



# Economics Group

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## Core CPI Inflation Holds Firm As 2018 Comes to a Close

*Reflecting another substantial drop in gasoline prices, headline consumer prices slipped 0.1% in December. Core price inflation, however, remained firm and consistent with the Fed's inflation goal as 2019 begins.*

### Gasoline Prices Fall Further

Led by gasoline, inflation cooled somewhat as 2018 came to a close. The headline Consumer Price Index (CPI) slipped 0.1% month-over-month in December, following a flat reading in November and marking the weakest monthly print since March. For the second consecutive month, substantially lower energy prices played a leading role in tamping down the pace of headline consumer inflation. Retail gasoline prices dropped 7.5% last month, reflecting the sharp drop in crude oil prices over the course of the fourth quarter. Crude oil prices have stabilized at the start of the year, suggesting another outsized monthly decline in retail gasoline prices is unlikely when the January report is released.

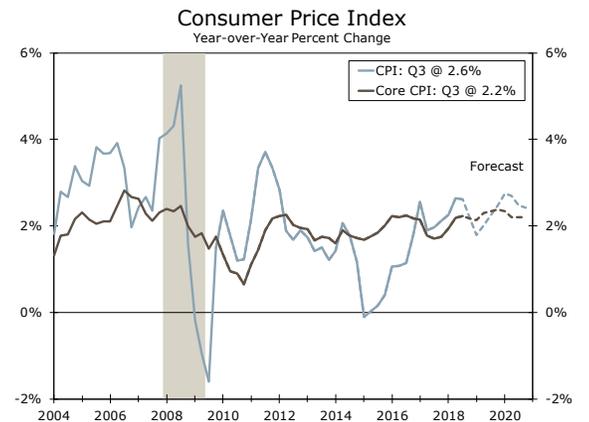
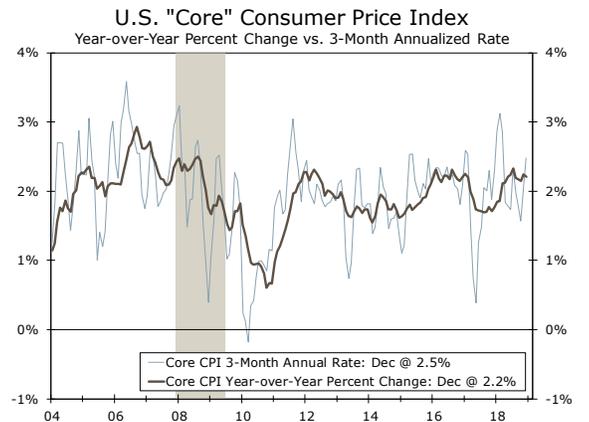
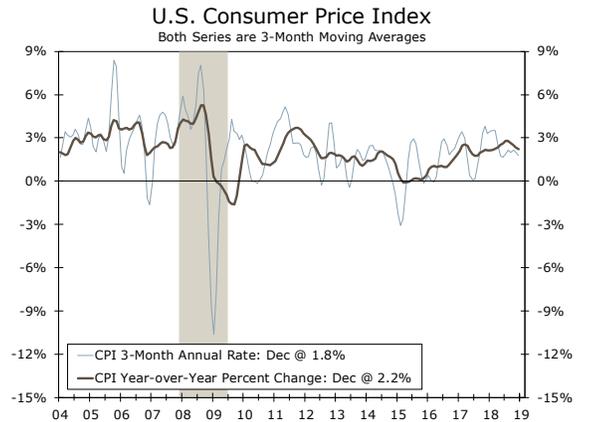
Meanwhile, food prices showed some strength, rising 0.4%. Prices for food away from home increased 0.4%, the largest monthly gain since August 2011. Looking at the year ahead, the food inflation outlook appears to be mixed. The U.S. Department of Agriculture projects food prices at grocery stores to increase between 1% and 2%—potentially marking the fourth year in a row of lower-than-average retail food price inflation (20-year average of 2.1%). Food away from home prices, however, are projected to increase at a steadier trend pace between 2% and 3% (20-year average of 2.7%).

### Broad Based Gains in Core Inflation

Despite the recent dampening influences of energy, core consumer inflation held firm in December, rising 0.2% for the third straight month. Shelter costs remained firm, rising 0.3% for the second straight month and up 3.2% over the past year. Prices for medical care also contributed, increasing 0.3%. Recent outsized gains in used motor vehicles prices did not repeat, slipping 0.2%. Concerns about a loss in momentum of core inflation were assuaged, as core CPI inflation has increased at a 2.5% annualized pace over the past three months.

### Inflation Remains Critical Piece to Fed Hike Calculus

In the December FOMC meeting minutes, officials' discussion on inflation was relatively dovish—in our reading—as participants acknowledged that core inflation had “edged lower” and that lower inflation breakeven measures (TIPS) intimated “some moderation in inflation pressure.” That said, officials continue to view price developments as consistent with their symmetric 2% target objective. Yesterday, Chairman Powell reiterated this view, stating he believes inflation will remain around 2% this year given expectations for extended, above-potential GDP growth and a tight labor market. We concur, projecting core CPI to run moderately above a 2% annual pace this year. No doubt a close eye will be kept on every inflation measure going forward to gauge the likelihood of additional Fed rate hikes. If the downside risks pressure core consumer inflation lower, then the Fed will take stock of its economic and policy outlook. However, if core inflation holds firm, the Fed will continue to consider additional rate hikes this year.



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