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October Consumer Price Index: Core Inflation Beginning To Stir?

- > The total CPI rose 0.1 percent (0.108 percent unrounded) in October; the core CPI was up 0.2 percent (0.225 percent unrounded)
- > On a year-over-year basis, the total CPI was up 2.0 percent and the core CPI was up 1.8 percent in October

The total CPI rose by 0.1 percent in October with the core CPI up 0.2 percent, both matching our forecasts, which in turn matched the consensus forecasts. October's gains leave the total CPI up 2.0 percent year-on-year and the core CPI up 1.8 percent. As expected, the October data continue to reflect, to varying degrees, effects of Hurricanes Harvey and Irma. In that sense, the September and October CPI reports are more noise than signal, but down in the details there are some signs that core inflation may be beginning to stir. Tentative signs, to be sure, but if you're, say, a central banker looking hard for signs of inflation heading your way, you'll take what you can get at this point.

After having spiked by 13.1 percent (not seasonally adjusted) in September, reflecting Hurricane Harvey taking down over 20 percent of the nation's refining capacity, gasoline prices as measured in the CPI data fell by 5.4 percent in October, thus acting as a drag on the total CPI. We'll caution, however, that gasoline prices are not done wreaking havoc on the headline CPI – with prices rising thus far in November, counter to typical seasonal declines, gasoline prices will be up big on a seasonally adjusted basis in the November CPI data. The difference between November and September, however, is that this month's increases in retail gasoline prices reflect crude oil prices having taken up residency in the mid-\$50s and, to the extent they stay there, the most recent increases in gasoline (and other energy) prices cannot simply be dismissed as transitory, though they will have an outsized impact on the seasonally adjusted CPI data.

Food prices were flat in October after having risen just 0.1 percent in September. This is in contrast to our expectations of some firming in October, and is also at odds with the jump reported in the October Producer Price Index. Prices for food consumed at home were down slightly while prices for food consumed away from home were up a scant 0.1 percent, well below trend for this series. Lodging prices held up better than we had anticipated in October, rising by 1.6 percent and thus building on hefty increases in the wake of the hurricanes. Prices for used motor vehicles were up 0.7 percent in October, ending a nine-month string of declines. Firmer demand in the wake of the hurricanes has been a support for used vehicle prices, so it remains to be seen whether or not October's increase will stick. New vehicle prices, however, fell by 0.2 percent in October.

In our weekly *Economic Preview*, we noted the September CPI data showed oddly small increases in rents and that we expected payback in the October data. While we were right on this point, what we did not expect was that the increase in owners' equivalent rents (up 0.32 percent) would top the increase in market rents (up 0.27 percent). It could be that owners' equivalent rents are catching up to rapid house price appreciation across many parts of the U.S., and we do expect continued deceleration in market rents given what for some time now has been a bulging pipeline of multi-family rental units under construction. Still, October's increase leaves market rents up 3.7 percent year-on-year.

With rents accounting for over 40 percent of the core CPI, it's important to look at non-shelter core inflation as a gauge of broader inflation pressures. Sure, at 0.7 percent in October this metric is hardly screaming "hyper-inflation is nigh" but it is nonetheless up from the prior several months. Core goods prices were flat in October, though this still leaves them down year-on-year – only once in the past 4 1/2 years have core goods prices been up year-on-year. If there is going to be a meaningful turn in the inflation data, non-shelter core inflation is where we'll see it first, making the October print more relevant.

The FOMC will see one more CPI report before making a decision on interest rates at their December meeting. How much clarity the November data will bring, however, is an open question, even with the focus on core inflation. That said, the October data suggest those who have argued the recent deceleration in inflation is transitory may find it a bit easier to make their case even, if it isn't an open and shut case.

