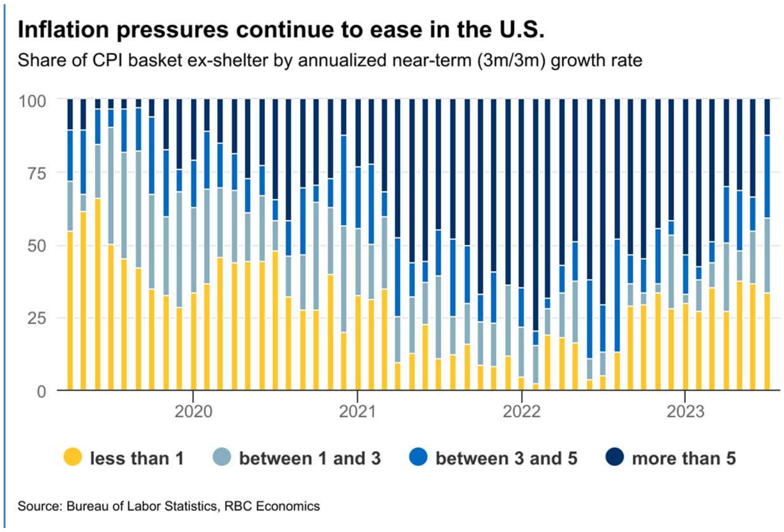
Economic Update

August 10, 2023

Inflation pressures keep receding in the U.S.

- Headline CPI growth in the U.S. ticked slightly higher in July, to 3.2% year-over-year upon rising (but still negative) energy inflation. But that was after a full percentage point decline in June.
- Energy prices were still down 12.5% from a year ago, but that was a smaller decline than the 16.7% drop in June. That trend likely continued in August with oil prices drifting higher in recent weeks upon rising concerns about a widening supply gap.



- Grocery price growth saw another big drop, to 3.6% year-over-year in July from 4.7% in June. That was the lowest rate since August 2021. Inflation for dining out also slowed but to more elevated 7.1%, as demand for local services holds up.
- Excluding food and energy products, 'core' CPI in the U.S. slowed marginally to 4.7% year-over-year – still well above the Fed's 2% inflation objective. But recent month-over-month increases have been softer, including the 0.2% rise from June in July.
- That slowing in 'core' CPI has a lot to do with moderations in home rent and used cars prices – two of the largest contributors to earlier CPI growth. In July, rent prices again grew at its slowest pace in a year (+0.4% from June). Prices for used vehicles outright declined.
- Core services ex-shelter prices (the 'super core' measure preferred by the Fed as a gauge of domestically driven price pressures) grew by 1.7% on a three-month annualized basis in July, up slightly from 1.4% in June but still below the 2.5% average run rate over the two years pre-pandemic (2018 and 2019).

Claire Fan | Economist, RBC Economics | Royal Bank of Canada | T. (416) 974-3639s
For more economic research, visit our website at *https://thoughtleadership.rbc.com/economics/*

- The scope of inflation pressures has narrowed significantly – the share of the CPI basket seeing above 3% inflation (on an annualized 3-month basis) dropped to 40% in July, still above pre-pandemic but similar to the share seen in early 2021.
- **Bottom line:** Easing inflation pressures in the U.S. against a resilient macroeconomic backdrop have been encouraging and have raised hopes that inflation can slow back to the Fed's 2% inflation objective without a substantial deterioration in the economy. We still think that is unlikely, given early signs that consumer purchasing power is already taking a hit. Household financial cushions are thinning, and delinquencies are already on the rise. Elevated interest rates will continue to suppress credit demand, making it more challenging to borrow to support spending. Indeed, monetary policy at its current level is already very restrictive. Absent a larger reacceleration in inflation, the Fed is unlikely to push interest rates higher. We expected the Fed will keep rates steady into 2024, while waiting for more signs of a softening economy to show up.

U.S. CPI Growth

	Apr-23	May-23	Jun-23	Jun-23
	MoM % change (SA)			*YOY % change (NSA)*
Headline	**0.4**	**0.1**	**0.2**	**3.0**
Food	0.0	0.2	0.1	5.7
Energy	0.6	-3.6	0.6	-16.7
Core	**0.4**	**0.4**	**0.2**	**4.8**
Goods ex food and energy	0.6	0.6	-0.1	1.3
Used cars and trucks	4.4	4.4	-0.5	-5.2
Services ex energy	0.4	0.4	0.3	6.2
Rent of shelter	0.5	0.5	0.4	7.9