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## August rebound and resurging energy prices

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- The CPI accelerated in August after two consecutive months of mild growth. Although growth was above expectations this month, inflation continues to decelerate with a “slow burn,” the most probable way the Fed can achieve a soft landing. Given the relative strength of the labor market and consumer spending, it would have been ambitious to expect August to continue along the same disinflationary path that we saw in June and July.
- Fuel prices were a big driver of headline price growth in August, helping push retail sales higher as well. Monetary policy has little impact on energy prices, so this shouldn’t significantly influence the Fed’s decision in the upcoming FOMC meeting. Energy prices become problematic from the Fed’s perspective when there is a risk of inflation expectations becoming de-anchored or if higher costs feed into the broader economy. Right now, those risks are largely tamed.

### August rebound

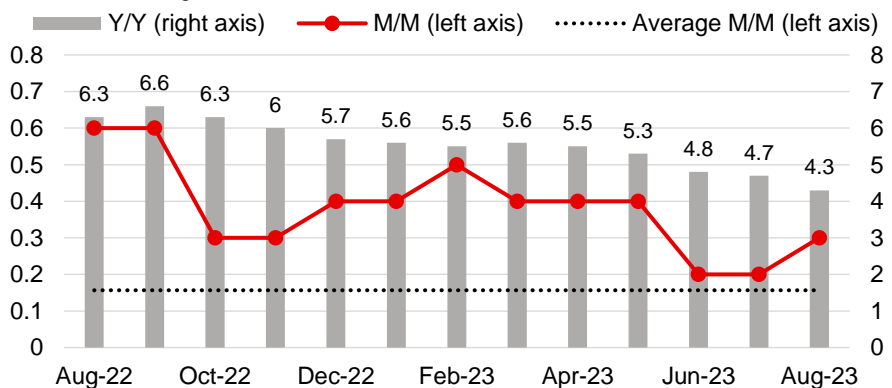
Core CPI rose by 0.3% month-over-month in August, up from 0.2% in both June and July. For context, monthly growth in core CPI averaged 0.35% over the first 7 months of the year. The August rise is still consistent with “slow burning” inflation where price growth eases rather than falls precipitously. Annual growth in core CPI, where base effects are notable, fell to 4.3% in August, down from 4.8% in June and 4.7% in July.

June and July were months of strong disinflation, with monthly growth just above the pre-pandemic average. Much of that was driven by monthly deflation in core goods and somewhat stronger disinflation of core services and shelter.

Core goods remained deflationary in August, growing by -0.1% month-over-month. However, goods including household furnishings, new vehicles, and auto parts moved into positive growth territory. Core services accelerated slightly to 0.39%, driven by a surge in professional services in medical care, as well as accelerated growth in leased autos and motor vehicle insurance.

### Monthly price growth accelerated in August to 3-month high

Core CPI, % change



Note: Average monthly change is from 2010-2019  
Source: BLS, MUFG Bank Economic Research

The auto industry continues to play a significant role on inflation, and the latest negotiations between the US auto makers and the UAW could potentially exacerbate price growth for new and used vehicles. Higher wages for auto workers wouldn't significantly impact overall wage growth in the US, but it would raise labor costs for the big 3 American auto makers. Additionally, a strike could upend production of new cars and trucks and reduce supply. Both potential outcomes could impact the margins of the US auto makers, but the outcome on inflation would depend on their ability to pass higher costs and/or the effects of lower supply onto the consumer. Demand will be a key factor.

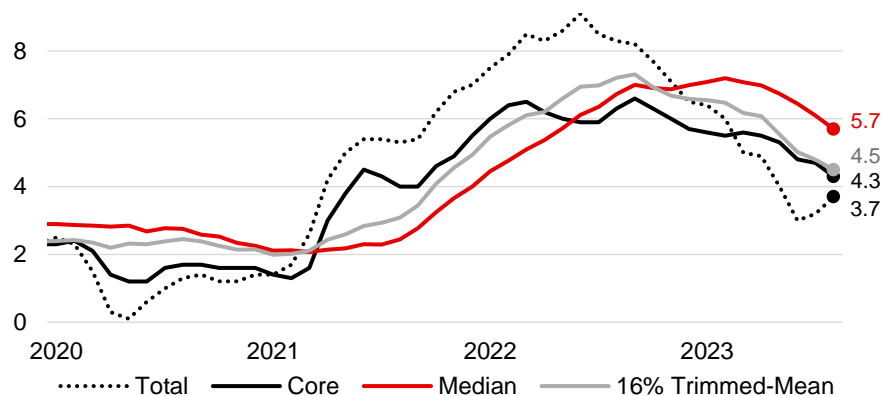
### Resurging energy prices

For headline inflation, the story centers around energy prices, which rebounded strongly, growing 5.6% month-over-month in August, compared to 0.6% in June and 0.1% in July. This is the highest monthly growth rate since June 2022 and it is a key reason that total annual CPI jumped from 3.2% in July to 3.7% in August.

High energy prices also explain the relatively strong August retail sales report. Overall, retail and food services sales grew by 0.6%, but that falls to 0.2% when excluding gasoline stations. Gas station sales grew by 5.2% in August, up from -0.6% in June and 0.1% in July.

### Disinflation continues at a slow pace

CPI, % Y/Y



Source: BLS, Cleveland Fed, MUFG Bank Economic Research

From the Fed's perspective, this latest energy price surge is unlikely to significantly influence their decision at this month's FOMC meeting. Monetary policy has little impact on energy prices and growth only becomes problematic to underlying inflation when high prices extend for several months or more. This leaves open the potential of energy price inflation feeding into the broader economy by either raising production costs or by de-anchoring inflation expectations. But so far, we only have one month of strong energy price growth. Even if OPEC signals further production cuts, it's not enough physical evidence for the Fed to justify being more hawkish based on energy prices alone. A pause at this month's FOMC meeting is still the likely outcome.

Overall, inflation continues to trend downward, albeit at a slow rate. A recession is likely the only way that inflation could quickly fall to 2%, so the Fed may be willing to accept price growth that is above target well into 2024, as long as the overall trend points downward.

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