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January 15, 2025

US CPI (December): A late Christmas present for Powell

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Consumer Price Index (monthly change, %)	Dec 2024	Nov 2024	Oct 2024	Sep 2024	Aug 2024	Jul 2024	Dec NSA YoY%
All items	0.4	0.3	0.2	0.2	0.2	0.2	2.9
Ex-food/energy	0.2	0.3	0.3	0.3	0.3	0.2	3.2
• Ex-food	0.4	0.3	0.3	0.1	0.2	0.2	2.9
• Ex-energy	0.2	0.3	0.3	0.3	0.3	0.2	3.1
Energy	2.6	0.2	0.0	-1.9	-0.8	0.0	-0.5
Services	0.3	0.3	0.4	0.4	0.3	0.3	4.4
Housing	0.3	0.3	0.4	0.2	0.3	0.4	4.1
Fuels & util.	0.7	0.1	0.8	0.5	-0.7	0.1	3.4
Food/beverages	0.3	0.4	0.2	0.4	0.1	0.2	2.4
• Food	0.3	0.4	0.2	0.4	0.1	0.2	2.5
Apparel	0.1	0.2	-1.5	1.1	0.3	-0.4	1.2
Transportation	1.4	0.4	0.3	-0.2	0.1	-0.1	1.6
Medical care	0.1	0.3	0.3	0.4	-0.1	-0.2	2.8
Recreation	0.1	0.3	0.4	-0.4	-0.1	0.1	1.1
Education, comm.	0	-0.4	-0.3	0.0	0.1	0.2	0.6
Other good, serv.	-0.1	0.5	0.4	0.2	0.2	0.2	3.3
Commodities	0.6	0.4	0.0	-0.2	-0.1	-0.1	0.3

Source: Haver Analytics.

- Jay Powell got a late Christmas present in the December inflation report. Core CPI prices rose 0.23% m/m in the month, a bit below consensus expectations of 0.3%. Three-month annualized core CPI came down four ticks to 3.3%. But headline inflation increased by 0.4% m/m in the month, matching forecasters' predictions. In year-over-year terms, headline rose by two ticks to 2.9%, while core edged down a tick to 3.2%. The improvement in core was mainly due to softer core goods prices in the month as used car prices cooled a bit after a few hot months. Service inflation, including shelter costs, was steady in the month. Today's report, while very much welcomed, doesn't change the game plan for the Fed. The labor market and growth remain on solid footing, so they can comfortably wait for continued inflation progress and more insight into the future directions of fiscal and trade policy. Expect that message from Powell later this month.
- Based on the PPI data and today's CPI, we estimate core PCE will come in at 0.2% m/m. That will put the three-month annualized pace at around at 2.3% for core PCE in December. For the most part, the PCE data has looked very good in the second half of 2024, something Powell predicted some time ago when he argued seasonal factors are depressed in second half of the year as compared to the first. 6-month annualized core PCE inflation sits at 2.4%

as of December, down nearly a percentage-point from June. CPI has shown less progress over that stretch, in large part because of the different composition of the consumer basket as well as some methodological differences.

- Turning to the details of today's report, shelter remained tame at 0.3% m/m, with both Owner's Equivalent Rent and the Rent sub-index registering that pace. Lodging away from home pulled back after a the sharp surprise in the month prior. It feels like we are over the hump on shelter inflation with the latest three-month annualized price changes for OER and Rent sitting at 3.8% and 3.3%, both down over a percentage-point from their recent peaks this past fall. The disinflation in shelter has taken a lot longer than expected and January's reweighting of single family homes could introduce more volatility again but the Fed will likely have more confidence that cooling housing costs will help bring underlying and headline inflation back to target next year, assuming Trump's policies don't get in the way.
- Non-housing services inflation cooled by a tick in December to 0.2% m/m. Most non-housing categories came down in the month with the notable exception of transportation services. Transportation costs spiked driven mostly by a 4% jump in airfares, but given that sub-category represents just 0.8% CPI and about 1% of the core CPI basket, it wasn't enough to offset the disinflation seen in medical services and other categories. With wages and labor demand on a cooling trend as firms are staffed up -- and "catch up" inflation in car insurance mostly behind us as insurance providers are returned to profitability -- prices in this segment have returned to a cooler pace, broadly consistent with 2% inflation again.
- Core goods prices rose 0.1% with most of that due to a pickup in used car prices which rose by 1.2% m/m. Used car prices, however, did slow down a bit compared to the 2% and 2.7% gains seen the months prior. Stripping out used cars, core goods returned to deflation, posting a 0.8% drop in the month. That has a lot to do with robust supply of goods, something that could turn out to be handy even trade policy becomes increasingly complicated over the next year.
- Overall, the strength in inflation seen during the fall is looking like another "bump" in the road that we have passed. 2024 was the year that underlying inflation came very close to target with a few hiccups along the way, especially measured in core PCE terms. The job market looks about balanced again, consumer spending remains above average, inflation expectations well-anchored, and the financial system has adapted well to higher rates. All of that means the Fed is very well positioned to manage a pause and some policy uncertainty into the first part of 2025.

Implications & actions

Re: Economic forecast — We expect the Fed will hold rates this month and there is a growing risk of a prolonged pause given the policy uncertainty. Core PCE should register about 0.2% in December.

Re: Markets — Bond yields and the broad dollar dropped after today's downside surprise on core CPI.

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