ECONOMIC UPDATE

REGIONS

February 10, 2021

January Consumer Price Index: New Year, Same Inflation Story. For Now, Anyway

- The total CPI rose by 0.3 percent in January (up 0.257 percent unrounded); the CPI was unchanged (up 0.031 percent unrounded)
- On a year-over-year basis, the total CPI is up 1.4 percent and the core CPI is up 1.4 percent as of January

The total CPI rose by 0.3 percent in January, matching our forecast, while the core CPI was unchanged, less than our forecast of a 0.1 percent increase and the consensus forecast of a 0.2 percent increase. On an over-the-year basis, both the total CPI and the core CPI are up 1.4 percent. The January CPI report incorporates the annual revisions to the recent historical data, though those revisions did not lead to any material changes in headline or core inflation as previously reported. The patterns in the inflation data at the beginning of 2021 were the same as those seen over the past several months of 2020, i.e., firming goods price inflation and listless services price inflation, with the latter acting as a drag on overall inflation given the relative weights attached to goods and services prices. While those patterns are likely to remain in place over the next few months, the inflation story is likely to change over the second half of 2021 as economic activity normalizes further.

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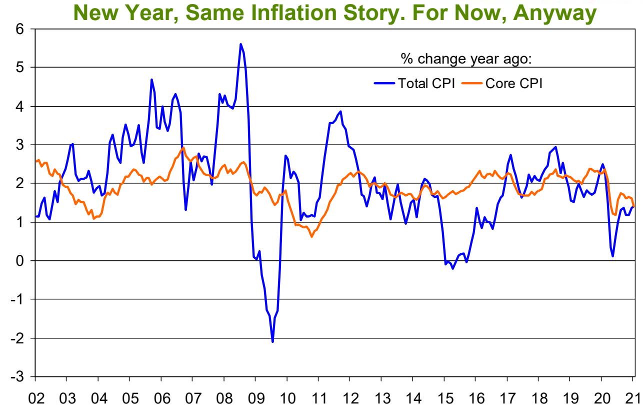
New Year, Same Inflation Story. For Now, Anyway



The broad energy index was up 3.5 percent in January but still down 3.6 percent year-on-year. On a not seasonally adjusted basis, retail gasoline prices were up by 6.9 percent in January, which translated into a 7.4 percent increase in the seasonally adjusted data and which accounted for most of the monthly change in the total CPI. With oil prices rising thanks to rising demand and tighter control over supply from within OPEC, gasoline prices have pushed higher, and while still shy of pre-pandemic levels, prices will likely to push higher in the months ahead if demand growth accelerates as we and most others expect will be the case. Food prices rose by 0.1 percent in January; while prices for food consumed at home reversed course, falling by 0.1 percent, prices for food consumed away from home rose by 0.3 percent. Overall, food prices are up 3.8 percent year-on-year.

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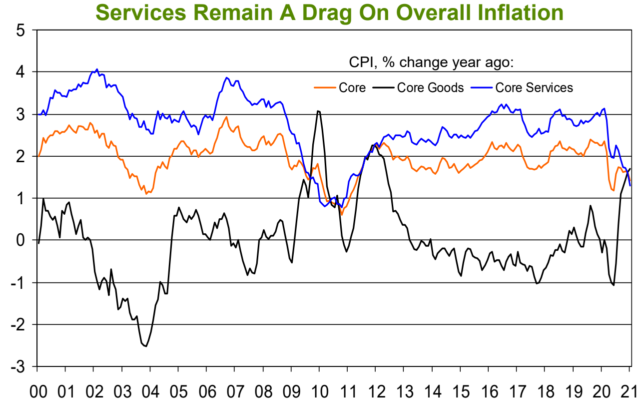
Services Remain A Drag On Overall Inflation



Core services prices were basically flat – an unrounded increase of 0.023 percent – in January, leaving them up 1.6 percent year-on-year. Our middle chart illustrates the point we made earlier about core services prices acting as a drag on overall inflation even as core goods price inflation continues to firm. Though these same patterns can be seen in the data on the PCE Deflator, the drag from services prices is somewhat overstated in the CPI data, reflecting the outsized weighting on rents in the core CPI. Primary rents were up 0.1 percent in January, the fifth month out of the past six with just a 0.1 percent increase. On an over-the-year basis, primary rents are up 2.05 percent, the smallest such increase since October 2011. Growth in owners' equivalent rents has also slowed sharply over the past several months, with a year-on-year increase of just 2.0 percent in January. Given that rents account for over 40 percent of the core CPI, sagging rent growth is having an undue impact on core services inflation. Still, in January prices for core services excluding shelter were up by only 1.3 percent.

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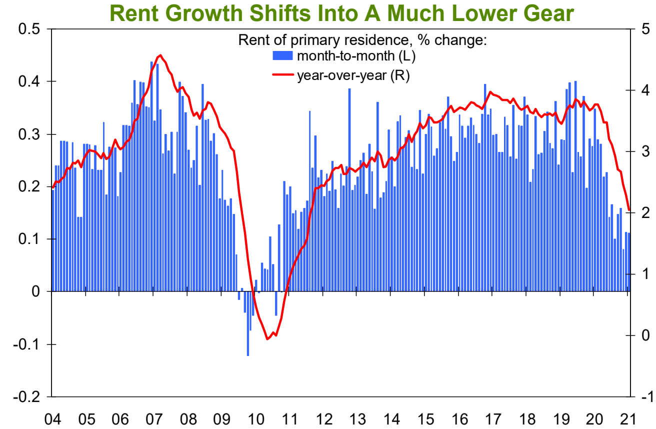
Rent Growth Shifts Into A Much Lower Gear



In contrast to softening services prices, prices of core goods (i.e., excluding food and energy) continue to firm. The 0.1 percent increase in January marks the seventh month of the past eight in which core goods prices rose. At 1.7 percent, the year-on-year increase in core goods prices in January is the largest such increase since April 2012, with most of the interim period characterized by persistent goods price deflation. Core goods prices are being pushed higher by continued strong consumer demand and a weaker U.S. dollar; while we expect the former to be sustained through 2021, we do not expect the weakness in the dollar to persist through the year. Still, on net, core goods prices will likely continue to push higher over the course of 2021.

As noted above, with services prices weighted much more heavily in the price indexes, core inflation is likely to remain muted for as long as segments of the services sector are at least partially shuttered. We, and most others, expect that once the economy is more fully reopened, there is bound to be a normalization in services prices, though we think this will be more of a one-off adjustment rather than a sustained period of rising services prices. Higher energy prices, however, are likely to provide a more lasting boost to headline inflation in 2021.

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