The Daily Dish

July Consumer Price Inflation

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The headline news in yesterday's release of the Consumer Price Index (CPI) data for July was the 7.7 percent (44 percent at an annual rate) decline in gasoline prices – a decline precipitous enough to leave the overall CPI unchanged from June to July. Zero inflation! The nation is saved!

Alas, that is too good to be true. The reality behind the headline is that the CPI showed no progress on inflation. The core (non-food, non-energy) CPI rose year-over-year at a 5.9 percent rate – unchanged from June. The bundle of food, energy, and shelter (FES) that constitutes over one-half of the typical monthly spending rose at a painful 11.3 percent rate. That constitutes an acceleration from 11.1 percent in June and reflects the fact that shelter inflation (one-third of the CPI) continued its unabated rise. Shelter inflation is now 5.7 percent year-over-year.

The absence of real progress means that the Fed will be compelled to continue aggressively raising rates and shrinking its portfolio. (Recall that selling of portfolio holdings pulls money out of the financial markets and tightens financial conditions.) That won't sound great to the Wall Street faint-of-heart who live for loose monetary policy. And it will concern those who, correctly, fear that the economy is facing a rising chance of entering a recession.

But the reality is that once inflation is ingrained in the economy (and it is), there are no good choices. The Fed is choosing the better of bad options by focusing on restoring some semblance of price stability as those are the conditions needed for sustained high employment and economic growth.