

May 4, 2023 10:00 PM GMT

US Economics | North America

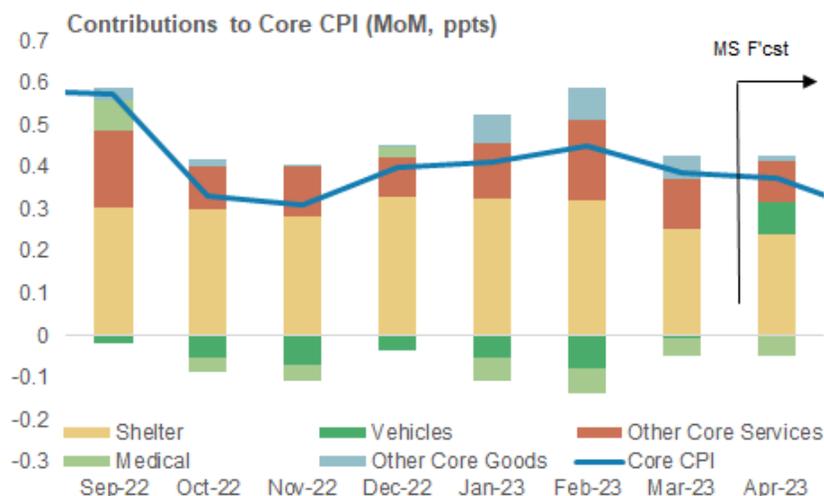
CPI Preview: Sideways in April

We expect monthly core inflation to move sideways in April. We see more deceleration in core services, coupled with a temporary pick-up in core goods. We forecast core CPI increased by 0.38%MoM (5.5%YoY), and headline by 0.46%MoM (5.1%YoY). We provide key components/risks to watch.

MORGAN STANLEY & CO. LLC

- Ellen Zentner**
CHIEF US ECONOMIST
Ellen.Zentner@morganstanley.com +1 212 296-4882
- Diego Anzoategui**
GLOBAL ECONOMIST
Diego.Anzoategui@morganstanley.com +1 212 761-8573
- Sarah A Wolfe**
ECONOMIST
Sarah.Wolfe@morganstanley.com +1 212 761-0857
- Lenoy Dujon**
US/CANADA ECONOMIST
Lenoy.Dujon@morganstanley.com +1 212 761-2779
- Ruth Cesar Heymann**
ECONOMIST
Ruth.Cesar.Heymann@morganstanley.com +1 212 761-0927

Exhibit 1: Core inflation to remain elevated on a pause in core goods deflation



Source: Bureau of Labor Statistics, Morgan Stanley Research forecasts

For important disclosures, refer to the Disclosure Section, located at the end of this report.

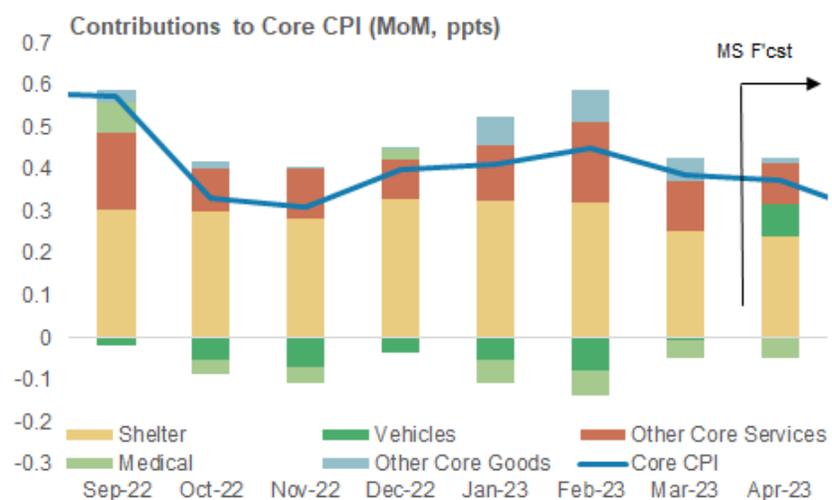
April CPI

Our estimates suggest core inflation experienced a short-lived pick-up in April, with no further acceleration beyond. We forecast core CPI increased by 0.38%M (vs. 0.3% cons), matching the March pace, while strong energy prices should lift headline CPI inflation (0.46% MSe vs 0.4% cons).

On a year-on-year basis, headline inflation is on track to rise to 5.1% after 5.0% in March due to base effects. Core inflation should see a small decrease to 5.5% YoY from 5.6% last month.

Goods prices accelerate, services prices slow down. Core goods prices are likely to tick up on the back of rising vehicle prices. We also expect airline fares to remain strong and shelter to reaccelerate following a weak print in March. However, gradual slowing in hotels and in other core services should help to offset strength in services elsewhere ([Exhibit 2](#)).

Exhibit 2: Core inflation to remain elevated on a pause in core goods deflation



Source: BLS, Morgan Stanley Research forecasts

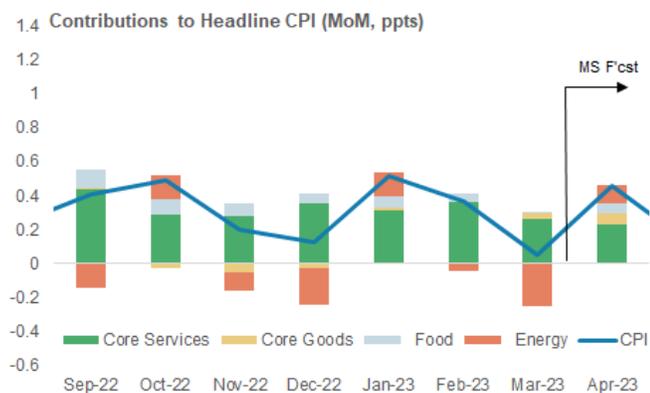
Core goods prices increased, on top of an up-tick last month. Vehicle prices play a key role in our forecast of strong deflationary pressures from the goods side throughout the year. After six months of sharp and larger-than-expected declines, and a higher but still negative March print, **our leading indicators point toward a more notable acceleration in April.** Our preliminary forecast points to a rebound in used car prices, coming in at 1.54%M after -0.88%M last month. We will update our forecast after the Manheim Index for the full month is released on Friday. Meanwhile, new car prices should also see a slight increase before turning marginally negative in the second half of the year. **News around price cuts from some of the major auto manufacturers further increases the probability of new car prices falling into deflation, but we expect a sharper decrease in prices for used cars throughout the year as the relationship between used and car prices normalizes** (see [here](#) for an analysis between used and new car prices). On the back of higher prices in the auto categories, core goods prices

overall should tick up this month, though broader deflation should set in across goods categories in coming months as weaker demand in our outlook takes its toll. Excluding autos, we see core goods inflation about flat at 0.04%M in April after three months of 0.3-0.4%M prints.

Despite a re-acceleration in housing inflation, core services inflation should slow at the margin again. After housing fell 23bp in March to 0.49%M, we are expecting a correction in April bringing housing back up to 0.58%M. This is due to the March report showing a significantly larger drop than the persistence in housing CPI indicates. This pickup in housing inflation should partly be counteracted by lower hotel prices after 4 prints above 1.0%M. Medical inflation should again be a major drag on core services inflation in April. On the back of a reset of health insurance inflation in October, **the medical component has been and will continue to be deflationary through September of this year.** Travel-related prices should remain elevated through April but not to the magnitude we saw in 2022. Surging jet fuel costs, pent-up demand, and low airline capacity drove airfare prices up by 15.7%M in April 2022. Though we expect prices will remain higher than pre-pandemic levels this spring, airline capacity improvements will keep airfare growth below last year's peak. **Relative to very strong February and March prints, sequential inflation should slow in airfares.**

With medical price deflation continuing and strong but decelerating travel inflation, **the core services ex-housing aggregate, a key focus of Fed Chair Powell, should moderate to 0.16%M after coming in at 0.40%M prior.** However, note that the Fed is mostly concerned with the PCE price index, which uses a different calculation for medical services that is not affected by the health insurance reset. **We currently track core services ex-housing PCE inflation at 0.24%M in April (vs 0.24%M in March).**

Exhibit 3: High energy prices will help drive the acceleration in headline inflation



Source: BLS, Morgan Stanley Research forecasts

Exhibit 4: Turnaround in core goods to be offset by somewhat softer core services

CPI %MoM	Jan-23	Feb-23	Mar-23	Apr-23 Fcst
Headline	0.52	0.37	0.05	0.46
Core	0.41	0.45	0.38	0.38
Energy	1.97	-0.56	-3.52	1.46
Food	0.51	0.39	0.01	0.44
Core Goods	0.07	-0.01	0.18	0.32
New Vehicles	0.23	0.18	0.38	0.57
Used Vehicles	-1.94	-2.77	-0.88	1.44
Apparel	0.83	0.81	0.26	0.20
Core Services	0.55	0.62	0.45	0.40
OER	0.67	0.70	0.48	0.57
Rent	0.74	0.76	0.49	0.58
Hotels	1.20	2.26	2.70	0.13
Medical Services	-0.68	-0.70	-0.50	-0.60
Airfare	-2.15	6.38	3.96	1.90
Core services ex-housing	0.36	0.50	0.40	0.16

Source: BLS, Morgan Stanley Research forecasts

Key Components in the April CPI

An increase in energy prices and some further acceleration in food inflation appear likely to weigh on headline CPI inflation, while core CPI faces cross-currents. Despite stronger headline and sticky core, underlying services details show material deceleration, which would still give the Fed something to hang onto for its inflation/policy narrative (Exhibit 3). Core services ex housing runs at 0.16% on the

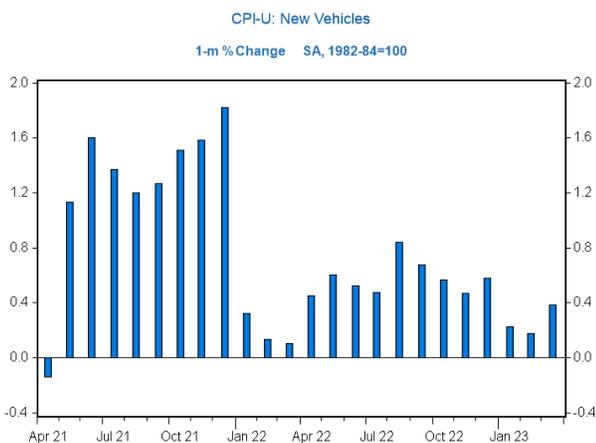
month, which would be the lowest print for the category over the last 9 months (Exhibit 4).

1. Autos:

New car prices decelerated in January and February but ticked back up in March (Exhibit 5). We see April new car prices continuing to accelerate as supply and inventories remain low at the same time that MoM sales came in above expectations. The April seasonal should help balance the acceleration of new car prices.

Used cars may see continued upward pressure as well – while the Manheim used car value index was down MoM in April, most of that decrease was due to seasonal adjustment (and Manheim uses different seasonal adjustment than the BLS for CPI), whereas unadjusted used car prices in Manheim were up MoM and other indicators, such as Black Book prices, are pointing to continued upside (Exhibit 6).

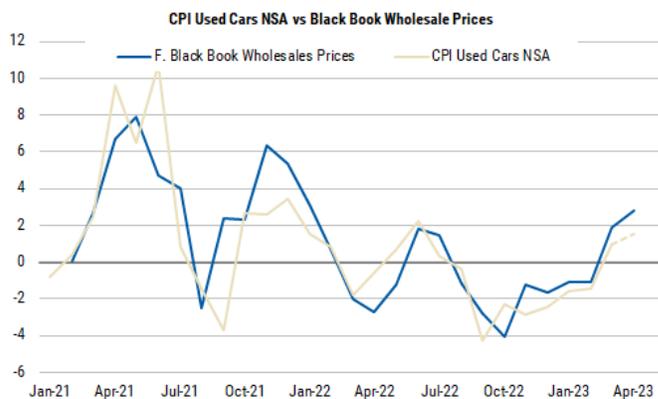
Exhibit 5: New Cars Came Up Last Month After Decelerating Prior



Source: BLS/Haver/Morgan Stanley Research

Source: Black Book, Morgan Stanley Research

Exhibit 6: Black Book Prices Indicate an Upside Risk to Used Cars in April

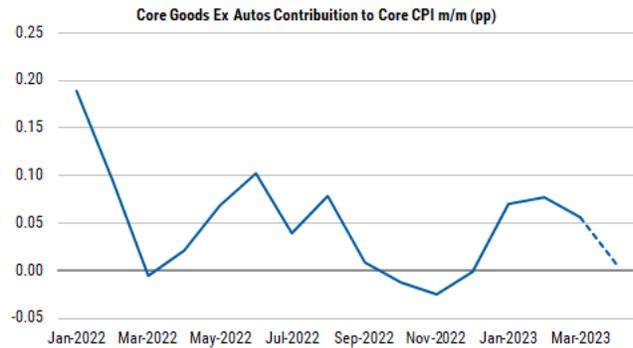


Source: BLS, Morgan Stanley Research Forecasts

2. Goods ex Autos:

Core goods prices ex autos have come very strong in the last three months (Exhibit 7). Upside in prices for alcohol, tobacco, apparel, and home furnishings helped keep core goods prices ex autos elevated. There is scope for more broadly based softening in some of these components – particularly apparel and home furnishings – in April, the declaration is also supported by the seasonal factors that will likely push to more significant downside.

Exhibit 7: Core Goods Ex Autos Risks to the Downside After Three Strong Prints



Source: BLS, Morgan Stanley Research forecasts

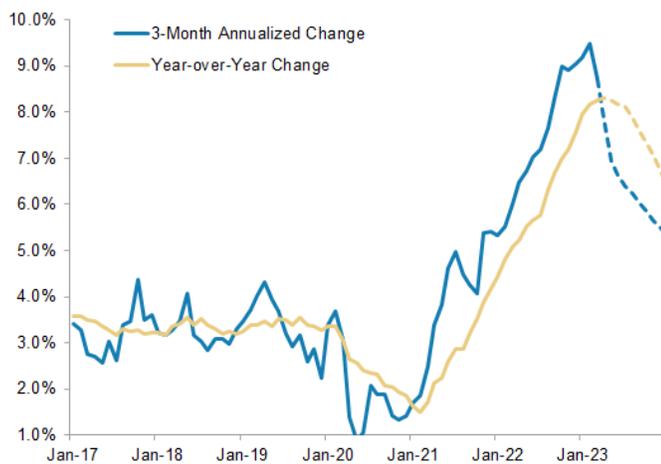
3. Rent & OER :

Rent and Owners' Equivalent Rent inflation dropped in March after months of very sticky prints. Given the higher-than-expected drop last month, we expect upside risk from a correction, bringing OER and rent back up to the 0.6%M territory (Exhibit 8).

Hotels should slightly help offset the pick up in Shelter coming from OER and rent. After seeing 4 months of over 1.0%M growth, we expect hotels to come back down as revenue per available room, the average daily rate and occupancy rate all saw significant declines in April (Exhibit 9).

Exhibit 8: CPI Shelter Saw a 16bp Decrease in March. Expect a Higher Print in April

CPI Rent of Shelter

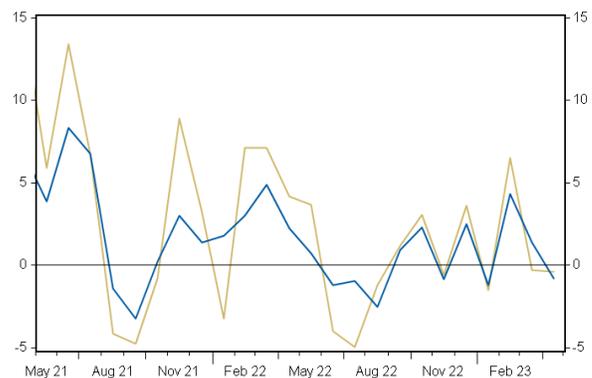


Source: BLS, Morgan Stanley Research forecasts

Exhibit 9: Hotel Indicators are Showing Signs of Easing

Hotels: Average Daily Rate (US\$) SA/m/m

Hotels: Revenue per Available Room (US\$) SA m/m



Source: Smith Travel Research/Haver Analytics/Morgan Stanley Research

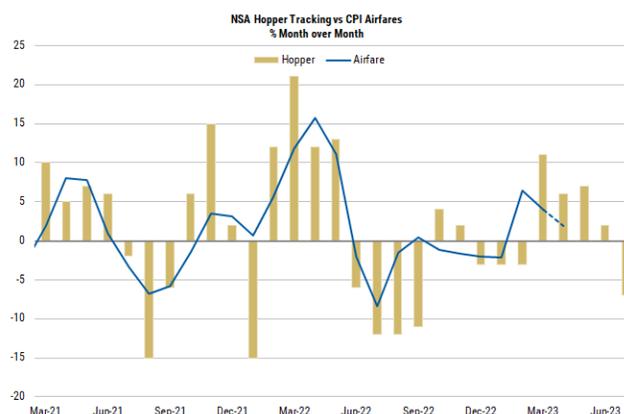
Source: Smith Travel Research, Morgan Stanley Research

4. Travel and Other Volatile Services:

After increasing 6.4%M and 4.0%M in February and March respectively, high frequency tracking data point to a still-elevated but lower print in April airfares (Exhibit 10). However, the seasonality in April, should help decrease the upside risk.

Chair Powell and the FOMC have emphasized the persistence in inflation in core services (ex housing). Excluding shelter, travel, and health insurance, CPI services inflation has been strong, but several of these services line items have been particularly volatile in recent months. Strength more recently kept services inflation from exhibiting a more substantial deceleration. We see core services ex housing coming down in April. However, given the volatility in the underlying sectors, motor vehicle insurance, motor vehicle maintenance & repair, communication services, and certain education services, all should be watched in the report as potential sources of surprise.

Exhibit 10: Airfare to Continue to Decelerate but Remain Elevated in April



Source: Hopper, BLS, Morgan Stanley Research forecasts

Based on our current Core CPI forecasts, core PCE is on track to increase 0.33%M, compared to 0.28%M in March.

Exhibit 11 details our monthly forecast across CPI and PCE inflation through December 2024.

Exhibit 11: Inflation Forecast Table

	% Change - Year-over-Year				% Change - Month-over-Month			
	Headline PCE	Core PCE	Headline CPI	Core CPI	Headline PCE	Core PCE	Headline CPI	Core CPI
Jan-22	6.1	5.2	7.5	6.0	0.53	0.47	0.61	0.56
Feb-22	6.4	5.4	7.9	6.4	0.59	0.37	0.71	0.47
Mar-22	6.8	5.4	8.5	6.5	0.95	0.37	1.01	0.31
Apr-22	6.4	5.0	8.3	6.2	0.20	0.31	0.40	0.47
May-22	6.5	4.9	8.6	6.0	0.61	0.38	0.92	0.63
Jun-22	7.0	5.0	9.1	5.9	0.99	0.63	1.19	0.60
Jul-22	6.4	4.7	8.5	5.9	-0.09	0.08	-0.03	0.31
Aug-22	6.3	4.9	8.3	6.3	0.27	0.55	0.23	0.58
Sep-22	6.3	5.2	8.2	6.6	0.34	0.46	0.41	0.57
Oct-22	6.1	5.1	7.7	6.3	0.42	0.31	0.49	0.33
Nov-22	5.7	4.8	7.1	6.0	0.17	0.22	0.21	0.31
Dec-22	5.3	4.6	6.5	5.7	0.20	0.37	0.13	0.40
Jan-23	5.4	4.7	6.4	5.6	0.60	0.56	0.52	0.41
Feb-23	5.1	4.7	6.0	5.5	0.30	0.35	0.37	0.45
Mar-23	4.2	4.6	5.0	5.6	0.08	0.28	0.05	0.38
Apr-23	4.4	4.6	5.1	5.5	0.40	0.33	0.46	0.38
May-23	3.9	4.5	4.2	5.1	0.15	0.25	0.13	0.29
Jun-23	3.0	4.0	3.1	4.8	0.11	0.19	0.11	0.23
Jul-23	3.2	4.1	3.2	4.6	0.08	0.16	0.08	0.20
Aug-23	3.1	3.7	3.3	4.2	0.23	0.15	0.32	0.18
Sep-23	2.9	3.4	3.1	3.8	0.16	0.15	0.20	0.19
Oct-23	2.6	3.2	2.7	3.8	0.06	0.16	0.10	0.27
Nov-23	2.6	3.2	2.8	3.7	0.18	0.16	0.28	0.27
Dec-23	2.7	2.9	3.1	3.6	0.27	0.15	0.43	0.26
Jan-24	2.1	2.5	2.7	3.4	0.07	0.15	0.11	0.26
Feb-24	1.9	2.3	2.5	3.2	0.12	0.15	0.19	0.25
Mar-24	2.0	2.2	2.7	3.1	0.14	0.15	0.22	0.25
Apr-24	1.8	2.0	2.5	2.9	0.21	0.14	0.32	0.24
May-24	1.7	1.9	2.4	2.9	0.01	0.14	0.02	0.23
Jun-24	1.7	1.8	2.5	2.9	0.16	0.14	0.24	0.23
Jul-24	1.7	1.8	2.6	2.9	0.06	0.13	0.11	0.22
Aug-24	1.7	1.8	2.6	2.9	0.23	0.13	0.36	0.22
Sep-24	1.7	1.7	2.6	3.0	0.14	0.13	0.23	0.22
Oct-24	1.6	1.7	2.6	2.9	0.02	0.12	0.04	0.20
Nov-24	1.6	1.7	2.5	2.8	0.16	0.12	0.25	0.20
Dec-24	1.6	1.6	2.5	2.8	0.25	0.12	0.39	0.20

Source: BLS, BEA, Morgan Stanley Research forecasts

Disclosure Section

The information and opinions in Morgan Stanley Research were prepared by Morgan Stanley & Co. LLC, and/or Morgan Stanley C.T.V.M. S.A., and/or Morgan Stanley Mexico, Casa de Bolsa, S.A. de C.V., and/or Morgan Stanley Canada Limited. As used in this disclosure section, "Morgan Stanley" includes Morgan Stanley & Co. LLC, Morgan Stanley C.T.V.M. S.A., Morgan Stanley Mexico, Casa de Bolsa, S.A. de C.V., Morgan Stanley Canada Limited and their affiliates as necessary.

For important disclosures, stock price charts and equity rating histories regarding companies that are the subject of this report, please see the Morgan Stanley Research Disclosure Website at www.morganstanley.com/researchdisclosures, or contact your investment representative or Morgan Stanley Research at 1585 Broadway, (Attention: Research Management), New York, NY, 10036 USA.

For valuation methodology and risks associated with any recommendation, rating or price target referenced in this research report, please contact the Client Support Team as follows: US/Canada +1 800 303-2495; Hong Kong +852 2848-5999; Latin America +1 718 754-5444 (U.S.); London +44 (0)20-7425-8169; Singapore +65 6834-6860; Sydney +61 (0)2-9770-1505; Tokyo +81 (0)3-6836-9000. Alternatively you may contact your investment representative or Morgan Stanley Research at 1585 Broadway, (Attention: Research Management), New York, NY 10036 USA.

Global Research Conflict Management Policy

Morgan Stanley Research has been published in accordance with our conflict management policy, which is available at www.morganstanley.com/institutional/research/conflictolicies. A Portuguese version of the policy can be found at www.morganstanley.com.br

Important Disclosures

Morgan Stanley is not acting as a municipal advisor and the opinions or views contained herein are not intended to be, and do not constitute, advice within the meaning of Section 975 of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

Morgan Stanley Research does not provide individually tailored investment advice. Morgan Stanley Research has been prepared without regard to the circumstances and objectives of those who receive it. Morgan Stanley recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser. The appropriateness of an investment or strategy will depend on an investor's circumstances and objectives. The securities, instruments, or strategies discussed in Morgan Stanley Research may not be suitable for all investors, and certain investors may not be eligible to purchase or participate in some or all of them. Morgan Stanley Research is not an offer to buy or sell or the solicitation of an offer to buy or sell any security/instrument or to participate in any particular trading strategy. The value of and income from your investments may vary because of changes in interest rates, foreign exchange rates, default rates, prepayment rates, securities/instruments prices, market indexes, operational or financial conditions of companies or other factors. There may be time limitations on the exercise of options or other rights in securities/instruments transactions. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realized. If provided, and unless otherwise stated, the closing price on the cover page is that of the primary exchange for the subject company's securities/instruments.

The fixed income research analysts, strategists or economists principally responsible for the preparation of Morgan Stanley Research have received compensation based upon various factors, including quality, accuracy and value of research, firm profitability or revenues (which include fixed income trading and capital markets profitability or revenues), client feedback and competitive factors. Fixed Income Research analysts', strategists' or economists' compensation is not linked to investment banking or capital markets transactions performed by Morgan Stanley or the profitability or revenues of particular trading desks.

With the exception of information regarding Morgan Stanley, Morgan Stanley Research is based on public information. Morgan Stanley makes every effort to use reliable, comprehensive information, but we make no representation that it is accurate or complete. We have no obligation to tell you when opinions or information in Morgan Stanley Research change apart from when we intend to discontinue equity research coverage of a subject company. Facts and views presented in Morgan Stanley Research have not been reviewed by, and may not reflect information known to, professionals in other Morgan Stanley business areas, including investment banking personnel.

Morgan Stanley may make investment decisions that are inconsistent with the recommendations or views in this report.

To our readers based in Taiwan or trading in Taiwan securities/instruments: Information on securities/instruments that trade in Taiwan is distributed by Morgan Stanley Taiwan Limited ("MSTL"). Such information is for your reference only. The reader should independently evaluate the investment risks and is solely responsible for their investment decisions. Morgan Stanley Research may not be distributed to the public media or quoted or used by the public media without the express written consent of Morgan Stanley. Any non-customer reader within the scope of Article 7-1 of the Taiwan Stock Exchange Recommendation Regulations accessing and/or receiving Morgan Stanley Research is not permitted to provide Morgan Stanley Research to any third party (including but not limited to related parties, affiliated companies and any other third parties) or engage in any activities regarding Morgan Stanley Research which may create or give the appearance of creating a conflict of interest. Information on securities/instruments that do not trade in Taiwan is for informational purposes only and is not to be construed as a recommendation or a solicitation to trade in such securities/instruments. MSTL may not execute transactions for clients in these securities/instruments.

Morgan Stanley is not incorporated under PRC law and the research in relation to this report is conducted outside the PRC. Morgan Stanley Research does not constitute an offer to sell or the solicitation of an offer to buy any securities in the PRC. PRC investors shall have the relevant qualifications to invest in such securities and shall be responsible for obtaining all relevant approvals, licenses, verifications and/or registrations from the relevant governmental authorities themselves. Neither this report nor any part of it is intended as, or shall constitute, provision of any consultancy or advisory service of securities investment as defined under PRC law. Such information is provided for your reference only.

Morgan Stanley Research is disseminated in Brazil by Morgan Stanley C.T.V.M. S.A. located at Av. Brigadeiro Faria Lima, 3600, 6th floor, São Paulo - SP, Brazil; and is regulated by the Comissão de Valores Mobiliários; in Mexico by Morgan Stanley México, Casa de Bolsa, S.A. de C.V. which is regulated by Comisión Nacional Bancaria y de Valores. Paseo de los Tamarindos 90, Torre 1, Col. Bosques de las Lomas Floor 29, 05120 Mexico City; in Japan by Morgan Stanley MUFG Securities Co., Ltd. and, for Commodities related research reports only, Morgan Stanley Capital Group Japan Co., Ltd; in Hong Kong by Morgan Stanley Asia Limited (which accepts responsibility for its contents) and by Morgan Stanley Bank Asia Limited; in Singapore by Morgan Stanley Asia (Singapore) Pte. (Registration number 199206298Z) and/or Morgan Stanley Asia (Singapore) Securities Pte Ltd (Registration number 200008434H), regulated by the Monetary Authority of Singapore (which accepts legal responsibility for its contents and should be contacted with respect to any matters arising from, or in connection with, Morgan Stanley Research) and by Morgan Stanley Bank Asia Limited, Singapore Branch (Registration number T14FC0118J); in Australia to "wholesale clients" within the meaning of the Australian Corporations Act by Morgan Stanley Australia Limited A.B.N. 67 003 734 576, holder of Australian financial services license No. 233742, which accepts responsibility for its contents; in Australia to "wholesale clients" and "retail clients" within the meaning of the Australian Corporations Act by Morgan Stanley Wealth Management Australia Pty Ltd (A.B.N. 19 009 145 555, holder of Australian financial services license No. 240813, which accepts responsibility for its contents; in Korea by Morgan Stanley & Co International plc, Seoul Branch; in India by Morgan Stanley India Company Private Limited; in Vietnam this report is issued by Morgan Stanley Singapore Holdings; in Canada by Morgan Stanley Canada Limited; in Germany and the European Economic Area where required by Morgan Stanley Europe S.E., regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin) under the reference number 149169; in the United States by Morgan Stanley & Co. LLC, which accepts responsibility for its contents. Morgan Stanley & Co. International plc, authorized by the Prudential Regulatory Authority and regulated by the Financial Conduct Authority and the Prudential Regulatory Authority, disseminates in the UK research that it has prepared, and approves solely for the purposes of

section 21 of the Financial Services and Markets Act 2000, research which has been prepared by any of its affiliates. RMB Morgan Stanley Proprietary Limited is a member of the JSE Limited and A2X(Pty) Ltd. RMB Morgan Stanley Proprietary Limited is a joint venture owned equally by Morgan Stanley International Holdings Inc. and RMB Investment Advisory (Proprietary) Limited, which is wholly owned by FirstRand Limited. The information in Morgan Stanley Research is being disseminated by Morgan Stanley Saudi Arabia, regulated by the Capital Market Authority in the Kingdom of Saudi Arabia, and is directed at Sophisticated investors only.

The trademarks and service marks contained in Morgan Stanley Research are the property of their respective owners. Third-party data providers make no warranties or representations relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages relating to such data. The Global Industry Classification Standard (GICS) was developed by and is the exclusive property of MSCI and S&P.

Morgan Stanley Research, or any portion thereof may not be reprinted, sold or redistributed without the written consent of Morgan Stanley.

Indicators and trackers referenced in Morgan Stanley Research may not be used as, or treated as, a benchmark under Regulation EU 2016/1011, or any other similar framework.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (DIFC Branch), regulated by the Dubai Financial Services Authority (the DFSA), and is directed at Professional Clients only, as defined by the DFSA. The financial products or financial services to which this research relates will only be made available to a customer who we are satisfied meets the regulatory criteria to be a Professional Client. A distribution of the different MS Research ratings or recommendations, in percentage terms for Investments in each sector covered, is available upon request from your sales representative.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (QFC Branch), regulated by the Qatar Financial Centre Regulatory Authority (the QFCRA), and is directed at business customers and market counterparties only and is not intended for Retail Customers as defined by the QFCRA.

As required by the Capital Markets Board of Turkey, investment information, comments and recommendations stated here, are not within the scope of investment advisory activity. Investment advisory service is provided exclusively to persons based on their risk and income preferences by the authorized firms. Comments and recommendations stated here are general in nature. These opinions may not fit to your financial status, risk and return preferences. For this reason, to make an investment decision by relying solely to this information stated here may not bring about outcomes that fit your expectations.

© 2023 Morgan Stanley