ECONOMIC UPDATE

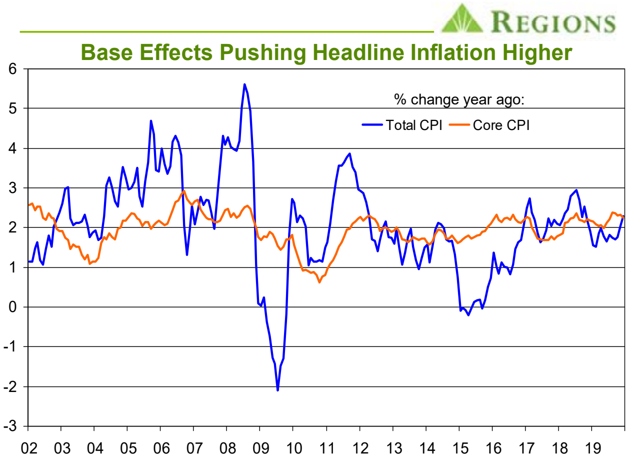
REGIONS

January 14, 2020

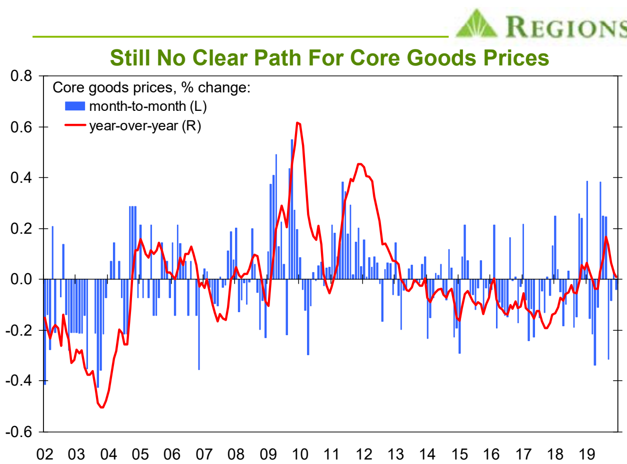
December Consumer Price Index: Few Signs Of Meaningful Inflation Pressure

- The total CPI rose by 0.2 percent (0.219 percent unrounded) in December; the core CPI rose by 0.1 percent (0.113 percent unrounded)
- On a year-over-year basis, the total CPI is up 2.3 percent and the core CPI is up 2.3 percent as of December

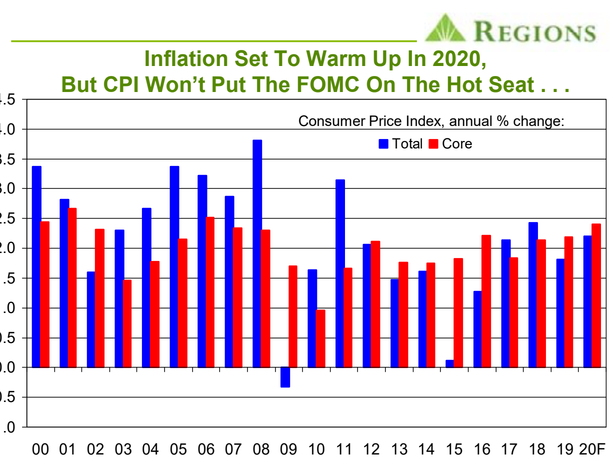
The total CPI rose by 0.2 percent in December, while the core CPI rose by 0.1 percent, in each case one-tenth of a point lighter than we and the consensus expected. On an over-the-year basis, both the total CPI and the core CPI are up 2.3 percent as of December. On an annual average basis, the total CPI was up 1.8 percent in 2019 with the core CPI up 2.2 percent. One reason headline inflation has pushed above 2.0 percent is that the over-the-year comparisons are flattered by what were weak prints in late-2018; that this weakness carried into early-2019 means base effects will exaggerate the over-the-year increases in the data for January and February of 2020. We think that is worth keeping in mind given what remains a lack of meaningful inflation pressures in most of the broad CPI categories. It is also worth keeping in mind that the disparity between core CPI inflation and core PCE inflation, the FOMC's preferred gauge of inflation, has been wider than normal for the past several months. Though the December data on the PCE Deflator are not yet available, core PCE inflation for 2019 as a whole will come in no higher than 1.6 percent. While inflation will likely warm up a bit in 2020, it will not do so to the extent that the FOMC's seat will become uncomfortably hot, meaning that if growth plays out as the FOMC and most private sector analysts expect, it will be hard to make a case for any changes in the Fed funds rate in 2020.



On a seasonally adjusted basis, retail gasoline prices were up by 2.8 percent in December. Yet, the overall energy index was up by just 1.4 percent, less than our forecast anticipated thanks in part to a decline in electricity prices. Food prices were up by 0.2 percent in December, with prices for food consumed at home up by 0.1 percent and prices for food consumed away from home up 0.3 percent. For 2019 as a whole, prices for food consumed at home were up 0.9 percent, the largest annual increase since 2015, while prices for food consumed away from home were up 3.1 percent. The disparity between the two series has been notably wide over the past few years, with restaurant operators having at least some latitude to pass along higher input costs, including labor costs, in the form of higher menu prices, while grocers have come under increased pressure from online ordering/delivery platforms, thus limiting their pricing power.



Market rents rose by 0.2 percent in December, extending the softness seen over the back half of 2019. The same pattern is seen with owners' equivalent rents, which were also up 0.2 percent in December. To be sure, on an over-the-year basis, market rents were up 3.7 percent and owners' equivalent rents were up 3.3 percent as of December, but in each case the pace of over-the-year growth has slowed. We anticipate this will continue over coming months as the large and persistent backlog of under construction multi-family units begins to clear, even if at a slow pace. That rent growth on single family homes remains strong is acting as a support for rents as measured in the CPI. But, with rents accounting for over 40 percent of the core CPI, any slowdown in overall rent growth will act as a drag on the pace of core CPI inflation..



Any momentum that had built up in core goods prices over the summer months fizzled over the latter months of 2019. After having declined in September and October, core goods prices were unchanged over the final two months of the year, and as of December were flat on an over-the-year basis. That tariffs had only limited effects on core goods prices, with importers/suppliers bearing most of the burden, means any unwinding of tariffs is unlikely to have an appreciable effect on core goods prices, but if the U.S. dollar weakens modestly over the course of 2020 as we anticipate, that could act as a modest tailwind for core goods prices. Still, core goods prices are unlikely to provide appreciable support for overall core inflation in 2020. To the extent service providers are able to pass along higher costs, primarily labor costs, in the form of higher prices, core services prices could provide more meaningful support for core inflation in 2020, which is what we expect will be the case. Either way, even if core inflation pushes modestly higher in 2020, it will not do so to the extent that inflation becomes a pressing concern for the FOMC.

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