

From the desk of Chief Economist Beth Ann Bovino

Energy inflation pass-through: Silence of the core

Despite the war in the Middle East entering its third month, so far the jump in energy spikes have not shown up dramatically in core prices. The core Consumer Price Index (CPI) was tame, down by 0.1% to 2.6% in March, with the jump in airline fares likely from higher energy prices. And while short-term inflation expectations are high, long-term inflation expectations, what the Fed watches, appear to be stable.

On the flip side, the Fed's other mandate, maximum employment, is also holding up relatively well. While hiring has slowed with the jobs market cooling, most workers are still holding onto their jobs as indicated by stable initial jobless benefits claims. March retail data, at 1.7% month-over-month, was the fastest monthly gain in more than three years, partly from higher gas prices (gas stations were up 15.5%). Still, overall spending was broad-based. Households may be smoothing consumption by either dipping into savings or turning to credit.

But while retail sales in the U. S. and other markets have shown short-term resilience despite the war's impact, fatigue will eventually set in as cost pressures mount.

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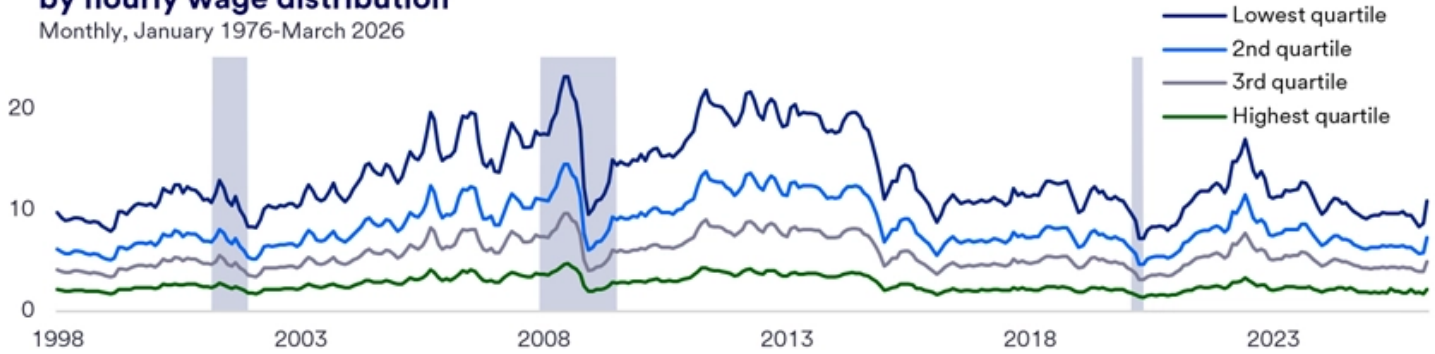
Beth Ann Bovino, chief economist, U.S. Bank

To measure the cost on consumer budgets, a good rule of thumb is that for every \$10 increase in a barrel of West Texas Intermediate crude (WTI), 25 cents is added to a gallon of gas, an extra \$144 cost for the average driver each year.

The average worker in the U.S. needs to work five hours to pay for the gasoline required to commute to work each month. Given current fuel efficiency, that's much lower than the nine hours needed in 1976. But workers with lower paying jobs need to work almost 11 hours to pay for their commute today, while workers with higher paying jobs only need to work less than 2 hours. Higher spending for gasoline means less available for discretionary spending.

**Average hours of work needed for gas to drive to work each month
by hourly wage distribution**

Monthly, January 1976-March 2026



Sources: Census, St Louis FRED, AAA.com, EPA, U. S. Bank Economics calculations

The energy tax doesn't end with oil. The increase in core services prices was driven by a jump in airline fares, no doubt partially explained by higher fuel costs. In general, pass-through pressure to core prices is about 20bps for every 10% increase in a barrel of oil – an additional cost to consumer spending that is yet to be seen.

No policy action at the Fed's April meeting was no surprise, though Governor Miran did dissent for a 25 bps rate cut, despite his earlier acknowledgement that the inflation picture has deteriorated. The question is future policy action. Looking at risks today based on the data available, the damage from higher prices currently outweighs job market concerns. But with core inflation modest, wage gains softer and long-term inflation expectations low, I still expect the next cut to be delivered "just in time for the holidays," at year end. But after hotter March inflation readings, even more 'humbugs' may reason that the inflation outlook requires a more cautious stance, increasing chances that the FOMC will be on hold this year.

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