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October CPI

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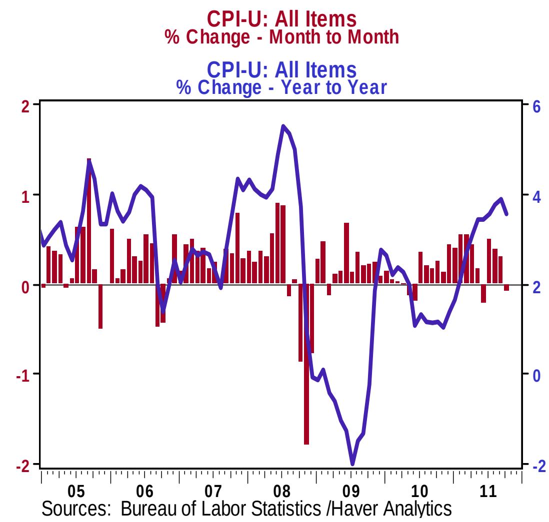
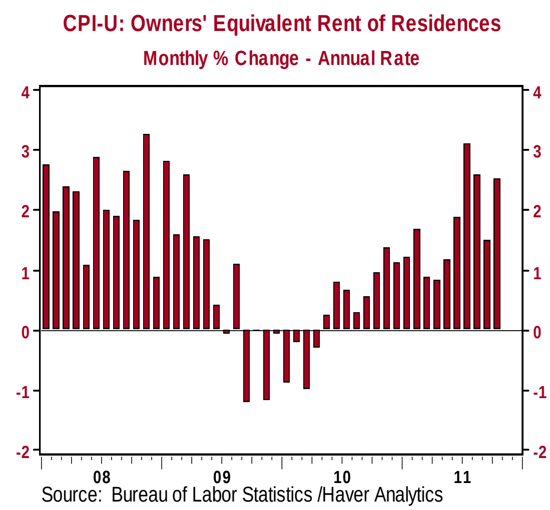
- The Consumer Price Index (CPI) declined 0.1% in October. The consensus expected no change. The CPI is up 3.5% versus a year ago.
- "Cash" inflation (which excludes the government's estimate of what homeowners would charge themselves for rent) slipped 0.2% in October, but is up 4.1% in the past year.
- The decline in the CPI was due to a 2.0% drop in energy prices. Food prices were up 0.1% and the "core" CPI, which excludes food and energy, was up 0.1%, matching consensus expectations. Core prices are up 2.1% versus last year.
- Real average hourly earnings – the cash earnings of all employees, adjusted for inflation – increased 0.3% in October but are down 1.6% in the past year. Real *weekly* earnings are down 1.7% in the past year.

Implications: Like producer prices, consumer prices also took a breather in October, with the CPI down 0.1%. However, the slight dip in consumer prices is going to be temporary and the Federal Reserve should not assume it has more room to execute another round of quantitative easing. The reason the overall CPI fell in October was that energy prices dropped 2%. But now, with oil pushing $100 per barrel again, we already know energy prices will likely be up in November. Meanwhile, despite the decline in overall prices in October, the CPI is still up 3.5% from a year ago. "Cash" inflation, which excludes the government's estimate of what homeowners would pay themselves in rent, is up 4.1% in the past year. In our opinion, this is a more accurate measure of the inflation actually being felt by consumers. "Core" prices, which exclude food and energy (what the Fed seems to focus on) are up 2.1% in the past year, held down by owners' equivalent rent (up just 1.6% in the past 12 months), which makes up one-third of the core. But, because of the shift from home ownership to rental occupancy, rents are now accelerating (see chart to right). As a result, core inflation is likely to accelerate in the year ahead. The best news in today's report was that "real" (inflation-adjusted) earnings per hour were up 0.3% in October. Although these earnings are down 1.6% from a year ago, consumers have been able to increase their spending by slowing the pace at which they're paying down debt. This makes sense with consumers' financial obligations now at the smallest share of income since the early 1990s.





CPI - U *All Data Seasonally Adjusted*	Oct-11	Sep-11	Aug-11	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	**-0.1%**	0.3%	0.4%	2.4%	2.1%	3.5%
Ex Food & Energy	**0.1%**	0.1%	0.2%	1.8%	2.4%	2.1%
Ex Energy	**0.1%**	0.1%	0.3%	2.2%	2.7%	2.5%
Energy	**-2.0%**	2.0%	1.2%	4.6%	-3.2%	14.2%
Food and Beverages	**0.1%**	0.4%	0.5%	4.2%	4.0%	4.5%
Housing	**0.1%**	0.2%	0.2%	2.1%	2.1%	1.9%
Owners Equivalent Rent	**0.2%**	0.1%	0.2%	2.2%	2.1%	1.6%
New Vehicles	**-0.3%**	0.0%	0.0%	-1.5%	2.8%	3.4%
Medical Care	**0.5%**	0.2%	0.2%	3.7%	3.2%	3.1%
Services (Excluding Energy Services)	**0.2%**	0.2%	0.2%	2.4%	2.3%	2.1%
Real Average Hourly Earnings	**0.3%**	0.0%	-0.6%	-1.2%	0.2%	-1.6%

Source: U.S. Department of Labor