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## Consumers didn't surprise in August

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- Consumer spending in August eased, driven by a decline in goods consumption, namely on new motor vehicles. Services consumption remained positive, with a big increase in air transportation and a positive increase in health care. Overall, August presents a more passive consumer, but the end of the summer months and colder weather could come with more domestic spending.
- The core PCE Price Index fell to below 4% on an annual basis for the first time since June 2021. The rate of disinflation has accelerated a bit, with core inflation falling to 2% as early as November of next year under the current linear trend. Risks remain however with energy prices rising and that feeding into the broader economy.

### Slower consumption and price growth

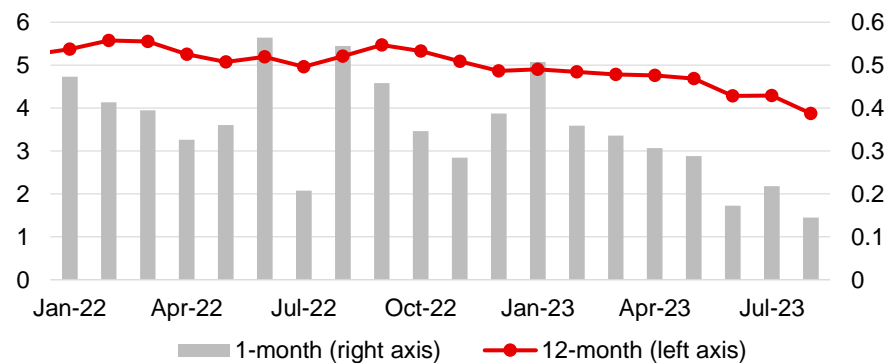
Real consumer spending rose by 0.1% in August, down from 0.6% in July and 0.3% in June. Much of the slower growth can be attributed to the drop in real consumption of motor vehicles, which fell by 0.2% in August after growing by 0.8% in July and 0.2% in June.

The auto industry will be in focus for the next several weeks at the very least. Not only because motor vehicles comprise a significant share of goods consumption, but also because the UAW strike is set to hit more automotive factories and the impact on inventories and prices will not be known for weeks after it ends. If the strike is short lived, the impact on GDP will likely be minimal. Historically, production rebounds strongly following resolutions, recovering what was lost. If the strike extends over months, the impact on economic growth will be much more noticeable and inventories would likely be severely impacted. If this is the case, prices on motor vehicles can be impacted.

So far, however, motor vehicles are still deflationary. Monthly price growth in motor vehicles has been negative in 9 of the past 11 months, helping push core price growth below 0.3% over the past 4 months. In August, prices fell for motor vehicles and parts by 0.38% on an annual basis, helping push annual core PCE price growth down to 3.9% from 4.2% in July.

### Core inflation has fallen below 4% for the first time since 2021

Core PCE Price Index, %

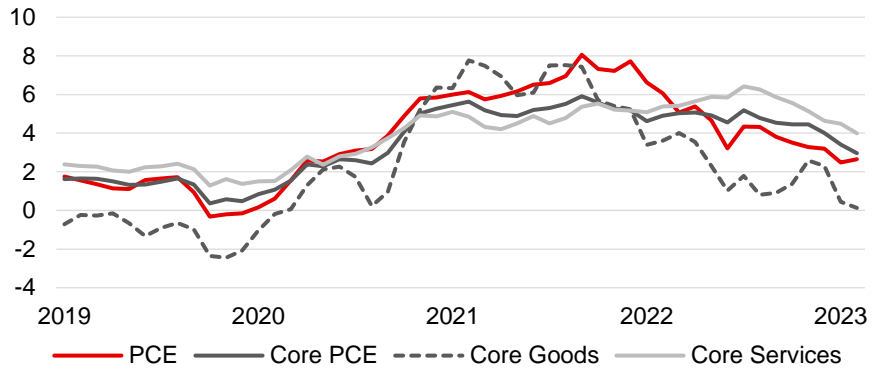


Source: BEA, MUFG Bank Economic Research

Motor vehicles have led core goods price growth to fall near 0%, but more progress needs to be made. For inflation to fall to the Fed's 2% target, core goods will likely need to have negative price growth for a considerable period. The auto workers strike does threaten this possibility in the short-run.

**Core goods inflation has fallen down to near 0%**

*PCE Price Index, 6-month change, % AR*



Source: BEA, MUFG Bank Economic Research

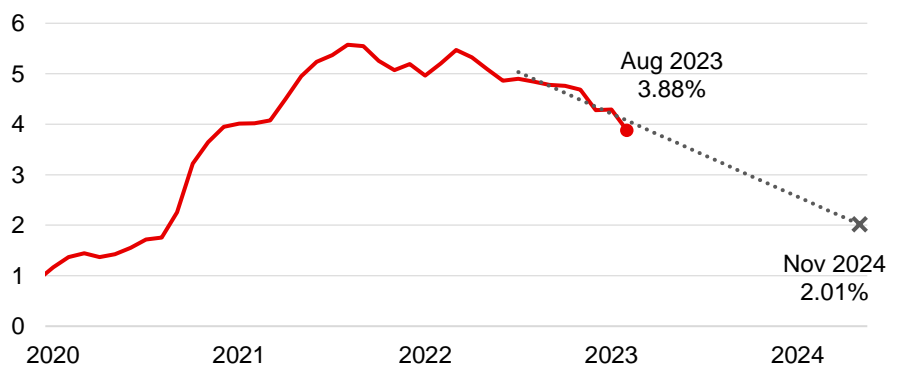
Core services price growth will almost certainly remain positive, though disinflation is continuing. Air transportation was a strong contributor to core services price growth in August, but that will likely reverse as the summer ends. Overall, disinflation is continuing, and the downward path has even accelerated a bit.

From July's PCE, the linear trend suggested that annual inflation wouldn't fall to the Fed's 2% target until mid-2025. This trend steepened in August, with November 2024 now looking to be a plausible date.

Observing the linear trend does not function as a reliable forecast, but it does offer insight on the inflation trajectory. Inflation data are very noisy and volatile, and the Fed is not likely to view monthly or annual numbers with exact precision when making monetary policy decisions. For this reason, observing a simple linear trend can be useful.

**Current trend shows inflation falling to 2% by Nov 2024**

*Core PCE price index, 12-month change, %*



Source: BEA, MUFG Bank Economic Research

The risk to inflation continuing along with trend lies, in part, on the re-acceleration of energy prices. While monetary policy has little effect on energy prices themselves, they could feed into the broader economy if price growth is strong enough and lasts for a considerable time. Risks remain, but it is still too early to make that assumption.

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