ECONOMIC UPDATE

REGIONS

May 10, 2019

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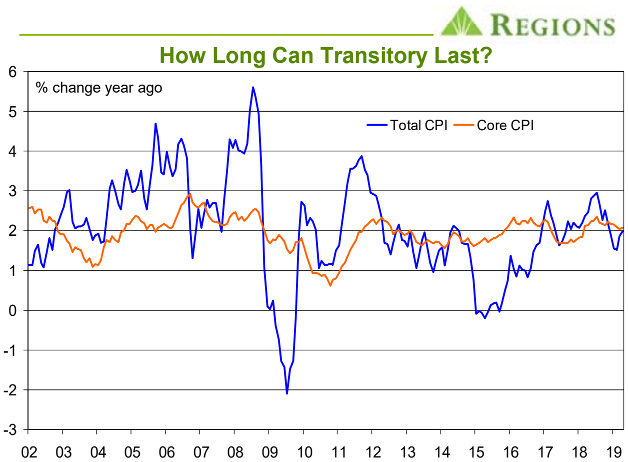
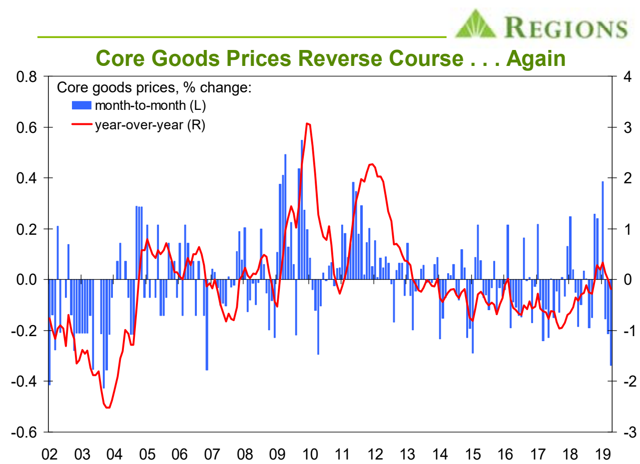
April Consumer Price Index: How Long Can Transitory Last?

- The total CPI rose by 0.3 percent (0.319 percent unrounded) in April; the core CPI rose by 0.1 percent (0.138 percent unrounded)
- On a year-over-year basis, the total CPI was up 2.0 percent and the core CPI was up 2.1 percent in April

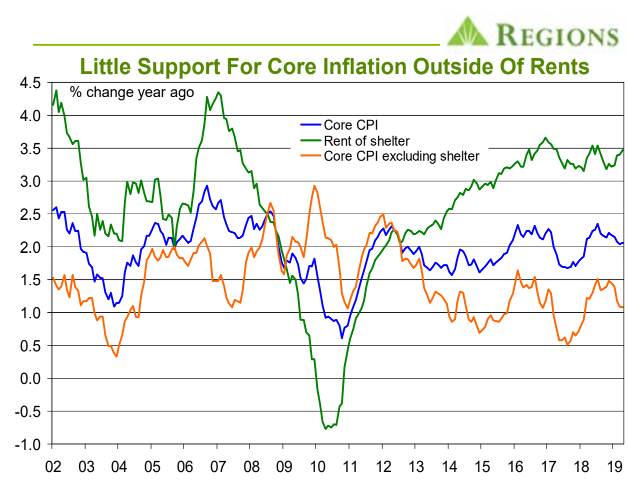
The total CPI rose by 0.3 percent in April while the core CPI rose by 0.1 percent, below the 0.4 percent and 0.2 percent increases, respectively, we and the consensus expected. On an over-the-year basis, the total CPI is up 2.0 percent and the core CPI is up 2.1 percent. Food prices pulled a U-turn in April, turning down after having posted notably large increases in February and March, which along with a smaller than expected increase in gasoline prices accounts for the increase in the total CPI falling short of expectations, while another steep decline in apparel prices – which reflects a change in methodology – and a sizeable decline in used car prices dampened the increase in the core CPI. While the CPI data do not suggest inflation pressures are set to intensify to a meaningful degree any time soon, the recent CPI data contain enough noise to rule out inflation changing course later in the year. All of which begs the question of exactly how long can something (i.e., dormant inflation) persist and still be considered transitory. If the data don't answer this question over coming months, the FOMC will ultimately have to.



As measured in the CPI data, not seasonally adjusted retail gasoline prices were up by 10.3 percent in April. This is below the better than 11.0 percent increase reported in the EIA series that we track, hence our miss on the change in seasonally adjusted gasoline prices – the CPI show them up 5.7 percent in April. Still, on an over-the-year basis, retail gasoline prices are up "only" 3.1 percent – keep in mind that the large monthly increases in March and April follow significant declines from November 2018 through January 2019. The broader energy index was up 2.9 percent in April, with lower prices for home heating oils and natural gas (for utilities) helping offset higher gasoline prices. The broad index of food prices fell by 0.1 percent April, dragged down by falling grocery store pries, as prices for food consumed at home fell by 0.5 percent. This comes after February and March brought the largest two-month increase in this series since mid-2014. Prices for food consumed away from home were up by 0.3 percent in April, which is in line with what has been the run rate over the past several months.



A methodological change led to a 1.94 percent decline in apparel prices in the March CPI data, the largest decline on record. What we were unsure of, however, was whether apparel prices would bounce back, at least to some extent, in the April data, and our forecast assumed a modest rebound. Instead, apparel prices fell an additional 0.8 percent in April, leaving them down 2.9 percent year-on-year. To us, the issue isn't so much whether the new methodology is a better reflection of actual apparel prices – it almost has to be given that it relies on actual data from an actual retailer – but instead that the change in methodology is impactful enough that in March it shaved one-tenth of a point off of the change in the core CPI, which has to be accounted for when interpreting the CPI data. This also impacts the broader measure of core goods prices in the CPI data; After having shown signs of firming in late-2018, core goods prices have now fallen in three straight months, and the 0.34 percent decline in April is the largest monthly decline since November 2006. Should tariffs be imposed on consumer goods imported from China, there will be a jump in the index of core goods prices, though rather than a one-off jump this will more likely be seen in a series of large monthly increases, which for a time will push measured core goods inflation higher, but that effect will be, well, transitory as pass-throughs of tariffs are not sustained over time.



Primary rents were up 0.4 percent in April, a mere rounding error from a 0.5 percent gain, with owners' equivalent rents up a trend-like 0.3 percent. This leaves primary rents up 3.8 percent year-on-year, the largest such increase since September 2017. Apartment rents have been resilient though that is likely to change once the backlog of under construction units begins to clear, but rents on single family homes continue to rise at a rapid clip, which is supporting the CPI measure of rents. As our bottom chart shows, however, apart from rents, which account for over 40 percent of the core CPI, there is little upward pressure on core inflation. The question is how long will this remain the case.

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