Seeking Alpha

Inflation Trends Are Embedded, Increasing Stagflation Odds

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Mott Capital Management
Investing Group Leader

Summary

CPI and Core CPI rose as expected, indicating trends consistent with high inflation rates.

Retail sales were disappointing and stagnant, suggesting a potential stagflation-like environment.

The economy may be experiencing a stagnating or stagflationary period, with unclear implications for the future.

I am Mott Capital, aka Michael Kramer, a former buy-side trader and portfolio manager with 30 years of experience. I lead Reading The Markets, an investing group designed to help you position your portfolio to benefit from macro trends and thematic growth opportunities.

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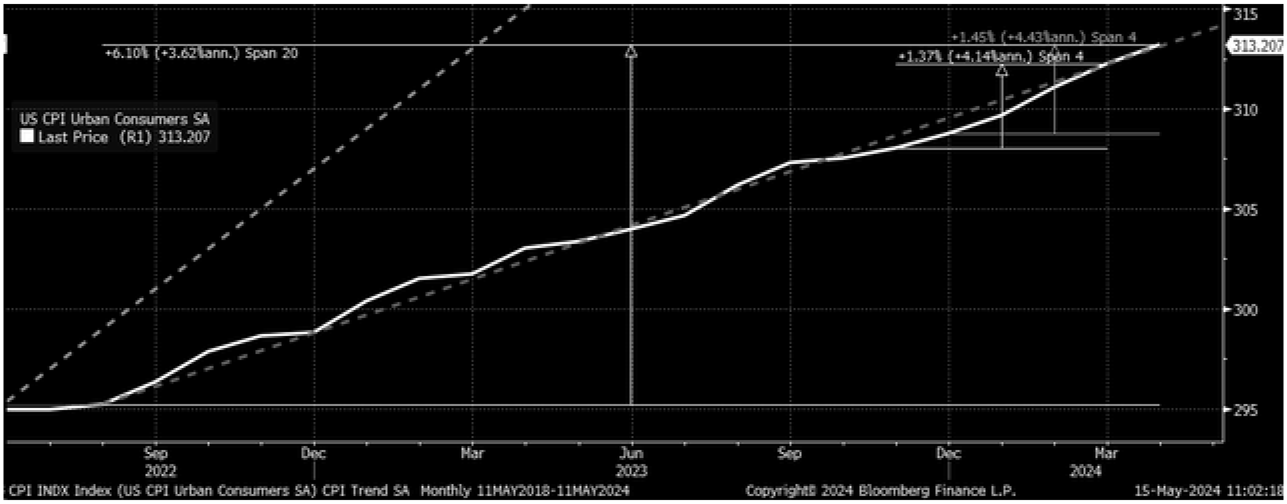
The CPI report came in as expected, rising by 3.6% year-over-year on the core and 3.4% on the headline. Core CPI also rose by 0.3% m/m in line with expectations, while CPI m/m came in at 0.3% vs. 0.4%. The data continues to point to the same trends we saw before the release of the data.

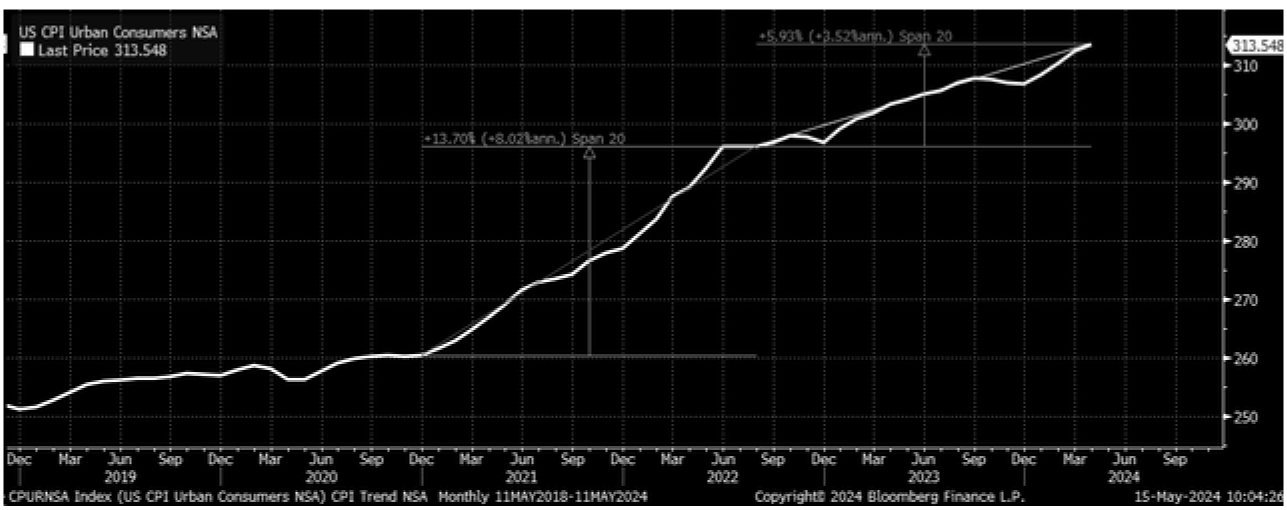
Trends Are Crystal Clear

Currently, the CPI and Core CPI are not running at trends consistent with a 2% inflation rate, and today's data did little, if anything, to change that. It may have confirmed those trends, since both data points appeared to be pretty close to their respective trend lines.



Bloomberg

The CPI, on a seasonally adjusted basis, has been running at an annualized growth rate of 3.6% over the past 20 months, and today's result came in right on trend. Additionally, the CPI has risen at a 4.4% annualized growth rate over the last four months. Even when looking at the CPI on a non-seasonally adjusted basis, it has been rising at an annualized growth rate of 3.5% over the past 20 months and also came in right on trend.



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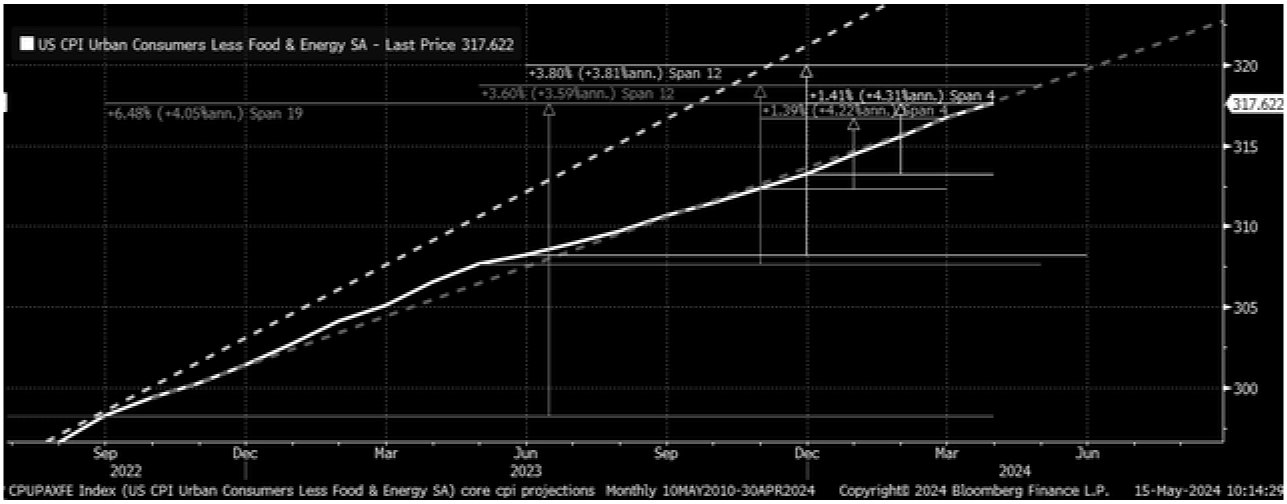
Core CPI seasonally adjusted also came in on trend in April and has now risen at an annualized growth rate of 4.0% over the past 19 months. If the current trend continues, we will likely see the core CPI values start rising again and moving back to a y/y rate of change at around 4% once we get past the May inflation report.



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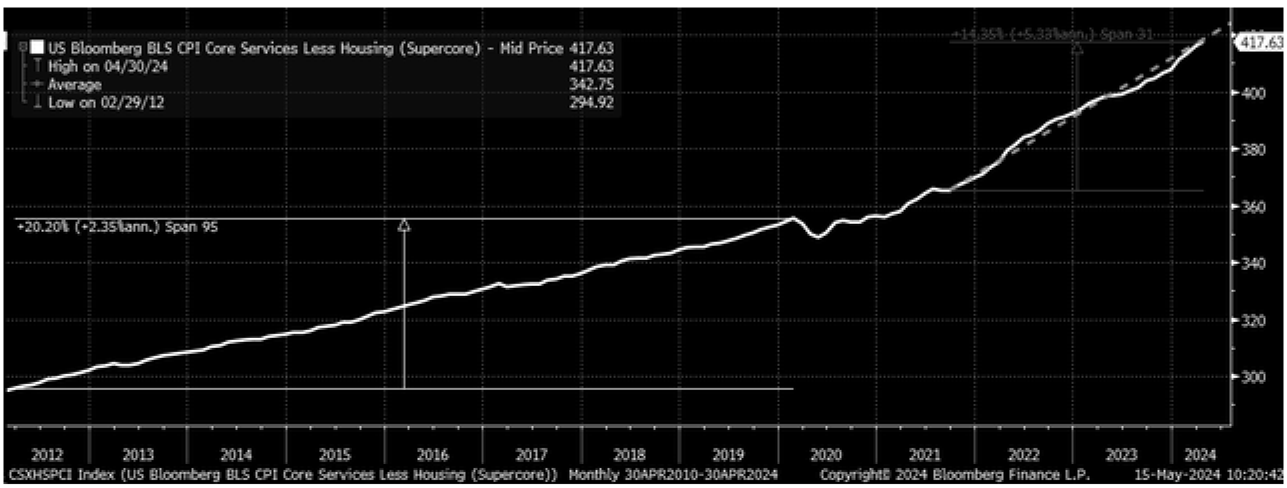
Meanwhile, super core less housing has also been running at a 5.3% annualized growth rate for the past 31 months and appears to be on trend as well, just following the previous path.



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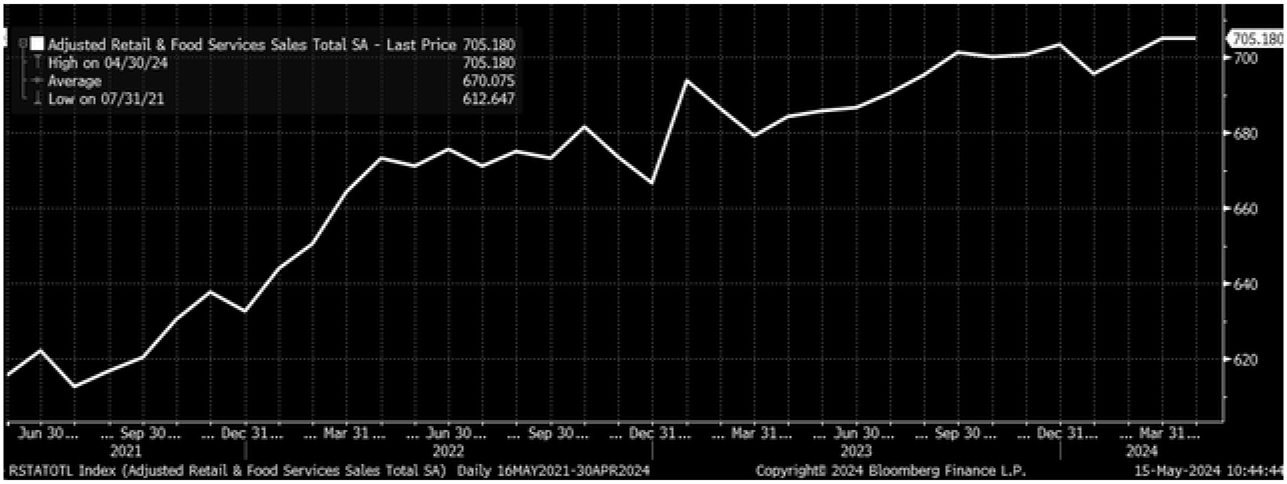
Of course, the trends can change, and if monetary policy is really restrictive, the trends should shift to a lower slope over time. Now, the last time the Fed raised rates was in July 2023, and one would think that if the path doesn't change soon, the current path suggests that policy is not yet having the desired effect, at least on inflation, and may not be tight enough to actually alter the path.

How long a trend must persist before it's accepted as a problem or entrenched is unclear. However, a trend that continues for as long as these have already continued appears to be worth considering as a problem.

Retail Sales Have Stalled Out

Meanwhile, today's retail sales were disappointed, coming in flat versus expectations for a gain of 0.4%. Last month's figure was revised lower to 0.6% from 0.7%. The slower sales and the 3.5% trend inflation rates over many months again point to a stagflation-like environment developing in the economy. The seasonally adjusted retail sales index has flattened out since the fall of 2023.



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There appears to be a strange dynamic occurring across the economy with high service inflation and core and headline CPI stuck in an uptrend running in the 3.5% to 4% range while retail sales are stagnant.

Overall, the idea of a stagnating or stagflationary economy is becoming increasingly real, and how that will play out over time is anyone's guess. If you want to think that real disinflation is taking, that's fine, but the trends and the data show that clearly not the case.

This article was written by

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Mott Capital, aka Michael Kramer, is a former buy-side trader, analyst, and portfolio manager with 30 years of experience tracking market fundamentals. He focuses on long-only macro themes and studies trends and unusual options activities to identify long-term thematic growth opportunities.

He leads the investing group Reading The Markets where he helps members better understand what is driving trading and where the market is likely heading, both short and long-term. Features of the investing group include: daily written commentary and videos analyzing the driving factors behind price action, general macro trend education to help members make well-informed decisions based on market conditions, interest rates, currency movements and how they all interact, chat for questions and community dialogue, and regular Zoom videos sessions to discuss current ideas and answer questions. Learn more.