ECONOMIC UPDATE

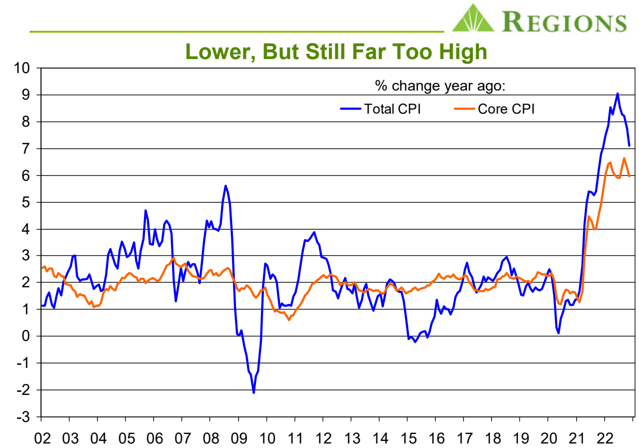
REGIONS

December 13, 2022

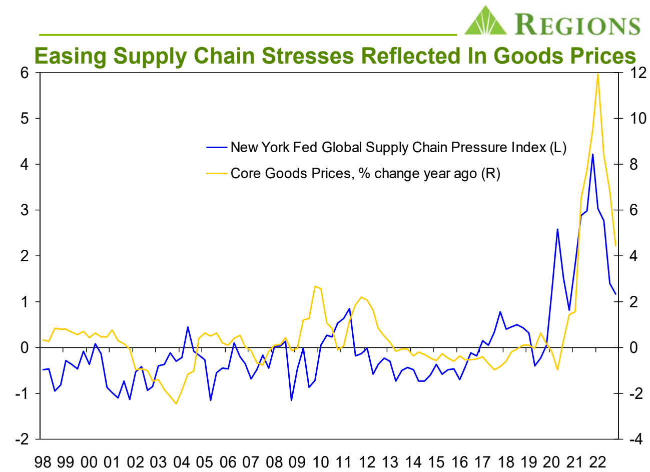
November Consumer Price Index: Lower, But Still Far Too High

- The total CPI rose by 0.1 percent in November (up 0.096 percent unrounded); the core CPI rose by 0.2 percent (up 0.199 percent unrounded)
- On a year-over-year basis, the total CPI is up 7.1 percent, and the core CPI is up 6.0 percent as of November

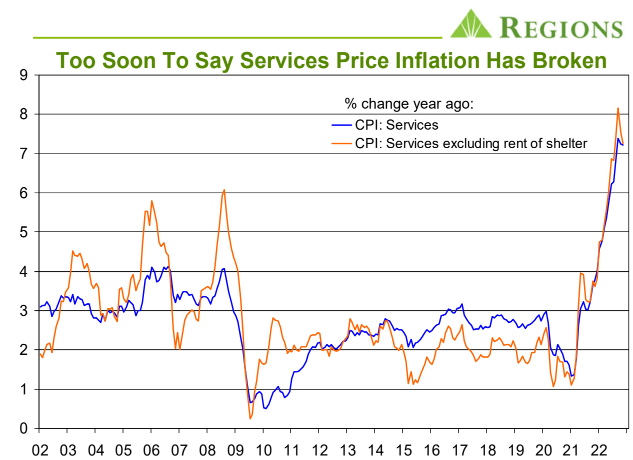
The total CPI rose by 0.1 percent in November, falling short of our below-consensus forecast of a 0.2 percent increase, while the core CPI rose by 0.2 percent, shy of the 0.3 percent increase we and the consensus expected. Falling energy prices, falling prices for core goods that go beyond another steep decline in prices for used motor vehicles, lower air fares and lodging rates, and another steep decline in prices for health insurance all contributed to the softer than expected increases in the CPI in November. Some of these factors, however, carry considerably less weight than others. For instance, two straight monthly declines of at least 4.0 percent in prices for health insurance reflect no more than a change in methodology which tells us nothing about underlying economic conditions but which will nonetheless be felt in the CPI data until next fall. At the same time, while ongoing steep declines in prices for used motor vehicles are having an outsized impact on core goods prices, there is much more behind falling core goods prices. Ahead of the release of the November CPI data there was considerable discussion as to what the data might mean for the FOMC. Our answer after the release of the data is the same as was our answer before the release of the data, which is that the November CPI data will change nothing. Inflation is clearly decelerating even if some noise in the data makes it hard to gauge the true speed of that deceleration, but despite decelerating, inflation remains far above the FOMC's target. To us, this simply bolsters the case for the FOMC beginning to wind down its course of Fed funds rate hikes but being far from considering rate cuts.



The broad energy index fell by 1.6 percent in November, with retail gasoline prices down by 2.0 percent on a seasonally adjusted basis. While prices for fuel oil were up, prices for electricity and residential gas service fell, the latter by 3.5 percent. Though still well above their year-ago levels, energy prices are nonetheless falling on a sequential basis, and the data we have to date suggests falling gasoline prices will be a powerful drag on the December CPI. Food prices were up by 0.5 percent in November, the smallest monthly gain since last December. Prices for food consumed at home were up by 0.5 percent, matching the increase seen in prices for food consumed away from home; in the latter category, this is the smallest increase since March.



Core goods (consumer goods excluding food and energy) prices were down by 0.5 percent in November, a second straight monthly decline which brings the over-the-year increase down to 3.7 percent, the smallest such increase since March 2021. Prices for used motor vehicles fell by 2.9 percent in November, the fifth straight monthly decline. The BLS's measure of prices for core goods excluding used motor vehicles was flat in November, and while we had expected it to be down slightly it is nonetheless up by "just" 5.4 percent year-on-year, the smallest such increase since September 2021. One factor helping relieve pressure on core goods prices is the further normalization of global supply chains, and as supply chain stresses continue to abate core goods prices will come under further downward pressure, particularly given elevated retail inventories of goods.



While core goods prices are turning into a drag on overall inflation, they account for a much lower weight in the overall CPI than do core services prices, meaning it is the latter that hold the key to how rapidly inflation will decelerate in the months ahead. Still, as noted above, the noise from health care services makes it hard to assess that, but it is also worth noting that the methodological change impacting the CPI data does not impact the PCE Deflator, the FOMC's preferred gauge of inflation. More fundamentally, even though rent growth notched higher after an unexpectedly small increase in October, it is clear that rent growth has slowed dramatically and it is only a matter of time before that is picked up in the CPI data. We have been expecting consumer spending on discretionary services to soften, so in that sense it is interesting that air fares, lodging rates, and rental car rates fell in November. If this is a reflection of softening demand, it could be that core services inflation decelerates at a faster rate than is generally expected to be the case. But, keep in mind that we are now at the cycle peak for core services inflation – 6.8 percent – so even a faster rate of decline leaves us with a long way down to go.

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