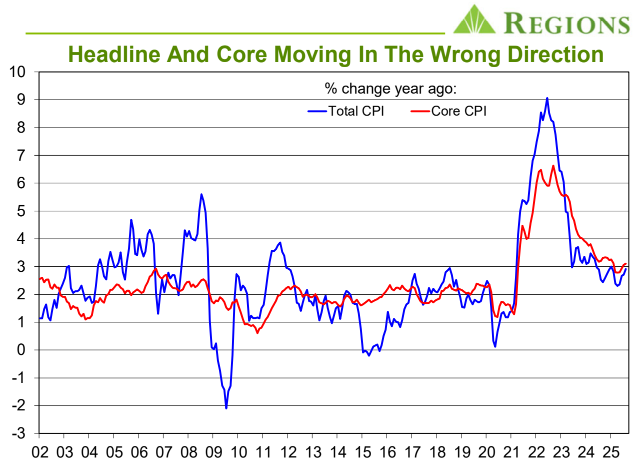
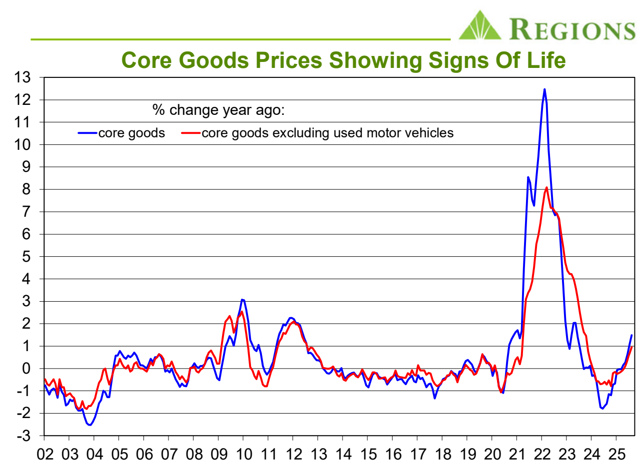
August Consumer Price Index: Moving In The Wrong Direction

- The total CPI rose by 0.4 percent in August (up 0.382 percent unrounded); the core CPI rose by 0.3 percent (up 0.346 percent unrounded)
- On a year-over-year basis, the total CPI is up 2.9 percent and the core CPI is up 3.1 percent as of August

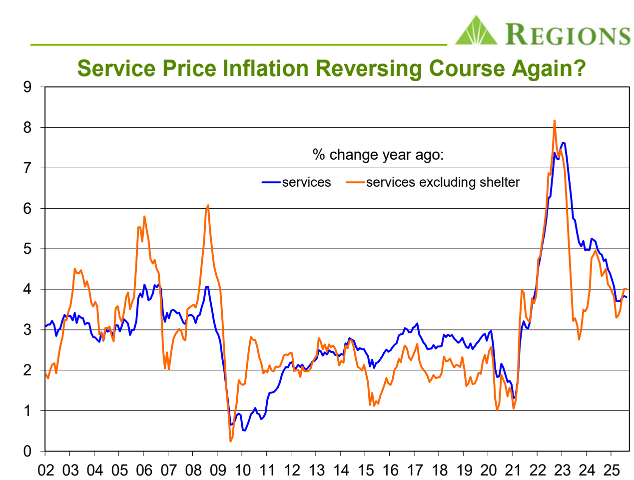
The total CPI rose by 0.4 percent in August, matching our above consensus forecast, while the core CPI rose by 0.3 percent, matching the consensus forecast but short of our forecast of a 0.4 percent increase. Kind of. On an unrounded basis, our forecast printed at 0.364 percent while the actual unrounded increase was 0.346 percent, while the year-on-year increase of 3.1 percent matches what we and the consensus expected. This goes to the point we made in our preview of the CPI data, which was that most forecasts, ours included, of the monthly change in the core CPI were right on the border of 0.3/0.4 percent, and that it would be the year-on-year change that captured most of the attention. What, at least in terms of our forecast, ended up being the swing factor in the monthly change in the core CPI is that medical care costs were more tame than our forecast anticipated. More broadly, the August data show the largest year-on-year increase in core (non-food, non-energy) goods prices since June 2023, and we continue to expect those increases to get larger over coming months. At the same time, while core services price inflation was stable in August, with the year-on-year increase of 3.6 percent matching those of June and July, the pace of price increases for discretionary services picked up at the same time owners' equivalent rents heated up. Again, softer prices for medical care services provided an offset in August, but that seems unlikely to persist, meaning that core services price inflation could pick up pace in the months ahead. If so, then core inflation will push even higher than the 3.1 percent pace seen over the past two months. With heightened concern over labor market conditions, this won't stop the FOMC from cutting the Fed funds rate at next month meeting, but we continue to argue that lingering inflation pressures leave the FOMC less scope to cut the funds rate than many market participants are anticipating will be the case.



The overall index of food prices was up by 0.5 percent in August, topping the 0.4 percent increase our forecast anticipated. Either way, the July PPI data showed a significant jump in food prices, which we thought would be passed through to the CPI data, which proved to be the case. Prices for food consumed at home jumped by 0.6 percent, the largest monthly increase since October 2022, with outsized increases in prices for meats, produce, and coffee. The August PPI data show a far smaller increase in food prices, so we'll look for that to be reflected in the September CPI data. The overall index of energy prices was up by 0.7 percent, a touch lighter than our forecast anticipated. While the 1.8 percent in gas prices on a seasonally adjusted basis was in line, electricity prices posted a more moderate advance than we anticipated would be the case.



Core goods prices rose by 0.3 percent, the largest monthly advance since May 2023. Prices for new (0.3 percent) and used (1.0 percent) motor vehicles rose in August, but we look for a larger increase in new vehicle prices in the September CPI data. The BLS's index of core goods prices excluding used motor vehicles, which we look to as a more reliable gauge of core goods price pressures, was up by 0.2 percent, matching July's increase, but is up 1.0 percent year-on-year, the largest such increase since October 2023. Apparel prices were up by 0.5 percent, but the not seasonally adjusted data show the largest August increase since 2011. There is no rhyme or reason amongst the other categories, with some, such as major appliances, showing significant declines after having shown significant increases in earlier months, and others, such as televisions, showing large increases for the first time. To be sure, the year-on-year changes may seem modest but, as our middle chart shows, there is clear upward momentum in core goods prices. Moreover, even the modest pace of core goods price inflation is at odds with the experience over much of the decade prior to the pandemic, when falling core goods prices were a drag on overall inflation.



Again, we look for core goods price inflation to pick up pace in the months ahead, and if we're correct the path of services price inflation will take on added importance. The softness seen in discretionary services prices earlier in the summer has given way to firmer prices, in part reflecting an upturn in demand and in turn reflecting less favorable seasonal adjustment. At the same time, if the 0.4 percent increase in owners' equivalent rents marks renewed firming in rents, that will be added fuel for core services price inflation.

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