Annual inflation in the U.S. has slowed over the past year, decreasing by 2.9 percentage points from February 2023 to February 2024 and settling at 2.5%, as measured by the personal consumption expenditures (PCE) price index. Despite progress toward the Fed’s 2% target, FOMC participants in March 2024 projected only a 0.4-percentage-point drop in PCE inflation over the coming year. Why is progress toward 2% inflation expected to slow? Historical experience—specifically, disinflationary episodes of the early and late 1980s—suggest that goods price inflation tends to fall quickly, while the last mile of disinflation is driven primarily by a lengthier disinflation of services.

**Goods Inflation: Major Contributor to Increases (and Decreases) in Headline Inflation**

Figure 1 shows the contribution to inflation from energy, goods (excl. energy), services (excl. energy and housing), and housing (excl. energy). Historically, energy and goods inflation have been the most volatile, with their contributions both falling within a spread of 6.3 percentage points. Similar to the episodes in the early and late 1980s, energy and goods inflation have driven inflation’s recent peak in June 2022, climbing from averages of near zero to 2.4 and 2.3 percentage points, respectively. Services inflation has been less volatile than goods inflation, with its contribution typically ranging between 1 and 4 percentage points. Housing inflation has been the most stable. Beginning in 1992, its contribution to headline inflation has hovered around 0.5 percentage points, though it peaked at 1.3 percentage points in April 2023.

**Services Disinflation: Likely Needed to Drive the Last Mile of Disinflation**

Figure 2 presents a closer look at inflation components during three disinflationary periods. It plots the 12-month inflation rate of each component for periods beginning in
In the 1989 period, both goods and services disinflation fell by roughly 3 percentage points, and services disinflation was again the longer process. In comparing the first 12 months of disinflation after their respective peaks in the current period, services inflation had come down by only 1.2 percentage points, while goods inflation had come down by 3 percentage points.

The projected change in headline inflation over 2024 is consistent with recent historical episodes. Steep goods disinflation contributed to a reduction in headline inflation during 2023. History indicates that, absent any shocks to the economy, the future pace of progress toward 2% inflation will likely be set by a delayed, protracted, and gradual disinflation in services.

Notes
1 See the difference in Q4 year-over-year inflation projections for 2023 in the December 2023 Summary of Economic Projections and for 2024 in the March 2024 Summary of Economic Projections.
2 The standard deviations of the unweighted component inflation rates are 2.1, 2.4, 2.7, and 12.2 percentage points for housing, services, goods, and energy, respectively. While the distributions of the rates are not symmetric, the standard deviations still hint at the relative volatility of each component, with a greater standard deviation representing greater volatility.