ECONOMIC UPDATE

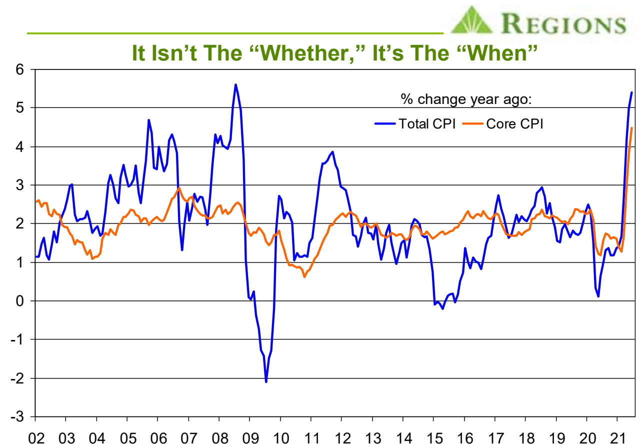
REGIONS

July 13, 2021

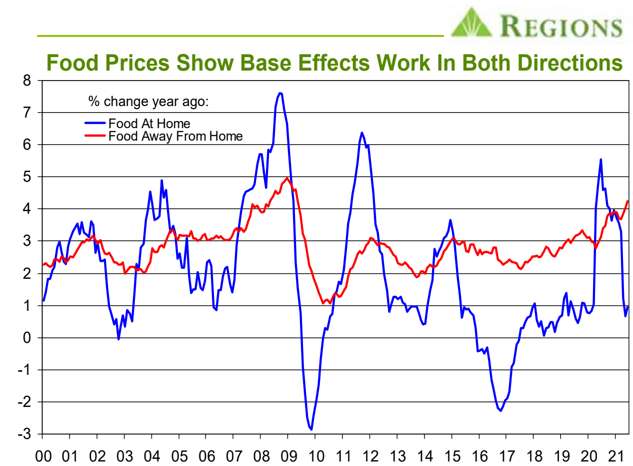
June Consumer Price Index: This Too Shall Pass, But When?

- The total CPI <u>rose</u> by 0.9 percent in June (up 0.905 percent unrounded); the core CPI <u>rose</u> by 0.9 percent (up 0.878 percent unrounded)
- On a year-over-year basis, the total CPI is <u>up</u> 5.4 percent and the core CPI is <u>up</u> 4.5 percent as of June

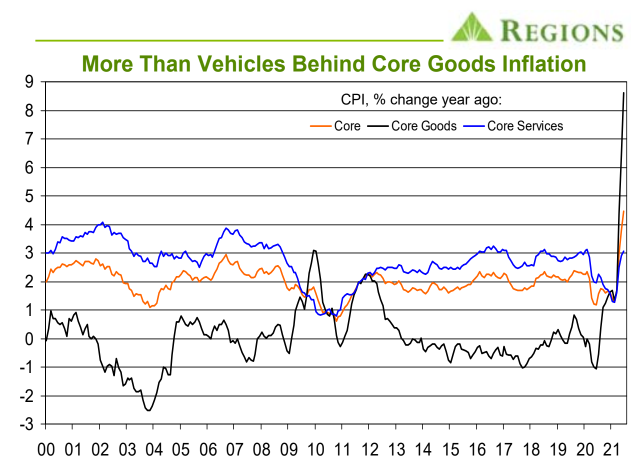
The total CPI and the core CPI each rose by 0.9 percent in June, more than our above consensus forecast which called for increases of 0.6 percent and 0.5 percent, respectively. On an over-the-year basis, the total CPI is up 5.4 percent, the largest such increase since August 2008, while the core CPI is up 4.5 percent, the largest such increase since November 1991. In the "for what it's worth, which is apparently not as much as a used car is worth" category, prices for used motor vehicles jumped by 10.5 percent in June, accounting for one-third of the increase in the total CPI. As such, many will downplay the June CPI data, particularly as wholesale prices for used vehicles dipped in June, indicating some relief may be in sight on the retail level. While mindful of the impact of higher prices for used motor vehicles, we're not willing to dismiss the June data, as we see plenty of indications that, while not at the pace seen in May and June, inflation will nonetheless remain elevated for some time to come. In addition to further normalization of services prices, the effects of which will fade from the data over coming months, inadequate supplies of goods, higher transport costs, and higher labor costs all figure to be more persistent sources of inflation pressure. It is almost becoming trite to characterize inflation pressures as transitory, as it isn't the "whether" as much as it is the "when," and, on that latter point, no one really has much insight at this point.



On a seasonally adjusted basis, retail gasoline prices were up by 2.5 percent in June, leaving them up 44.8 percent year-on-year. The overall energy index rose by 1.5 percent in June and is up 24.5 percent year-on-year. Food prices rose by 0.8 percent in June, with prices for food consumed at home up by 0.8 percent and prices for food consumed away from home up by 0.7 percent. Meats, fish, and fruits and vegetables were the main factors behind the larger than expected increase in prices of food consumed at home, while restaurant prices posted another sizable increase. Note from our middle chart that, on an over-the-year basis, prices for food consumed at home are up "just" 0.9 percent as of June, but the point of comparison is last June, by which time grocery store prices had risen significantly in the early phases of the pandemic. So, unlike total inflation, where base effects are exaggerating over-the-year increases, base effects are at present holding down over-the-year increases in prices for food consumed at home. This illustrates a useful point to keep in mind when headline inflation starts to ease, which is that it is the cumulative effects that matter in terms of household budgets – prices rising at a slower rate still leaves us with higher prices.



After April and May brought the largest monthly increases on record, we had expected a smaller increase in core goods prices in June. Instead core goods prices rose by 2.2 percent, now the highest monthly increase on record, which leaves them up 8.6 percent year-on-year, the largest such increase since February 1981. To be sure, the 10.5 percent increase in prices for used motor vehicles played a large role in this increase, but there are other factors in play. Prices for new motor vehicles rose by 2.0 percent as limited supplies pushed prices higher and continued to divert demand into the market for used vehicles. These supply constraints are unlikely to ease for several months. Prices for major appliances rose by 2.7 percent in June and are up 13.7 percent year-on-year, another instance of robust demand running into lean supplies. Apparel and furniture also added support for core goods prices in June. Core services prices rose by a relatively tame 0.4 percent in June, but as has been the case over the past several months flat prices for medical care services acted as a drag on core services prices. The "normalization" effect is still very much in play, with hotel rates up 7.0 percent, air fares up 2.7 percent, and rental car rates up 5.2 percent. While prices of such services will not continue to rise at rates this rapid, one counter will be firming rent growth after rents acted as a drag on core services prices during the pandemic. Thus far, owners' equivalent rents are firming more than market rents, which is no surprise given heady rates of house price appreciation, but we look for market rents to gain momentum in the months ahead. If we are correct, faster rent growth will counter much of the effect of slower growth in other services prices.



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