August 10, 2022

U.S. inflation surprised on the downside in July

- Headline CPI reading slowed to 8.5% from 9.1% in June led by lower gasoline prices
- Core inflation held flat (versus expectations for an increase) as higher rents offset lower used car prices and airline fares
- Headline inflation to slow further but level still too high, and pressure too broad, to deter Fed's rate hike

RBC Inflation Watch: a tracker of key indicators on price trends in the US.

Read Report

July saw a larger than expected easing in headline inflation reading in the U.S., to 8.5% from 9.1% in June but was still the highest since 1981. Gasoline prices led the decline, dropping month-over-month in July after driving much of the run-up in CPI to-date. Food prices continued to surge, with year-over-year growth ticking up slightly to 10.9% in June thanks to an acceleration in grocery prices. Excluding food and energy items, core CPI growth stayed at 5.9% year over year. That was despite a sharp slowing in the month-over-month increase to 0.3% from June, from the 0.6% average pace over the second quarter of this year. Strengthening home rents again supported core CPI gain, offsetting lower prices for used vehicles and airfares. In the months ahead, headline inflation readings will likely continue to decline, as gasoline prices keep chasing energy commodity prices lower. Meantime, resilient demand for rental homes and travel and leisure activities which is expected to extend through the summer should work to buffer some of the slowdown, keeping core inflation high.

It is not unreasonable to expect headline inflation to have turned a corner. Globally, commodity prices have been weakening and shipping time and costs have both been persistently trending lower. More importantly, domestic U.S. consumer demand for goods that surged during the onset of the pandemic has finally cooled. That should continue to dial lower in the months ahead, as high inflation and rising borrowing costs bite more significantly into household real buying power. Indeed, after accounting for inflation there has been virtually no growth in real income since pre-pandemic. In July, average hourly earnings deflated with CPI actually declined by an annualized 0.4%, compared to levels in February 2020. Still, current readings are too high, and pressures to broad to deter the Fed from acting more aggressively in the near-term. By our count as much as 87% of consumer basket (outside of shelter) was seeing above-target rate of inflation in July. That will keep the Fed on track to deliver more rate hikes this year, with our forecast assuming another 50bps increase in the next meeting in September.

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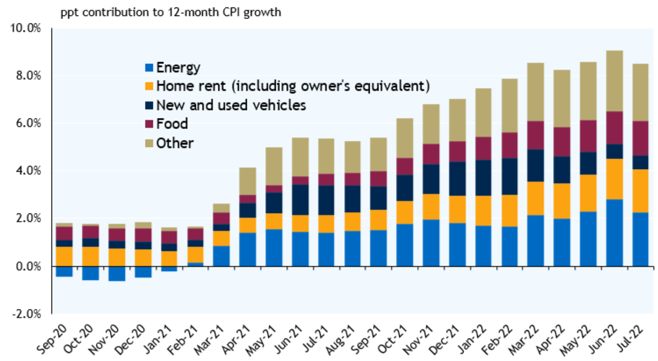
U.S. CPI Growth				
	May-22	Jun-22	Jul-22	Jul-22
	MoM % change (SA)			YoY % change
Headline	1.0	1.3	0.0	8.5
Food	1.2	1.0	1.1	10.9
Energy	3.9	7.5	-4.6	32.9
Core	0.6	0.7	0.3	5.9
Goods ex food and energy	0.7	0.8	0.2	7.0
Used cars and trucks	1.8	1.6	-0.4	6.6
Services ex energy	0.6	0.7	0.4	5.5
Car and truck rental	1.7	-2.2	-9.5	-11.9

Decline in gas prices sent U.S. inflation lower in July



Source: Bureau of Labor Statistics, RBC Economics Research