

## US Watch

## June CPI Inflation: A lot to like

## Key takeaways

- The June CPI report was softer-than-expected as both headline and core CPI rose by 0.2% m/m.
- A decline in used car prices contributed to the softer print, but there were broad signs of disinflation.
- Despite the softer-than-expected print, recent data keep us confident that the Fed will raise rates by 25bp in July.

## Softer than expected

The June Consumer Price Index (CPI) report was softer than expected. Headline CPI rose by 0.2% m/m (0.180% unrounded) resulting in the y/y rate falling a full percentage point to 3.0%, its lowest reading since March 2021. Core inflation also rose by a soft 0.2% m/m (0.158% unrounded) which led to a five-tenth decline in the y/y rate to 4.8%. In short, the inflation data are beginning to show more progress towards the Fed's two-percent target.

## Lower grocery bills

Food and energy prices increased again in June. The former advanced by 0.1% m/m, while the latter rose by 0.6% m/m after falling by 3.6% m/m in May. Energy inflation remains choppy, but the trend is generally lower. While food inflation rose on the month, food at home ticked down by 5bps, its third decline in the last four months. We think there is scope for further deflation within this component given declining input costs. That said, food away from home inflation should remain sticky due to high labor costs.

## Used car prices begin to retrace

Core goods inflation fell 0.1% m/m, its first decline since last December. The decrease was driven by a 0.5% m/m drop in used car prices. While we did not forecast used car prices to decline this month, we have been expecting prices to reverse the increase seen in April and May given recent declines in wholesale prices. Therefore, we think the June decline is just the start of a series of decreases that should put downward pressure on core and headline inflation. Additionally, we have seen meaningful disinflation in core goods ex used cars of late. The component was unchanged for a second consecutive month and is up just 0.2% annualized over the last three months, which is down from 4.75% in March. While we haven't seen deflation in the category yet, disinflation has been rapid in 2Q and likely reflects softer demand coupled with improving supply chains.

*(Continued on next page)*

12 July 2023

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## Glossary

CPI = Consumer Price Index

PPI = Producer Price Index

PCE = Personal Consumption  
Expenditures (Price Index)

OER = Owners' Equivalent Rent

NSA = Not Seasonally Adjusted

OIS- Overnight Indexed Swap

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Timestamp: 12 July 2023 10:38AM EDT

## Services: only a shelter story in June

Core services rose by 0.3% m/m, a modest deceleration from the 0.4% m/m average seen over the previous three months. Within services, the main driver was shelter inflation, which rose by 0.4% m/m. Rent and owners' equivalent rent (OER) moderated slightly on an unrounded basis in June, broadly in line with our expectations. We expect rent and OER to continue to moderate in the second half of the year given earlier declines in asking rent inflation.

## A positive for Chair Powell's oft-cited measure

In addition to the slight moderation in rent and OER seen in June, core services ex rent and OER inflation fell from 0.2% m/m in May to 0.0% m/m in June. Over the last three months, the measure has increased at an annualized rate of 1.4%, down from 5.2% in March. One major reason for the recent disinflation of this measure is the recent decline in travel related expenses—airfares and lodging away from home.

Airfares fell by 8.1% m/m in June and have declined 43% annualized over the last three months. The recent decline likely reflects a few factors. First, jet fuel prices have been declining rapidly. Second, growth in demand for domestic air travel is slowing. Lodging away from home, meanwhile, fell by 2.0% m/m its second decline in the last three months. We suspect the industry is seeing a better balance between supply and demand of late.

While travel related expenses have played a big role in the recent disinflation of core services ex rent and OER of late, we do not expect that trend to persist in 2H. Moreover, the measure is likely to be boosted in 4Q by medical care services inflation when the new data on health insurance are incorporated.

## Fed: July is a done deal

Despite the softer-than-expected print for June CPI, we think the totality of the data over the past several months on activity, labor markets, and inflation keep us confident that the Fed will raise its policy rate by another 25bp in July. We continue to expect a second 25bp rate hike in September, but action beyond July remains highly data dependent, both in terms of the timing of hikes and whether they happen.

## Rates strategy view

The curve bull steepened following CPI, with declines across the curve led by real rates. As discussed in [US Rates Alpha: Enter 10yT longs](#), the weaker print has acted as a catalyst for rates to rally closer to fundamentals. We anticipate that July seasonals will continue to support this correction in 10y rates near-term. The market remains convicted in a July hike, with market pricing unchanged following the print. However, the market has reduced chances for incremental hikes with the combined September + November FOMC OIS now pricing 9bps of hikes vs 12bps before the print. The market is pricing a higher probability that the July hike may be the Fed's last; our analysis has previously suggested investors should buy the last Fed hike. The largest movers in FOMC OIS have been late '24 expiries which are 11bps lower as pricing for cuts remains conditional on the market's outlook for inflation. The 1y inflation swap fell 7bps and is now pricing 2.23%. We continue to believe that stickier, more persistent inflation vs what is priced is likely to challenge long duration positions and we like owning inflation as a nominal rate hedge.

**Exhibit 2: CPI Forecast vs. Actual (SA % m/m unless specified otherwise)**

Below is a table that compares our bottom-up CPI forecasts to actuals

	June Forecast		
	Actual	Forecast	Error
<b>NSA Index (level)</b>	<b>305.109</b>	<b>305.393</b>	<b>-0.284</b>
<b>Headline CPI (All Items)</b>	<b>0.18%</b>	<b>0.27%</b>	<b>-0.09%</b>
Food	0.1%	0.1%	0.0%
Energy	0.6%	0.3%	0.3%
<b>Core CPI</b>	<b>0.16%</b>	<b>0.29%</b>	<b>-0.13%</b>
<b>Core goods</b>	<b>-0.05%</b>	<b>0.17%</b>	<b>-0.22%</b>
Household furnishings and supplies	-0.3%	-0.2%	-0.1%
Apparel	0.3%	0.2%	0.1%
Transportation commodities less motor fuel	-0.2%	0.3%	-0.5%
<i>Of which:</i>			
New vehicles	0.0%	-0.1%	0.1%
Used cars and trucks	-0.5%	1.0%	-1.5%
Medical care commodities	0.2%	0.5%	-0.3%
Recreation commodities	-0.4%	-0.1%	-0.3%
Other recreational goods	-0.1%	0.2%	-0.3%
Education and communication commodities	-0.1%	-0.3%	0.2%
Alcoholic beverages	0.0%	0.4%	-0.4%
Other goods	0.1%	0.5%	-0.4%
<b>Core Services</b>	<b>0.25%</b>	<b>0.33%</b>	<b>-0.08%</b>
Shelter	0.4%	0.4%	0.0%
<i>Of which:</i>			
Rent	0.4%	0.4%	0.0%
Lodging away from home	-2.0%	-0.9%	-1.1%
OER	0.4%	0.5%	0.0%
Water and sewer	0.4%	0.4%	0.0%
Medical care services	0.0%	-0.3%	0.2%
<i>Of which:</i>			
Health insurance	-3.6%	-3.7%	0.1%
Transportation services	0.1%	0.7%	-0.5%
<i>Of which:</i>			
Airfares	-8.1%	-1.0%	-7.1%
Recreation services	0.5%	0.2%	0.2%
Education and communication	-0.3%	0.3%	-0.5%
Other personal services	0.2%	0.8%	-0.6%

Source: BofA Global Research, Bureau of Labor Statistics, Bloomberg

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**Exhibit 3: CPI heatmap (%m/m)**

Headline CPI rose by 0.2% m/m in June

May-23 weight	Component	Jun-23	May-23	Apr-23	Mar-23	Feb-23	Jan-23	Dec-22	Nov-22	Oct-22	Sep-22	Aug-22	Jul-22
<b>100.0</b>	<b>Headline CPI</b>	<b>0.180%</b>	<b>0.12%</b>	<b>0.37%</b>	<b>0.05%</b>	<b>0.37%</b>	<b>0.52%</b>	<b>0.13%</b>	<b>0.21%</b>	<b>0.49%</b>	<b>0.41%</b>	<b>0.23%</b>	<b>-0.03%</b>
13.4	Food	0.11%	0.20%	0.02%	0.01%	0.39%	0.51%	0.45%	0.55%	0.68%	0.78%	0.83%	1.08%
6.9	Energy	0.60%	-3.59%	0.56%	-3.52%	-0.56%	1.97%	-3.06%	-1.41%	1.68%	-1.74%	-3.89%	-4.70%
<b>79.7</b>	<b>Core CPI</b>	<b>0.158%</b>	<b>0.44%</b>	<b>0.41%</b>	<b>0.38%</b>	<b>0.45%</b>	<b>0.41%</b>	<b>0.40%</b>	<b>0.31%</b>	<b>0.33%</b>	<b>0.57%</b>	<b>0.58%</b>	<b>0.31%</b>
4.4	Household Furnishings and Supplies	-0.27%	-0.41%	-0.40%	0.37%	0.76%	0.51%	0.25%	0.36%	0.04%	0.48%	0.88%	0.62%
2.6	Apparel	0.31%	0.29%	0.27%	0.26%	0.81%	0.83%	0.21%	0.10%	-0.25%	0.04%	0.28%	-0.12%
7.8	Motor Vehicles & parts	-0.17%	1.49%	1.45%	-0.04%	-0.90%	-0.71%	-0.62%	-0.66%	-0.50%	-0.16%	0.37%	-0.14%
4.3	New Vehicles	-0.03%	-0.12%	-0.22%	0.38%	0.18%	0.23%	0.58%	0.47%	0.56%	0.67%	0.84%	0.47%
2.8	Used Cars and Trucks	-0.45%	4.42%	4.45%	-0.88%	-2.77%	-1.94%	-1.99%	-1.99%	-1.71%	-1.10%	-0.18%	-0.82%
1.5	Medical Care Commodities	0.19%	0.65%	0.46%	0.59%	0.15%	1.06%	0.11%	0.19%	-0.02%	-0.09%	0.24%	0.59%
2.3	Recreation Commodities	-0.36%	-0.05%	0.29%	0.24%	0.44%	0.12%	0.09%	-0.34%	0.78%	-0.05%	0.64%	0.15%
0.9	Education and Communication Commodities	-0.07%	-0.20%	-0.18%	-0.50%	-0.77%	-0.09%	-0.92%	-1.69%	-1.53%	-0.53%	-0.40%	-0.46%
0.8	Alcoholic Beverages	0.01%	0.51%	0.47%	0.14%	-0.28%	0.41%	0.65%	0.64%	0.69%	0.31%	0.36%	0.43%
1.2	Other Goods	0.08%	0.59%	0.24%	0.53%	0.74%	0.77%	-0.07%	0.62%	0.58%	0.39%	1.15%	0.34%
34.7	Shelter	0.37%	0.56%	0.42%	0.56%	0.76%	0.74%	0.79%	0.64%	0.72%	0.74%	0.67%	0.57%
25.5	Owners' Equivalent Rent of Residences	0.45%	0.52%	0.54%	0.48%	0.70%	0.67%	0.79%	0.65%	0.62%	0.79%	0.69%	0.63%
7.6	Rent of Primary Residence	0.46%	0.49%	0.56%	0.49%	0.76%	0.74%	0.79%	0.77%	0.72%	0.81%	0.74%	0.70%
1.2	Lodging Away From Home	-2.01%	1.80%	-2.96%	2.70%	2.26%	1.20%	1.10%	-0.52%	3.49%	-0.51%	-0.09%	-1.74%
1.1	Water & Sewer & Trash Collection Services	0.40%	0.58%	0.33%	0.27%	0.79%	0.85%	0.25%	0.31%	0.17%	0.79%	0.49%	0.35%
0.9	Household Operations	0.78%	-1.19%	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A	#N/A
6.4	Medical Care Services	-0.02%	-0.05%	-0.14%	-0.50%	-0.70%	-0.68%	0.30%	-0.49%	-0.38%	0.83%	0.68%	0.39%
5.9	Transportation Services	0.13%	0.84%	-0.18%	1.38%	1.14%	0.85%	0.63%	0.33%	0.60%	1.91%	0.99%	-0.40%
0.6	Airline Fares	-8.11%	-2.95%	-2.55%	3.96%	6.38%	-2.15%	-2.05%	-1.63%	-1.16%	0.44%	-1.53%	-8.39%
3.1	Recreation Services	0.46%	-0.09%	0.74%	0.01%	1.19%	0.73%	0.29%	0.94%	0.78%	0.19%	0.03%	0.50%
4.8	Education and Communication Services	-0.27%	-0.15%	0.07%	0.29%	0.21%	0.45%	0.26%	0.98%	0.17%	0.17%	0.21%	-0.04%
1.5	Other Personal Services	0.23%	0.47%	1.52%	0.47%	1.06%	0.54%	-0.15%	0.82%	0.36%	0.27%	0.30%	0.40%

Source: BofA Global Research, Bureau of Labor Statistics

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**Exhibit 4: CPI heatmap (%y/y)**

Headline CPI rose by 3.0% y/y in June

May-23 weight	Component	Jun-23	May-23	Apr-23	Mar-23	Feb-23	Jan-23	Dec-22	Nov-22	Oct-22	Sep-22	Aug-22	Jul-22
<b>100.0</b>	<b>Headline CPI</b>	<b>2.97%</b>	<b>4.05%</b>	<b>4.93%</b>	<b>4.98%</b>	<b>6.04%</b>	<b>6.41%</b>	<b>6.45%</b>	<b>7.11%</b>	<b>7.75%</b>	<b>8.20%</b>	<b>8.26%</b>	<b>8.52%</b>
13.4	Food	5.74%	6.69%	7.65%	8.50%	9.49%	10.13%	10.41%	10.63%	10.95%	11.24%	11.37%	10.93%
6.9	Energy	-16.74%	-11.66%	-5.06%	-6.42%	5.19%	8.70%	7.31%	13.07%	17.63%	19.79%	23.81%	32.93%
<b>79.7</b>	<b>Core CPI</b>	<b>4.83%</b>	<b>5.33%</b>	<b>5.52%</b>	<b>5.59%</b>	<b>5.54%</b>	<b>5.58%</b>	<b>5.71%</b>	<b>5.96%</b>	<b>6.28%</b>	<b>6.63%</b>	<b>6.32%</b>	<b>5.91%</b>
4.4	Household Furnishings and Supplies	3.24%	4.08%	4.77%	5.79%	6.33%	6.37%	7.28%	8.28%	8.81%	9.90%	10.60%	10.78%
2.6	Apparel	3.07%	3.47%	3.65%	3.25%	3.26%	3.06%	2.91%	3.55%	4.09%	5.46%	5.06%	5.13%
7.8	Motor Vehicles & Parts	-0.75%	0.12%	-0.30%	-1.82%	-3.18%	-2.26%	-0.95%	2.37%	5.48%	8.40%	9.10%	8.80%
4.3	New Vehicles	4.07%	4.66%	5.42%	6.12%	5.83%	5.78%	5.89%	7.20%	8.39%	9.40%	10.05%	10.44%
2.8	Used Cars and Trucks	-5.15%	-4.22%	-6.56%	-11.15%	-13.58%	-11.62%	-8.83%	-3.34%	2.03%	7.18%	7.78%	6.61%
1.5	Medical Care Commodities	4.21%	4.42%	4.01%	3.59%	3.19%	3.39%	3.21%	3.13%	3.06%	3.67%	4.09%	3.65%
2.3	Recreation Commodities	1.96%	2.73%	2.90%	3.16%	2.85%	3.27%	4.11%	3.63%	4.31%	4.05%	3.84%	4.12%
0.9	Education and Communication Commodities	-7.10%	-6.88%	-8.29%	-10.17%	-10.47%	-10.26%	-10.08%	-9.68%	-9.08%	-8.32%	-7.33%	-6.99%
0.8	Alcoholic Beverages	4.42%	4.77%	4.64%	4.53%	4.92%	5.82%	5.78%	5.54%	5.01%	4.09%	4.28%	4.22%
1.2	Other Goods	6.13%	6.58%	6.80%	6.91%	6.96%	7.15%	7.17%	7.51%	7.21%	7.90%	7.57%	6.73%
34.7	Shelter	7.83%	8.04%	8.11%	8.18%	8.10%	7.88%	7.51%	7.12%	6.92%	6.59%	6.24%	5.69%
25.5	Owners' Equivalent Rent of Residences	7.81%	8.05%	8.12%	8.04%	8.01%	7.76%	7.53%	7.13%	6.89%	6.68%	6.29%	5.83%
7.6	Rent of Primary Residence	8.33%	8.66%	8.80%	8.81%	8.76%	8.56%	8.35%	7.91%	7.52%	7.21%	6.74%	6.31%
1.2	Lodging Away From Home	4.54%	3.41%	3.31%	7.26%	6.73%	7.69%	3.18%	3.24%	5.86%	2.91%	4.03%	1.04%
1.1	Water & Sewer & Trash Collection Services	5.71%	5.71%	5.41%	5.39%	5.25%	4.97%	4.94%	5.01%	4.77%	4.93%	4.63%	4.35%
0.9	Household Operations	5.21%	4.55%	8.01%	#N/A	#N/A	#N/A	#N/A	#N/A	6.57%	#N/A	6.61%	#N/A
6.4	Medical Care Services	-0.76%	-0.08%	0.41%	1.03%	2.15%	2.99%	4.12%	4.38%	5.45%	6.51%	5.65%	5.09%
5.9	Transportation Services	8.23%	10.18%	11.03%	13.88%	14.64%	14.63%	14.58%	14.19%	15.19%	14.60%	11.32%	9.15%
0.6	Airline Fares	-18.85%	-13.44%	-0.87%	17.70%	26.54%	25.56%	29.14%	35.90%	43.02%	42.64%	33.70%	26.60%
3.1	Recreation Services	5.92%	5.76%	6.39%	5.94%	6.34%	5.75%	5.71%	5.38%	3.94%	4.06%	4.24%	4.53%
4.8	Education and Communication Services	2.38%	2.79%	3.13%	3.25%	2.86%	2.77%	2.41%	2.24%	1.32%	1.36%	1.53%	1.52%
1.5	Other Personal Services	6.46%	6.67%	6.30%	5.25%	5.21%	5.34%	5.55%	6.49%	5.76%	5.93%	5.77%	5.91%

Source: BofA Global Research, Bureau of Labor Statistics

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