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INVESTMENT SERVICES

Weekly Relative Value

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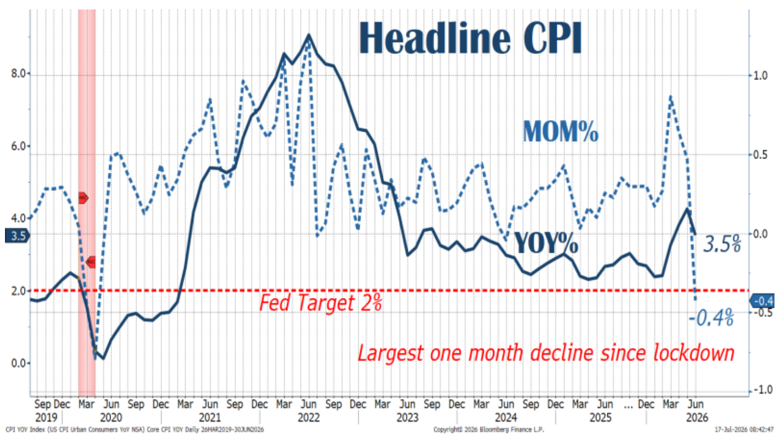
WEEK OF JULY 20, 2026

All About Inflation — Until It Isn't

*"It's one data point.... I don't want to overread or cherry pick data...There might be some who look at this morning's data and say, **'Well, mission accomplished, everything is swell.' That is not my view."***
Kevin Warsh, when asked about the June Consumer Price Index (CPI)

The June headline CPI came in at negative 0.4% month over month. That was the biggest one-month decline in the CPI since April 2020 — when the economy was virtually shut down by the pandemic. On an annual basis, inflation slowed from **4.2% to 3.5%**, well below market expectations.



Sounds like great news until you look at where the drop came from. **Energy fell 5.7% in June, driven by gasoline dropping 9.7% because oil markets briefly priced in a resolution to the Iran situation in June**. Given gasoline's relatively large weight and high volatility, this alone removed several tenths of a percentage point from headline inflation.

However, that relief is already proving to be short lived. Renewed fighting in the Gulf has effectively undermined the ceasefire and pushed crude oil prices to a four-week high.

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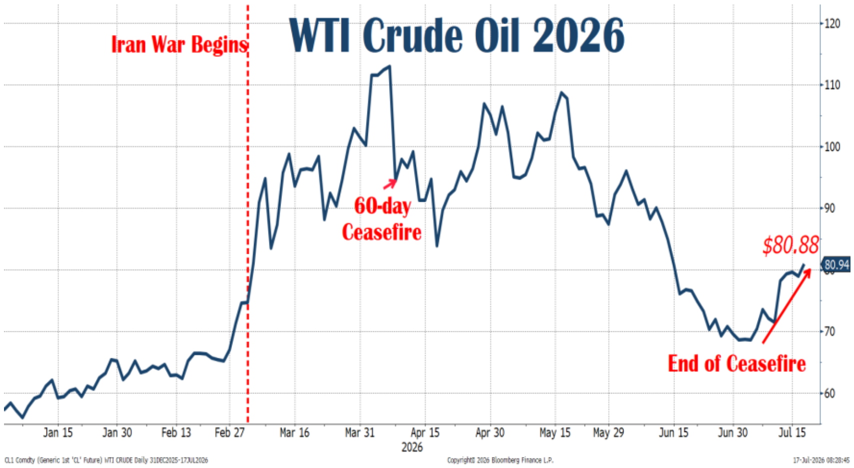
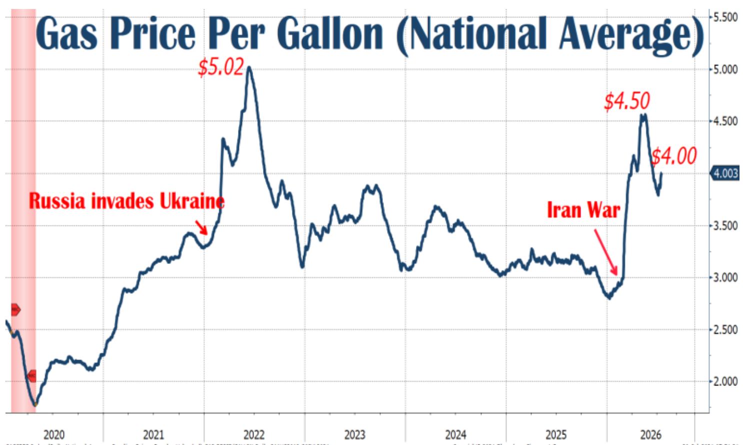
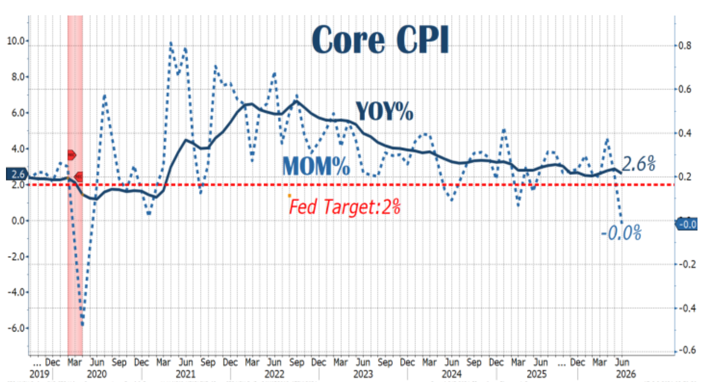


The U.S. national average gasoline price had already rebounded to $4.00 per gallon, suggesting energy could once again become an upward driver of inflation during July.



Moving on. The core CPI, which strips out food and energy, rang in flat instead of climbing +0.2% as was universally anticipated. The last time we printed a zero on core? Try January 2021. The six-month annualized trend in the core CPI is now running at +2.6%, and the three-month pace is at +2.3%.

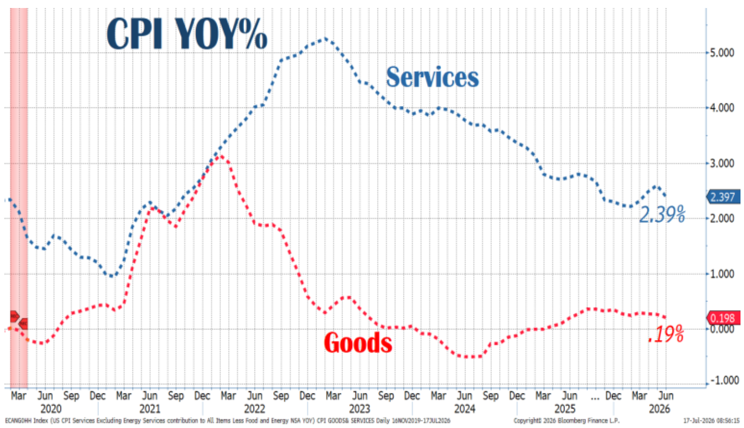


In fact, going a step further, the core index excluding shelter inched -0.1% lower after a tepid +0.1% increase in May — again, something we have not seen since May 2020. Many are not aware of this.

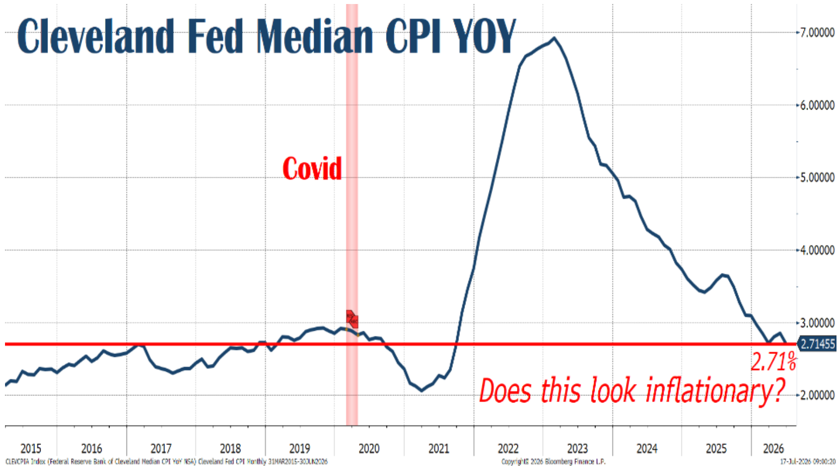
The Powell super core (CPI excluding energy/rents services) also fell by -0.2% in a sequential decline that matches the largest down-moves since January 2021. In fact, in the past three months, the Powell super core, which maps out the contours of the labor market (that many at the Fed believe is "solid" since they myopically focus on the headline inflation rate), has slowed right into the central bank's target at +2.1%.

Maybe the Fed should switch its concern to deflation. Because the "D" label was written all over this report. To wit: The core goods index, despite all the tariff action, dipped -0.1% month over month for the second consecutive month. Apparel, autos, appliances, home improvement and drugs — all weak in terms of any pricing power.

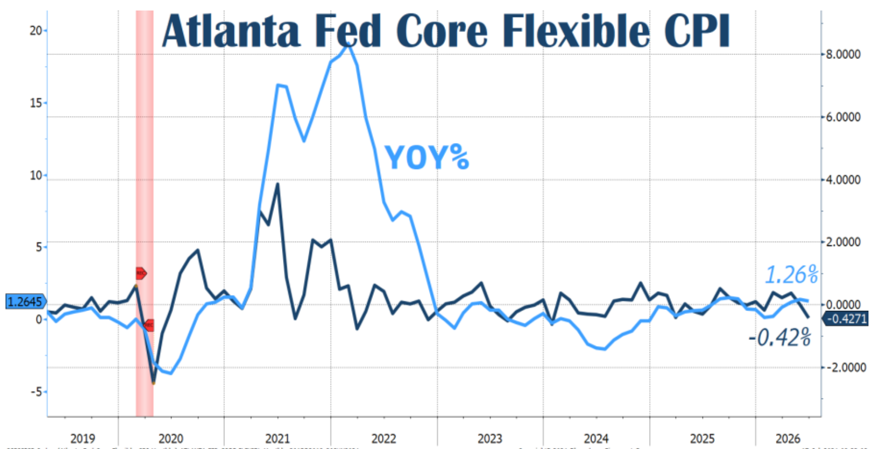
Services inflation was also unexpectedly subdued. Owners' Equivalent Rent continued to rise by 0.2%, but this was offset by weakness across several discretionary service categories. Hotel and motel prices fell 2.3%, despite continued strength in travel demand, while healthcare inflation eased to 0.1%, with health insurance prices declining 0.5%**.**



The Cleveland Fed's trimmed-mean measure came in nearly flat sequentially in June for the first time since April 2020, and before that, try February 2010. Then July 2009 and April 2003. The year-over-year trend on this metric softened from +2.9% to +2.6%, the slowest pace in more than five years. The Cleveland Fed trimmed mean matters because it asks the right question: Was June just an energy story, or did the inflation impulse cool more broadly? The answer was the latter. When the trimmed mean is nearly flat and running at its slowest year-over-year pace in more than five years, the "sticky inflation" argument starts looking less sticky.



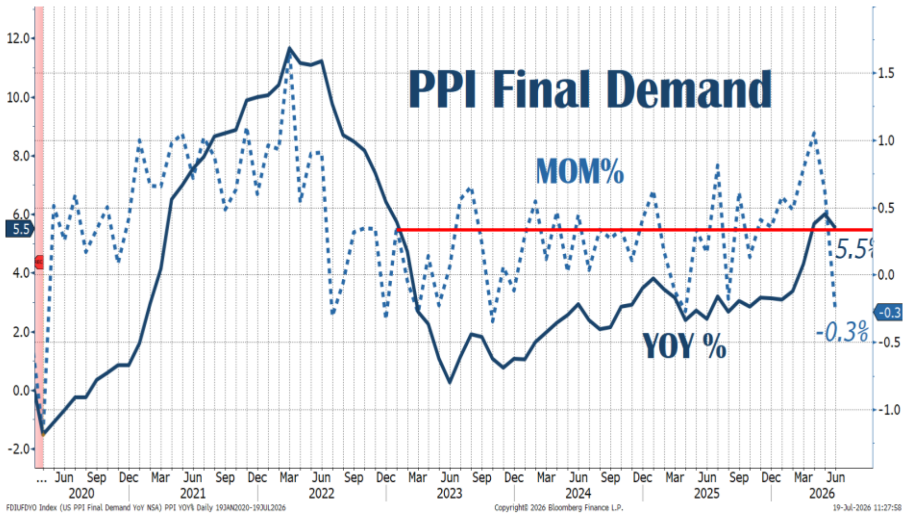
The Atlanta Fed core flexible CPI matters because it is the inflation measure most likely to move first when pricing pressure turns and it is extremely sensitive to the economic cycle. In June, it did not just cool — it outright deflated. The core flexible CPI fell **-0.4% in June** and slowed to **+1.3% year over year**, which argues against the idea that inflation pressure is reaccelerating beneath the surface. That is hard to square with the idea that inflation is quietly reaccelerating under the surface.



Bottom line: From my perch whether it be tariffs, oil or memory chips, there has yet to be any sign of meaningful spillover from these shocks into the core price indices, market-based inflation expectations or even wages. (These second-round effects are what should really be dominating the Fed's mindset, but instead, they seem to relish in reporting rather than analyzing the data.)

PRODUCER PRICE INDEX (PPI) COMES IN TAME

CPI was not the only report to undercut expectations — PPI did too. Producer prices fell -0.3% month over month in June versus expectations for a flat reading, while May's alarming +1.1% jump was revised down to +0.6%. It was the first monthly decline since last August, and the year-over-year rate eased to +5.5% from +6.0%, below the +6.2% consensus.



Core PPI, excluding food and energy, rose +0.2% month over month, slightly below the +0.3% consensus. May was also revised down sharply, to just +0.1% from the previously reported +0.4%.

The report was also encouraging at the earliest stage of production. The core crude-goods index excluding food and energy, which is a pipeline measure for future goods inflation, dropped a hefty -1.2% month over month and has now fallen in two of the past three months.

Bottom line: With the CPI and PPI details in hand, we can now estimate that the headline Personal Consumption Expenditures (PCE) deflator for June will come in at -0.1% month over month and the core at less than +0.2% (+0.16% to the second decimal place).

THE FED DOESN'T KNOW THE REAL INFLATION RATE

At last week's congressional testimony Kevin Warsh said:

"My commitment to you is to take sticky prices and to unstick them."

It was encouraging to hear Fed Chairman Warsh finally kyboshing this newly found narrative that artificial intelligence (AI) is going to prove to be a source of inflation just because of the impact on memory chip prices (adding, "I don't view a one-time change in prices as necessarily being inflationary because I think there's a supply response.") Indeed, as was the case with telecom equipment in the late 1990s and housing in the mid-2000's.

In answer to a question about the Dallas Fed Trimmed Mean PCE and core PCE, he said:

"None of those are very good measures of underlying inflation."

That was a revelation, especially since very recently, the former was his favorite metric, and he said so publicly. Maybe back then, to placate the president.

He then went on to say that this is one of the reasons he formed a task force to look into inflation measures, because:

“We need new measures to understand the underlying changes in inflation” and that he is “super interested in finding new measures to do a better job to help us inform our decisions.”

He did not indicate what might be used to judge underlying inflation pressures, or he was just gaslighting the committee.

Here’s the takeaway: If he doesn’t trust the current inflation data, what grounds would he have to tighten policy, at least before the findings of his task force?

Bottom line: So far, many Federal Open Market Committee (FOMC) officials are unimpressed with the latest benign core CPI and PPI data — at least they are skeptical over their durability. The only one who does not appear hawkish is the chairman himself, but he has a gang that wants to raise rates as the rhetoric suggests. Can he convince them otherwise? That is the issue. And as for the money market, all it has done is shift the timing for a hike to October and take this month off the table.

It’s a shame that the Fed isn’t drawing the distinction between demand-led and supply-fueled inflation. This time around, it is 100% a cost squeeze from what has happened in the U.S.-Iran war.

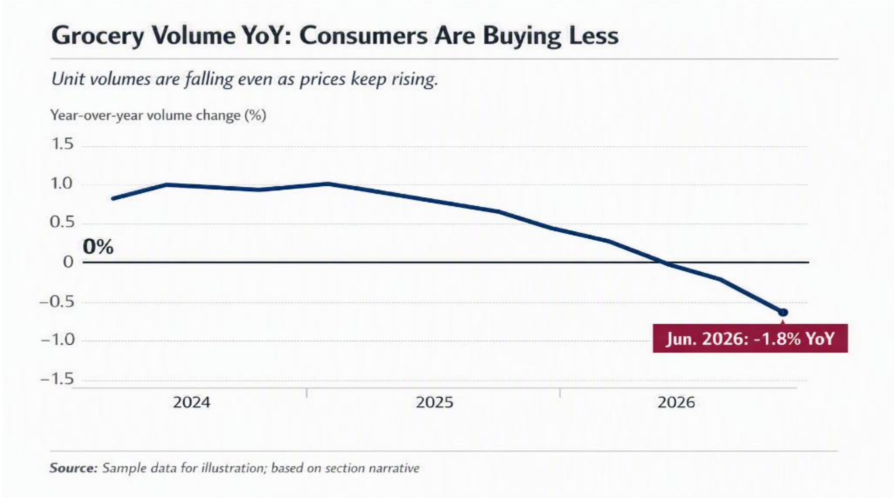
Many at the Fed want to hike once, as is the situation with the dots, but even the dots revert to rate cuts next year. But what is the point? Because combating inflation that is supply-induced requires a whole lot of policy tightening to correct and will only be solved by driving demand into the ground.

Is it really worth it?

CUTTING BACK ON GROCERIES

“The consumer is worse than anticipated." — PepsiCo's CEO

Americans are buying fewer groceries. Unit sales fell 1.8% in June, the sharpest drop since the pandemic, even as prices kept climbing. A grocery run that cost $300 in 2019 now costs $400. Bain data shows 80% of Americans are actively trying to spend less, 49% are simply buying fewer items and 44% are leaning harder on coupons and promotions. Rising GLP-1 adoption is another factor, with users buying fewer groceries.



Groceries have become a market-share battle, and the leaders are starting to distance themselves from the laggards. NielsenIQ Homescan data show that value players — discount, mass and club retailers — are gaining shoppers. Survey data also show that 22% of consumers are visiting more stores to hunt for the best deals. But that does not solve the unit-sales problem for value-focused grocers. Consumers are still buying less overall, which points to a longer stretch of soft sales until the macro backdrop improves.

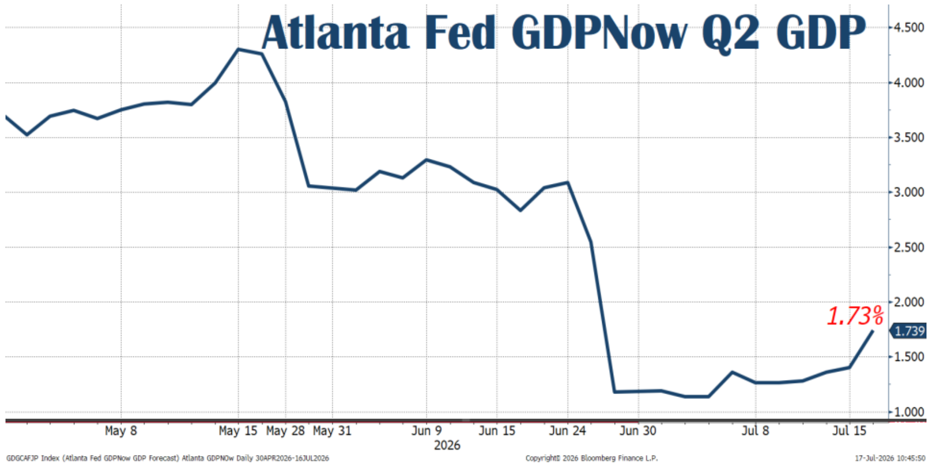
The grocers that gain ground will sharpen their value proposition by showing that value is about more than the lowest shelf price. Not every grocer can be the cheapest, and Bain’s research shows they do not need to be. The advantage goes to retailers that price sharply on the items shoppers notice most, while using promotions, loyalty programs and private brands with enough precision to make the value story credible.

Bottom line: It’d be great to see consumers balk on the high prices at the grocery store. Frankly, it’s long overdue and should pressure food prices lower as we move forward.

Also, I have very little sympathy for these food companies. They spent three years jacking up prices and calling it inflation while their margins hit records. Now consumers have stopped playing along, and the same CEOs are acting surprised. PepsiCo's CEO blamed gas prices, but his company raised prices aggressively when gas was cheap too. The playbook was always "charge more, sell less, report record earnings," and it worked until people started leaving items on the shelf. Now they're running promotions like they're doing us a favor.

WILL THE FED RAISE RATES IN A SOGGY ECONOMY?

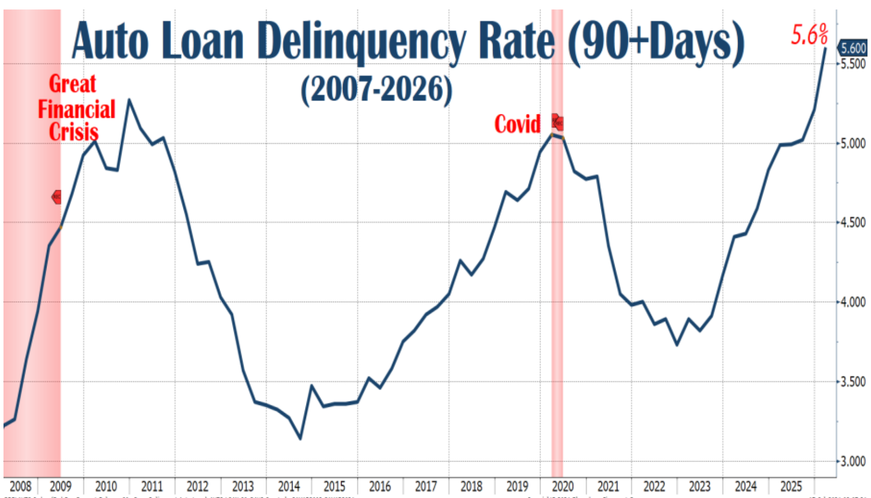
You would never have thought the Fed could so quickly dismiss the soggy jobs data — or the Atlanta Fed Nowcast slipping to +1.7% annualized growth instead of the +3.0% that had been expected from World Cup stimulus and stepped-up income-tax refunds.



Bottom line: Only a sadistic Fed would be tightening into a +1% growth economy and one showing clearly that when we do see wartime pressures abate (though they are perking back up for now) there really is no inflation to be worried about. That is the message from the latest CPI and PPI reports.

AUTO DELINQUENCIES RISE

Approximately 6% of auto loans are now 90+ days due, the highest rate since the pandemic peak and well above the 3.59% long-term average. That's out of 108 million open loans worth $1.67 trillion.



A new Philadelphia Fed paper argues that this overstates the number of borrowers truly in distress. The reason: Lenders are allowing borrowers to skip payments and push them to the end of the loan, temporarily making those loans appear current. But many of those borrowers fall behind again within months, so the same loans keep cycling in and out of delinquency. As a result, the stock of troubled loans keeps rising even though new delinquencies have been flat since late 2022.

To me, the Philly Fed may have unintentionally made the picture look worse. If lenders are granting extensions and borrowers still fall behind again, then losses are being delayed, not avoided. Meanwhile, ~29% of new-car trade-ins now involve negative equity, meaning borrowers owe more than their cars are worth. They cannot sell their way out of the loan; they are stuck.

Subprime is the real problem. Buy Here Pay Here (BHPH) dealers — which finance cars directly for poor-credit borrowers — have grown loan balances 200% since 2018, and their loans are more than 16 times as likely to end in repossession as traditional auto loans. Tricolor Holdings, a major BHPH operator, collapsed last September amid fraud allegations, costing two banks roughly $200 million each.

The Philly Fed's argument depends on new delinquencies staying flat — and that only holds if the labor market does.

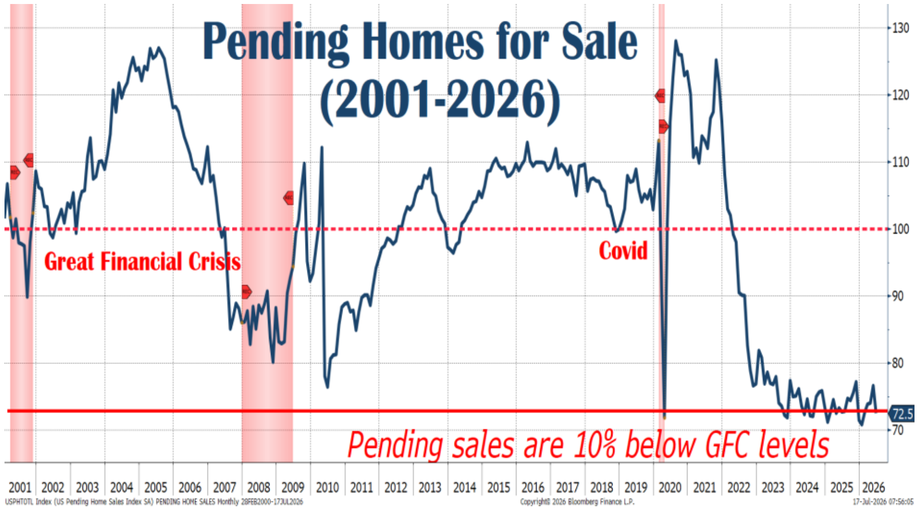
Bottom line: Lenders are using payment extensions that temporarily make troubled loans look current. Many borrowers fall behind again soon after, meaning losses may be delayed rather than avoided. The biggest risk is concentrated in subprime and BHPH lending, where loan balances have surged and repossession risk is far higher. The whole argument depends on the labor market holding up; if it weakens, delinquencies could rise quickly.

NOTHING PENDING

I find it amusing when people call 5% the "new normal" for interest rates. The long bond is elevated because of the war, reset Fed expectations, and ballooning AI mega-cap debt issuance. Remember, the 10-year Treasury yield had slipped below 4% just before U.S.-Iran hostilities began — and that was not long ago. Once the war ends and the AI bubble bursts, who is to say 3% will not become the new normal?

One reason I think today's rate structure is unsustainable is that it is pushing an already moribund housing market even deeper into the ground. In June, pending home sales — a leading indicator — fell 5.4% to a four-month low and are now nearly 10% below the worst levels seen during the 2008-2009 Great Recession.

Funny how little anyone talks about housing anymore now that everything is about AI. Fair enough: Go find a kitchen, sofa and TV in your local data center and move right in.

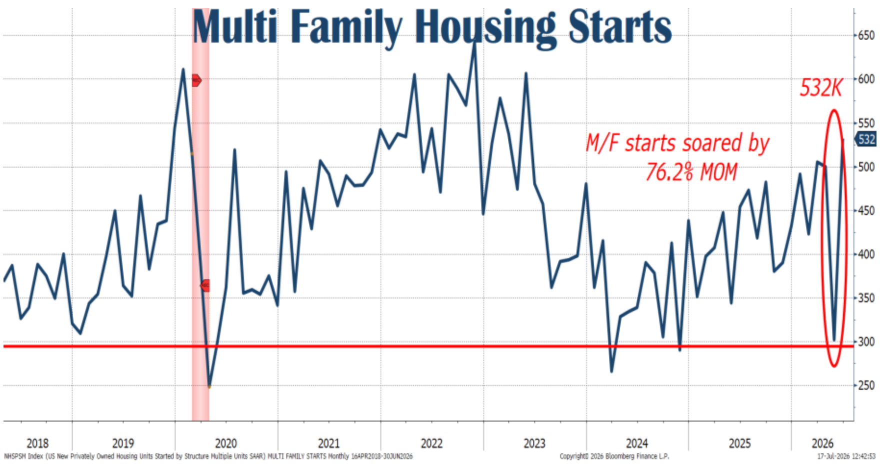


Bottom line: Pending home sales have fallen to a four-month low and sit nearly 10% below Great Recession lows, suggesting the housing market remains extremely weak — even if markets are more focused on AI than real-economy stress.

BLOWING THE ROOF OFF!

June housing starts blew off the roof. The headline number surged by +19% month over month to 1.427 million annualized units — the consensus was at 1.310 million, so a big miss here to the upside. But there were several caveats here.

The mix in the housing start data was not at all constructive. All of the big run-up, and then some, was in the lumpy and notoriously volatile multi-family sector, where starts soared by a near-record +76.2% month-over-month rate to a three-year high of +532,000 annualized units.



The problem is going to be rental supply overhang — which should help reinforce the downtrend in the shelter components in the CPI — **because multi-family starts are up +17.2% on a year-over-year basis, whereas new housing demand in the market for condos and co-ops is down -2.7%!** That can best be described as a disinflationary supply-demand mix for developers and landlords alike. Perhaps the Fed will shift its attention here at some point and away from what the AI craze is doing to memory chip prices.

Single-family starts edged lower by -0.2%, and that makes it three consecutive months of decline to a five-month low of 895,000 units at an annual rate. This is important because the gross domestic product (GDP) impact from the single-family sector is far more powerful than is the case in the multi-family space. Single-family permits, again, were at play, dropping by -2.4% month over month and down in three of the past four months (and down to the lowest level since last August).

Bottom line: June housing starts looked strong only at the headline level. Starts surged 19% month over month, but the gain was driven entirely by a volatile 76% jump in multi-family construction, while single-family starts and permits continued to weaken. That mix points to more rental supply, softer owner-occupied housing demand and added downward pressure on shelter inflation — not a genuinely strong housing market.

THE GRAND ILLUSION

June retail sales looked fine on the surface: +0.2% headline and +0.5% on the core control group. Nonstore sales were the only drivers of retail sales, and Amazon captures roughly 36% to 40% of total U.S. online/non-store e-commerce sales. In broader terms, this translates to Amazon accounting for over 10% of all U.S. retail spending overall.

Even still, the strength was largely a calendar illusion.

This is why. Amazon moved Prime Day into June from its usual July slot, and the seasonal factors did not fully account for the shift. Other retailers also run competing promotions around Prime Day, so the pull-forward was broad. Prime Day ran June 23-26 this year versus July 8-11 in 2025, making 2026 only the second June event outside the pandemic years.

The raw data makes the distortion clear. Non-store retailing rose +3.9% this June, compared with June declines of -3.6% in 2025, -5.8% in 2024, -4.8% in 2023 and -4.0% in 2022. Normally, consumers hold back in June and spend in July; last July, non-store sales rebounded +7.2%. That usual July bump is unlikely this year because Prime Day already happened, yet the seasonal factors will still expect it.

That sets up a likely July payback. The raw data will lose the Prime Day lift just as seasonal adjustment depresses the number further, making July look artificially weak after June looked artificially firm.

Watch for payback in July. The non-store line will likely print artificially soft on a seasonally adjusted basis because July is missing the Prime Day bump the model expects. A cleaner read will require combining June and July together. Strip out online activity, and June already looked weak: headline retail sales fell -0.2% month over month, core control dipped -0.1%, nearly two-thirds of categories declined, and restaurant sales were basically flat despite World Cup tourism.

Bottom line: Prime Day, World Cup spending and one-time tax-refund support all helped prop up Q2 consumption. Those supports are now gone, which matters as we move into the second half of the year.

A CHURCH WITH A CASINO ATTACHED

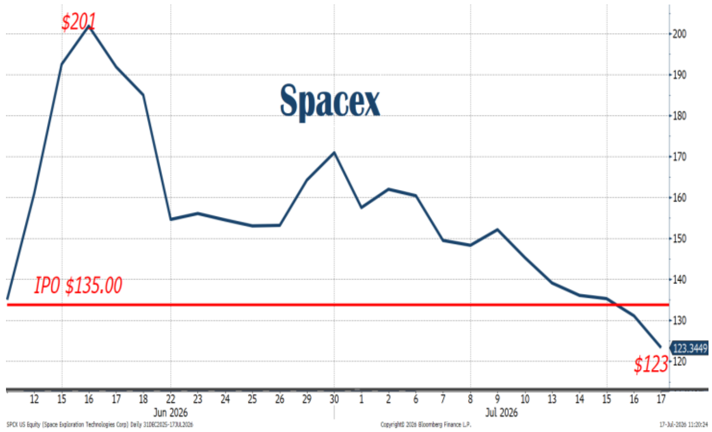
> *"Hype comes before a fall. Huge IPO issuance can signal dangerous euphoria, teeing up a plunge in markets. While we aren't broadly in euphoria yet, expectations for everything AI and U.S. tech are pretty frothy. Hence, firms lining up for IPOs. Elevated sentiment makes positive surprises harder to attain. That favors extreme caution." — Ken Fisher, Founder and co-CIO, Fisher Investments (and a notorious market bull!)*

Warren Buffett told CNBC it's "tough to find values when everybody is preferring gambling." His company Berkshire Hathaway is holding $397 billion in cash and has been selling more stock than it buys for over a year. In May he called the market "a church with a casino attached." He was specifically talking about same-day options, which are essentially bets on whether a stock goes up or down within hours. Volume on those is at record levels. Meanwhile, retail investors pile into Micron and the SpaceX initial public offering (IPO).

The semiconductor index is down nearly 20% from its record and has erased $3.3 trillion since June. Micron dropped more than 10% in a single day. SanDisk has plummeted by 42% in 25 days.

Oh yes, and how could I forget?

SpaceX, after soaring to $201 per share on June 16, has plunged by ~40% and is now 9% under its $135 IPO level. From the peak in June, fully $1 trillion of market cap has been wiped out. (The stock still trades with a forward P/E multiple of only 182x or a six-fold premium of the average S&P 500 member.) How many people chased this thing? A lot. The real story is the collapse of IPO euphoria. SpaceX has now become one of the more spectacular unwinds of the year.



As I have discussed previously, the internet was real. Most of the companies built on it during the dot-com era went bankrupt anyway. Amazon went from $107 to $7 and Cisco never recovered its high. The technology survived, but most of the business models didn't.

The parallels to where we are now are hard to ignore. Massive infrastructure buildout outpacing actual demand (fiber optic then, data centers now). Unprofitable companies going public at peak hype after the largest IPO in history.

Vendor financing is where the seller lends money to the buyer to keep the cycle moving. Nvidia just launched a program to finance its own customers. In the late 1990s, telecom companies like Lucent and Nortel did the same thing. Both ended in some of the largest corporate bankruptcies in American history at the time.

Tell me about the cash flows. Tell me about the return on investment. WHERE IS IT?

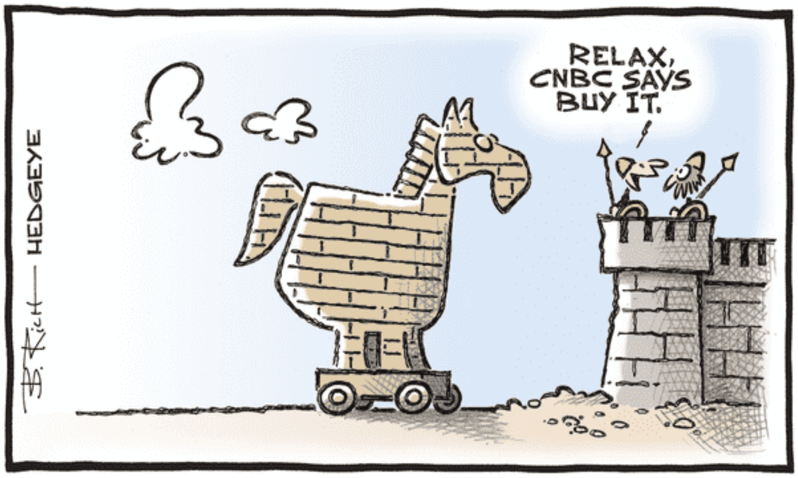
AI is the BIGGEST bubble the world has ever seen. This one could be worse than the dot-com era because of what's underneath the equity layer. The dot-com bubble was mostly stocks. This one has private credit, project finance bonds, off-balance-sheet joint ventures and insurance company money all stacked into data center infrastructure.

Anthropic has $90 billion in compute leases and zero profit heading into an IPO. The technology is real. So was the internet in 1999. Whether the technology works was never in doubt. Whether the companies selling it can justify what investors are paying is a different question, and it's about to get answered in public filings.

Buffett is describing something bigger than a stock market cycle. You can bet on sports from your phone in 38 states. Robinhood turned same-day options into a slot machine. Crypto never stopped. DraftKings turned every NFL game into a portfolio of micro-bets. The entire culture has shifted toward treating everything as a wager, and the financial industry spent the last five years making it easier, faster and more addictive.

Buffett also said there's "more money in cultivating gamblers than cultivating investors," and that applies well beyond Wall Street. The brokerages, the sports books and the crypto exchanges all run the same business model. They don't need you to win. They need you to play. The house edge on same-day options and leveraged exchange-traded funds is enormous, and customers keep coming because the product is designed to feel like entertainment, not risk.

Everyone in this market is playing the same game: They know prices are stretched, but they stay fully invested because they're convinced they'll be the first ones out the door when things go wrong. Millions of investors all standing next to the same exit, all believing they'll beat everyone else through it. On the way up, nobody complained because we were all drunk on making money. But the car also runs in reverse.



Bottom line: Buffett's holding $397 billion in cash because he can't find anything priced like an investment instead of a lottery ticket.

MARKET OUTLOOK AND PORTFOLIO STRATEGY

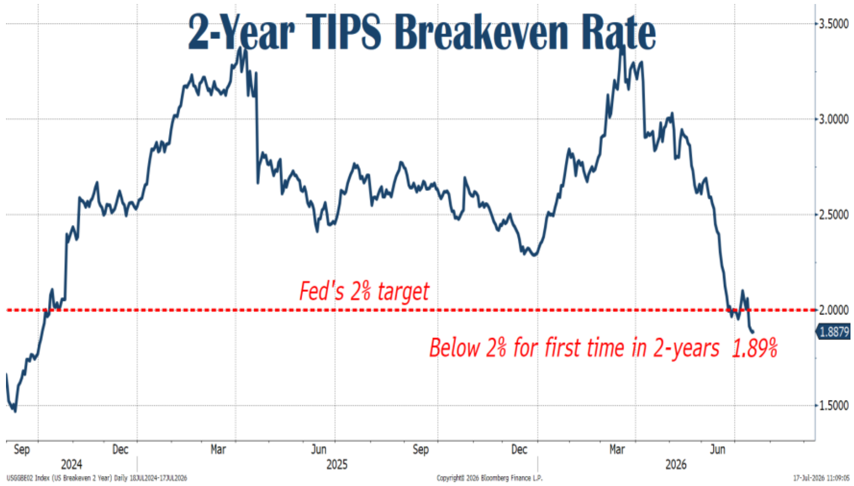
“The U.S. economy has demonstrated notable resiliency this year, with stronger business investment and hiring. This strength is being supported by several tailwinds, including AI-driven capital investment, fiscal stimulus and the benefits of more efficient regulation. However, several risks are shifting below the surface like tectonic plates, including geopolitical tensions and wars, sticky inflation, large global fiscal deficits and elevated asset prices. We cannot predict how these forces will ultimately play out. They may remain manageable, but they could also cause meaningful disruptions when they shift or collide.” — Jamie Dimon, Chairman and CEO, JPMorgan Chase, July 14, 2026

I think inflation fears are overstated and rate-hike expectations should soon reverse.

The inflation today is nothing like 2021-2022 because there is no demand pressure to reinforce what supply squeeze may come our way. The cost pressures hit the wall in the labor market and, eventually, profit margins. Not final inflation this time. For sustainable inflation, you also need the demand curve to shift out. That is not happening in an economy where the construction of AI data centers is the dominant macro force.

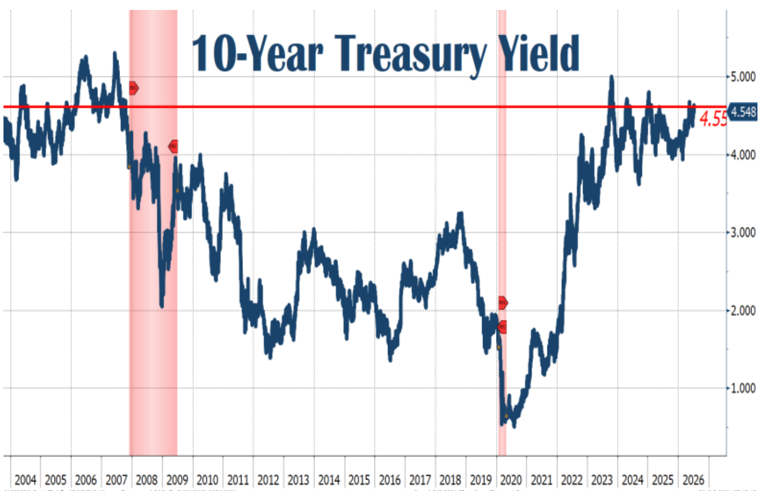
The **2-year Treasury Inflation-Protected Securities (TIPS) breakeven** matters because it is one of the market’s cleanest real-time gauges of **near-term inflation expectations**. In plain English, it compares the yield on a regular 2-year Treasury with the yield on a 2-year inflation-protected Treasury. The gap between the two is the inflation rate investors are implicitly pricing over the next two years.

Now look at that 2-year TIPS inflation breakeven level for some guidance — slicing below the Fed’s 2% target for the first time in nearly two years… when the two-year T-note yield was trading close to 3.75%. And why not? For the first time in three years, less than half of the 180 items in the CPI bucket are now posting sequential price increases.



If investors really believed inflation was about to reaccelerate, the front-end breakeven would not be slipping below 2%. Instead, it is telling you the opposite: The bond market sees the current inflation scare as temporary, not durable. That is why the bullish bond case is still very much alive.

On Treasury yields, I find it striking that after multiple supply shocks, six years of extraordinary fiscal stimulus, an AI boom and record-high equities, the 10-year note can still barely reach 4.5%. That's it? Without the recurring shocks since 2020, core inflation would likely be at 2% already. Core CPI excluding shelter is already running at 2.1%, a fact too few people seem to appreciate. There are pockets of inflation, but the broader story still looks overhyped.



Remember, the 10-year Treasury yield was below 4.0% before the war. Since then, oil prices have jumped, Fed expectations have reset, and AI-related debt issuance has lifted real rates. I do not think any of that is permanent, and I am not interested in overcomplicating it. Meanwhile, only 2% of portfolio managers expect a recession over the next year. With that kind of pro-cyclical consensus, the 10-year should arguably be closer to 6.0%. The fact that it is not may be the real story.

Despite all the market volatility of late along with the selloff in most of the tech darlings, retail investors have continued to plow money into equity-based mutual funds this summer and bullish sentiment remains at extreme levels. The Market Vane Index is at 76, the third highest reading in its 25-year history. For bonds, bullish sentiment is at 29% — flirting near the lowest reading in a decade. Incredibly, only 15% of University of Michigan respondents are now dovish on interest rates (down from 43% at the turn of the year), the lowest share since November 2023. You don't need to be the biggest contrarian to know what these epic sentiment gaps between stocks and bonds imply.

Frankly, given that extreme consensus, I am impressed Treasury yields are still 50 basis points below the cycle peak. After the November midterms, political gridlock and fiscal drag should pressure GDP forecasts lower and likely keep the Fed barking but not biting.

In case you're wondering why I'm the last man standing when it comes to having a bullish bias on bonds.

Bottom line: Inflation pressure looks less durable than feared, the economy looks weaker than markets admit and the Fed risks tightening into a slowdown driven more by supply shocks and speculation than genuine demand-led inflation.

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MORE INFORMATION

For more information about credit union investment strategy, portfolio allocation and security selection, please contact the author at **tom.slefinger@alloyacorp.org** or (630) 276-2753.

As Alloya's Market Strategist, **Tom Slefinger** leverages nearly 40 years of investment strategy expertise to deliver insightful commentary on the economy and market events to optimize balance sheet performance at the credit union level. With thousands of subscribers, Tom's daily and weekly publications are widely read amongst credit union executives.

Prior to becoming the corporate's Market Strategist, Tom served as the Senior Vice President of Institutional Fixed Income Sales at Alloya Investment Services, a division of Alloya Solutions, LLC. In this role, Tom developed and managed operations associated with institutional fixed income sales in addition to developing investment portfolio strategies, identifying appropriate sectors and securities, and optimizing portfolio performance at the credit union level.

Tom holds a B.S. in business administration from the University of Maine. In addition, he holds a Series 7 and 63 through ISI.