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## Macro Alert

# Inflation Is Spiking, But You Only Reopen the Economy Once

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Core CPI jumped to 3.0 percent year-over-year in April, the fastest pace since 1996. While the base effect from low readings in April 2020 was widely expected by markets, the monthly pace of inflation also rose notably. Core CPI increased 0.92 percent from March to April, the largest monthly gain since 1981.

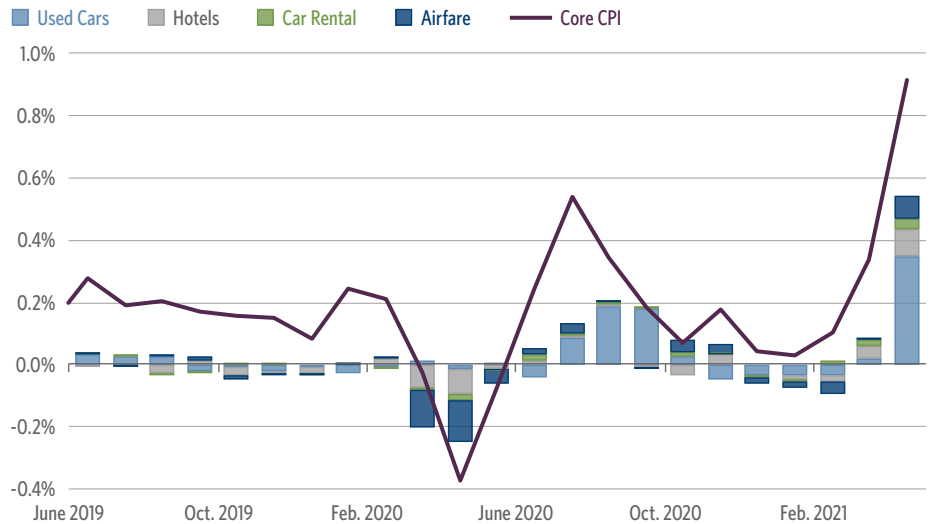
The market seems to think this may be the start of an enduring trend of higher inflation, given record fiscal stimulus, ultra-easy Federal Reserve (Fed) accommodation, and ongoing supply bottlenecks. But a closer look at the data suggests that this spike in prices is a one-time adjustment as the economy reopens.

Spooked bond investors pulled forward Fed rate hike expectations after the CPI release, despite the Fed repeatedly emphasizing that they view this reopening-induced rise in prices as transitory. Investors should believe the Fed when they say they will look through this temporary inflation noise and fade the bond selloff.

The month-to-month gains in the core CPI were largely driven by a few small categories related to economic reopening and temporary pandemic-induced shortages. 54 of the 92 basis point increase came from used cars, rental cars, airfares, and hotels, despite these categories having a weight of just 5 percent in the core CPI basket. The contribution was so large because the monthly price increases were so huge (e.g. 10 percent gain in used car prices). These increases are unlikely to be sustained beyond the next few months, especially once prices in depressed categories recover back to the pre-COVID trend.

### Small, Temporary Factors Boosted April CPI

Contribution to Monthly Percent Change in Core CPI

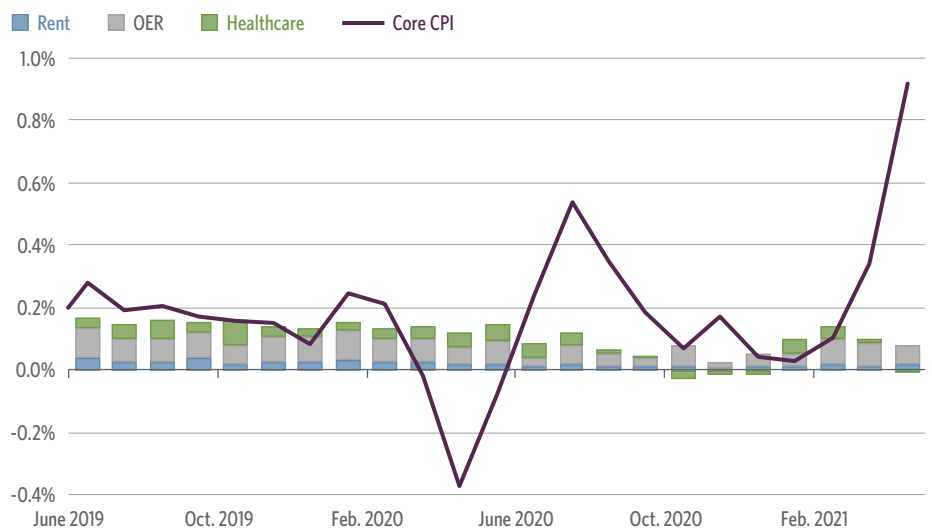


Source: Guggenheim Investments, Haver Analytics. Data as of 4.30.2021.

To the Fed, what matters is the trend in the larger, more durable inflation categories that influence the longer-term inflation outlook. In those categories, sequential inflation was much more muted: rents (including owners' equivalent rent) and healthcare services contributed just 8 basis points to the monthly gain, despite making up 49 percent of the core CPI index. The Fed is more focused on the chart below than the chart above—and the bond market should be too.

### Larger, More Durable Inflation Categories Remain Tame

Contribution to Monthly Percent Change in Core CPI



Source: Guggenheim Investments, Haver Analytics. Data as of 4.30.2021. OER is owner's equivalent rent.

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Basis point - One basis point is equal to 0.01 percent.

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