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TD Economics

Data Release: Core inflation rose to 2.3% in June

- Consumer prices rose 0.2% in June, slightly below market expectations for a 0.3% gain. Core inflation (excluding food and energy) matched the headline increase, rising by 0.2% on the month. The pace of headline inflation matched the prior month's print, at 1.0% on a year-over-year basis. On the other hand, core inflation continued to rise, and at 2.3% y/y it is in line with its peak from earlier this year.
- Once again, energy prices were a contributor to the headline gain, rising by 1.3% (month-over-month). This was driven by a rise in gasoline prices, up 3.3% m/m, but somewhat offset by falling electricity prices (-0.5%).
- Gains in core prices continued to be led by services (+0.3% m/m), which saw relatively broad-based price growth across categories. Core services inflation remained steady at its post-recession high of 3.2% y/y. On the other hand, core goods prices fell for the fourth consecutive month (-0.2%), pulled down by apparel (-0.4%), new vehicles (-0.2%), and used vehicles (-1.1%).

Key Implications

- The report suggested still limited price pressures overall with the headline number at just one-half of the Fed target. Still, with oil prices likely to continue to rise modestly over the remainder of this year, headline inflation should accelerate later this year and hit a peak of around 2.7% by the first quarter of next year given the favorable base year effects before decelerating somewhat closer to the core measure.
- We expect core inflation to maintain its current pace for the remainder of the year as the disinflationary impetus from a higher U.S. dollar weighs on core goods prices and helps balance the much hotter core services goods inflation – resulting from producers attempting to pass on the rising production costs, partly related to building wage pressures.
- While inflation is not an immediate concern for the economy or the Federal Reserve, financial markets appear somewhat complacent to the risk of higher inflation. We expect the Fed's preferred inflation gauge, the core personal consumption expenditure deflator, to head higher as the year progresses. While we ultimately don't expect the Fed to rush into further tightening, rising inflation should nudge up the chances that the Fed slips in a rate hike before the year ends.

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