Datanote: U.S. Producer Prices, May 2024

In one line: May core PCE likely rose just 0.11%, well below the Fed's expectations.

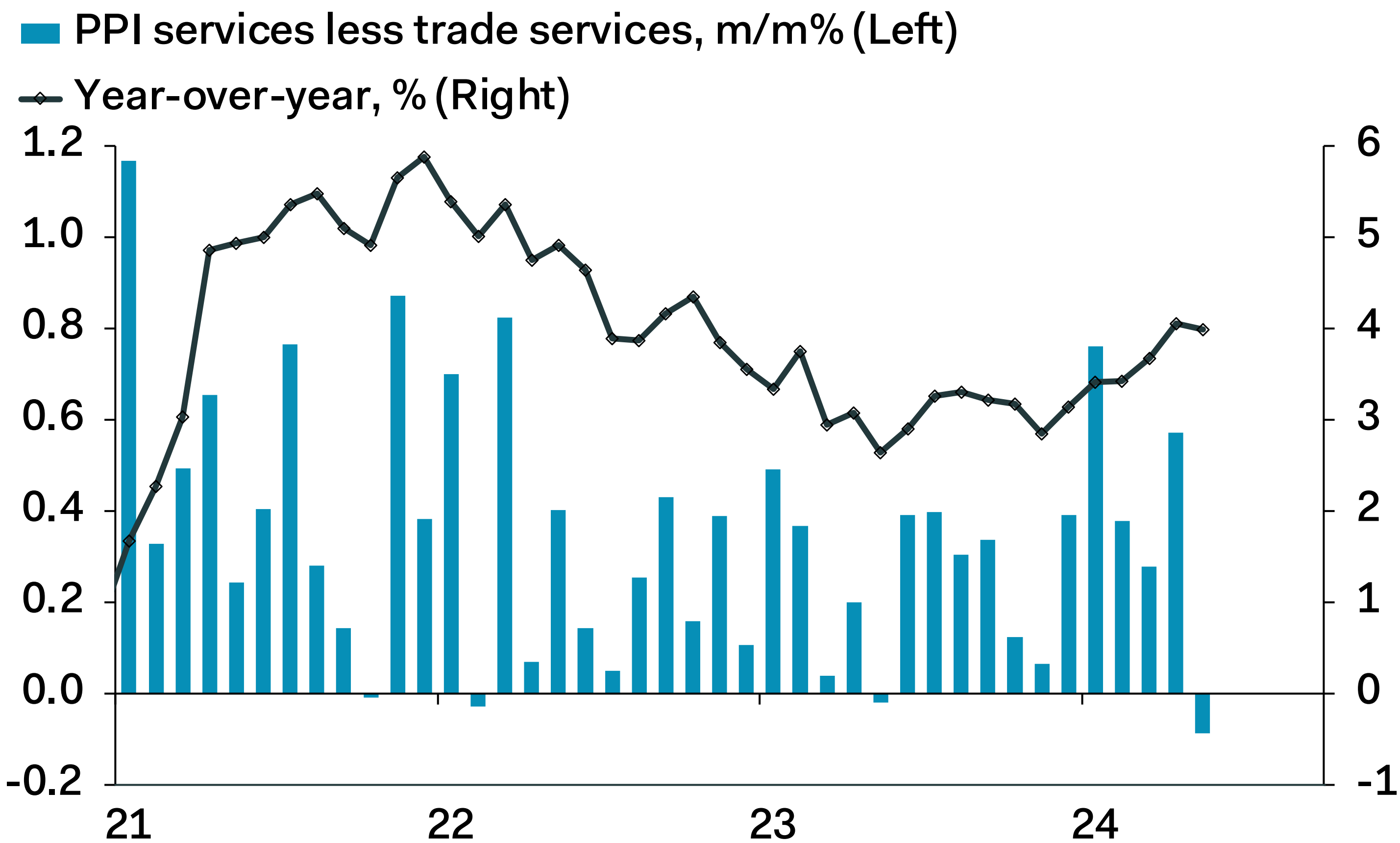
- The headline May PPI fell by 0.2%, below the consensus, +0.1%.
- The core was unchanged, well below the consensus, 0.3%.
- The core ex-trade services was also unchanged, also well below the consensus, 0.3%.

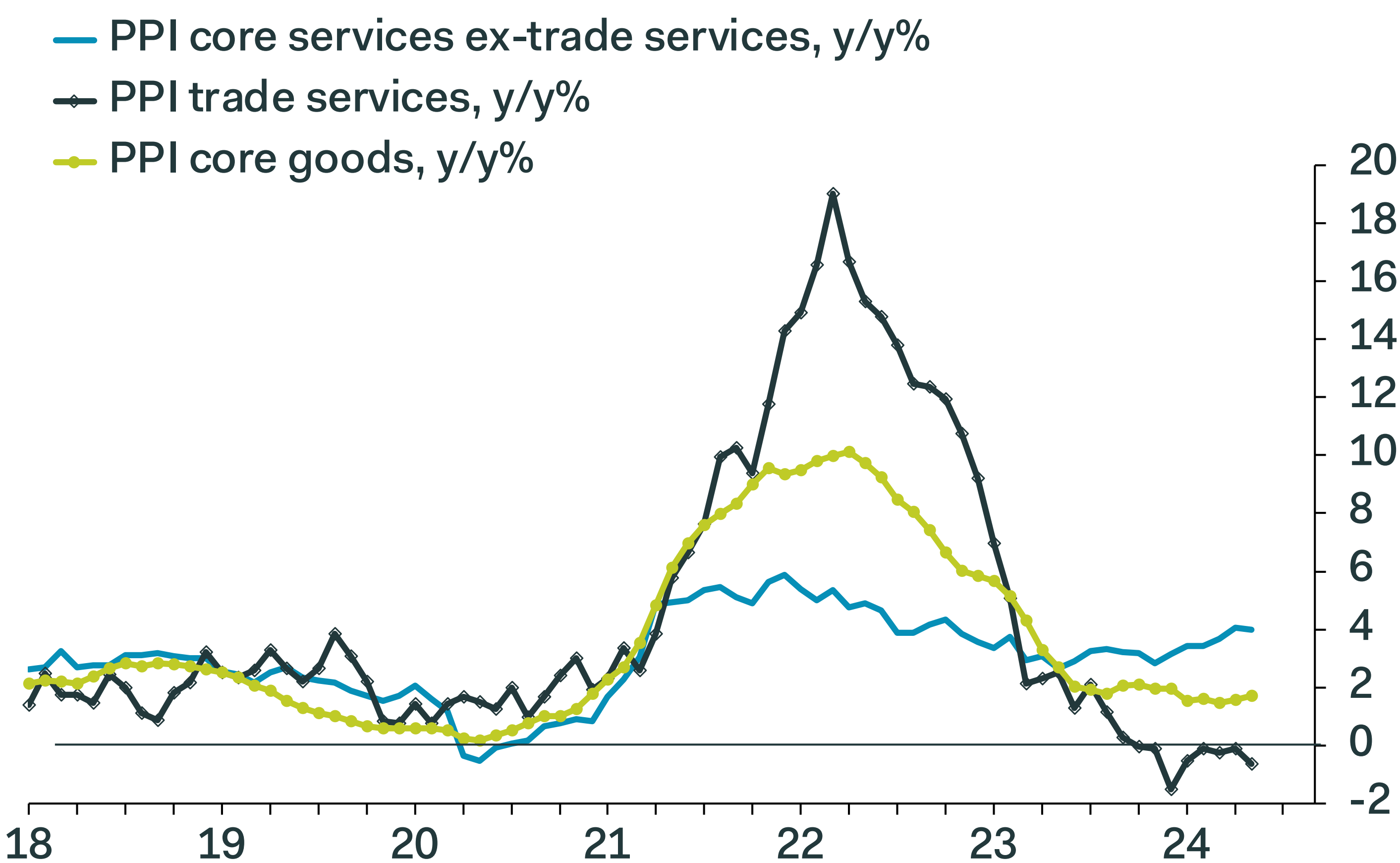
May’s PPI figures add to the growing mosaic of evidence that disinflation is back on track, after a hiatus in Q1. PPI services ex-trade services fell by 0.1%, the first decline since April 2020, well below the 0.5% average increase in the first four months of this year. Admittedly, the slowdown was partly due to a 3.9% decline in domestic airline fares, but this component is unadjusted and tends to fall in May. Fares also were dragged down by a fall in jet fuel prices, which have subsequently stabilized. In addition, the 1.7% drop in portfolio management charges reflects the pause in the rally in stocks, which has since resumed. Nevertheless, PPIs for a broad array of other services, such as physician care, car rental, accommodation services and telecoms, also rose less quickly in May than in previous months, consistent with the recent slowdown in wage growth and slowing growth in households' spending.

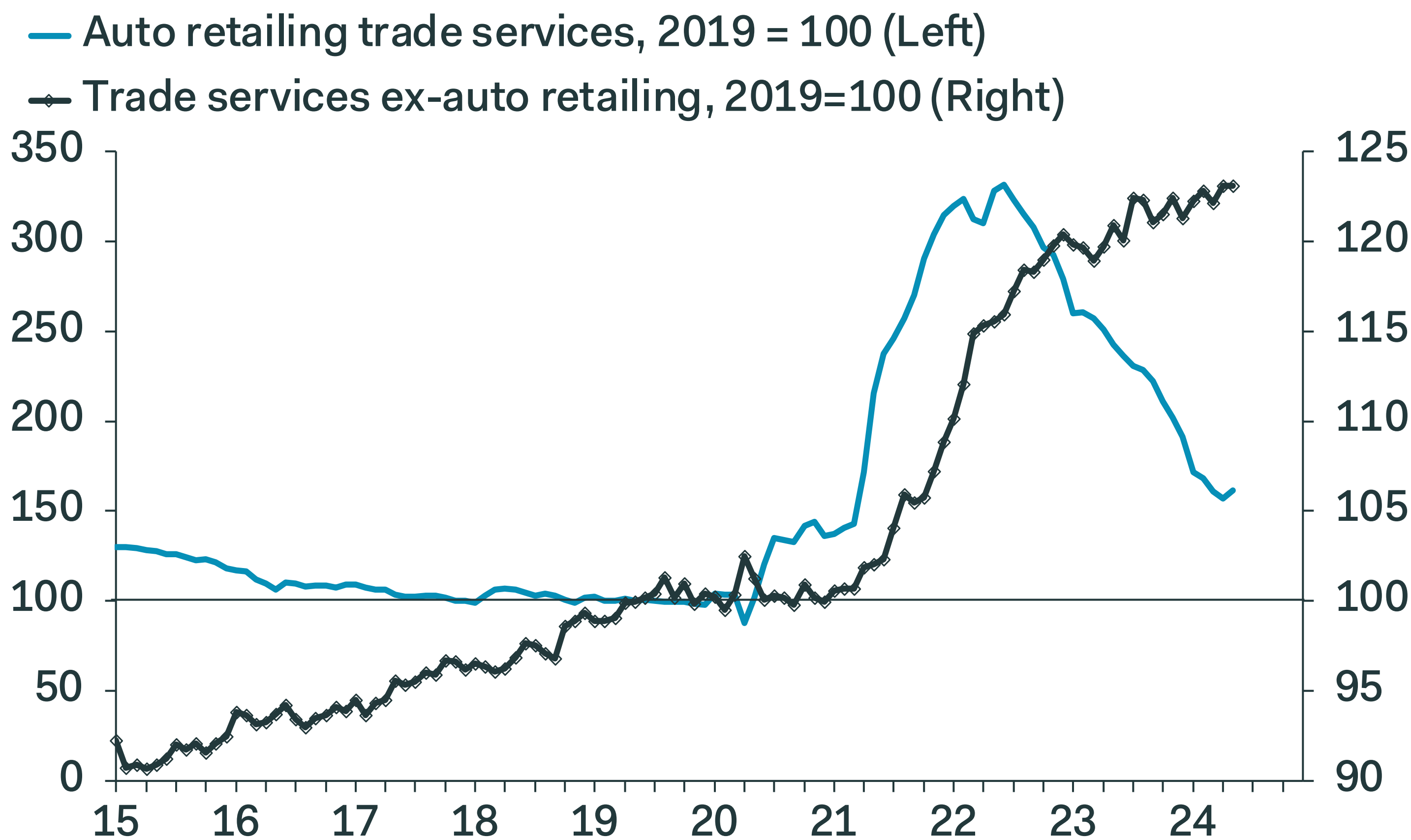
Meanwhile, gross retail and wholesale margins—aka "trade services"—rose by

0.2%, but they fell by 0.2% excluding the volatile fuel component. Margins ex-fuel remain well above the level implied by their pre-Covid trend, but they are now falling, down 0.7% year-over-year in May. A prolonged period of decline lies ahead, assuming the slowdown in consumers' spending growth continues, as we expect. Auto dealers have already seen a rapid and substantial reversal of their pandemic-era margin surge as sales have stalled, suggesting that other retailers will follow suit as they adjust to slower demand.

Our mapping of the PPI and CPI data suggests that the core PCE deflator increased by only 0.11% in May, well below the 0.32% average increase in the first four months of this year. It is impossible to predict the core PCE print perfectly, as the seasonal adjustment performed by the BEA is difficult to replicate for some components, and some components are based on non-CPI/PPI data sources. Nevertheless, the Fed's new forecasts imply they expect the core PCE deflator to rise at a 0.19% average pace between May and December. We don’t know what policymakers specifically pencilled in for May, but our estimate points to a material downside surprise. Meanwhile, the outlook for slower rent gains, falling wage inflation, and margin compression at retailers suggests that the core PCE deflator will continue to rise more slowly than the Fed predicted this week, laying the foundations for the first rate cut to come in September and multiple easings this year.


PPI services less trade services, m/m% (Left)
Year-over-year, % (Right)
1.2
1.0
0.8
0.6
0.4
0.2
0.0
-0.2
6
5
4
3
2
1
0
-1
21
22
23
24


PPI core services ex-trade services, y/y%
PPI trade services, y/y%
PPI core goods, y/y%
20
18
16
14
12
10
8
6
4
2
0
-2
18
19
20
21
22
23
24


Auto retailing trade services, 2019 = 100 (Left)
Trade services ex-auto retailing, 2019=100 (Right)
350
300
250
200
150
100
50
0
125
120
115
110
105
100
95
90
15
16
17
18
19
20
21
22
23
24