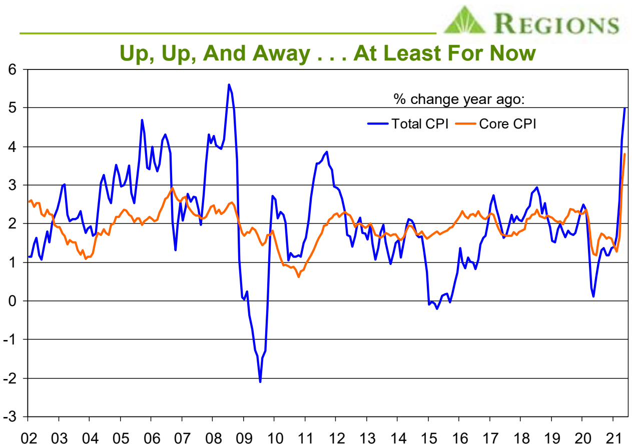
ECONOMIC UPDATE
REGIONS
June 10, 2021

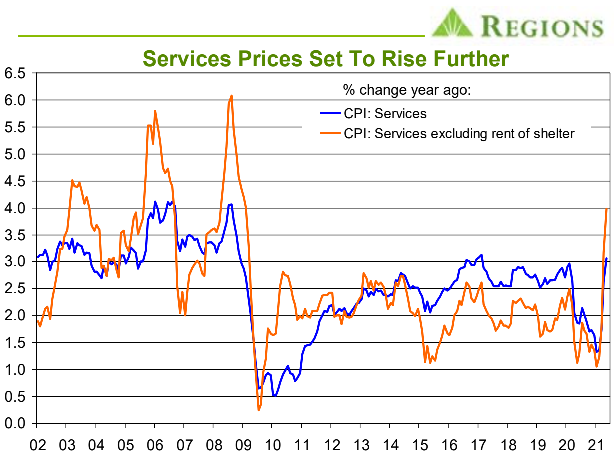
May Consumer Price Index: Up, Up, And Away . . . At Least For Now

- The total CPI rose by 0.6 percent in May (up 0.644 percent unrounded); the core CPI rose by 0.7 percent (up 0.737 percent unrounded)
- On a year-over-year basis, the total CPI is up 5.0 percent and the core CPI is up 3.8 percent as of May

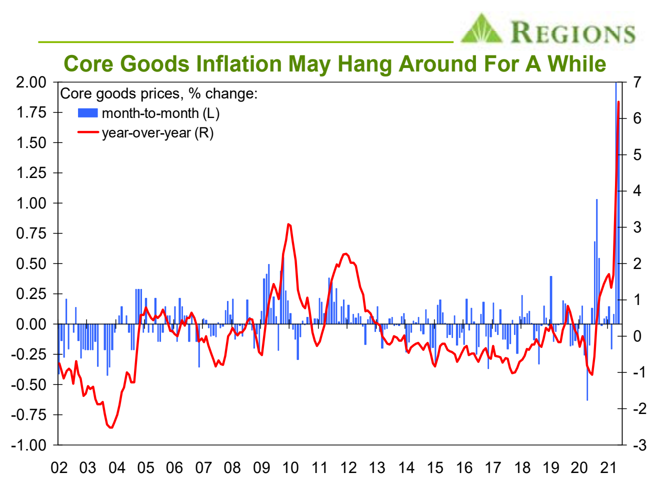
The total CPI rose by 0.6 percent in May while the core CPI increased by 0.7 percent, each one-tenth higher than our above-consensus forecasts. On an over-the-year basis, the total CPI is up 5.0 percent, the largest such increase since August 2008, while the core CPI is up 3.8 percent. The over-the-year increases, however, continue to reflect base effects, which are more pronounced in the May data than in any other month given that it was last May that prices bottomed after having fallen as the economy shut down with the onset of the pandemic. Additionally, the May data reflect the further normalization of services prices as the economy reopens more fully and consumer demand returns. We have, for several months, been pointing to base effects and the normalization of services prices as factors that would, well, inflate the inflation data beginning this March and likely carrying through the summer months. Were these the only factors influencing the inflation data, the argument that inflation pressures are purely transitory would carry the day with little debate. But, we see factors such as supply chain/logistics bottlenecks, rising shipping costs, and rising labor costs as impacting the inflation data and having the potential to persist. So, sure, if you wait long enough, anything is transitory, but the longer inflation pressures persist, the greater the odds that inflation expectations come unmoored, which one can argue is already happening amongst consumers, and the greater the odds that inflation leads to disruptions in the financial markets and the real economy.



While not seasonally adjusted gasoline prices rose in May, the increase was smaller than the typical May increase, which resulted in the seasonally adjusted data showing gasoline prices falling by 0.7 percent. This offset increases in prices for electricity and natural gas, thus leaving the broad energy index unchanged. Food prices rose by 0.4 percent, with prices for food consumed at home up by 0.4 percent and prices for food consumed away from home up 0.6 percent. While we'd expect stronger demand, higher input costs, and higher labor costs to lead to hefty increases in restaurant prices, May's increase in prices for food consumed away from home was more driven by higher prices at schools and employee facilities, which could simply reflect such facilities opening back up after having been shut down. That said, restaurant prices bear watching in the months ahead.



Prices for core goods, or, consumer goods excluding food and energy, rose by 2.0 percent in April, the largest such increase on record, and that was followed up by a 1.8 percent increase in May. Many have dismissed these increases out of hand, as motor vehicle prices have been a key factor behind them, with prices for used motor vehicles up by 7.3 percent in May after a 10.0 increase in April, and prices for new motor vehicles up by 1.6 percent in May after a 0.5 percent increase in April. Vehicle prices reflect short supplies of new vehicles, thanks largely to the global chip shortage, and limited inventories of new vehicles are pushing some demand to used vehicles, where supplies have been thin for some time. To be sure, at some point supplies will normalize, but when that will be remains to be seen. But, this is not the only instance in which supply-side issues are impacting core goods prices, such as furniture and appliances, with higher shipping costs and a weaker U.S. dollar also impacting core goods prices. Core services prices rose by 0.4 percent in May, a smaller than expected increase that in part reflects a decline in medical care costs. As for normalization of services prices, air fares rose by 7.0 percent in May, lodging costs rose by 0.4 percent, and rental car rates rose by 12.1 percent, all smaller than the increases seen in April. Again, these sources of support for core services prices will fade, but rent growth is showing signs of picking up and, as such, will support core services inflation.



To be sure, base effects and normalization of services prices have done a lot of the heavy lifting in producing the upside beats in the April and May CPI data. That should not lead to evidence of more lasting inflation pressures being overlooked, particularly at a time when labor costs are rising rapidly. While headline inflation will not remain at 5.0 percent, there is still a lot of room between that and 2.0 percent.

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