ECONOMIC UPDATE

REGIONS

August 11, 2021

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July Consumer Price Index: More Moderate Increase In July Settles Nothing

- The total CPI rose by 0.5 percent in July (up 0.474 percent unrounded); the core CPI rose by 0.3 percent (up 0.329 percent unrounded)
- On a year-over-year basis, the total CPI is up 5.4 percent and the core CPI is up 4.3 percent as of July

The total CPI rose by 0.5 percent in July, matching the consensus forecast but shy of the 0.6 percent increase we anticipated, while the core CPI rose by a smaller than expected 0.3 percent. On an over-the-year basis, the total CPI is up 5.4 percent while the core CPI is up 4.3. Many will dismiss the over-the-year comparisons and point instead to the monthly increases, which in July were much smaller than those seen in each of the past three months, as proof of the transitory nature of inflation pressures. We are less than convinced, as factors such as global supply chain bottlenecks and higher shipping costs could easily persist into 2022, while labor costs will continue to increase. And, it is worth noting that even monthly increases of just 0.2 percent through December would be sufficient to keep headline CPI inflation above 5.0 percent and core CPI inflation above 4.0 percent into early-2022. Obviously, the yet-to-be determined impact of the Delta variant of the COVID-19 virus looms as a source of considerable uncertainty. To the extent that the spread of the Delta variant leads to people cutting back on things like traveling, dining out, and frequenting recreation and entertainment venues, there would be a downward pull on services prices, but you could argue this would also set the stage for a rebound at some point down the road. More broadly, even as we expected the effects of what has, at least until now, been a normalization of services prices to fade from the data, we've also pointed to rent growth and medical care costs as two factors that could take up the slack and act as sources of inflation pressures. So, while the more moderate increases in the total and core CPI in July are welcome, they settle nothing.

Retail gasoline prices were up by 2.4 percent in July, leaving them up 41.6 percent year-on-year. Obviously the over-the-year comparison is skewed by the effects of the pandemic last year, but despite crude oil prices having eased of late, retail gasoline prices have continued to push higher and should be a support for the total CPI in the August data. Food prices rose by 0.7 percent in July, with prices for food consumed at home up 0.7 percent and prices for food consumed away from home up 0.8 percent. To our earlier point, restaurant prices will bear watching in the August data for hints that the upturn in COVID cases is having an impact on dining out. Still, even if that is the case, it could just be that upward pressure on food prices simply migrates away from restaurants and toward grocery stores, with little net impact on overall food prices.

After the three largest monthly increases on record from April through June, core goods prices rose by a more moderate 0.5 percent in July. As tipped by the Manheim Index, which measures prices on the wholesale level, retail prices of used motor vehicles rose by just 0.2 percent in July on the heels of a 10.5 percent increase in June. Still, prices for new motor vehicles rose by 1.7 percent, down slightly from June's 2.0 percent increase, with the ongoing shortage of semiconductor chips continuing to hold down production, which is in turn helping support prices. Other categories in which lean supplies have been running up against robust demand, such as home furnishings and appliances, turned in mixed performances in July but continue to show hefty over-the-year increases.

Core services prices were up by 0.3 percent in July, a more modest increase than our forecast anticipated. Lodging rates were up 6.0 percent in July after a 7.0 percent increase in June, while air fares slipped by 0.1 percent and car rental rates fell by 4.6 percent. Prices for recreation and entertainment services showed no signs of easing in July, so the "reopening effect" was a mixed bag in the July data. While the increase in market rents printed at 0.2 percent, matching the prior five months, the unrounded increase was 0.156 percent, smaller than in prior months. We still look for rent growth to pick up in the months ahead, thus acting as a stronger support for core inflation. We're not quite so sure with medical care costs, which remain a meaningful drag on core CPI inflation. One thing that stands out is the string of large declines in health insurance premiums, which are now down 8.5 percent year-on-year. Medical care costs join rents as a swing factor that could easily turn from a drag on to a driver of pressure on core inflation in the months ahead.

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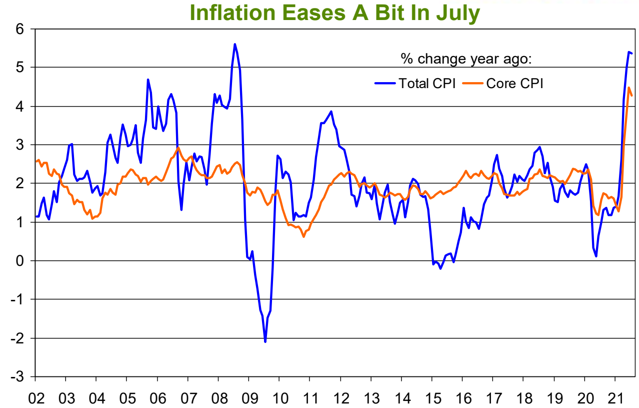
Inflation Eases A Bit In July



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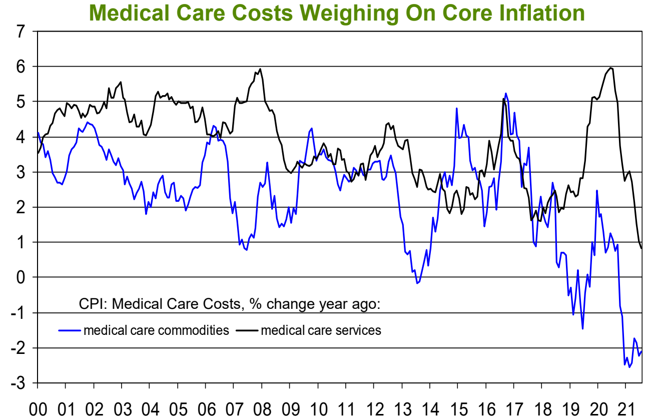
Medical Care Costs Weighing On Core Inflation



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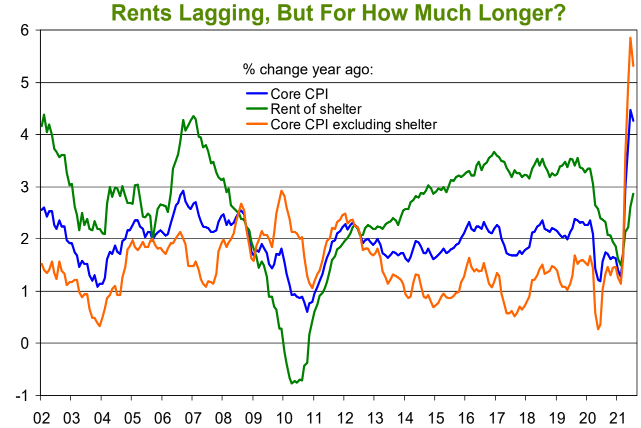
Rents Lagging, But For How Much Longer?



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