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Making Sense

Consumer Price Index | July 11, 2024

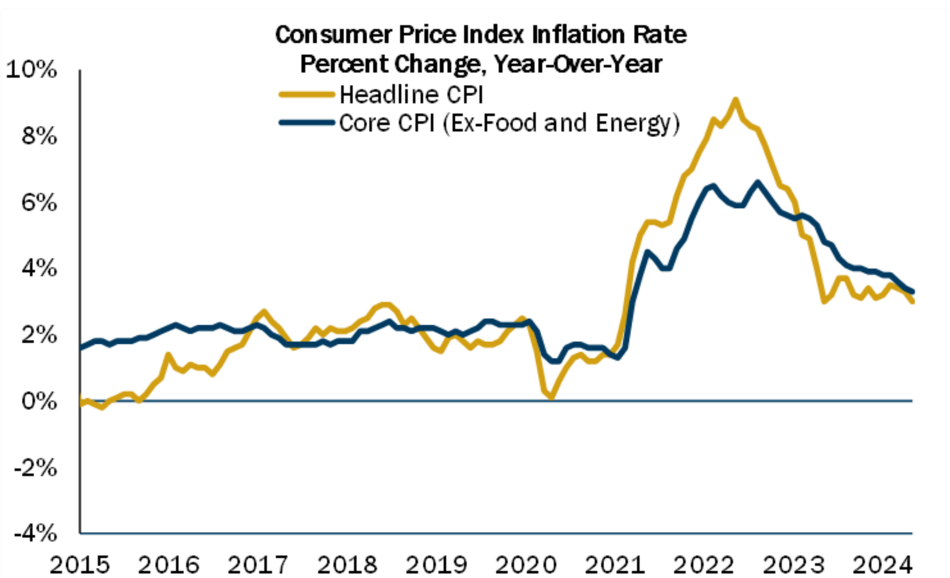
Softer-Than-Expected Inflation Data Paves the Way for Rate Cuts

The June Consumer Price Index report was very soft, and inflation rates are at their lowest since the beginning of the post-Covid inflation outbreak. The headline price index declined slightly in June, and core prices (ex-food and energy) rose by less than expected. Markets reacted strongly to the news: yields on the 2-year and 10-year Treasury notes both plunged to their lowest levels since March.

Markets were highly attentive to this morning's report for a signal on whether the surprisingly high inflation readings from earlier this year looked likely to persist or if instead prices were continuing their disinflationary trend toward 2%. Today's data strongly support the latter view. **In recent weeks, Federal Reserve policymakers have expressed the need to see further evidence that inflation is heading reliably toward their 2% objective before lowering interest rates. Today's data likely provide Fed policymakers with that evidence.**

It remains important to weigh both the higher-frequency inflation data and the broader trends. Price levels remain very high compared to a few years ago. Year-on-year inflation rates are still above the Fed's 2% target. Monthly swings in inflation can be driven by one-off factors. But at the same time, recent information must play a part in a balanced assessment of the inflation picture, and the latest data point toward inflation trending much softer.

The narrative around inflation and interest rates could move quickly from here. We have been firm that one month does not make a trend, but price data have undershot expectations for multiple months now. **At the last Fed meeting, in June, policymakers' projections indicated that most officials expected just one interest-rate cut this year. However, market pricing suggests 2-3 rate cuts over the next six months is the likely outcome.**



Source: Bloomberg

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Takeaways

- Headline inflation (year-over-year): 3.0%
- Core inflation (year-over-year): 3.3%

What does it mean for you?

- Inflation remains elevated but continues to improve.
- We continue to believe the Fed will cut rates later this year, likely starting in September.

What to watch:

- Producer inflation data comes out tomorrow (7/12).
- Employment data, half of the Fed's dual mandate, remains in focus.
- The next Fed rate decision is July 31.
- Stay informed and submit your questions at FirstCitizens.com/Market-Outlook.

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