Consumer Price Index July 2024

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Tame CPI report bolsters the case for a September cut

- The July Consumer Price Index (CPI) report offered more convincing evidence that inflation pressures are abating. Headline CPI rose 0.2% month over month (m/m), in line with expectations, with energy prices unchanged on the month and food prices up 0.2%. Core CPI rose a modest 0.2% (0.165% to be precise) — somewhat firmer than the June reading but softer than the average 0.3% m/m gain in H1.
- As a result, headline CPI inflation eased 0.1 percentage point (ppt) to 2.9% year over year (y/y) — the lowest since March 2021. Meanwhile, core CPI inflation eased for a fourth consecutive month and fell 0.1ppt to 3.2% y/y in July — the slowest pace since April 2021.
- Disinflation momentum should accelerate in the coming months as favorable year-on-year comparisons in August and September will likely push headline CPI inflation markedly lower toward 2.5% to 2.6%, a pace we expect will be maintained throughout year-end. Meanwhile, core CPI inflation is likely to gradually ease toward 3% y/y in the coming months.
- Softer consumer spending growth due to increased pricing sensitivity, reduced markups, moderating wage growth and declining rent inflation will continue to provide a healthy disinflationary impulse heading into 2025. We foresee headline and core CPI inflation reaching 2.6% y/y and 3% y/y in Q4, respectively.
- Overall, the sustained moderation in inflation in recent months provides ample room for the Fed to start its policy recalibration, in our view. And the latest CPI data only strengthened the case for a September Fed rate cut amid signs that the labor market slowdown is accelerating. We continue to expect three 25 basis points (bps) rate cuts before year-end, in September, November and December, and foresee an additional 125bps of rate cuts in 2025.

Energy prices were unchanged in July with gasoline prices flat on the month, and food prices rose 0.2% on modest gains in restaurant and grocery store prices of 0.2% and 0.1%, respectively. Grocery store prices have moderated markedly from their August 2022 peak of 13.5% y/y and have maintained a subdued pace of around 1% y/y over the past 10 months.

Core goods prices surprised on the downside with a 0.3% m/m decline — the weakest reading since January. The decline in prices was driven by a 2.3% plunge in used car prices, which have fallen in four of the five past months. New vehicles prices also fell for a sixth consecutive month, down 0.2%. Apparel prices were down 0.4%, following a mere 0.1% increase in the prior month.

Meanwhile core services prices rose 0.3%, a modest step up from the soft 0.2% and 0.1% increases seen in May and June, respectively. Shelter costs regained some momentum and grew 0.4% in July, suggesting that the significant moderation in rents seen in the June data was likely overstated. Rent and owners' equivalent rent rose 0.4% and 0.5%, respectively, after posting their weakest gains since mid-2021. We still expect gradual shelter cost disinflation to continue in the coming months, helping drive lower headline and core inflation. Hotel prices grew 0.2% following their 2% plunge in June while airfares dropped for a fifth consecutive month, down 1.6%, indicating more consumer prudence with travel and leisure activities.

The Fed's favored (but perhaps misleading) "supercore" CPI measure — core services excluding shelter costs — rose 0.21% after declining for two consecutive months. However, the advance is still much slower than the average 0.5% in the first four months of the year. Motor vehicle insurance prices, which are a key driver of supercore inflation, regained some momentum and rose 1.2% in July. Auto insurance prices are still rising at a staggering 18.6% year-on-year rate, though inflation is off its peak reached earlier this year of around 23% y/y.

Overall, short-term inflation dynamics were again very encouraging: On a three-month annualized basis, headline CPI inflation eased 0.7ppt to 0.4% while core CPI inflation fell 0.5ppt to 1.6%. On a six-month annualized basis, headline CPI inflation eased 0.3ppt to 2.5% and core CPI inflation eased 0.5ppt to 2.8%.

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