August 11, 2017

# *Economics Group*

WELLS FARGO SECURITIES

**Sam Bullard, Senior Economist**
sam.bullard@wellsfargo.com • (704)-410-3280
**Sarah House, Economist**
sarah.house@wellsfargo.com • (704)-410-3282

# Consumer Inflation Remains Soft in July

***Coming in shy of expectations, headline and core CPI inflation ticked higher in July. Debate amongst Fed officials should remain robust as they assess whether the inflation backdrop warrants a near-term rate hike.***

## Inflation Pressures Remain Tame

Following soft monthly performances in May and June, the headline Consumer Price Index (CPI) edged higher in July, rising at 0.1 percent. The modest gain, however, missed expectations and, therefore, continues to paint a backdrop of tame inflationary pressures.

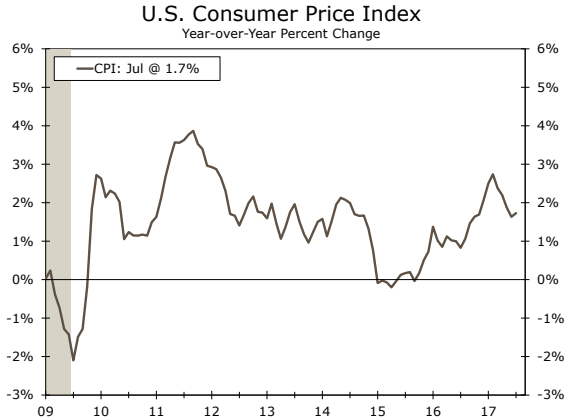
Marking its third consecutive decline, the energy index slipped 0.1 percent in July as natural gas prices registered their largest monthly decline since April 2015. Retail gasoline prices were unchanged on the month. Consumer food prices increased 0.2 percent in July, supported by matching increases in food both at, and away from, home.

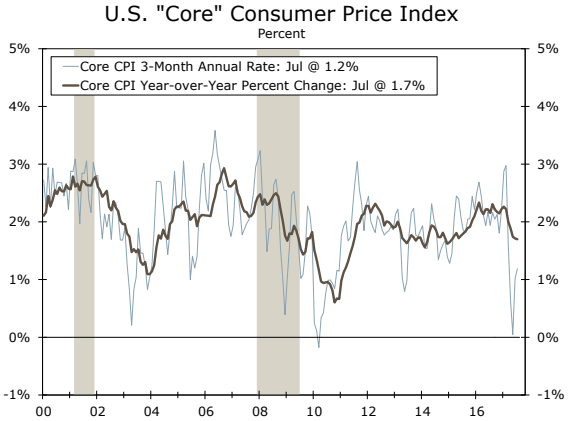
Inflation pressures were no greater when excluding food and energy. Core CPI also edged up a weaker-than-expected 0.1 percent on the month, keeping the year-over-year pace steady at 1.7 percent. The shelter index recorded its smallest increase since March (0.1 percent). This modest gain, however, was primarily due to the record 4.2 percent plunge in lodging. Weakness was also seen in new vehicles, down 0.5 percent, its largest monthly decline since August 2009, and wireless services (-0.3 percent). Encouragingly, both apparel and airfares ended multi-month slides, rising 0.3 percent each, and medical care continues to post solid monthly gains.

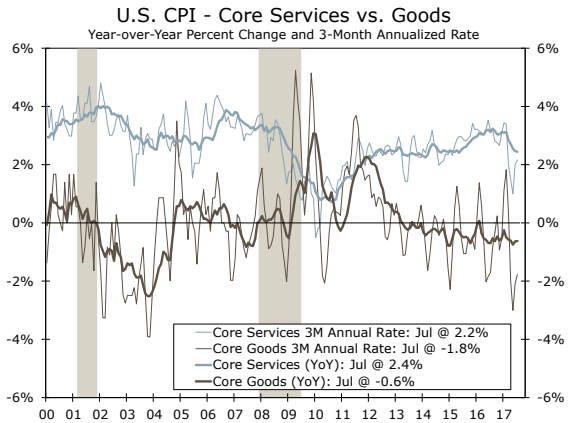
## Plenty of Runway to December, But Trajectory Needs to Turn

As we have cautioned, the runway to a potential December Fed interest rate increase is still somewhat long, giving opportunity for a change of trajectory to take place (note, four more CPI updates before the December 13 FOMC meeting). While this month's performance missed the chance to show a start to that quickening in the pace of inflation needed to cement the third Fed rate hike this year, it is encouraging that the recent slide stabilized somewhat.

In the July FOMC policy statement, officials continued to characterize consumer inflation as running below target, though they reaffirmed confidence that the target will be met over the medium-term horizon. Today's CPI performance does not inspire a lot of confidence that officials are on course for another rate hike this year, though any concerns over a September balance sheet normalization announcement not unfolding have fully dissipated. As previously cited, the Fed will remain on attentive watch for all incoming inflation indicators to better gauge attainability of their symmetric inflation goal. Our outlook projects a gradual firming in the pace of consumer inflation over the coming quarters. That quickening in the pace of consumer inflation is needed for officials to seriously consider further rate tightening at year's end. If the pace of inflation fails to turn higher over the coming months, projections for another rate hike this year should dissipate even further and push the next Fed rate hike into 2018.




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

# Wells Fargo Securities Economics Group


| | | | |
|---|---|---|---|
| Diane Schumaker-Krieg | Global Head of Research, Economics & Strategy | (704) 410-1801<br>(212) 214-5070 | diane.schumaker@wellsfargo.com |
| John E. Silvia, Ph.D. | Chief Economist | (704) 410-3275 | john.silvia@wellsfargo.com |
| Mark Vitner | Senior Economist | (704) 410-3277 | mark.vitner@wellsfargo.com |
| Jay H. Bryson, Ph.D. | Global Economist | (704) 410-3274 | jay.bryson@wellsfargo.com |
| Sam Bullard | Senior Economist | (704) 410-3280 | sam.bullard@wellsfargo.com |
| Nick Bennenbroek | Currency Strategist | (212) 214-5636 | nicholas.bennenbroek@wellsfargo.com |
| Anika R. Khan | Senior Economist | (212) 214-8543 | anika.khan@wellsfargo.com |
| Eugenio J. Alemán, Ph.D. | Senior Economist | (704) 410-3273 | eugenio.j.aleman@wellsfargo.com |
| Azhar Iqbal | Econometrician | (704) 410-3270 | azhar.iqbal@wellsfargo.com |
| Tim Quinlan | Senior Economist | (704) 410-3283 | tim.quinlan@wellsfargo.com |
| Eric Viloria, CFA | Currency Strategist | (212) 214-5637 | eric.viloria@wellsfargo.com |
| Sarah House | Economist | (704) 410-3282 | sarah.house@wellsfargo.com |
| Michael A. Brown | Economist | (704) 410-3278 | michael.a.brown@wellsfargo.com |
| Jamie Feik | Economist | (704) 410-3291 | jamie.feik@wellsfargo.com |
| Erik Nelson | Currency Strategist | (212) 214-5652 | erik.f.nelson@wellsfargo.com |
| Michael Pugliese | Economic Analyst | (704) 410-3156 | michael.d.pugliese@wellsfargo.com |
| E. Harry Pershing | Economic Analyst | (704) 410-3034 | edward.h.pershing@wellsfargo.com |
| Hank Carmichael | Economic Analyst | (704) 410-3059 | john.h.carmichael@wellsfargo.com |
| Ariana Vaisey | Economic Analyst | (704) 410-1309 | ariana.b.vaisey@wellsfargo.com |
| Abigail Kinnaman | Economic Analyst | (704) 410-1570 | abigail.kinnaman@wellsfargo.com |
| Shannon Seery | Economic Analyst | (704) 410-1681 | shannon.seery@wellsfargo.com |
| Donna LaFleur | Executive Assistant | (704) 410-3279 | donna.lafleur@wellsfargo.com |
| Dawne Howes | Administrative Assistant | (704) 410-3272 | dawne.howes@wellsfargo.com |