U.S. CPI Inflation Slows in July; Bank of Mexico Hikes Rates; More Data Confirm China’s Expansion is Slowing

UNITED STATES: The consumer price index for urban consumers (CPI-U or more commonly just CPI) rose 0.5% in July from June, matching consensus expectations, and slowing from June’s 0.9% increase. July’s increase was the lowest since February. Energy prices rose 1.6% in July on a 2.4% increase in gasoline prices. Food prices rose 0.7% on the month, with food away from home up 0.8%. “Core” CPI excluding food and energy rose 0.3% from June, down from a 0.9% increase in June and the smallest monthly increase since March. From a year earlier, the CPI rose 5.4% in July, tying June for the fastest year-ago increase since 2008, and the core CPI rose 4.3% after June’s 4.5% increase, which was the highest since 1991.

The prices that made core inflation surge in the first half of 2021 calmed down in July. Used car and truck prices rose 0.2% after surging 30% March to June; airline fares fell 0.1% after surging 21.6% February to June; car and truck rental prices fell 4.6% after surging 64% January to June. New vehicles were an exception, up 1.7% in June after rising 4.1% March to June. The cost of lodging away from home surged again, up 6.0% in July and up a cumulative 27% from February. As bottlenecks improve and consumer preferences normalize, the surge in these prices will slow further.

Core prices unaffected by pandemic-related surges in demand rose much more slowly. In July, rent of primary residence rose 0.2% from June and 1.9% from a year earlier; owners’ equivalent rent of residence (what homeowners think their homes would rent for) rose 0.3% from June and 2.4% from a year earlier. The big increases in house prices since the pandemic began have not flowed through to the CPI basket yet. Medical care services costs rose 0.3% from June and 0.8% from a year earlier. Medical care commodity prices rose 0.2% on the month and fell 2.1% on the year.

The producer price index (PPI) for final demand increased 1.0% in July, same as June and outpacing the CPI. Final demand energy prices rose 2.6% and final demand transportation and warehousing costs rose 2.7%. Trade services—the markups of wholesalers and retailers—rose 1.7% on the month. Producer prices of foods fell 2.1% on the month after rising 12% between August 2020 and June 2021. The PPI final demand excluding food, energy, and trade services rose 0.9% in July after a 0.5% increase in June. Energy prices heavily influence “core” producer prices since the basket includes transportation costs. From a year earlier, the producer price index for final demand rose 7.8%, the highest increase since comparable data began in 2010. The producer price index for all commodities, an older aggregation of producer prices, rose 19.8% in July in year-ago terms, the fastest increase since 1974. July saw notable increases in producer prices of unprocessed fuel, up 11.2%; transportation of passengers, up 9.0%; and final demand construction costs, up 1.5% on the month.

Initial claims for unemployment insurance fell by 12,000 in the week ending August 7, to 375,000. Claims for the previous week were revised slightly higher, to 387,000 from 385,000. The four-week moving average of claims, which smooths out some of the week-to-week volatility, rose by 1,750 in the week ending August 7, to 396,250. Initial claims have been around 400,000 per week since June—the lowest since the pandemic came to the U.S., but still about double their pre-pandemic level. Total beneficiaries of unemployment benefits, including pandemic-related benefits, fell by nearly a million on the week in the week ending July 24, to 12.055
GLOBAL ECONOMIC HIGHLIGHTS

million from 12.975 million the previous week (not seasonally adjusted). The sharp drop in unemployment beneficiaries reflects both job gains and the expiration of benefits in many states.

The University of Michigan’s Consumer Sentiment Indicator fell sharply in the first estimate for August and was the lowest in 11 years—that is, even lower than its April 2020 trough. The expiration of unemployment benefits, surging consumer prices, and the delta variant are likely behind the drop.

The Federal Reserve’s release of the July industrial production report on August 17 is expected to show a 0.5% monthly increase, while the advance estimate of July retail sales released the same day is forecast to show a 0.2% monthly decline on the month, held back by another drop in new car sales.

MEXICO: The Bank of Mexico raised its policy interbank rate 0.25 percentage point to 4.50% at its August 12 Monetary Policy Committee decision. The Bank revised up its short-term forecasts for inflation, citing the same price shocks affecting the United States; while their forecasts for inflation in the second half of 2022 are little changed relative to their June round of forecasts, they see risks to the upside. The Bank of Mexico is likely to continue raising interest rates by a quarter percentage point quarterly through the second half of 2022.

CHINA: The Chinese government closed the Meishan terminal in the Ningbo-Zhoushan port on August 11 after a worker tested positive for coronavirus; the terminal accounts for a quarter of container traffic in the port, which is the world’s third busiest. The port closure will further prolong the supply chain disruptions that have held back the manufacturing recovery and fueled inflation this year.

China’s monthly indicators for July were soft: Retail sales, value added of industry, and investment in fixed assets slowed more than expected, and the unemployment ticked up on the month (though this is probably just seasonality; the rate is not seasonally adjusted and increased from the second to third quarters in each of the three pre-crisis years for which data have been published). Retail sales growth slowed to 8.5% in year-ago terms in July versus 10.9% expected, following a 12.1% increase in June; value added of industry grew 6.4% versus 7.9% expected, and down from 8.3% in June; and investment in fixed assets grew 10.3% in the year through July versus 11.3% expected, and down from 12.6% in June. In seasonally-adjusted terms, industrial value added growth slowed to 0.3% in July from 0.6% in June and was the slowest since February 2020’s plunge. Retail sales fell 0.1% after a 0.5% expansion in June; they most recently contracted in January due to restrictions on activity ahead of the Lunar New Year holiday. Seasonally-adjusted growth in fixed assets slowed to 0.2% in July from 0.3% in May and June and 0.4% in April.

China’s July slowdown is due to reduced demand for made-in-China exports as consumers in advanced economies redirect spending toward services and away from goods; less expansionary fiscal and monetary policy; and rolling lockdowns that are preventing a faster recovery of high-contact services activity. Despite July’s slowdown, China’s policy stance—fiscal, monetary, and credit policy—will stay less supportive in the second half of 2021 than at the turn of the year. Chinese policymakers need to balance the growth outlook against the global uptick in inflation and tapering quantitative easing programs in the U.S. and Europe, which could make capital flows to emerging markets more volatile in the next few quarters. PNC forecasts for Chinese real GDP growth to slow to 7.5% in year-ago terms in the fourth quarter of 2021 and 5.9% in the fourth quarter of 2022.

EUROZONE: Industrial production fell a seasonally-adjusted 0.3% percent in June from May and was up 9.7% from a year earlier after a 20.6% increase in May. The August 17 release of quarterly employment for the second quarter of 2021 will likely show a 0.3% quarterly increase, or a 0.9% year-over-year increase; this implies a solid quarterly increase in productivity, since employment in more labor-intensive service-providing jobs continues to lag the overall recovery.

UNITED KINGDOM: As expected, the easing of pandemic restrictions fueled a big jump in real GDP in the second quarter of 2021. Real GDP surged 4.8% in quarterly terms (not seasonally adjusted), according to the Office of National Statistics’ first estimate. Real GDP was still 4.4% below the pre-crisis peak in the fourth quarter of 2021; this is much worse than in the United States, where real GDP was already above the pre-crisis level in the second quarter of 2021. Output of services-providing sectors jumped 5.7% on a near doubling of accommodation and food service activity, which rose 87.8% on the quarter. Industrial production
rose 0.5% with manufacturing up 1.8% despite a 16.7% drop in motor vehicle production; construction output rose 3.3%. Foreign trade was a drag in the quarter: Goods exports rose 9.6% and goods imports rose 10.0%, while service exports fell 4.7% and service imports fell 3.8%.

**BRAZIL:** Consumer prices as measured by the IPCA index increased 1.0% in July from the prior month, the biggest rise since 2002, in line with consensus expectations, and following a 0.5% reading in June; prices were up 9.0% in July from twelve months earlier, the highest reading since 2016. The high year-over-year inflation was mainly driven by the surge in electricity prices (7.9%), household goods prices (12.2%) and transportation prices (15.9%). IPCA inflation has overshoot the upper limit of the central bank’s target for five straight months. Prices accelerated in July amidst a weak currency and a water crisis. Core inflation as measured by the trimmed means index was stable at 0.6% in July from June and increased to 4.8% in year-ago terms from 4.3%. Central Bank of Brazil President Roberto Campos Neto stated August 12 that the central bank will use “all the tools available to anchor inflation in the medium and long term.”

PNC Economics expects the central bank to increase the benchmark Selic rate by a full percentage point to 6.25% at the next scheduled policy meeting in September. The IBC-BR Economic Activity Index, a proxy of GDP, rose 1.1% in June from May, above consensus expectations for a 0.6% increase; the IBC-BR Economic Activity Index was up 9.1% in the twelve months to June. Brazil’s economy returned to its pre-pandemic level at the end of the first quarter of 2021 thanks to massive fiscal stimulus and recovering demand for its commodity exports. Business confidence is above the pre-pandemic level and consumer confidence has increased for four straight months. The economic outlook remains solid as the vaccination campaign progresses and the global economy recovers from the pandemic.

**INDIA:** CPI inflation cooled to 5.6% in July in year-over-year terms, back within the central bank’s 2%-to-6% target range, from 6.3% in the prior month. The largest driver of the lower inflation reading was the food and beverages category, with inflation declining to 4.5% in July from 5.6% in June. Core inflation (excluding food, fuel, and light) cooled to 6.0% in July from 6.3% in June. The deceleration in inflation is likely temporary; inflation will return to above the central bank’s target range in the near term as pandemic-driven supply dislocations and pent-up demand put upward pressure on consumer and producer prices. Industrial output increased 13.6% in June, largely due to base effects, following a downwardly-revised 28.6% rise in the prior month.

**JAPAN:** Real GDP grew 1.3% annualized in the second quarter of 2021, beating expectations for a 0.5% increase; the first quarter’s contraction was revised to 3.7% annualized from 3.9% annualized in the prior release. Private residential investment grew 8.6% annualized in the second quarter and private nonresidential investment grew 7.0% annualized; while exports grew a solid 12.3% annualized, imports grew by a much faster 21.9%, making trade a net drag on real GDP in the quarter. Even with a slightly better than expected second quarter, real GDP is still below its level in the fourth quarter of 2020 due to the contraction in the first quarter of 2021. Real GDP in the second quarter was 3.4% below its pre-crisis peak in the third quarter of 2019, prior to the following quarter’s hike in the value-added tax (a kind of national sales tax).