Economic Indicator — August 14, 2024

July CPI: No Bad News Is Good News

Economist(s)

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

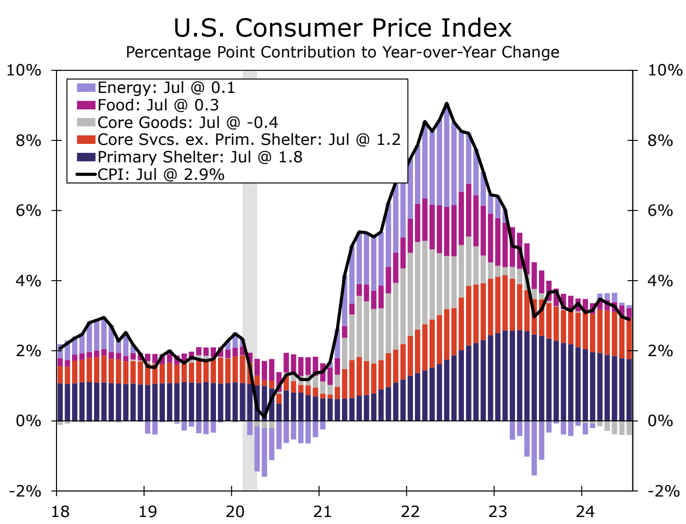
Michael Pugliese
Senior Economist | Wells Fargo Economics
Michael.D.Pugliese@wellsfargo.com | 212-214-5058

Summary

The July CPI data were largely in line with expectations. Both headline and core CPI increased by 0.2% in July (0.15% and 0.17%, respectively), just a basis point or two off from our forecast going into the release. The details of the report contained a few surprises. Core goods prices fell more than we expected, led by another large (-2.3%) decline in used vehicle prices. Core services inflation was a bit hotter than anticipated, led by rebounds in inflation for housing, recreation and communication services.

The broad narrative of continued disinflation remains unchanged. Headline CPI fell below 3% year-over-year for the first time since March 2021. Core CPI declined to 3.2% year-over-year, the slowest pace since April 2021 and roughly half the 6.6% peak hit in September 2022. Furthermore, the annualized pace of core CPI inflation over the past six and three months has been 2.8% and 1.6%, respectively.

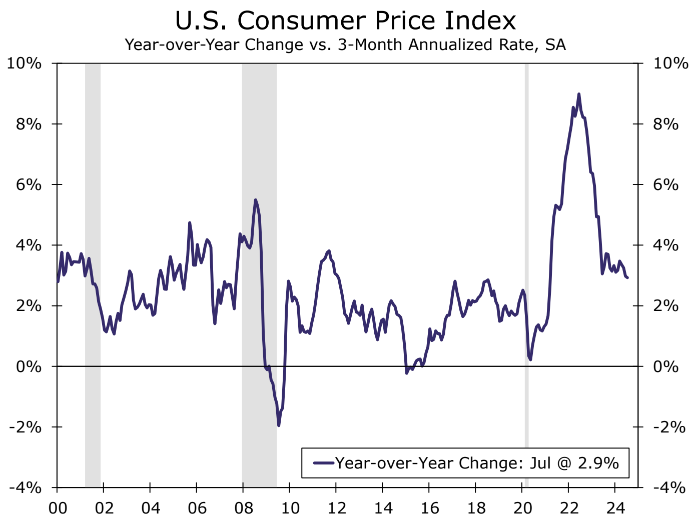
Today's data leave the FOMC in a holding pattern and do not settle the 25 bps or 50 bps debate for September. As we go to print, markets view September as roughly a coin flip between the two outcomes. The continued steady slowdown in inflation, when paired with the rise in the unemployment rate and deterioration in other labor market indicators, leads us to believe the FOMC will want to move quickly towards a more neutral policy stance in the months ahead. As a result, we expect a 50 bps rate cut at the September FOMC meeting, but the decision ultimately may be determined by the August employment report to be released on September 6 and the August CPI report to be released on September 11. Chair Powell's expected speech at the Jackson Hole conference on August 23 looms large as the FOMC weighs the balance of risks to its dual mandate.



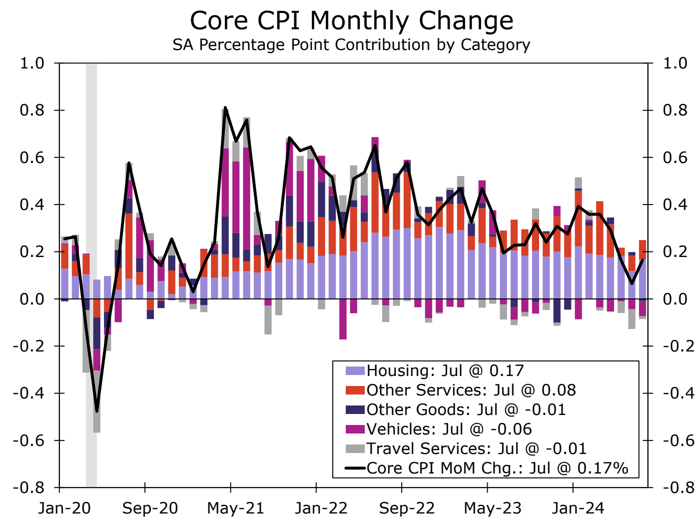
Source: U.S. Department of Labor and Wells Fargo Economics

Summer Inflation Data Remains Tame

Consumer prices increased 0.2% in July (0.15% unrounded), more or less in line with consensus expectations. Energy prices were roughly unchanged in the month amid flat prices for gasoline and electricity. Gasoline prices in July were about 2% lower than they were in July 2023, while electricity prices were 4.9% higher over the same period. Food prices registered a 0.2% increase in the month and a 2.2% gain over the past year. After peaking at more than 11% in 2022, food inflation appears to have settled back into the ~2% pace that prevailed before the pandemic. Relatively restrained energy and food inflation helped push the year-ago rate of CPI inflation down to 2.9%, the first reading below 3% since March 2021 (chart).



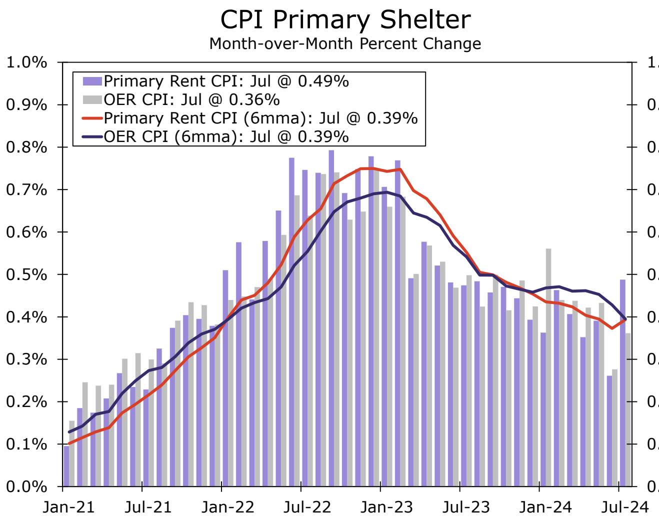
Source: U.S. Department of Labor and Wells Fargo Economics



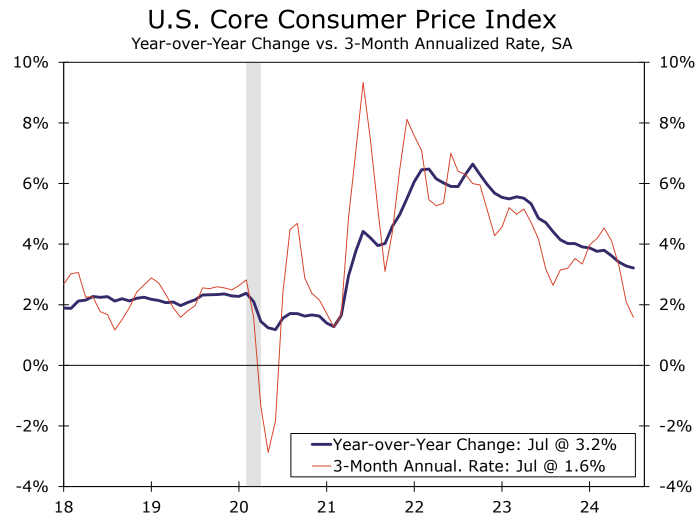
Source: U.S. Department of Labor and Wells Fargo Economics

Core prices also came in as expected, advancing 0.2% (0.17% unrounded). Goods deflation remains in force, with prices falling 0.3%. A 2.3% drop in used vehicles was a key driver of the drop, but excluding used vehicles core goods prices inched down 0.1% amid declines in apparel (-0.4%) and recreational goods (-0.3%).

Unlike core goods, core services inflation sprang back in July (+0.3%) after increasing just 0.1% in June. The pickup was tied in part to somewhat firmer growth in primary shelter prices. Rent of primary residences jumped 0.5% in July, which was stronger than the 0.4% average monthly gain in the first half of the year and looks unlikely to persist with the BLS's more-forward looking measure of new tenant rents having slowed sharply in recent quarters. Owners' equivalent rent also increased at a faster pace than June, but the 0.36% rise still points to slowing on trend when compared to the first half average increase of 0.43% (chart). Ex-housing, core services inflation picked up due to a smaller drop in the volatile travel category. The remaining portion of core services (i.e., ex-shelter and travel) rose 0.2% again in July as a drop in medical care prices was offset by rebounds in motor vehicle insurance, recreation and communication services.



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



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

Inflation clearly continues to slow on trend. The core CPI increased 3.2% over the past year, down from a peak of 6.6% in September 2022 (chart). Furthermore, the annualized pace of core CPI inflation over the past six and three months has been 2.8% and 1.6%, respectively. Through the see-saw ride of recent monthly prints, the moderation in core inflation has broadened beyond goods, with services inflation—most notably housing—also cooling over the past year. A bottoms-up approach to inflation forecasting suggests more housing and other services disinflation is on the way. From a top-down perspective, a weakening labor market and more price-conscious consumers also suggest a bit more disinflation is in the pipeline.

With both the CPI and PPI data in hand for July, we estimate both the headline and core PCE rose 0.13% last month. Core PCE inflation was just 0.12% in July 2023, so the 12-month change would remain at 2.6%, but if realized, this outcome would nonetheless highlight the resumption of progress in lowering inflation with the three-month annualized pace slipping back below 2% (1.8%).

Today's data leave the FOMC in a holding pattern and do not settle the 25 bps or 50 bps debate for September. As we go to print, markets view September as roughly a coin flip between the two outcomes. We expect a 50 bps rate cut at the September FOMC meeting, but the decision ultimately may be determined by the August employment report to be released on September 6 and the August CPI report to be released on September 11. A robust employment report and/or hot inflation data for August could be enough to change our minds, but for now we are sticking with our current forecast. Chair Powell's expected speech at the Jackson Hole conference on August 23 may offer critical insights into how the FOMC is thinking through the balance of risks to its dual mandate.

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 George	Economic Analyst	704-410-2911	Aubrey.B.George@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 Burton	Administrative Assistant	704-410-6010	Coren.Burton@wellsfargo.com

Required Disclosures

This report is produced by the Economics Group of Wells Fargo Bank, N.A. (“WFBNA”). This report is not a product of Wells Fargo Global Research and the information contained in this report is not financial research. This report should not be copied, distributed, published or reproduced, in whole or in part. WFBNA distributes this report directly and through affiliates including, but not limited to, Wells Fargo Securities, LLC, Wells Fargo & Company, Wells Fargo Clearing Services, LLC, Wells Fargo Securities International Limited, Wells Fargo Securities Europe S.A., and Wells Fargo Securities Canada, Ltd. Wells Fargo Securities, LLC is registered with the Commodity Futures Trading Commission as a futures commission merchant and is a member in good standing of the National Futures Association. WFBNA is registered with the Commodity Futures Trading Commission as a swap dealer and is a member in good standing of the National Futures Association. Wells Fargo Securities, LLC and WFBNA are generally engaged in the trading of futures and derivative products, any of which may be discussed within this report.

This publication has been prepared for informational purposes only and is not intended as a recommendation, offer or solicitation with respect to the purchase or sale of any security or other financial product, nor does it constitute professional advice. The information in this report has been obtained or derived from sources believed by WFBNA to be reliable, but has not been independently verified by WFBNA, may not be current, and WFBNA has no obligation to provide any updates or changes. All price references and market forecasts are as of the date of the report or such earlier date as may be indicated for a particular price or forecast. The views and opinions expressed in this report are those of its named author(s) or, where no author is indicated, the Economics Group; such views and opinions are not necessarily those of WFBNA and may differ from the views and opinions of other departments or divisions of WFBNA and its affiliates. WFBNA is not providing any financial, economic, legal, accounting, or tax advice or recommendations in this report, neither WFBNA nor any of its affiliates makes any representation or warranty, express or implied, as to the accuracy or completeness of the statements or any information contained in this report, and any liability therefore (including in respect of direct, indirect or consequential loss or damage) is expressly disclaimed. WFBNA is a separate legal entity and distinct from affiliated banks, and is a wholly-owned subsidiary of Wells Fargo & Company. © 2024 Wells Fargo Bank, N.A.

Important Information for Non-U.S. Recipients
For recipients in the United Kingdom, this report is distributed by Wells Fargo Securities International Limited ("WFSIL"). WFSIL is a U.K. incorporated investment firm authorized and regulated by the Financial Conduct Authority (“FCA”). For the purposes of Section 21 of the UK Financial Services and Markets Act 2000 (the “Act”), the content of this report has been approved by WFSIL, an authorized person under the Act. WFSIL does not deal with retail clients as defined in the Directive 2014/65/EU (“MiFID2”). The FCA rules made under the Act for the protection of retail clients will therefore not apply, nor will the Financial Services Compensation Scheme be available. For recipients in the EFTA, this report is distributed by WFSIL. For recipients in the EU, it is distributed by Wells Fargo Securities Europe S.A. (“WFSE”). WFSE is a French incorporated investment firm authorized and regulated by the Autorité de contrôle prudentiel et de résolution and the Autorité des marchés financiers. WFSE does not deal with retail clients as defined in MiFID2. This report is not intended for, and should not be relied upon by, retail clients.

SECURITIES: NOT FDIC-INSURED - MAY LOSE VALUE - NO BANK GUARANTEE