Bandhan Mutual Fund

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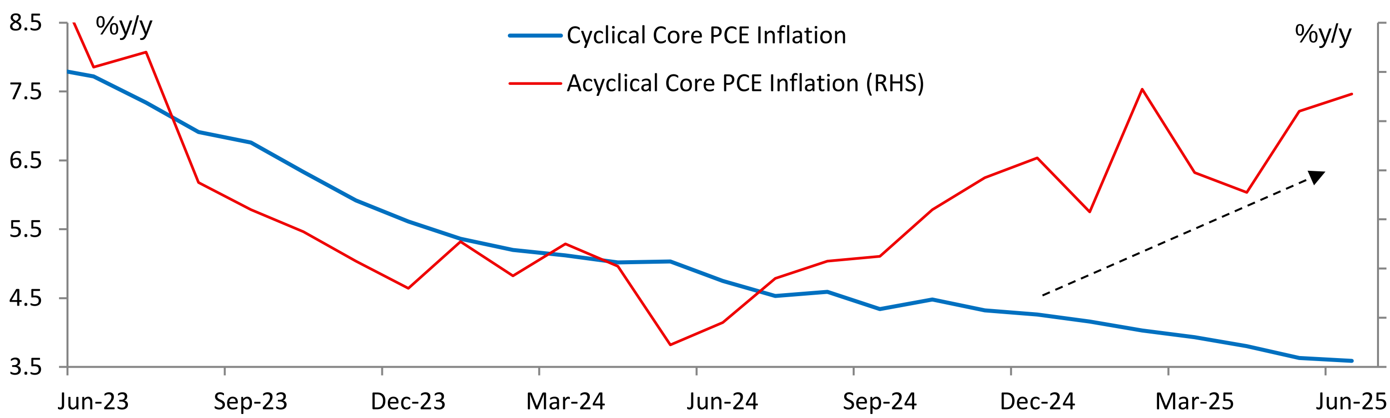
US Inflation: Driven Less by Cyclicals Now?



July US CPI was flat at 2.7% y/y, driven by benign price momentum in food, energy and apparel. Core CPI moved up from 2.9% in June to 3.1% as air fares, new & old vehicles, and medical services picked up. Thus, non-housing-core services momentum increased, while core goods were flat, although goods inflation more recently has been going up.

However, a split of Core PCE inflation suggests acyclical components (less sensitive to economic conditions and more to industry specific factors) have been the main driver in the last one year (*figure above*). In fact, non-healthcare acyclical services have been the major contributor. Health care is separated given its reliance on administered prices. We had previously written about the higher share of acyclical sectors in non-farm payroll additions.

This further raises the question on the outlook for US growth, the health of cyclical sectors, and whether growth and the labor market are weaker than what headlines suggest. Growth in private domestic demand (consumption plus investment) has already been weakening. This also has important implications for monetary policy which impacts the cyclical economy more and idiosyncratic sector specific factors less.

Source for the chart: Federal Reserve Bank of San Francisco, Bandhan MF Research. Note: PCE- Personal Consumption Expenditure.

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