

AGRON NICAJ
US Economist

Economic Research Office

T: +1 (646) 357 6180
E: anicaj@us.mufg.jp

MUFG Bank, Ltd.
A member of MUFG, a global financial group

Status quo monetary policy

May 15, 2024

- April's CPI print provides little insight as to when the "data dependent" Fed will begin cutting rates. From an annual price growth perspective, the general trend remains largely the same: core inflation is gradually easing, energy prices are growing, and food inflation remains elevated. When observing monthly growth, the trend now appears flat (as opposed to accelerating) with growth in core CPI less shelter and Owners' Equivalent Rent (OER) falling in April. More rapid disinflation or a deterioration in the labor market will be needed for the Fed to break the status quo.

Easing, but elevated April growth

Annual growth in core CPI fell to 3.6% in April, down from 3.8% in March. Core goods inflation remains comfortably in negative territory (-1.3%) while core services inflation hovers above 5% (Chart 1). Energy prices are trending upward, but the magnitude will likely need to be much higher and the duration longer for it to passthrough into core prices. Food inflation remains elevated, which on its own does not signal much for the broader picture given the unique and volatile drivers in the food industry, but sustained price growth can upend inflation expectations. The risk as of now, though, appears low.

For annual growth, the general trend can be characterized as slow and steady disinflation, but base effects certainly play a large role. When observing the month-to-month trend, we could see much more of an acceleration in prices since the middle of last year, even when excluding the elevated shelter component. Monthly growth in core CPI excluding shelter has been trending upward since July 2023, with the only sign of a reversal coming now in April where annualized growth fell to 2.7%, down from 3.8% in March (Chart 2). For the months ahead, easing price growth is expected to continue given that delayed inflation from key spending categories that exhibit sticky-prices, or infrequent price change, likely drove much of the monthly acceleration prior to April.

Chart 1: Annual core inflation continues to ease, with support from negative price growth of core goods

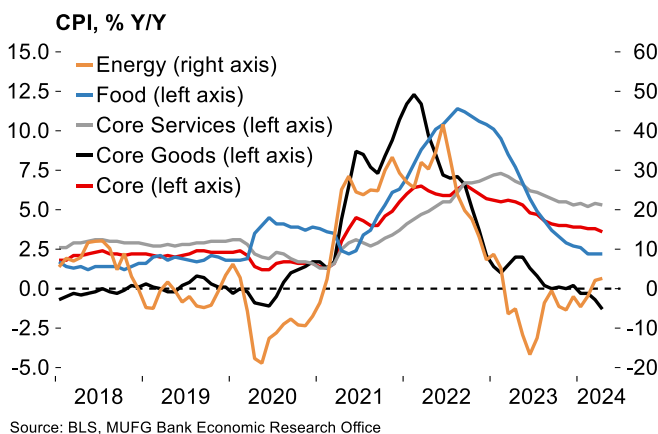
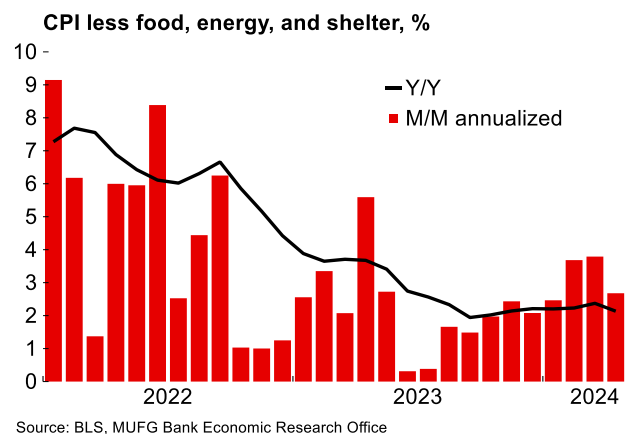


Chart 2: The trend of accelerating monthly price growth reversed in April



One example of this is motor vehicle insurance, where prices surged in the beginning of 2023 and in the beginning of 2024 (Chart 3). Prices infrequently change for this spending category, and when they do, they reflect past inflationary pressures. In this case, the rise in auto insurance was likely a delayed response to the rise in prices of cars, car parts, and mechanic labor costs from months prior.

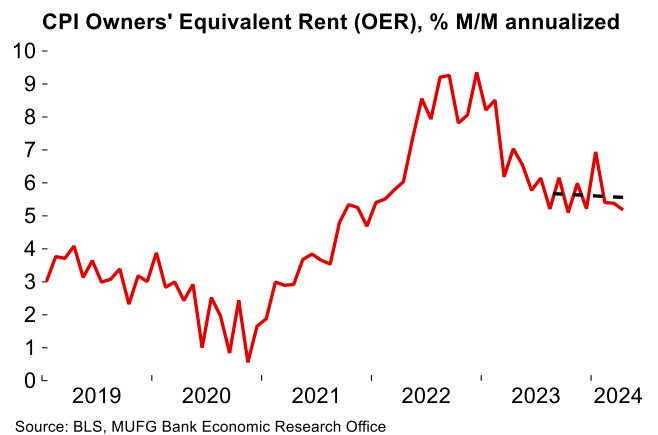
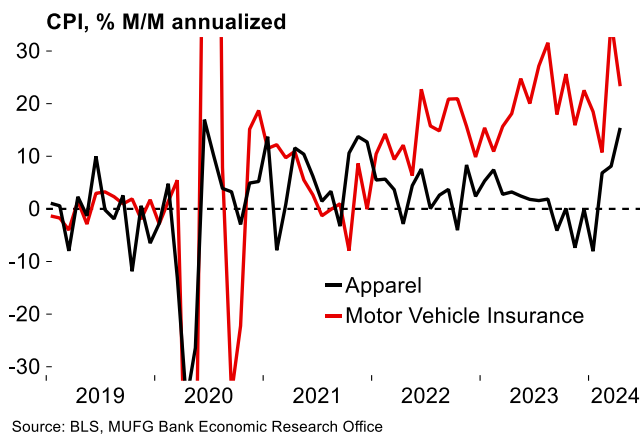
With that said, not all of the acceleration can be attributed to sticky-priced items and delayed inflation. For one, apparel prices have been accelerating in recent months, where price changes are much more flexible (Chart 3). Part of this may be a correction from months of deflation, but strong demand is likely also be a factor.

Additionally, there has been little progress in the shelter component of inflation, specifically in Owners' Equivalent Rent (OER). Since August of last year, monthly price growth has been virtually flat and well above what will be needed to bring overall core prices down close to target (Chart 4).

There is an expectation that monthly inflation will ease in the coming months, but the pace of easing will likely be slow given that upward price pressures are still present in many industries. Wage growth remains elevated above what would be consistent with 2% inflation, the labor market continues to be tight, and consumer spending remains strong. Inflation will need to decelerate at a much stronger pace for the Fed to consider rate cuts as early as this summer.

Chart 3: Delayed price growth for auto insurance and re-accelerating apparel prices helped drive recent inflation trend

Chart 4: The shelter component of the CPI continues to lack disinflationary momentum



Analyst Certification

The views expressed in this report solely reflect the personal views of Agron Nicaž, the primary analyst responsible for this report, about the subject securities or issuers referred to herein, and such views may not necessarily reflect the thoughts and opinions of MUFG Bank, Ltd. and its affiliates or management team. No part of such analyst's compensation was, is, or will be directly or indirectly related to the specific recommendations or views expressed herein.

Disclaimers

The information and views contained herein are not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation or which would subject MUFG Bank, Ltd. (collectively with its various offices and affiliates, "MUFG Bank") to any registration requirement within such jurisdiction or country. The information and views contained herein are provided for general informational purposes only, are subject to change, and are not intended to be, nor should be used, or considered, as an offer, or the solicitation of an offer, to sell or to buy or to subscribe to or for securities or any other financial instruments, and do not constitute specific investment, legal, tax or other advice or recommendations. The information contained herein reflects the thoughts and opinions of the noted authors only, and such information does not necessarily reflect the thoughts and opinions of MUFG or its management team. Neither this nor any other communication prepared by MUFG Bank should be construed as investment advice, a recommendation to enter into a particular transaction or pursue a particular strategy, or any statement as to the likelihood that a particular transaction or strategy will be effective and it does not take into account the specific investment objectives, financial situation, or the particular needs of any specific person who may receive this information. Any information relating to performance contained herein is illustrative and no assurance is given that any indicative returns, performance or results, whether historical or hypothetical, will be achieved. Before entering into any particular transaction, you should consult an independent financial, legal, accounting, tax, or other advisor as may be appropriate under the circumstances. In any event, any decision to enter into a transaction will be yours alone, not based on information prepared or provided by MUFG Bank. MUFG Bank hereby disclaims any responsibility to you concerning the characterization or identification of terms, conditions, and legal or accounting, or other issues or risks that may arise in connection with any particular transaction or business strategy. While MUFG Bank believes that any relevant factual statements contained herein, and any assumptions on which such statements are based, are in each case accurate, neither the authors nor MUFG have independently verified its accuracy, and such information may be incomplete or condensed. The information is provided "AS IS". The authors and MUFG do not warrant the accuracy of the materials provided herein, either expressly or implied, for any particular purpose and expressly disclaims any warranties of merchantability or fitness for a particular purpose. The authors and MUFG cannot and do not guarantee the accuracy, validity, timeliness or completeness of any information or data made available to you for any particular purpose. MUFG Bank may have issued, and may in the future issue, other reports that are inconsistent with or that reach conclusions different from the information and views contained herein. Such other reports, if any, reflect the different assumptions, views and/or analytical methods of the analysts who prepared them, and MUFG Bank is under no obligation to ensure that such other reports are brought to your attention.

© 2024, MUFG Bank, Ltd. All Rights Reserved.

About MUFG and MUFG Americas

Mitsubishi UFJ Financial Group, Inc. (MUFG) is one of the world's leading financial groups. Headquartered in Tokyo and with over 360 years of history, MUFG has a global network with approximately 2,000 locations in more than 40 countries. MUFG has nearly 120,000 employees and offers services including commercial banking, trust banking, securities, credit cards, consumer finance, asset management, and leasing. The Group aims to "be the world's most trusted financial group" through close collaboration among our operating companies and flexibly respond to all the financial needs of our customers, serving society, and fostering shared and sustainable growth for a better world. MUFG's shares trade on the Tokyo, Nagoya, and New York stock exchanges.

MUFG's Americas operations, including its offices in the U.S., Latin America, and Canada, are primarily organized under MUFG Bank, Ltd. and subsidiaries, and are focused on Global Corporate and Investment Banking, Japanese Corporate Banking, and Global Markets. MUFG is one of the largest foreign banking organizations in the Americas. For locations, banking capabilities and services, career opportunities, and more, visit www.mufgamericas.com.