ECONOMIC PREVIEW

REGIONS

Week of August 6, 2018

Indicator/Action Economics Survey:	Last Actual:	Regions' View:
Fed Funds Rate: Target Range Midpoint *(After the September 25-26 FOMC meeting):* Target Range Midpoint: 2.125 to 2.125 percent Median Target Range Midpoint: 2.125 percent	Range: 1.75% to 2.00% Midpoint: 1.875%	Inflation is front and center in a light week for top-tier data releases. Still, the July CPI report is likely to cause quite a stir – if our forecast (see below) is correct, headline CPI inflation will hit 3.0 percent for the first time since December 2011. Indeed, we heard one correspondent caution that there would be some "shock effect" from a three-handle on headline inflation. Shock effect? Dude, seriously, shock effect is an inflation rate of 46,305 percent, as was recently logged in Venezuela. So, before anyone breaks out the wage and price controls, we'll note that July should mark the peak for headline inflation in 2018. While energy has played a role in accelerating inflation over the past several months, base effects have played a larger role, as last year's sharp decline in prices for cell phone service plans have skewed over-the-year comparisons higher, which should not have come as even a mild surprise, let alone a shock, to anyone. Once we get past the July data, however, those base effects will fade and headline inflation will decelerate. The extent of that deceleration, however, remains to be seen. Firms across virtually every sector of the U.S. economy are contending with rising input costs, both labor and non-labor, and transportation costs are also rising at a faster clip. To the extent tariffs are extended to a broader swath of the economy, this only adds to mounting cost pressures. The FOMC has gone out of their way over recent months to stress that their inflation target is "symmetric," and we think coming months could test the Committee's tolerance for inflation running ahead of their 2.0 percent target.
July PPI: Final Demand Thursday, 8/9 Range: 0.0 to 0.4 percent Median: 0.2 percent	Jun = +0.3%	Up by 0.3 percent, which would translate into an over-the-year increase of 3.5 percent.
July PPI: Core Thursday, 8/9 Range: 0.1 to 0.3 percent Median: 0.3 percent	Jun = +0.3%	Up by 0.3 percent, for an over-the-year increase of 2.9 percent.
July Consumer Price Index Friday, 8/10 Range: -0.1 to 0.3 percent Median: 0.2 percent	Jun = +0.1%	Up by 0.2 percent, which would yield a year-on-year increase of 3.0 percent. As noted above, we think this will mark the peak for headline inflation in 2018, but that will still leave headline CPI inflation running at better than 2.0 percent at year-end.
July Consumer Price Index: Core Friday, 8/10 Range: 0.2 to 0.3 percent Median: 0.2 percent	Jun = +0.2%	Up by 0.3 percent, which would leave the core CPI up 2.3 percent year-on-year. We see downside risk to our forecast stemming from the path of lodging costs. Recall that lodging costs fell by 3.7 percent in June, which made only slightly less sense than the 2.9 percent increase reported in the May data. Our forecast anticipates a good part of the sharp decline in June will be reversed in July, which pushed our forecast for the core CPI up to 0.3 percent. Of course, if the sharp decline in June was merely a reversal of the steep increase in May, then there will be no reversal of that reversal in the July data and our forecast will be too high. Either way, other than making us, and you, probably, dizzy, this is of little significance in the grand scheme of things and we'll be much more interested in the usual suspects, i.e., rents, medical costs, and core goods prices. Our forecast anticipates a continuation of the gradual slowing in growth of primary rents and the gradual acceleration in growth of owners' equivalent rents, and with the latter carrying a significantly higher weight in the core CPI than the former, this will help sustain core CPI inflation. We look for a smaller increase in medical care costs in July than that seen in June, but this will leave the over-the-year change in line with the recent trend. A still-strong U.S. dollar continues to weigh on core goods prices, blunting the effects of tariffs (which at this point are mainly indirect, rather than direct, effects), and thus leading to another modest monthly decline in core goods prices that would leave them down year-on-year for the 62nd time in the past 64 months. At the same time, our forecast anticipates core services prices will be up 3.1 percent year-on-year and the steady acceleration over the past several months to a large extent reflects gradually rising labor costs. Prices for both new and used motor vehicles rose in June, the former was not surprising but the latter was. Our July forecast anticipates a modest increase in prices for new vehicles and a modest decline in prices for used vehicles, but this is another source of uncertainty in our forecast for the core CPI. All in all, while we think July will mark the peak for headline inflation in 2018, we see further upside for core inflation, whether measured by the CPI or the PCE deflator (the latter being the FOMC's preferred measure), particularly should coming months see tariffs imposed directly on imported consumer goods.

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