Consumer Prices Still Not Reflecting Tariff Costs

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Given what appears to be a significant slowdown in labor growth, Fed officials will now require inflationary pressure to behave in order reduce interest rates. That was generally the case last month as the Consumer Price Index (CPI) was essentially inline with forecasts. Headline CPI rose +0.2% in July after a +0.3% rise in June, while core CPI climbed +0.3% following a +0.2% June increase.

On an annual basis, overall CPI held steady at a +2.7% pace, while core CPI rose from +2.9% to +3.1%, *the highest since February*. Goods prices drove the increase in July, while continued easing of shelter costs and lower energy prices kept the index numbers in an acceptable range.

Overall food prices were unchanged, but the split between grocery store and restaurant prices widened. The food at home index was down -0.1%, while food away from home rose +0.3%. Energy prices fell -1.1%, with gasoline down -2.2% in July and -9.5% year-over-year. The fact that groceries and gasoline were restrained last month creates the feel of retreating price pressure for most consumers.

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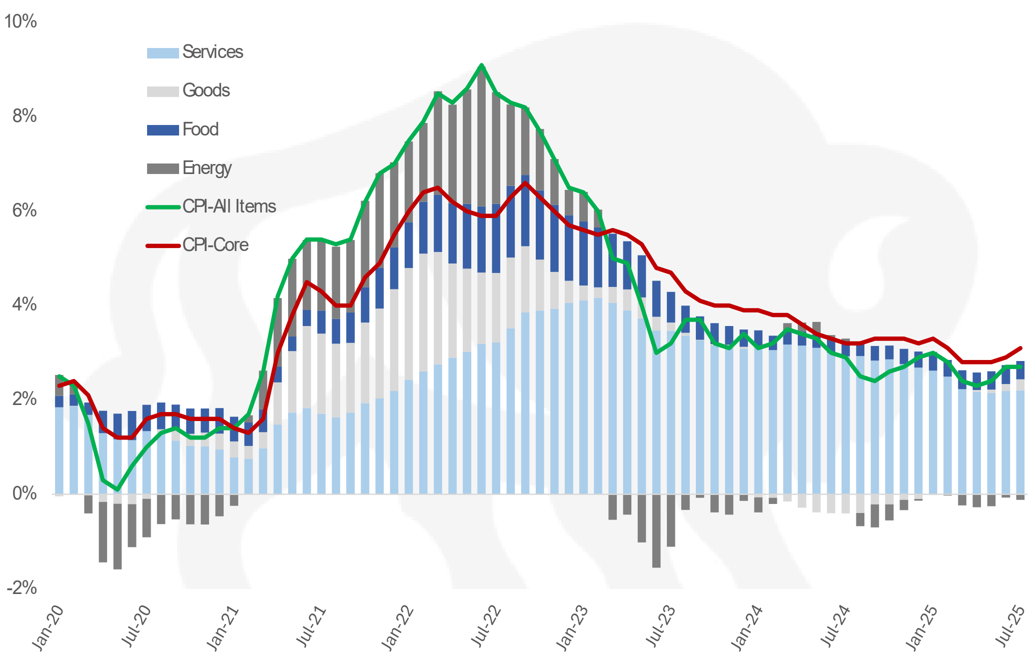
New vehicle prices were unchanged for the month, following -0.3% declines in the previous two months. With dealer lots well stocked at pre-tariff costs, more recent cost increases on new vehicles are not yet being passed to consumers. However, *used vehicle prices* climbed +0.5% for the month and +4.8% for the year. Affordability is an issue for many Americans, as the average price of a new auto was just under $49k in May, compared to $33k for a lightly used (1-5 years) model. On a related note, the cost of auto insurance continues to rise, up +5.3%.

Consumer Price Index (Year-over-Year Percent Change)



Source: Bureau of Labor Statistics

Although shelter costs remain the bigger component of consumer inflation, the gradual easing of housing prices is also the main reason why the overall trend is lower. Shelter costs climbed just +0.2% for the second straight month and +3.7% year-over-year.

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The bond market reaction is mixed in early trading with short yields down slightly and longer yields up. The futures market has almost fully priced-in a September rate cut. The fact that inflation met expectations in July should allow for a quarter point reduction at the next FOMC meeting on September 17, although Fed officials will see the August CPI numbers as well as the August employment report before making any decisions.

Market Indications as of 8:54 A.M. Central Time

DOW	Up 220 to 44,195 (HIGH: 45,014)
NASDAQ	Up 83 to 21,468 (NEW HIGH)
S&P 500	Up 42 to 6,415 (NEW HIGH)
1-Yr T-bill	current yield 3.90%; opening yield 3.93%
2-Yr T-note	current yield 3.75%; opening yield 3.77%
3-Yr T-note	current yield 3.73%; opening yield 3.74%
5-Yr T-note	current yield 3.84%; opening yield 3.84%
10-Yr T-note	current yield 4.31%; opening yield 4.29%
30-Yr T-bond	current yield 4.89%; opening yield 4.86%