

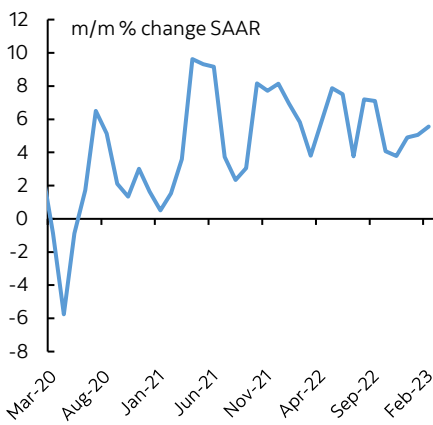
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Chart 1

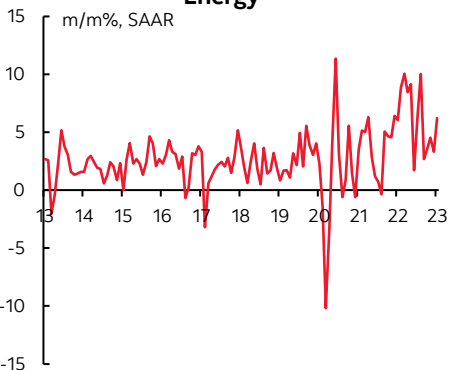
US Core CPI Inflation



Sources: Scotiabank Economics, BLS.

Chart 2

US Core Services Ex-Housing & Energy



Sources: Scotiabank Economics, Bloomberg.

CPI and the FOMC — Haste Makes Waste

- Core CPI exceeds expectations...
- ...including Powell's favourite measure
- Breadth was high
- Markets are back to pricing most of a quarter point hike next week
- It would be a misstep for the Fed to pause, let alone cut

US headline / core CPI, m/m % change, SA, February:

Actual: 0.4 / 0.5
 Scotia: 0.4 / 0.3
 Consensus: 0.4 / 0.4
 Prior: 0.5 / 0.4

Most of a quarter point Fed hike is back to being priced for next Wednesday's decision in the wake of an upside surprise to core CPI and further evidence of stabilizing markets. Major rallies across US regional banks are unfolding on day two of the aftermath of weekend developments.

I'm still not buying the case for the Fed to pause next week—let alone cut. That seemed to be an overly hasty and impulsive view in the markets. I think there remains a strong case to hike 25bps which is my expectation. These developments add to why and on top of previously expressed views ([here](#)) on how the magnitude and scope of the response by regulators ringfenced systemic risk while preserving the safety, soundness and functioning of the core banking industry in functioning markets engaging in price discovery.

If the FOMC is uncomfortable with most of a hike being priced then watch for a media plant in blackout like they did last summer, but that would be more likely closer to the meeting if at all. Powell does not like to surprise markets on game day with the here-and-now decisions.

On the future guidance, the FOMC may not go as high with revised terminal rate projections in next week's dot plot as they would have otherwise, but it would be a misstep in my opinion for them to signal panic and abandon the fight against inflation at the first whiff of trouble. Trouble that is being contained. They can work caution into the bias by not going as high on the terminal rate given a rate equivalence to tightened financial conditions and signal that it's just a dot plot, but that they will take all decisions meeting-by-meeting while monitoring conditions. Chair Powell needs to be a steady hand on the tiller and resist the flightiness that has characterized some market voices. It's not a shoe-in call, but I'll be disappointed in the Chair if he caves.

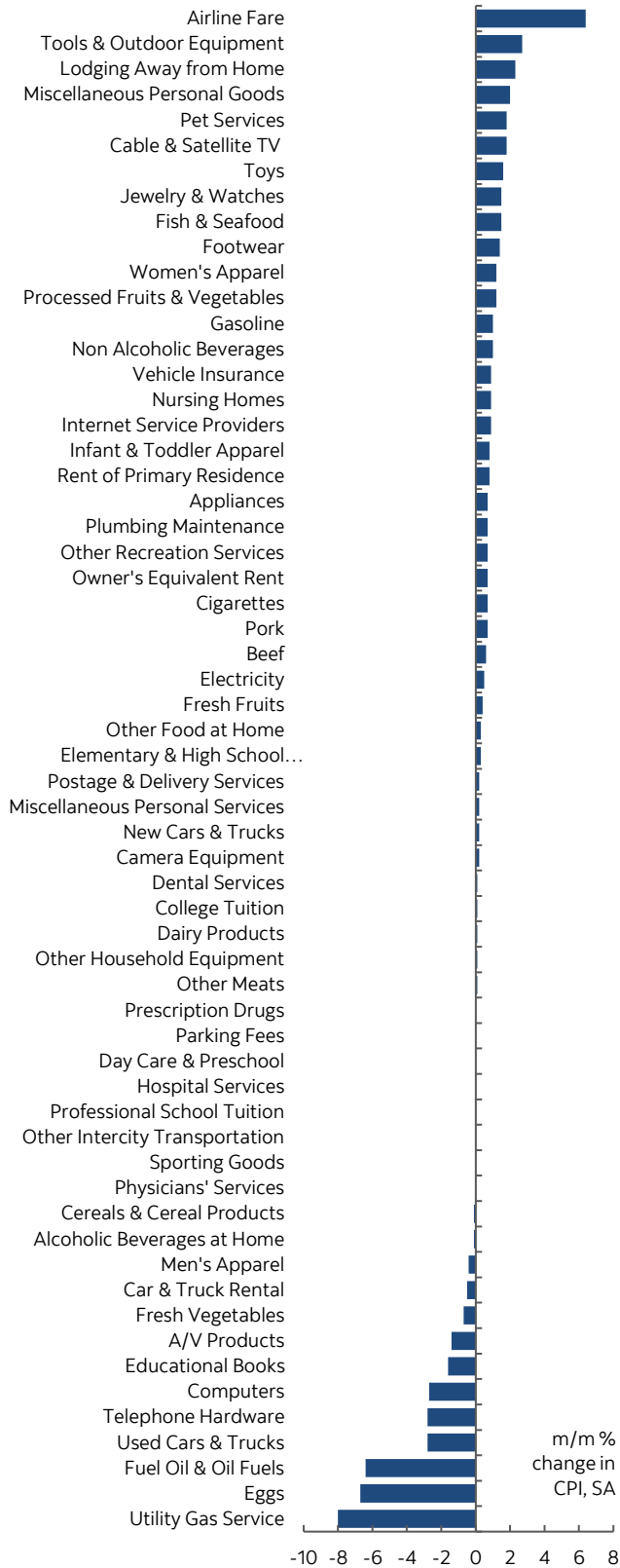
INFLATION DETAILS

Core inflation is still not cooling. In fact, it accelerated last month. Core inflation ex-food and energy ran at a seasonally adjusted and annualized pace of 5.6% m/m in February. That's the hottest since last September, a half point hotter than the prior month and more importantly continues to show that the mild ebbing that we saw last Fall is being left in the dust (chart 1). Forget the media headlines that look at irrelevant year-over-year core inflation that was down a tick to 5.5%. At issue is evidence on inflationary pressures at the margin, not prices relative to year-ago base effects.

Powell may see even hotter pressures in this report by emphasizing the measure of inflation that he has been most concerned about since last Fall. That measure is core PCE inflation minus shelter and energy services. We won't get that gauge until March 31st, but in the meantime, we do have it in CPI terms. This measure was up by 6.2% m/m which is the hottest since six months ago (chart 2).

Chart 3

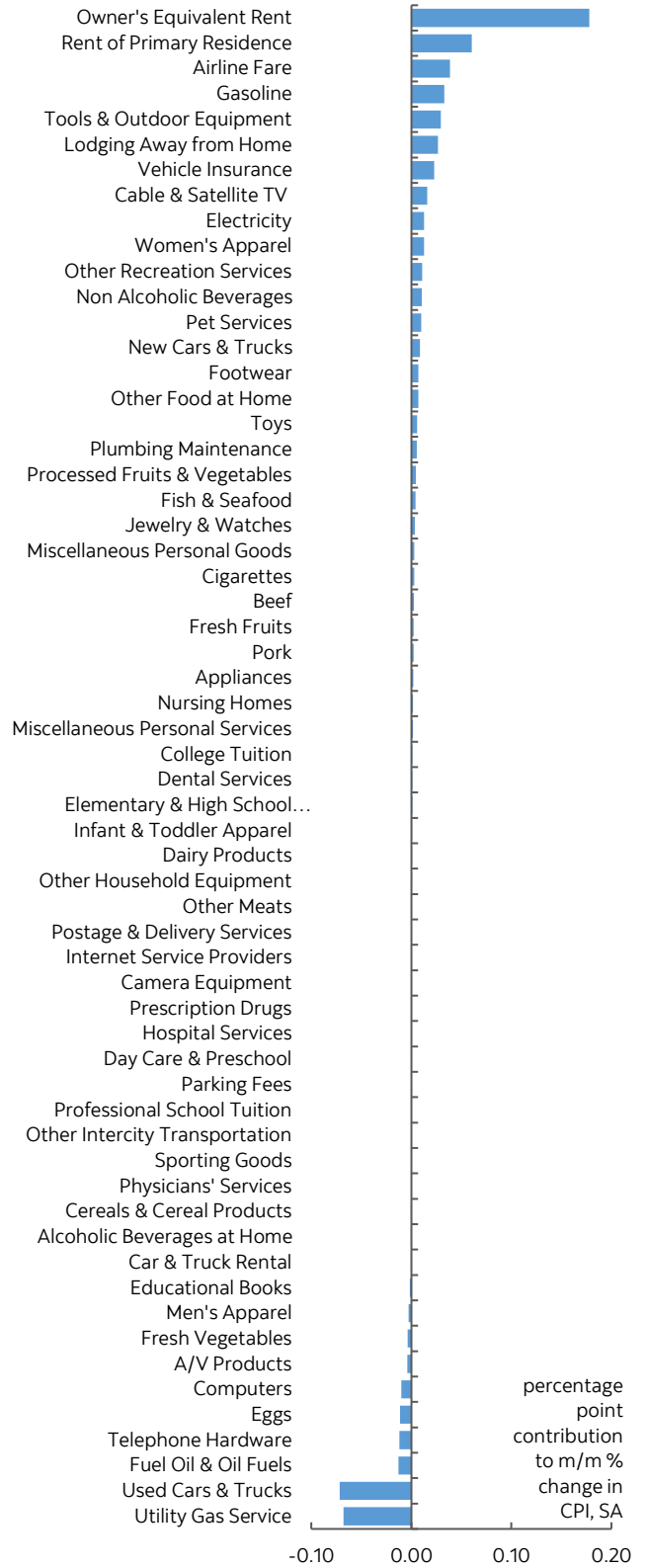
February Changes in US Headline CPI Categories



Sources: Scotiabank Economics, US BLS.

Chart 4

February Weighted Contributions to Monthly Change in US Headline CPI



Sources: Scotiabank Economics, US BLS.

Chart 5

February 12-Month Changes in US Headline CPI Categories

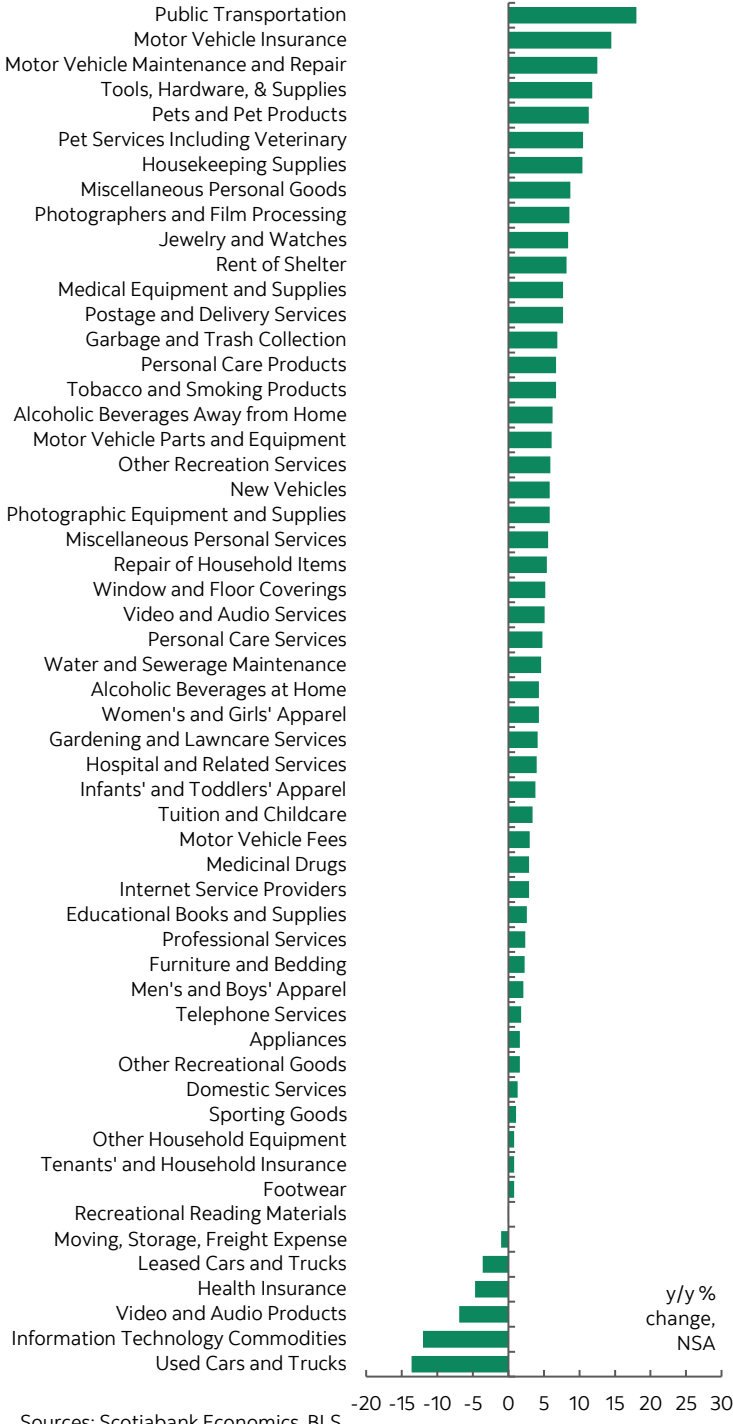
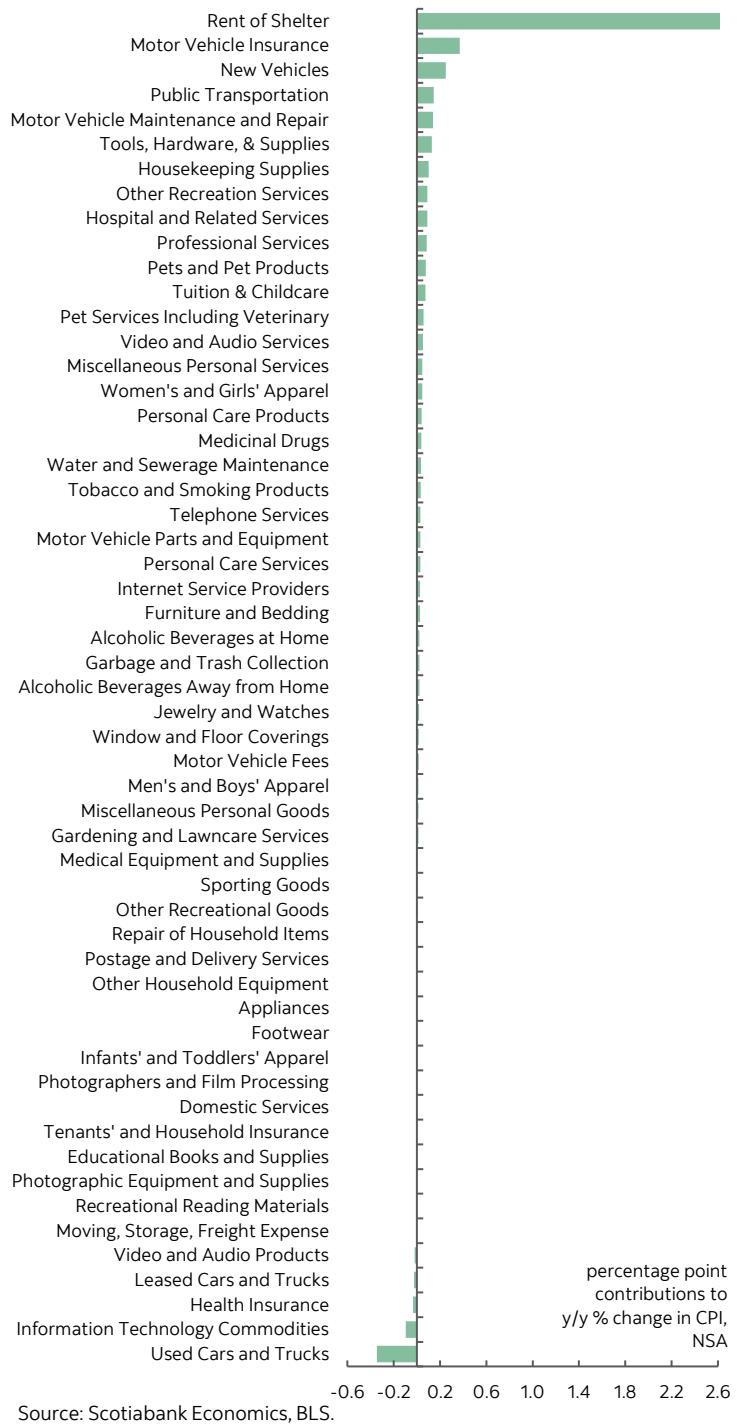


Chart 6

February Weighted Contributions to the 12-Month Change in US Headline CPI



This is the controversial measure that Powell emphasizes with his argument being that it is closely connected to wage growth. That's loosely true, but the way he speaks implies it's a leading relationship (ie: wage pressures driving this measure of inflation in future) when in reality it's more of a contemporaneous one.

The breadth of price pressures remains high. Chart 3 shows the breakdown of the CPI basket in y/y unweighted terms and chart 4 shows the weighted contributions to year-over-year inflation by component. Charts 5 and 6 do likewise for month-over-month inflation.

OER was up 0.7% m/m SA again as we're not yet at the point at which cooling pressure arises via market rents moving through shelter gauges (chart 7). That is likely in the second half of 2023 into 2024. It matters much less to the Fed's preferred PCE gauges that attached about half the weight to shelter compared to CPI's weight.

In terms of influences upon headline CPI, gasoline was up 1% m/m SA and at a 3¼% weight offered an immaterial effect. Food was up 0.4% m/m that with very generous rounding added under 0.1% m/m to CPI in weighted terms (chart 8). Grocery prices were up 0.3% m/m while food away from home (restaurants, take-out etc) was up 0.6%.

New vehicle prices were flat (+0.2%) and at a 4.3% weight had nothing to offer to CPI in m/m terms (chart 9). Used vehicle prices fell 2.8% m/m and when rounding up at a 2.6% weight added almost 0.1% to m/m CPI.

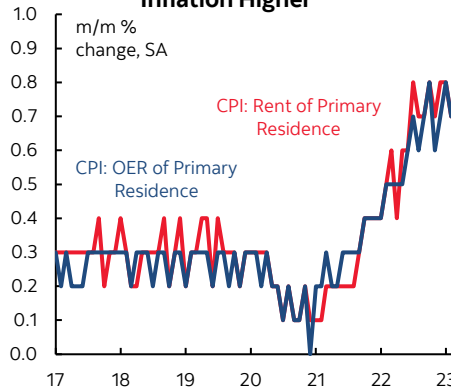
Airfare took off with a 6.4% m/m gain but the 0.57% weight kept the wheels on the ground in terms of weighted contributions (chart 10).

Other pandemic categories.... Vehicle rental prices slipped -0.5% but with no weighted effect. Lodging was up 2.3% m/m with very little effect at a 1.1% weight.

Please see the accompanying table for a further breakdown of the details along with micro charts and z-score measures of deviations compared to historical norms.

Chart 7

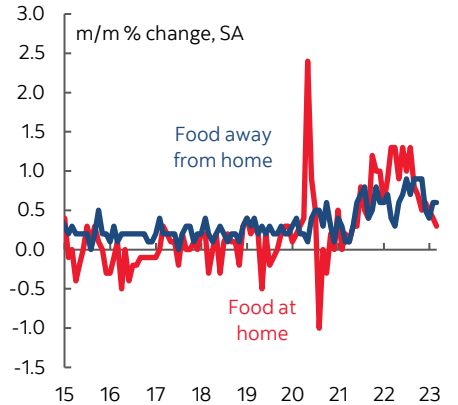
Housing Continues to Push Inflation Higher



Sources: Scotiabank Economics, BLS.

Chart 8

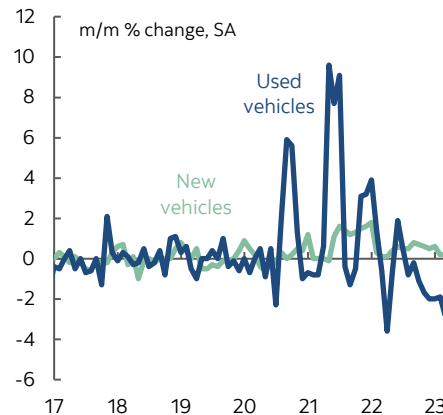
US Food Prices



Sources: Scotiabank Economics, BLS.

Chart 9

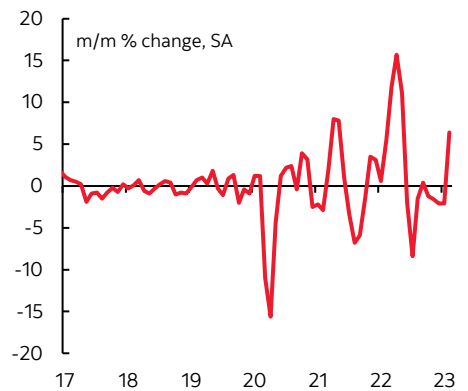
New vs Used Vehicle Inflation



Sources: Scotiabank Economics, BLS.

Chart 10

US Airfare



Sources: Scotiabank Economics, BLS.

March 14, 2023

Feb 2023				Weighted Contributions (pts)*			5-Year Pre-Pandemic			10-Year Pre-Pandemic			
US INFLATION COMPONENT BREAKDOWN	y/y % change	10-year trend	Pandemic trend (Jan 2019–Present)	m/m % change	Weights (%)	y/y	m/m	2015–2019 avg. y/y	Std. Dev.	Z-Score	2011–2019 avg. y/y	Std. Dev.	Z-Score
Food	9.5			0.4	13.52	1.28	0.05	1.3	0.8	10.8	1.7	1.1	6.8
Food, home	10.2			0.3	8.73	0.89	0.03	0.2	1.1	8.8	1.2	1.9	4.9
Cereals & bakery products	14.6			0.3	1.17	0.17	0.00	0.4	0.9	16.2	0.9	1.7	8.1
Meats, poultry, fish & eggs	6.8			-0.1	1.85	0.13	0.00	-0.2	3.2	2.2	2.1	3.9	1.2
Dairy & related products	12.3			0.1	0.81	0.10	0.00	-0.6	1.6	8.0	1.1	3.1	3.6
Fruits & vegetables	5.3			0.2	1.51	0.08	0.00	0.4	1.7	2.8	1.0	2.0	2.1
Non-alcoholic beverages	12.3			1.0	1.05	0.13	0.01	0.6	1.0	11.2	0.5	1.6	7.5
Other food at home	12.4			0.3	2.34	0.29	0.01	0.5	0.6	18.5	1.0	1.6	7.3
Food, away	8.4			0.6	4.80	0.40	0.03	2.7	0.3	19.2	2.5	0.5	11.3
Full services meals & snacks	8.0			0.6	2.30	0.18	0.01	2.6	0.4	14.7	2.4	0.5	11.2
Limited services meals and snacks	7.2			0.7	2.23	0.16	0.02	2.8	0.3	13.6	2.5	0.7	6.7
Food at employee sites and school	134.4			-0.2	0.08	0.10	0.00	2.8	2.4	53.8	2.8	1.9	68.6
Food from vending machines & mobile vendors	15.0			1.3	0.03	0.00	0.00	3.1	1.0	12.0	2.5	1.3	9.6
Other food away from home	5.7			0.6	0.17	0.01	0.00	2.5	1.3	2.4	2.3	1.0	3.4
Energy	5.2			-0.6	7.08	0.37	-0.04	-1.9	10.0	0.7	1.6	9.6	0.4
Energy comm.	-1.4			0.5	3.56	-0.05	0.02	-2.8	17.0	0.1	3.0	17.1	-0.3
Fuel oils & other fuels	5.7			-6.4	0.21	0.01	-0.01	-2.3	15.8	0.5	2.7	14.4	0.2
Motor fuel	-1.7			0.9	3.34	-0.06	0.03	-2.8	17.1	0.1	3.0	17.3	-0.3
<u>Gasoline</u>	<u>-2.0</u>			<u>1</u>	<u>3.25</u>	<u>-0.06</u>	<u>0.03</u>	<u>-2.8</u>	<u>17.1</u>	<u>0.0</u>	<u>3.0</u>	<u>17.4</u>	<u>-0.3</u>
<u>Other</u>	<u>16.5</u>			<u>-2</u>	<u>0.10</u>	<u>0.02</u>	<u>0.00</u>	<u>-2.3</u>	<u>19.5</u>	<u>1.0</u>	<u>3.6</u>	<u>17.9</u>	<u>0.7</u>
Energy serv.	13.3			-1.7	3.52	0.47	-0.06	0.0	2.4	5.4	0.5	2.7	4.8
Electricity	12.9			0.5	2.58	0.33	0.01	0.5	1.5	8.4	1.0	1.7	7.1
Utility (piped gas service)	14.3			-8.0	0.94	0.13	-0.08	-1.4	7.5	2.1	-0.9	7.3	2.1
All items less food and energy	5.5			0.5	79.40	4.37	0.40	2.0	0.2	15.5	1.8	0.4	9.0
Commodities less food and energy	1.0			0.0	21.33	0.21	0.00	-0.3	0.4	3.4	0.2	0.9	0.9
Household furnishings	6.3			0.8	3.77	0.24	0.03	-0.8	1.2	5.9	-0.9	1.2	6.0
Window & floor coverings	5.2			-1.3	0.32	0.02	0.00	-2.3	1.7	4.4	-2.8	1.8	4.5
Furniture & bedding	2.3			0.2	1.18	0.03	0.00	-0.3	1.7	1.5	-0.9	2.1	1.5
Appliances	1.6			0.7	0.29	0.00	0.00	-1.2	3.1	0.9	-1.6	3.0	1.0
Other household equipment	0.8			1.6	0.58	0.00	0.01	-3.5	1.8	2.3	-3.7	1.5	3.0
Tools & hardware	11.8			2.7	1.07	0.13	0.03	-0.1	1.0	11.5	-0.3	1.2	9.9
Housekeeping supplies	10.4			0.5	0.97	0.10	0.00	0.3	1.2	8.5	0.4	1.3	7.6

March 14, 2023

Feb 2023				Weighted Contributions (ppts)*			5-Year Pre-Pandemic			10-Year Pre-Pandemic			
US INFLATION COMPONENT BREAKDOWN	y/y % change	10-year trend	Pandemic trend (Jan 2019–Present)	m/m % change	Weights (%)	y/y	m/m	2015–2019 avg. y/y	Std. Dev.	Z-Score	2011–2019 avg. y/y	Std. Dev.	Z-Score
Apparel	3.3			0.8	2.53	0.08	0.02	-0.5	1.0	3.9	0.3	1.7	1.7
Men's & boys apparel	2.1			-0.4	0.67	0.01	0.00	-0.3	1.5	1.6	0.5	2.3	0.7
Women's & girls apparel	4.3			1.2	1.02	0.04	0.01	-1.3	1.9	3.0	-0.1	2.5	1.7
Footwear	0.8			1.4	0.51	0.00	0.01	0.2	1.3	0.4	0.8	1.7	0.0
Infant & toddler's apparel	3.8			0.8	0.10	0.00	0.00	0.4	3.8	0.9	0.5	3.6	0.9
Jewelry & watches	8.4			1.5	0.23	0.02	0.00	1.0	3.4	2.2	1.5	3.8	1.8
Trans. less fuel	-3.2			-0.9	7.64	-0.24	-0.07	-0.3	0.9	-3.3	0.4	1.5	-2.4
New vehicles	5.8			0.2	4.30	0.25	0.01	0.1	0.7	8.7	0.8	1.2	4.1
Used cars & trucks	-13.6			-2.8	2.61	-0.35	-0.07	-1.3	2.1	-5.9	1.1	4.8	-3.0
Motor vehicle parts & equipment	6.1			-0.5	0.49	0.03	0.00	0.2	1.1	5.6	0.9	2.2	2.4
Medical comm.	3.2			0.1	1.46	0.05	0.00	2.1	1.7	0.6	2.3	1.5	0.6
Medicinal Drugs	2.9			0.1	1.35	0.04	0.00	2.2	1.8	0.4	2.3	1.6	0.4
Medical equipment & supplies	7.7			0.2	0.11	0.01	0.00	0.4	1.2	5.9	0.3	1.2	6.2
Recreation comm.	2.9			0.4	2.28	0.07	0.01	-2.6	1.1	5.2	-2.3	0.9	5.7
Video & audio products	-6.9			-1.4	0.29	-0.02	0.00	-10.1	2.4	1.3	-9.2	2.2	1.1
Pets & pet products	11.3			1.1	0.67	0.08	0.01	0.4	1.5	7.4	0.5	1.5	7.4
Sporting goods	1.1			0.2	0.76	0.01	0.00	-0.7	1.5	1.2	-0.6	1.2	1.4
Photographic Equipment & supplies	5.8			0.2	0.02	0.00	0.00	-1.7	4.6	1.6	-3.0	4.0	2.2
Recreational reading materials	-0.1			0.3	0.11	0.00	0.00	1.6	1.9	-0.9	1.5	1.8	-0.9
Other recreational goods	1.6			1.2	0.44	0.01	0.01	-6.5	1.3	6.1	-5.2	1.7	3.9
Educ. & communication comm.	-10.5			-0.8	0.92	-0.10	-0.01	-3.7	1.0	-6.7	-3.5	0.9	-7.7
Educational books & supplies	2.6			0.0	0.10	0.00	0.00	2.2	3.0	0.1	3.6	2.7	-0.4
IT commodities	-12.0			-0.9	0.83	-0.10	-0.01	-6.1	1.9	-3.1	-6.8	1.8	-2.9
Alcohol	4.9			-0.3	0.84	0.04	0.00	1.3	0.3	10.5	1.4	0.4	9.6
Alcoholic beverages at home	4.3			-0.1	0.51	0.02	0.00	0.8	0.6	5.8	0.8	0.5	6.6
Alcoholic beverages away from home	6.2			-0.3	0.33	0.02	0.00	1.9	0.5	9.3	2.2	0.7	6.0
Other goods	7.0			0.7	1.24	0.09	0.01	1.4	0.9	6.6	1.4	0.7	7.8
Tobacco & smoking products	6.7			1.0	0.49	0.03	0.00	4.3	1.5	1.6	4.4	3.8	0.6
Personal care products	6.7			0.5	0.60	0.04	0.00	-0.3	0.6	12.0	-0.1	0.8	8.2
Miscellaneous personal goods	8.7			0.8	0.15	0.01	0.00	-2.4	3.1	3.6	-1.7	2.4	4.3

March 14, 2023

Feb 2023				Weighted Contributions (ppts)*			5-Year Pre-Pandemic			10-Year Pre-Pandemic			
US INFLATION COMPONENT BREAKDOWN	y/y % change	10-year trend	Pandemic trend (Jan 2019–Present)	m/m % change	Weights (%)	y/y	m/m	2015–2019 avg. y/y	Std. Dev.	Z-Score	2011–2019 avg. y/y	Std. Dev.	Z-Score
Services less energy services	7.3			0.6	58.08	4.24	0.35	2.8	0.2	19.3	2.4	0.6	7.8
Shelter	8.1			0.8	34.39	2.79	0.28	3.3	0.2	28.6	2.5	1.2	4.8
Rent of shelter	8.2			0.7	34.02	2.79	0.24	3.3	0.2	26.6	2.5	1.2	4.8
<i>Rent of primary residence</i>	<u>8.8</u>			<u>0.8</u>	<u>7.52</u>	<u>0.66</u>	<u>0.06</u>	<u>3.7</u>	<u>0.1</u>	<u>38.3</u>	<u>2.9</u>	<u>1.1</u>	<u>5.3</u>
<i>Lodging away from home</i>	<u>6.7</u>			<u>2.3</u>	<u>1.11</u>	<u>0.07</u>	<u>0.03</u>	<u>2.3</u>	<u>2.0</u>	<u>2.2</u>	<u>2.2</u>	<u>2.2</u>	<u>2.1</u>
<i>OER of residences</i>	<u>8.0</u>			<u>0.7</u>	<u>25.39</u>	<u>2.03</u>	<u>0.18</u>	<u>3.2</u>	<u>0.2</u>	<u>23.6</u>	<u>2.4</u>	<u>1.1</u>	<u>5.2</u>
Tenants' & household insurance	0.8			-0.1	0.37	0.00	0.00	1.4	1.2	-0.5	2.3	1.5	-1.0
Water, sewer, trash collection	5.2			0.8	1.06	0.06	0.01	3.6	0.6	2.8	4.3	1.0	0.9
Water & sewage maintenance	4.6			0.7	0.76	0.03	0.01	4.0	0.8	0.8	4.8	1.4	-0.2
Garbage & trash collection	6.9			0.9	0.30	0.02	0.00	2.5	1.5	3.0	2.5	1.1	4.1
Household ops.	6.6			0.1	0.83	0.05	0.00	3.8	1.3	2.2	2.6	1.6	2.5
Domestic services	1.3			-1.3	0.26	0.00	0.00	2.0	1.1	-0.6	1.6	1.0	-0.3
Gardening & lawn care	4.1			0.2	0.32	0.01	0.00	4.3	2.7	-0.1	2.8	2.6	0.5
Moving, storage, freight	-1.0			-3.2	0.11	0.00	0.00	5.6	3.9	-1.7	3.3	3.9	-1.1
Repair of household items	5.4			0.1	0.11	0.01	0.00	4.8	2.1	0.3	4.2	2.0	0.6
Medical serv.	2.1			-0.7	6.59	0.14	-0.05	2.9	1.0	-0.8	3.0	0.8	-1.1
Professional Services	2.4			-0.3	3.59	0.09	-0.01	1.5	0.9	1.0	1.8	0.8	0.7
Hospital & related services	4.0			0.1	2.27	0.09	0.00	3.8	1.1	0.2	4.5	1.3	-0.4
Health insurance	-4.7			-4.1	0.74	-0.03	-0.03	5.0	5.8	-1.7	3.6	6.0	-1.4
Transportation serv.	14.6			1.1	5.75	0.84	0.06	2.6	1.1	10.9	2.6	1.0	12.4
Leased cars & trucks	-3.6			1.0	0.73	-0.03	0.01	0.5	3.0	-1.4	-1.6	3.2	-0.6
Motor vehicle maintenance & repair	12.5			0.2	1.11	0.14	0.00	2.2	0.7	14.7	2.0	0.6	18.3
Motor vehicle insurance	14.5			0.9	2.53	0.37	0.02	5.5	2.6	3.4	4.8	2.0	4.7
Motor vehicle fees	3.0			0.4	0.50	0.01	0.00	1.8	0.7	1.7	2.2	1.9	0.4
Public transportation	18.0			3.2	0.77	0.14	0.02	-1.2	1.5	12.7	1.0	3.6	4.8
Recreation serv.	6.3			1.2	3.09	0.19	0.04	2.6	0.7	5.6	2.3	0.7	5.3
Video & audio services	5.1			1.6	0.98	0.05	0.02	2.7	1.4	1.7	2.6	1.3	1.8
Pet services	10.5			1.8	0.54	0.06	0.01	3.1	0.8	9.6	3.3	0.9	7.8
Photo services	8.6			1.2	0.04	0.00	0.00	-0.2	2.0	4.4	0.8	1.8	4.2
Other recreation services	5.9			0.7	1.53	0.09	0.01	2.4	0.6	5.8	1.7	1.1	3.9
Educ. & communication serv.	2.9			0.2	4.89	0.14	0.01	0.4	1.3	1.9	1.1	1.3	1.5
Tuition, school fees, child care	3.4			0.1	2.16	0.07	0.00	2.8	0.6	1.1	3.3	0.8	0.1
Postage & delivery	7.7			0.2	0.07	0.01	0.00	2.3	2.0	2.8	3.3	2.0	2.3
Telephone services	1.8			0.0	1.68	0.03	0.00	-2.4	3.0	1.4	-1.3	2.4	1.3
Internet services	2.9			0.9	0.97	0.03	0.01	-0.2	1.5	2.1	0.1	1.3	2.1
Other personal serv.	5.2			1.1	1.43	0.07	0.02	2.7	0.7	3.7	2.4	0.6	4.4
Personal care services	4.8			0.6	0.60	0.03	0.00	2.3	0.7	3.6	1.8	0.8	3.6
Miscellaneous personal services	5.6			1.4	0.83	0.05	0.01	2.9	0.9	2.9	2.7	0.7	4.0

*Number may not add due to rounding

Sources: Scotiabank Economics, BLS.

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