Core CPI comes in at expectations in July, good enough for a patient Fed

Headlines

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- **Core CPI matched expectations in July, rising 0.22% m/m after outright declining in June, while the year-over-year rate eased to 2.5%.** Falling gasoline prices pushed headline CPI even lower, with headline inflation up just 0.07% m/m**.**

- **Core goods inflation rebounded to +0.2% m/m after two consecutive negative months,** with used vehicles, household furnishings, and apparel all posting stronger readings. Still, three-month annualized core goods inflation sits at 0.0%, well below the pace seen earlier this year and close to the pre-tariff trend.

- **The July CPI report would have been notably stronger were it not for the relatively benign shelter reading,** which increased just 0.1% m/m, largely due to a nearly 3% decline in hotel and motel prices. In our view, disinflation from housing has largely run its course, and further improvement in inflation will need to come from either services or goods prices.

- **Outside of shelter, services inflation also rebounded, confirming that June's large declines were largely noise. Sticky services inflation will remain the key issue for the Fed going forward.** Declines in telecommunications, auto insurance, and hotel prices subtracted 0.15 percentage points from m/m core inflation in June, with those categories returning to more normal levels in July. These three categories alone explain much of the swing in core inflation between June and July.

- **What does this mean for the Fed?** Overall, the Fed should view this as a relatively benign inflation report, broadly consistent with what the more dovish members of the committee have said they would need to see to justify not hiking rates. Market pricing for a September rate hike fell below 40% following the release.

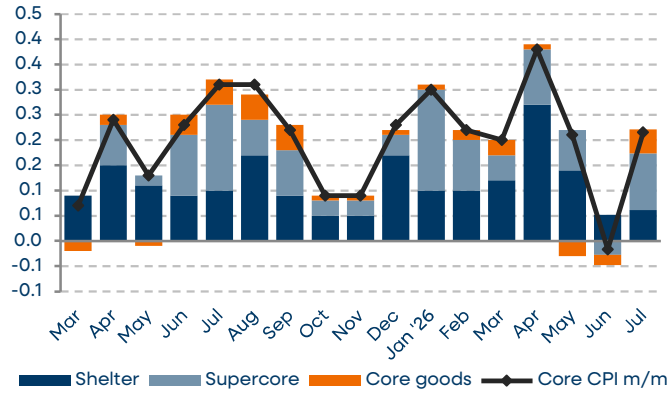
Table 1: CPI and components (% chg., m/m)

Indicator	Avg. 2025	Avg. YTD	Mar '26	Apr '26	May '26	Jun '26	**Jul '26**
Headline	0.22%	0.32%	0.87%	0.64%	0.47%	-0.42%	**0.07%**
Core	**0.22%**	0.20%	0.20%	0.38%	0.21%	-0.02%	**0.22%**
Shelter	*0.26%*	0.28%	0.27%	0.61%	0.32%	0.12%	**0.14%**
Core Services ex. Shelter	*0.24%*	0.23%	0.17%	0.35%	0.26%	-0.09%	**0.35%**
Core Goods	*0.12%*	0.04%	0.11%	0.03%	-0.11%	-0.09%	**0.20%**

Core inflation bounces back, but still a relatively benign print

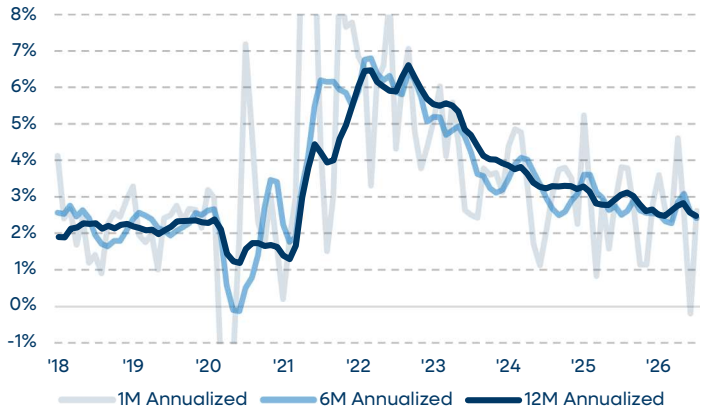
Core CPI matched expectations in July, rising 0.22% m/m after outright declining in June. This brought the year-over-year rate down to 2.5%, the lowest reading since early 2025. Falling energy prices in July pushed headline CPI even lower, with headline inflation rising just 0.1% on the month.

Figure 1: Core CPI and contributions (% chg., m/m)



Sources: BLS, PNC

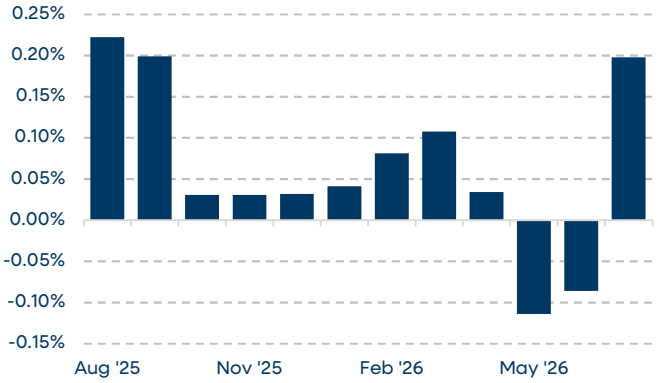
Figure 2: Core CPI (1M, 3M, and 12M annualized growth rates)



Sources: BLS, PNC

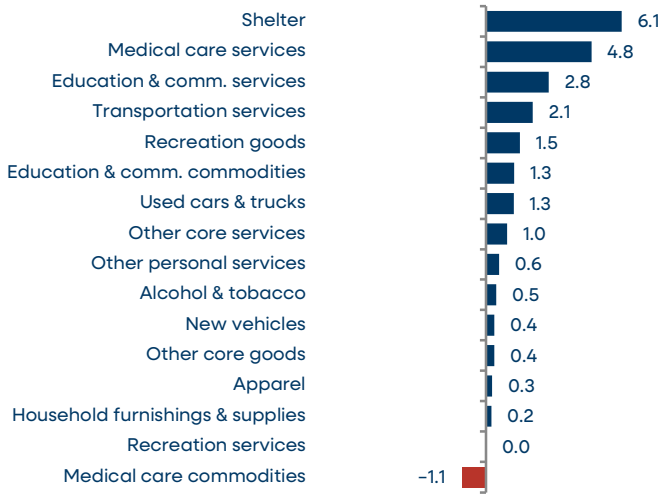
That said, the rebound from June's unusually weak inflation print was relatively broad-based. Core goods inflation increased 0.2% m/m after two consecutive monthly declines, with used vehicles, household furnishings, and apparel all posting stronger readings. Still, three-month annualized core goods inflation sits at 0.0%, well below the pace seen earlier this year and close to its pre-tariff trend.

Figure 3: Core Goods (% chg., m/m)



Sources: BLS, PNC

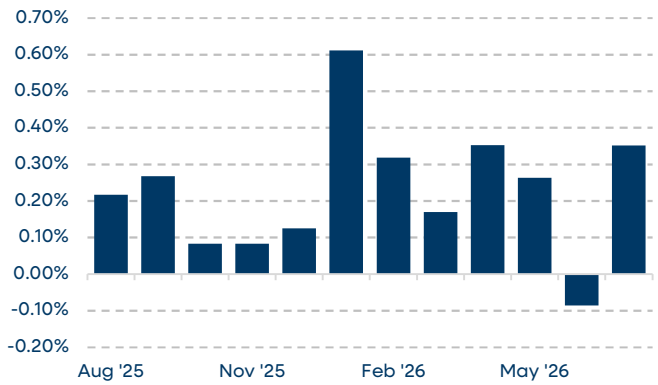
Figure 4: Contributions to core CPI in July (basis points, m/m)



Sources: BLS, PNC

Services inflation also rebounded, confirming that June's large declines were largely noise. Sharp declines in telecommunications, auto insurance, and hotel prices subtracted 0.15 percentage points from June's monthly core inflation reading, with those categories returning to more normal levels in July. In fact, these three categories alone explain much of the swing in core inflation between June and July.

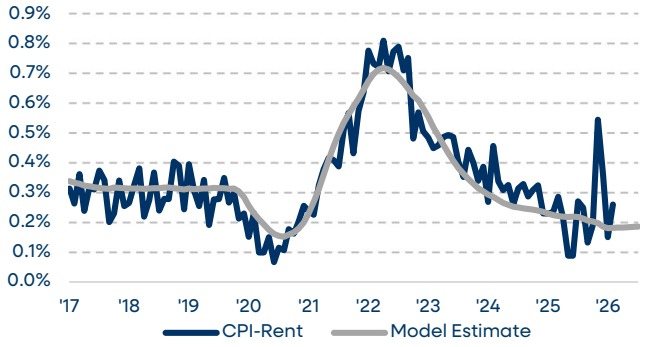
Figure 5: Core Services ex. Shelter (% chg., m/m)



Sources: BLS, PNC

The one bright spot was **shelter inflation**, which increased just 0.1% m/m after averaging 0.28% m/m year-to-date. Much of that weakness was concentrated in a nearly 3% monthly decline in hotel prices, however, with rental inflation coming in more in line with expectations. In our view, disinflation from housing has largely run its course, and further progress on inflation will need to come from either services or goods prices.

Figure 6: CPI rent vs. model estimate



Sources: CPI, PNC

July inflation gives the Fed room to remain patient ahead of September

Overall, the Fed should view this as a relatively benign inflation report. While tomorrow's PPI release will provide a clearer picture, today's CPI data is consistent with roughly a 0.2% m/m increase in core PCE, the Fed's preferred inflation measure (while core PCE has been running above core CPI of late, we expect this to unwind later this year). In our view, that is broadly consistent with what the more dovish members of the committee have said they would need to see to justify not raising rates. **Market pricing for a September rate hike fell below 40% following the release.**

Put differently, this report is likely good enough for the Fed to remain patient and see how the full August data picture develops before making a decision on rates in September.

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