ECONOMIC UPDATE

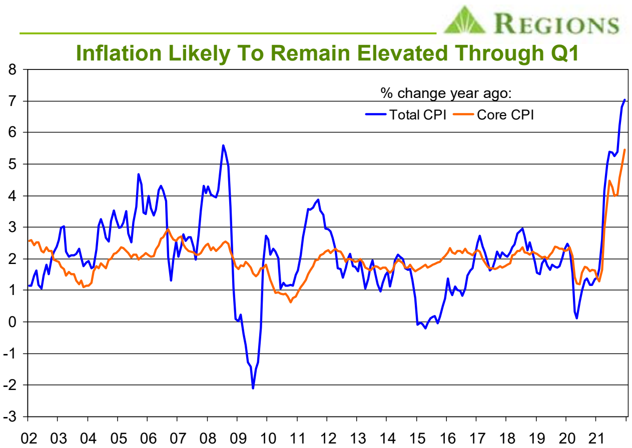
REGIONS

January 12, 2022

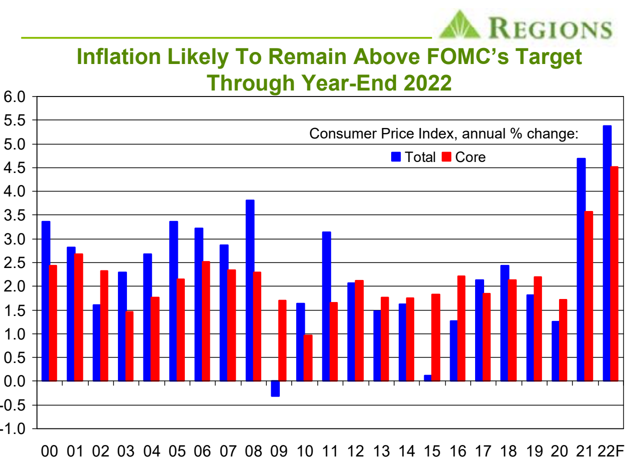
December Consumer Price Index: The Peak Is Near, But Then What?

- The total CPI rose by 0.5 percent in December (up 0.470 percent unrounded); the core CPI rose by 0.6 percent (up 0.550 percent unrounded)
- On a year-over-year basis, the total CPI is up 7.0 percent and the core CPI is up 5.5 percent as of December

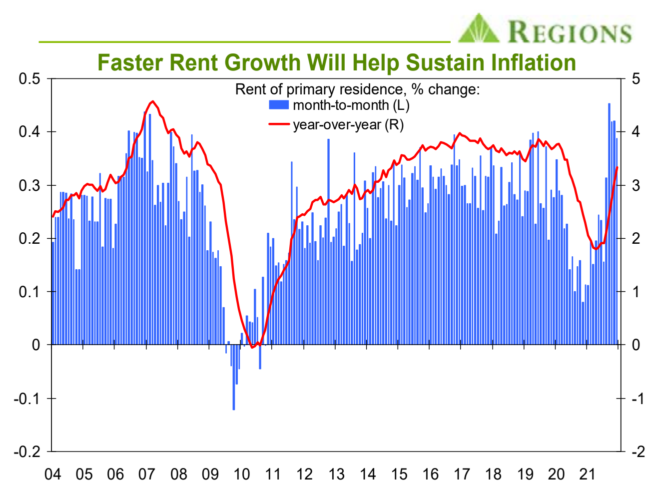
The total CPI rose by 0.5 percent in December while the core CPI rose by 0.6 percent, each matching our above-consensus forecast. On an over-the-year basis, the total CPI is up 7.0 percent as of December, and we'd note that this is the largest such increase since June 1982 but doing so would be "needlessly sensationalizing" a "brief period" of rapid inflation, so we won't. Oops. In any event, the core CPI is up 5.5 percent on an over-the-year basis, the fastest rate of core CPI inflation since February 1991. While lower energy prices acted as a drag on the total CPI in December, higher prices for food, apparel, and motor vehicles pushed the headline index higher. The drag from energy prices will prove to be short-lived as prices have bounced back from the rapid decline triggered by news of the emergence of the Omicron variant. While there are signs that global supply chain and logistics bottlenecks have begun to ease, it will take some time before that is apparent in core goods prices, and it will take more meaningful and sustained easing in these supply-side constraints before we see a pronounced easing in core goods prices. At the same time, we look for faster growth in services prices, including rents and medical care costs, and robust growth in labor costs to keep inflation easily above the FOMC's 2.0 percent target rate through year-end 2022.



Energy prices fell by 0.4 percent in December but were nonetheless up 29.3 percent year-on-year. Retail gasoline prices were down by 0.5 percent, but that followed two straight monthly increases of 6.1 percent. Pump prices have turned higher in recent weeks and with crude oil prices having pushed back above the $80 mark, retail gasoline prices will follow them up. Prices for home heating oil and residential gas service have followed a similar pattern, and their reversal will be hastened by the return of more normal winter weather. Food prices were up by 0.5 percent in December, the smallest monthly increase since August. Somewhat surprisingly, December's more moderate increase in overall food prices stems from prices for food consumed at home rising by "just" 0.4 percent, the smallest monthly increase since March, though this still leaves them up 6.5 percent year-on-year. Prices for meats fell by 0.9 percent in December (up 14.8 percent year-on-year), with less broad based increases in other categories than has been the case in recent months. Prices for food consumed away from home rose by 0.6 percent in December.



Prices for core goods (consumer goods excluding food and energy) rose by 1.2 percent in December, with a considerable push from vehicle prices. Prices for used motor vehicles rose by 3.5 percent, with prices for new vehicles up 1.0 percent. Though motor vehicle production has risen in recent months, that increase comes off of a very deep bottom and motor vehicles remain notably lean. Though not to the extent seen in December, vehicle prices will remain a support for inflation over coming months. Apparel prices were up by 1.7 percent in December, though there could be some issue with seasonal adjustment here, particularly given the lack of holiday season discounting this year brought about by inventories running well below normal. Lean inventories are also fueling continued hefty increases in prices for appliances (up 1.1 percent in December) and furniture/bedding (up 2.0 percent in December). While we do look for relief from supply chain and logistics bottlenecks over the course of this year, that relief is likely to come at a somewhat uneven pace, so it will be some time before that is reflected in core goods prices.



While goods price disinflation, if not outright deflation, will take some of the steam out of inflation as this year progresses, we anticipate faster growth in services prices, including rents and medical care, will take up much of the slack. Primary rents were up by 0.4 percent in December, leaving them up 3.3 percent year-on-year, with owners' equivalent rents also up 0.4 percent, good for a year-on-year increase of 3.8 percent, the largest such increase since April 2007. The CPI tends to lag other measures of rent growth, and we expect further acceleration in rent growth, particularly as labor market conditions continue to improve, which is one reason we expect inflation to remain above the FOMC's target rate through year-end 2022.

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