Economic Analysis

November’s Core CPI Lends Support to Liftoff

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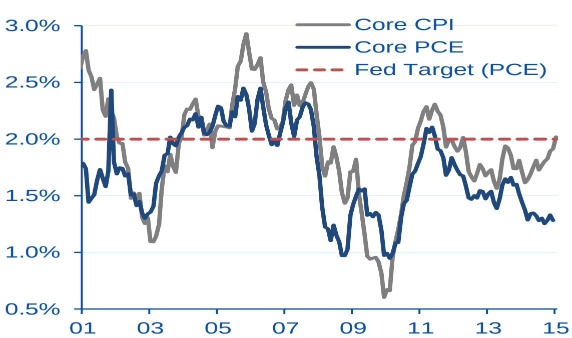
- **Headline CPI remained unchanged due to declines in food and energy prices**
- **Core CPI rose 0.2% MoM and 2% YoY, driven by gains in the core services index**
- **Despite weakness in core PCE, labor market and consumption gains support rate hike**

The continuing decline in oil prices seems to have kept headline CPI in check, with no change in the all items index in November. Headline CPI remained flat due to weakness in food and energy prices; the food index was down MoM for the first time since March, while the energy index declined 1.3% MoM after a slight rise in October. On a YoY level, the energy index was down for the 15th month in a row, declining 14.7%, with decreases in the prices of both energy commodities, such as gasoline, and energy services, such as electricity.

On the other hand, the core index, excluding the volatile food and energy categories, was up 0.2% MoM for the third consecutive month. On a YoY level, core CPI finally hit 2% for the first time since May 2014, which should lend further support to those supporting a December rate hike during the FOMC meeting that starts today. The core services index contributed most to the increase in core CPI, with MoM gains in shelter (0.2%), transportation (0.6%) and medical care services (0.4%). On the commodities side, this CPI release could provide some incentive for holiday shoppers to hit the stores (if they haven’t already) as the prices of several popular gift items were down on a monthly basis, such as toys and games (0.3%), jewelry and watches (1.1%), apparel (0.3%) and stationary and gift wrap (0.8%). This is the third consecutive decline for apparel prices, which have been impacted by low import prices and the strengthening dollar.

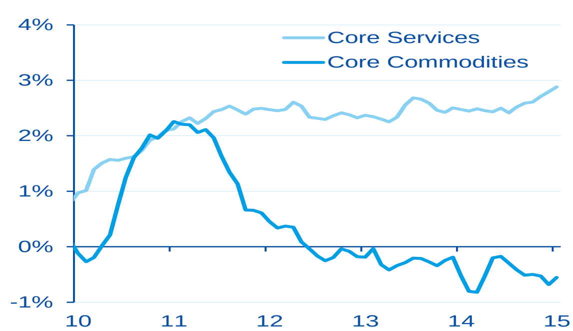
Although core CPI has reached a desired level, the Fed’s preferred inflation metric, the core PCE index, was up only 1.3% YoY in October for the seventh month in a row—remaining below the Fed’s 2% YoY target. Despite the ongoing weakness in core PCE, the promising core CPI level along with increasing consumption, a strengthening labor market, and continued wage gains, supports our expectation for a rate hike this month. Tomorrow’s announcement will reveal if the FOMC members were able to set aside their inflation concerns to kick start normalization.

Chart 1
Inflation Metrics (YoY % Change)



Source: BLS, BEA & BBVA Research

Chart 2
Core Services and Commodities (YoY % Change)



Source: BLS & BBVA Research

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