven by core goods. New and used vehicles provided a sizable lift to core goods prices the past few months, fueled by replacement demand following Hurricanes Helene and Milton and lower financing costs. Yet with the CPI for used autos vehicles largely realigned with wholesale auction prices, we look for more modest gains in vehicle prices in December (Figure 3). Other core goods prices are likely to be unchanged and continue to firm on a year-over-year basis as the deflationary impulse from un-kinked supply chains has faded.

Figure 3



Source: Bloomberg Finance L.P., U.S. Department of Labor and Wells Fargo Economics

Figure 4

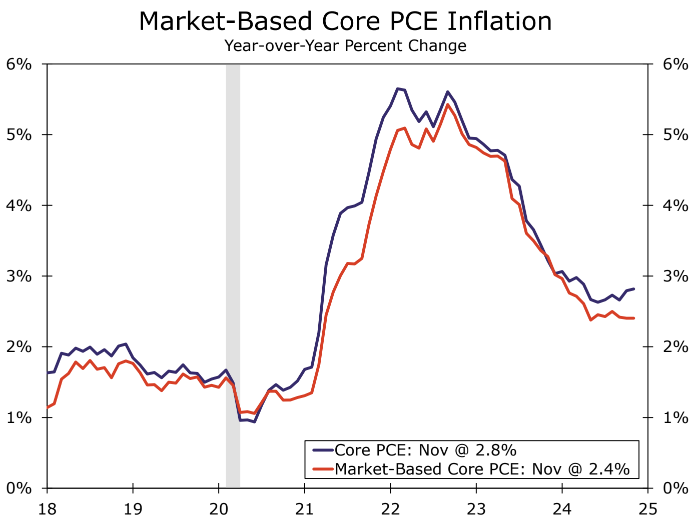


Source: U.S. Department of Labor and Wells Fargo Economics

We expect core services to advance 0.3% again in December, but for the drivers to look a little different from November. While the deceleration in primary shelter in November was a welcome sign that housing disinflation has further room to run, last month's move likely overstated the pace at which the trend is slowing. As a result, we look for the monthly change in primary shelter to edge back up to 0.3% in December from 0.2% in November (Figure 4). The pickup should be offset, however, by a partial reversal of last month's 3.2% jump in hotel prices. Among all non-housing core services, we look for the monthly change in inflation to ease from 0.3% in November to 0.2% in December, which would push the year-over-year change in the CPI "super core" down to a 12-month low of 4.2%.

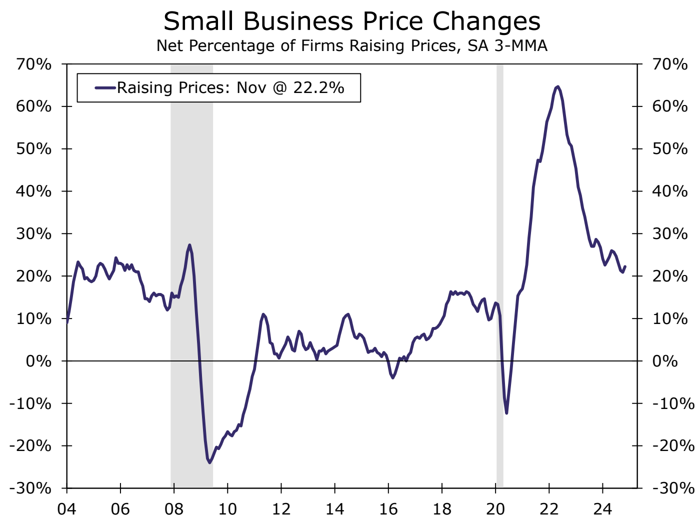
Our estimates point to the core PCE deflator advancing 0.2% in December, which would leave the year-over-year rate, at 2.8%, above its summer level. Yet Fed Chair Powell and other officials have been emphasizing that, excluding categories where prices are imputed rather than directly observed, progress on inflation has not gone into reverse (Figure 5). We estimate that the market-based core PCE, the Fed's inflation measure du jour, rose 0.2% in December to remain closer than the traditional core to the FOMC's target at 2.5% year-over-year.

Figure 5



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

Figure 6



Source: NFIB and Wells Fargo Economics

While Fed officials have not completely lost faith in further disinflation ahead, the slow progress over the past year has underscored that the last leg of inflation's journey back to target will be the most arduous. The path ahead looks even more challenging now with economic policies under the incoming administration likely to be inflationary. While downward forces remain in place from stronger productivity growth, the cooler labor market and more price-conscious consumers, business remain more willing to raise prices than before the pandemic as consumers have not fully gone into hiding and increases in tariffs are likely to leave them little choice (Figure 6). As a result, we look for the pace of inflation to be little changed this year, leaving it stuck above the FOMC's target for a fifth consecutive year (Table).

Wells Fargo U.S. Inflation Forecast

	Actual							Forecast								
	2023				2024				2025				2026			
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q
CPI (YoY)	5.7	4.0	3.6	3.2	3.2	3.2	2.6	2.7	2.7	2.6	3.0	2.9	2.7	2.7	2.7	2.6
QoQ Annualized	3.8	3.0	3.4	2.7	3.8	2.8	1.2	3.1	3.5	2.8	2.7	2.7	2.8	2.7	2.4	2.3
Core CPI (YoY)	5.5	5.2	4.4	4.0	3.8	3.4	3.2	3.3	3.0	2.9	3.1	3.0	3.0	3.0	2.9	2.7
QoQ Annualized	4.9	4.7	3.0	3.4	4.2	3.2	2.2	3.5	3.1	2.9	3.0	3.1	3.0	2.8	2.6	2.5
PCE Deflator (YoY)	5.0	3.9	3.4	2.8	2.7	2.6	2.3	2.4	2.3	2.3	2.5	2.6	2.5	2.4	2.3	2.2
QoQ Annualized	3.9	2.9	2.7	1.7	3.4	2.5	1.5	2.3	2.9	2.5	2.4	2.5	2.5	2.3	2.1	2.0
Core PCE Deflator (YoY)	4.9	4.6	3.9	3.2	3.0	2.7	2.7	2.8	2.5	2.5	2.6	2.6	2.6	2.6	2.5	2.3
QoQ Annualized	4.7	3.8	2.4	2.0	3.7	2.8	2.2	2.5	2.6	2.6	2.6	2.7	2.6	2.3	2.2	2.1

Forecast as of: January 10, 2025
Note: All numbers are percent change.

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

Subscription Information

To subscribe please visit: www.wellsfargo.com/economicsemail

Via The Bloomberg Professional Services at WFRE

Economics Group

Jay H. Bryson, Ph.D.	Chief Economist	704-410-3274	Jay.Bryson@wellsfargo.com
Sam Bullard	Senior Economist	704-410-3280	Sam.Bullard@wellsfargo.com
Nick Bennenbroek	International Economist	212-214-5636	Nicholas.Bennenbroek@wellsfargo.com
Tim Quinlan	Senior Economist	704-410-3283	Tim.Quinlan@wellsfargo.com
Sarah House	Senior Economist	704-410-3282	Sarah.House@wellsfargo.com
Azhar Iqbal	Econometrician	212-214-2029	Azhar.Iqbal@wellsfargo.com
Charlie Dougherty	Senior Economist	212-214-8984	Charles.Dougherty@wellsfargo.com
Michael Pugliese	Senior Economist	212-214-5058	Michael.D.Pugliese@wellsfargo.com
Brendan McKenna	International Economist	212-214-5637	Brendan.Mckenna@wellsfargo.com
Jackie Benson	Economist	704-410-4468	Jackie.Benson@wellsfargo.com
Shannon Grein	Economist	704-410-0369	Shannon.Grein@wellsfargo.com
Nicole Cervi	Economist	704-410-3059	Nicole.Cervi@wellsfargo.com
Jeremiah Kohl	Economic Analyst	212-214-1164	Jeremiah.J.Kohl@wellsfargo.com
Aubrey Woessner	Economic Analyst	704-410-2911	Aubrey.B.Woessner@wellsfargo.com
Delaney Conner	Economic Analyst	704-374-2150	Delaney.Conner@wellsfargo.com
Anna Stein	Economic Analyst	212-214-1063	Anna.H.Stein@wellsfargo.com
Ali Hajibeigi	Economic Analyst	212-214-8253	Ali.Hajibeigi@wellsfargo.com
Coren Miller	Administrative Assistant	704-410-6010	Coren.Miller@wellsfargo.com

Required Disclosures