Datanote: US CPI, June

In one line: Widespread disinflation; the Fed will cut soon.

- The June CPI fell by 0.1%, well below the consensus, 0.1%.
- The core increased by 0.12%, below the consensus, 0.2%.

June's CPI data bring more evidence of broad-based disinflation, giving the Fed the green light to ease multiple times this year. Prices for core services ex-rents were unchanged for the second straight month. Admittedly, a 5.0% drop in airline fares played a significant role; note that the airfares component of the core PCE deflator—the Fed's preferred inflation gauge—is derived from PPI data and often diverges from the CPI version. But our core-core services index, which removes the airline fare, auto repair and insurance, health insurance, hospital services, and accommodation services components from core services ex-rents, rose by just

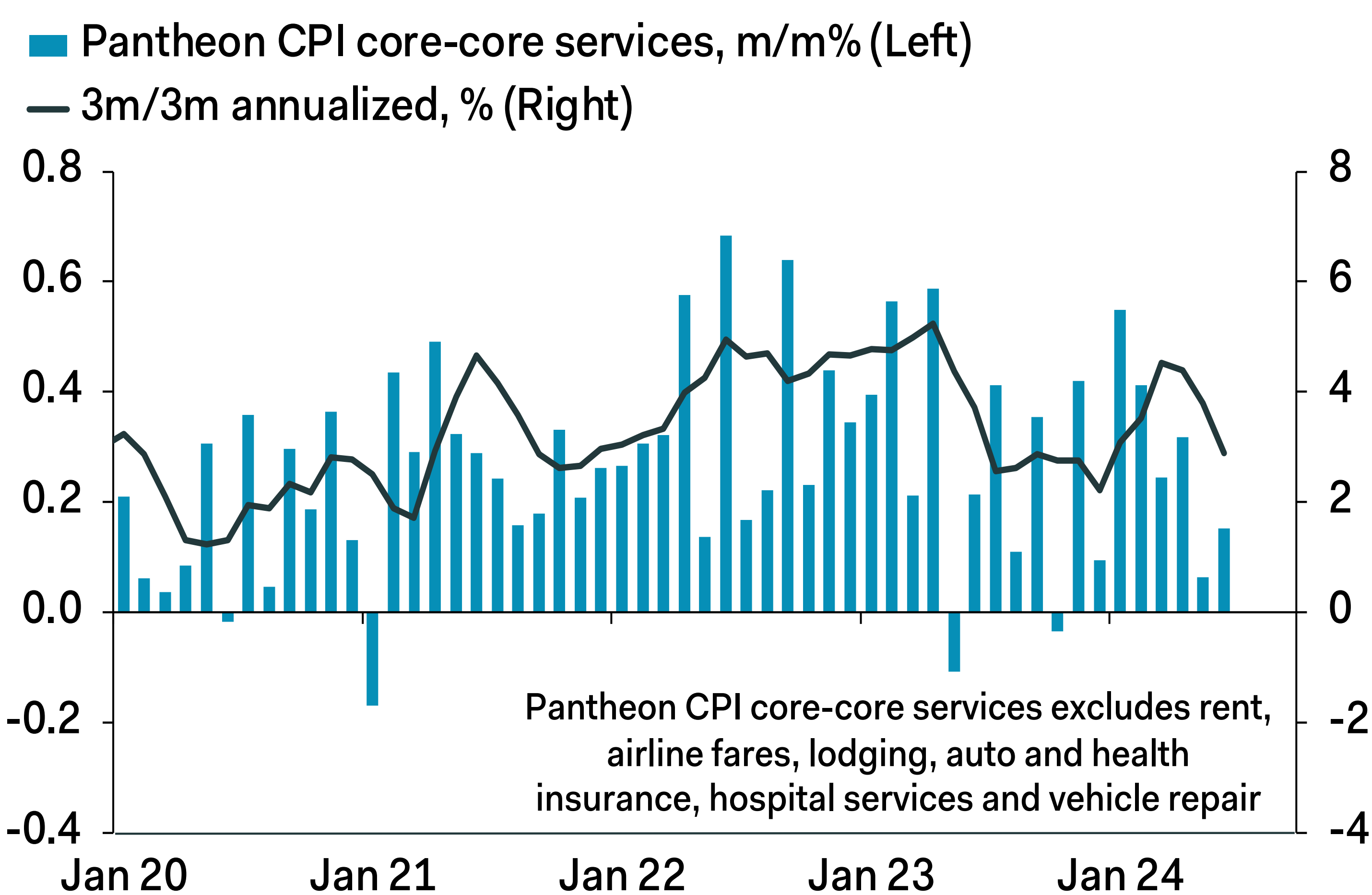
0.2%.

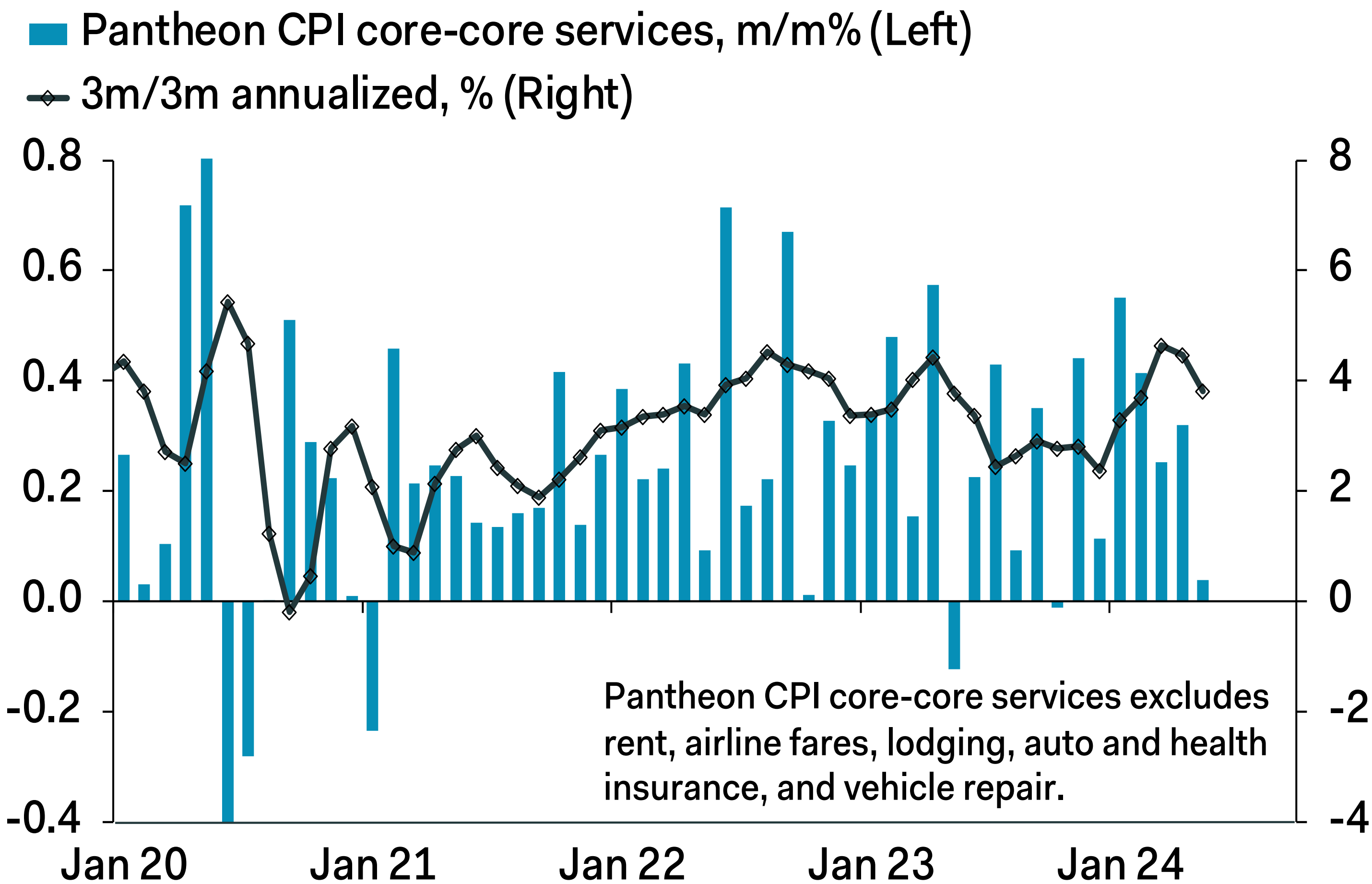
Meanwhile, primary rent increased by only 0.26% while owners' equivalent rent rose by 0.27%, both the smallest increases since April 2021. Zillow data for new rents have been signalling for some time that the run-rate of the whole-market CPI primary rent would slow, but this slowing trend had been masked in May by a fluke 1.8% jump in primary rents and OER in New York—see our second chart below—which in June rose by just 0.2%. We think the trend in both primary rents and OER will run at 0.30% in the second half of this year. Note that June is the final month in which the month-to-month change in OER could have been boosted by January's increase in the weight in the sample of single-family detached homes, which command higher rents than multi-family units. Remember, the reported month-to-month change in both OER and primary rents is the sixth root of the change in rents in the same panel of tenants across the past six months.

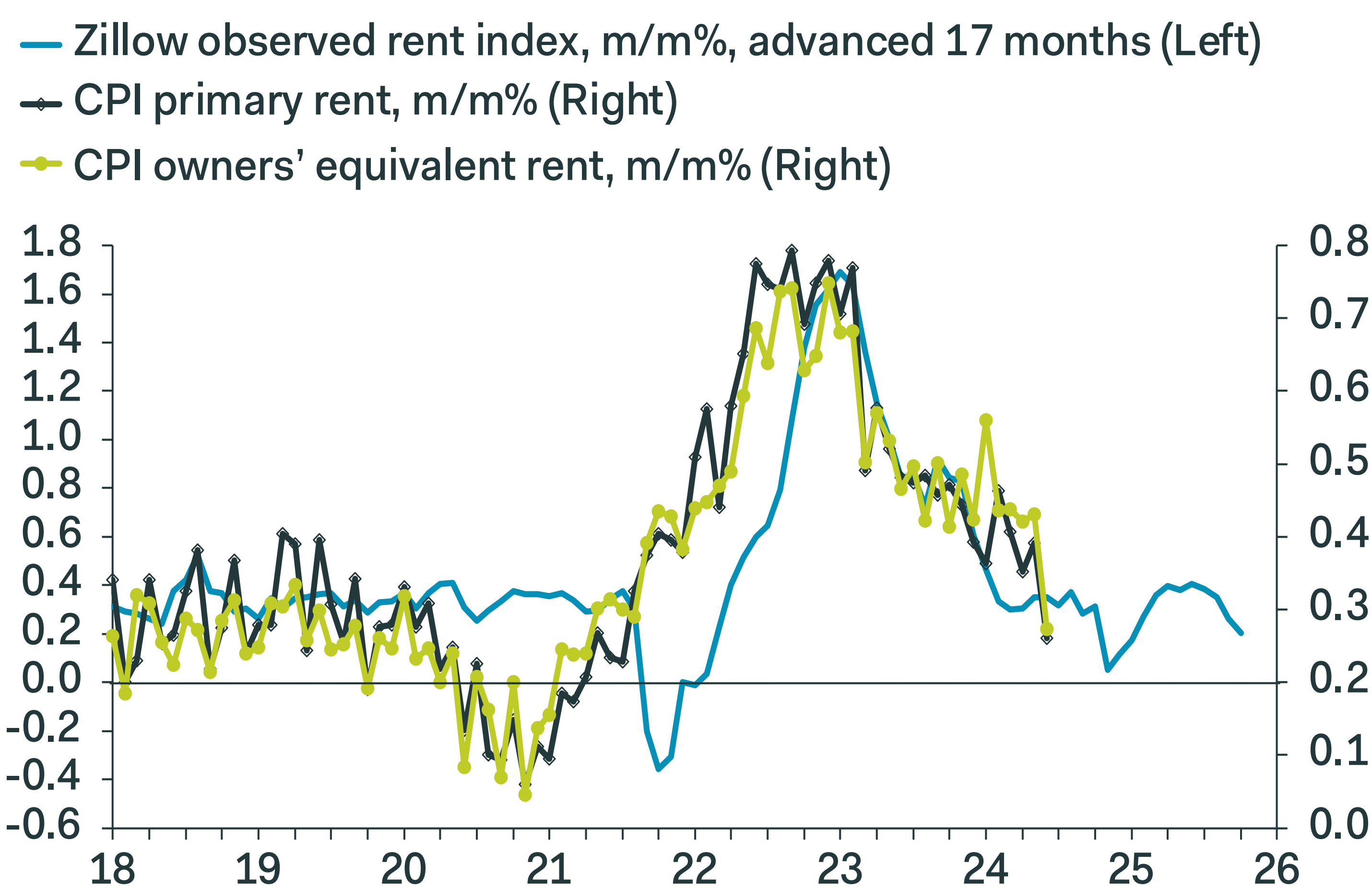
Elsewhere, core goods prices fell by 0.1%, driven by a hefty 1.5% drop in used car prices and a 0.2% decline in new motor vehicle prices, the fifth straight drop. Core goods ex-auto prices rose by just 0.1%, driven by a 0.5% jump in prices for household furnishings, but the trend still looks flat.

Two-thirds of the components of the core PCE deflator are derived from CPI data, with the bulk of the remainder derived from the PPI. After today's CPI data, we provisionally forecast that the core PCE deflator increased by 0.17% in June. That would exceed May's 0.08% increase but would be just half the 0.34% average in the first four months of this year, and likely would leave the FOMC much more confident that the annual rate is on course to hit its 2% target soon. We will update our estimate after tomorrow's PPI data, which are more volatile than the CPI figures.

Looking ahead, the foundations remain in place for CPI inflation to drop further in the second half of this year. Labor market slack is building, dragging on wage growth and new rent increases, while retailers' margins are under mounting pressure from increasingly budget-conscious consumers. Shipping costs have surged, but past experience suggests that consumer goods prices will be unaffected until the first half of next year, and both manufacturers and retailers likely will absorb a hefty chunk of the increase in costs. Indeed, below-average capacity utilization in the manufacturing sector and retailers' excess inventory levels suggest that the outlook for core goods CPI inflation remains benign. Meanwhile, global food and energy prices remain unthreatening, and falling vehicle prices point to scope for the inflation rates for auto insurance and repair to fall further in the second half of this year. Accordingly, the CPI data will not stand in the way of the FOMC cutting interest rates quickly later this year in response to a faltering labor market. We continue to expect 125bp of easing this year, beginning in September with a 25bp cut. The sooner the better.




Pantheon CPI core-core services, m/m% (Left)
3m/3m annualized, % (Right)
0.8
0.6
0.4
0.2
0.0
-0.2
-0.4
8
6
4
2
0
-2
-4
Pantheon CPI core-core services excludes rent, airline fares, lodging, auto and health insurance, and vehicle repair.
Jan 20
Jan 21
Jan 22
Jan 23
Jan 24


Zillow observed rent index, m/m%, advanced 17 months (Left)
CPI primary rent, m/m% (Right)
CPI owners' equivalent rent, m/m% (Right)
1.8
1.6
1.4
1.2
1.0
0.8
0.6
0.4
0.2
0.0
-0.2
-0.4
-0.6
0.8
0.7
0.6
0.5
0.4
0.3
0.2
0.1
0.0
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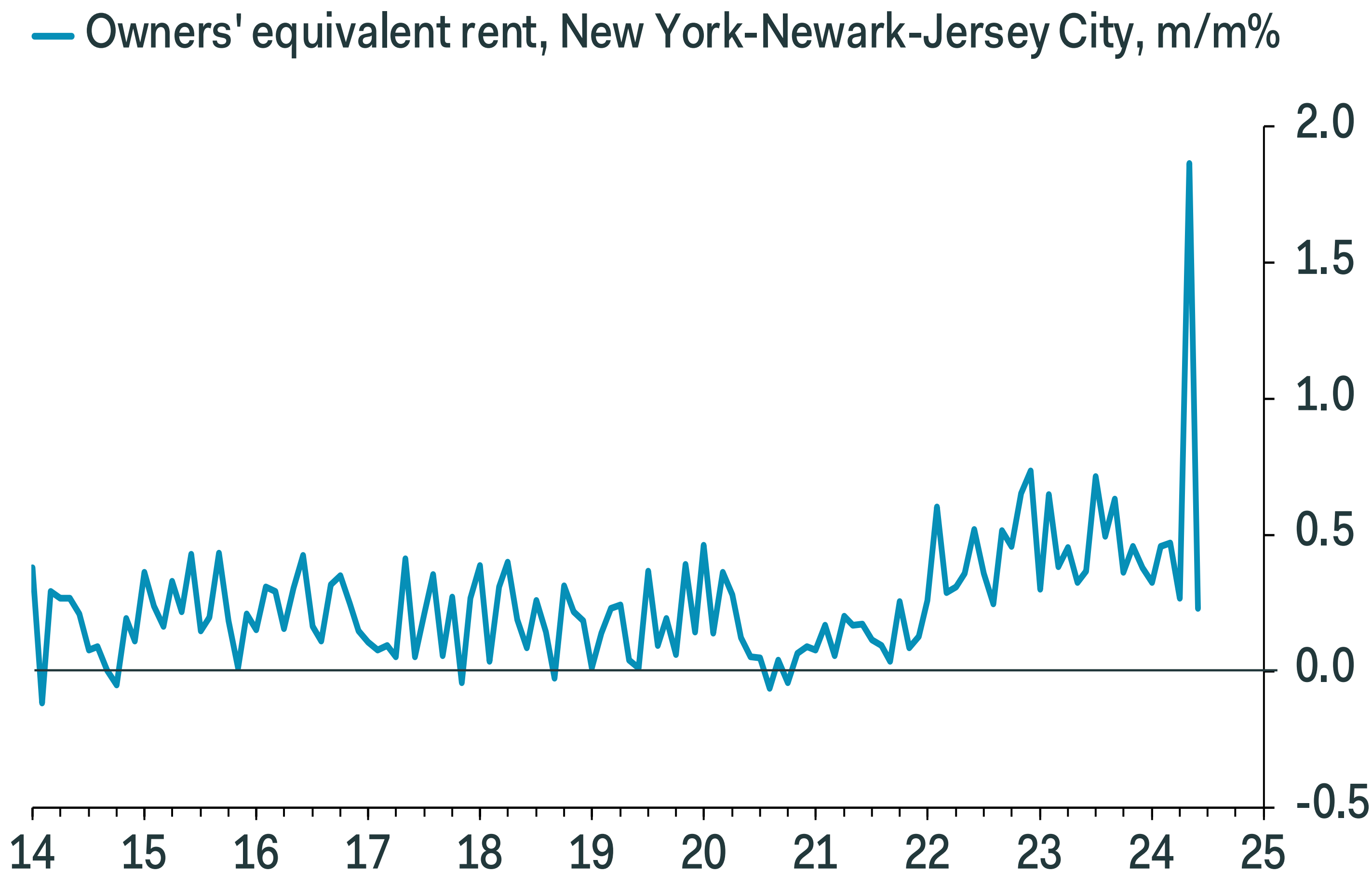

Owners' equivalent rent, New York-Newark-Jersey City, m/m%
2.0
1.5
1.0
0.5
0.0
-0.5
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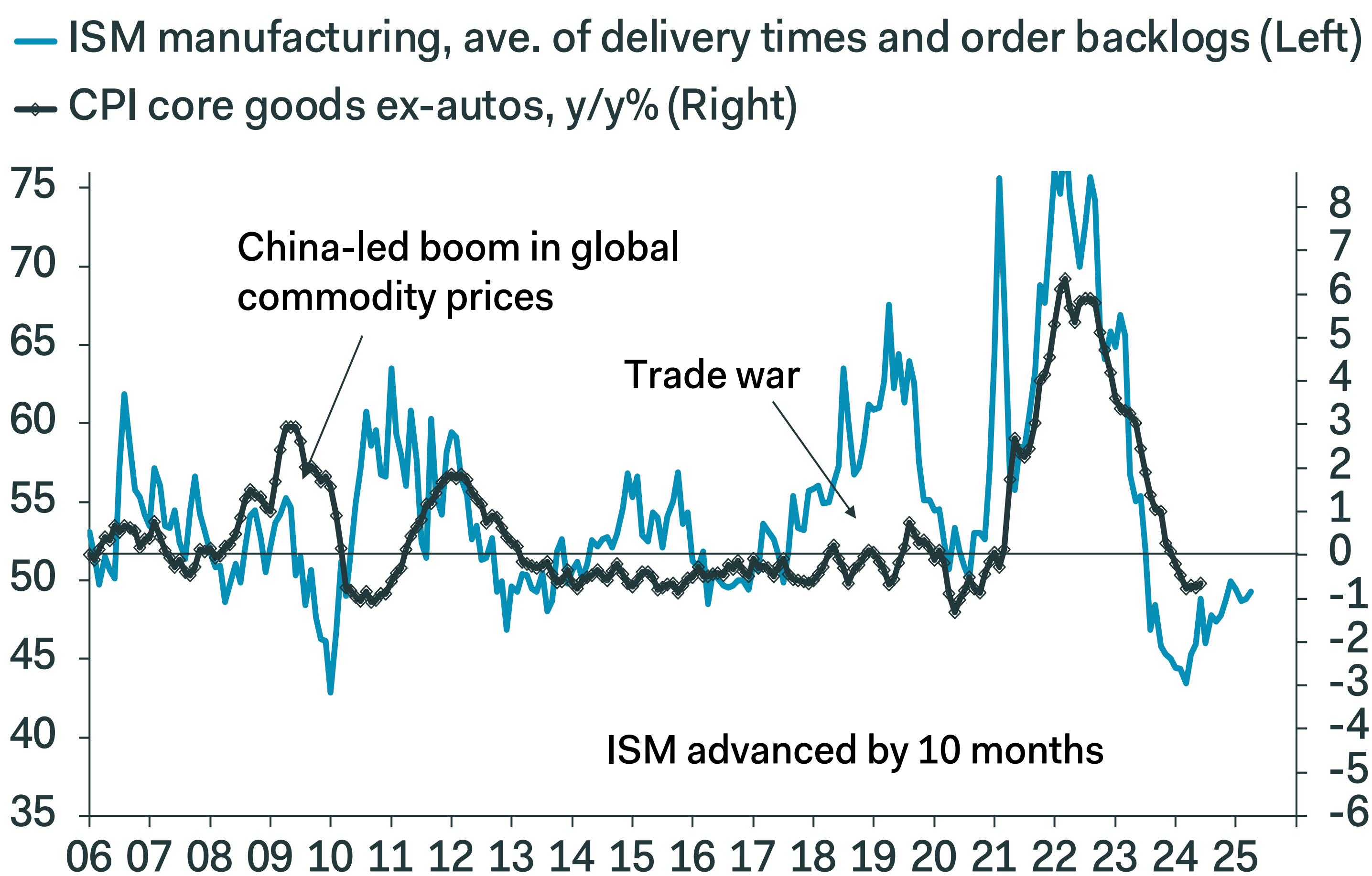

ISM manufacturing, ave. of delivery times and order backlogs (Left)
CPI core goods ex-autos, y/y% (Right)
China-led boom in global commodity prices
Trade war
ISM advanced by 10 months
75
70
65
60
55
50
45
40
35
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-1
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