U.S. Data Review

- CPI: energy prices continue to boost the headline as conflict in the Middle East remains largely unresolved; core inflation comes in below consensus

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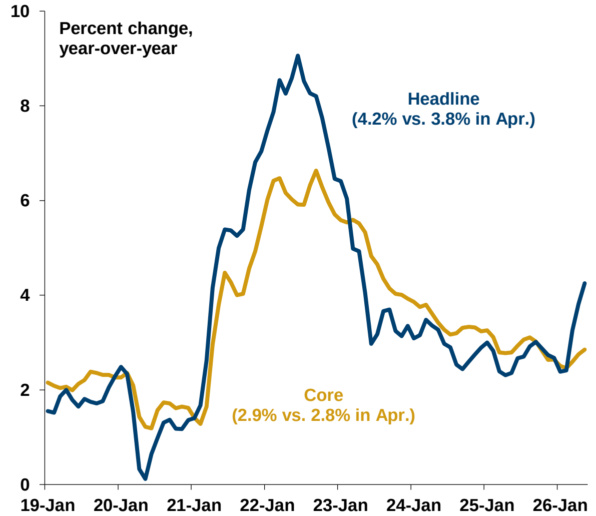
May CPI

- In line with market expectations, the headline CPI rose 0.5 percent in May, its third consecutive month-to-month increase at that pace or higher. Concurrently, the core index rose 0.2 percent – 0.1 percentage point below the median expectation from the Bloomberg economist survey. Those shifts equated to year-over-year advances of 4.2 percent for the headline (+4.249 percent, with less rounding, up from +3.811 percent in the prior month and the fastest increase since April 2023) and 2.9 percent for the core (+2.851 percent, up from +2.750 percent in April and the firmest advance since September 2025; chart, below left). Similar to recent reports, the war-driven oil shock contributed in no small part to the jump in the all-items index, with Bureau of Labor Statistics noting that the energy component accounted for over 60 percent of the May increase. However, on a more positive note, cost passthrough from tariffs to consumer prices is perhaps beginning to fade, evidenced by the one-month drop seen in core goods inflation (see below).

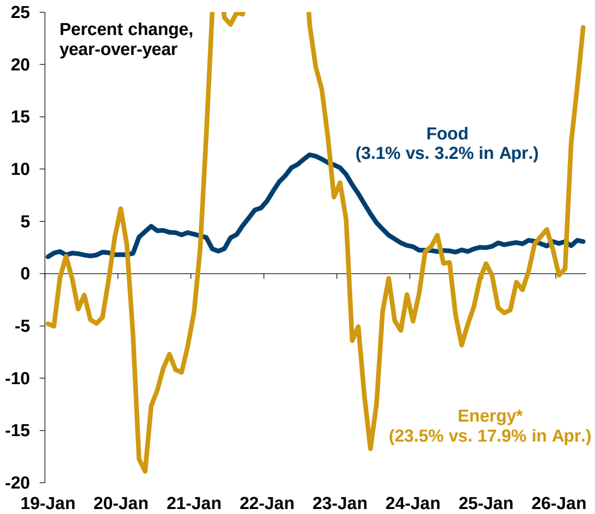
- As previously mentioned, ongoing conflict with Iran and related disruptions in the Strait of Hormuz were again felt in the energy component, with this area jumping 3.9 percent in May (+23.5 percent year-over-year, the sharpest advance since August 2022). Factoring into the firming, costs of energy commodities surged 6.7 percent (+40.6 percent year-over-year versus +29.2 percent in April), influenced primarily by the monthly jump of 7.0 percent in gasoline prices. Meanwhile, following a 1.6 percent advance in the prior month, costs for energy services rose a more subdued 0.4 percent (+5.3 percent year-over-year versus +5.4 percent previously). Additionally, the food category posted a 0.2 percent increase after an upside read of +0.5 percent in April (+3.1 percent year-over-year versus +3.2 percent in the prior month; chart, below right). Costs of food at home rounded up to an advance of 0.1 percent (+2.7 percent year-over-year versus +2.9 percent in April), with increases in the indexes for nonalcoholic beverages and beverage materials, cereals and bakery products, and fruits and vegetables acting as drivers for higher prices. At the same time, costs for food away from home (i.e., restaurant meals) rose 0.3 percent (not seasonally adjusted; +3.5 percent year-over-year versus +3.6 percent in April).

CPI: Headline & Core



Source: Bureau of Labor Statistics via Haver Analytics

CPI: Food & Energy

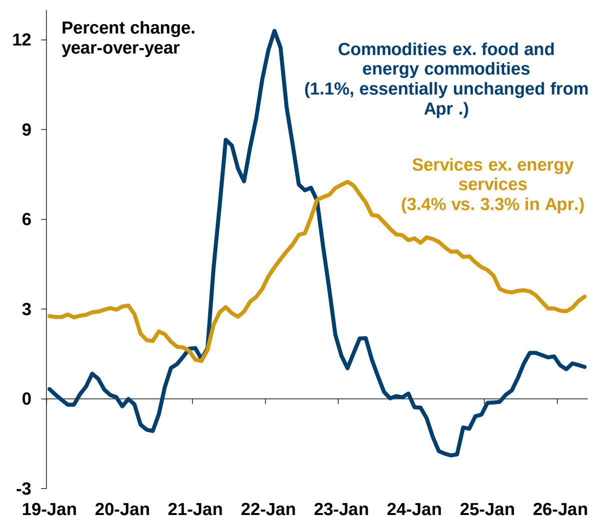


** COVID-related extremes truncated*
Source: Bureau of Labor Statistics via Haver Analytics

- Stripping away the volatile food and energy categories, the core index increased 0.208 percent in May, decelerating from the 0.376 percent advance in the prior month (which was the firmest one-month shift since January 2025). Turning to the internals, the core goods index eased 0.114 percent, its first monthly decline since May 2025 and the softest read since August 2024 (+1.1 percent year-over-year, essentially unchanged from April; chart, below left). Contributing to the latest softening, household furnishings and supplies eased 0.2 percent (its third consecutive monthly decrease; -0.5 percentage point to +2.4 percent year-over-year) and new vehicles declined 0.3 percent (+0.2 percent year-over-year, essentially unchanged from April). Conversely, tobacco prices jumped 1.0 percent (+0.2 percentage point to +7.8 percent year-over-year) and apparel costs rose 0.3 percent (+0.6 percentage point to +4.8 percent year-over-year). Thus, even amid pockets of residual pressure, effects of previously-enacted tariffs appear to be fading -- a view aligned with what former Fed Chair Powell expounded upon in his final post-FOMC press conference in April.

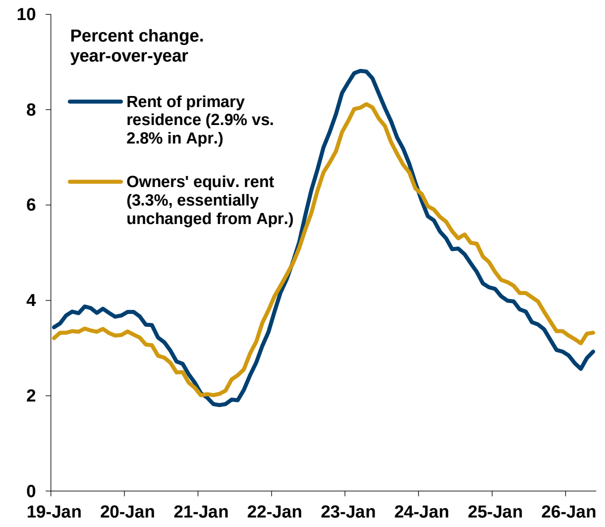
- Although moderating from a brisk advance of 0.500 percent in the prior month, May's increase of 0.295 percent for the core services area still contributed to a year-over-year acceleration (+0.1 percentage point to +3.4 percent). Standing out on the firm side was the 2.7 percent surge in airfares, an ongoing source of pressure since late 2025 that has been exacerbated by firms grappling with higher fuel costs since the inception of the war (+26.7 percent year-over-year, up from +20.7 percent in April). Moreover, following a 0.5 percent jump in the prior month, rent of primary residence advanced 0.4 percent in May (+0.1 percentage point to +2.9 percent year-over-year). Owners' equivalent rent, meanwhile, registered a 0.3 percent gain in May after a 0.5 percent increase previously (+3.3 percent year-over-year, essentially unchanged from April; chart, below right). Recall, last month's jump in the shelter area was primarily due to a one-off technical adjustment after last year's government shutdown disrupted data collection. Nonetheless, the year-over-year trends for both components remain squarely in line with pre-pandemic norms – which were broadly consistent with the 2 percent inflation target. Moreover, we view real-time measures of rents as suggestive of a resumption in cooling for the shelter components in the months ahead.

CPI: Core Goods & Core Services



Source: Bureau of Labor Statistics via Haver Analytics

CPI: Housing



Source: Bureau of Labor Statistics via Haver Analytics

- Broadly speaking, while results from the latest CPI report came in a touch softer than consensus expectations, underlying inflation still remains well above the FOMC's 2 percent inflation objective, which will seemingly keep policymakers squarely on the sideline for at least the next several meetings (with a hold at next week's gathering viewed as a near certainty). That being said, we suspect that an additional cut or two at the margin is more likely than renewed hikes later this year and into 2027 – especially as higher prices erode household spending and an uncertain outlook potentially generates a pickup in layoffs. However, with the war's ultimate impact on the economy and interest rates remaining highly uncertain, policymakers will endeavor to be nimble in their approach – especially as a new Fed Chair presides over his first FOMC meeting next week.