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Housing Market

Inflation rate inches closer to the Fed’s target of 2%

With inflation cooling and the job market weakening, an interest rate cut is appearing more likely

August 14, 2024, 11:23 am *By Jeff Andrews*

The Consumer Price Index (CPI) continues to point toward an interest rate cut in September.

In the monthly inflation report released Wednesday, the inflation metric met expectations

Housing costs, which rose 0.4%, accounted for 90% of the monthly inflation gain in July. This indicates that steadily increasing consumer pains at the grocery store and with other necessities has largely halted. When excluding housing costs from the CPI, annual inflation has averaged only 1.7% since May 2023.

It makes sense for the Federal Open Market Committee to cut interest rates in September, given that inflation is mainly tied to housing costs and housing costs are being driven by high mortgage rates. In addition, the labor market is weakening, as evidenced by a lackluster jobs report in which 114,000 new jobs were added in July, 35% fewer than expected.

Bright MLS chief economist Lisa Sturtevant raised the question of whether the Fed has waited too long to cut rates given how much housing costs are driving the metric. Fed Chair Jerome Powell acknowledged this as a risk in testimony to Congress last month.

"Until this month, the Fed seems to have been laser focused on inflation and progress toward the 2% target," Sturtevant said in a statement. "But shelter has been an outsized contributor to the Consumer Price Index. As the Fed has kept rates high, those higher rates have exacerbated housing costs by dampening new housing construction and increasing borrowing costs."

When including seasonal adjustments, inflation rose 0.2% year over year in July. The CPI rose 0.2% month over month after falling by 0.1% in June.

A drop in benchmark interest rates would end a brutal period of rate hikes between March 2022 and July 2023 while providing desperately needed relief for the housing industry. Although inventory is recovering, many buyers are either priced out or are waiting for rates to drop.

"In the medium-run, we expect the economy to land softly and housing inventory to continue to recover," **Realtor.com** senior economist Ralph McLaughlin said in a statement. "This should put downward pressure on mortgage rates this fall and winter and will set the stage for a much better season for homebuyers in 2025. … In our mid-year housing forecast update released today, we have downwardly revised our mortgage rate expectations at year's end to 6.3%."

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