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August CPI

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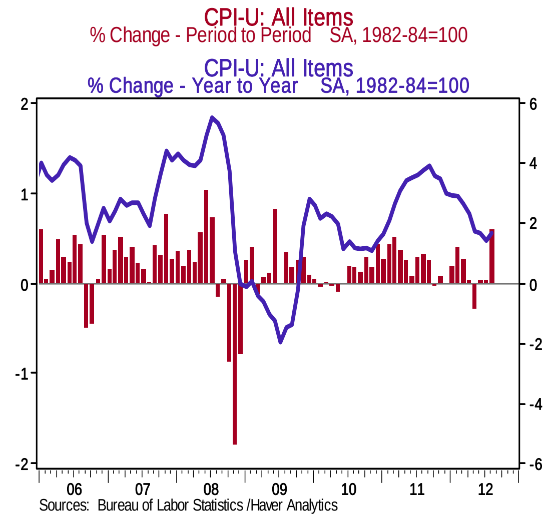
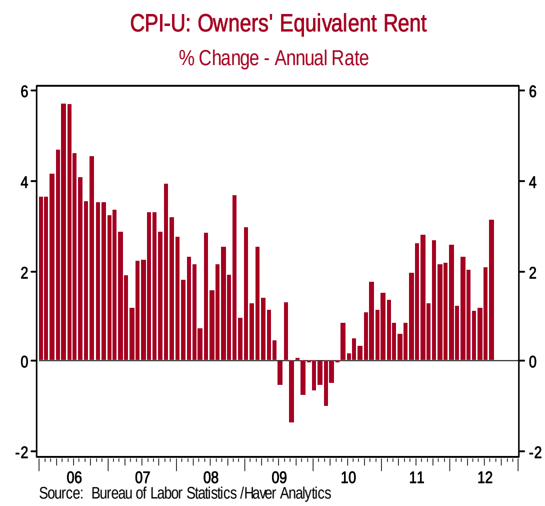
- The Consumer Price Index (CPI) was up 0.6% in August, matching consensus expectations. The CPI is up 1.7% versus a year ago.
- "Cash" inflation (which excludes the government's estimate of what homeowners would charge themselves for rent) rose 0.7% in August and is up 1.6% in the past year.
- The rise in the CPI in August was due to a 5.6% gain in energy. There were also widespread gains in most other major categories. The "core" CPI, which excludes food and energy, was up 0.1%, versus a consensus expected gain of 0.2%, and is up 1.9% versus last year.
- Real average hourly earnings – the cash earnings of all employees, adjusted for inflation – were down 0.7% in August but are unchanged in the past year. Real *weekly* earnings are up 0.3% in the past year.





Implications: Like yesterday's report on producer prices, consumer prices came back with a vengeance in August, rising 0.6%. Energy, which was up 5.6%, drove the lion's share of the price increases. Excluding energy, prices were up 0.1%, the same gain as the "core" CPI, which excludes food and energy. The overall CPI is up only 1.7% in the past year, while "core" prices are up only 1.9%, both lower than the Federal Reserve's 2% objective. But don't pop the champagne just yet. We expect inflation to pick up to 3%+ by the end of next year. Monetary policy is loose and rising housing costs (which are measured by rents, not asset values) are going to put upward pressure on the core CPI. Owners' equivalent rent was up 0.3% in August (the most for any month since 2008) and is up 2% versus a year ago. The ongoing shift from home ownership toward rental occupancy should boost this inflation measure even more in the year ahead. It's important to recognize that inflation getting above the Fed's stated objective will not change the Fed's monetary policy anytime soon. The Fed is now focused on the labor market and will allow inflation to exceed its supposed objective for a prolonged period of time. On the earnings front, "real" (inflation-adjusted) wages per hour were down 0.7% in August but are unchanged from a year ago. Worker hours are up 2% in the past year, which means their purchasing power is still growing.

CPI - U *All Data Seasonally Adjusted*	Aug-12	Jul-12	Jun-12	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	**0.6%**	0.0%	0.0%	2.8%	1.5%	1.7%
Ex Food & Energy	**0.1%**	0.1%	0.2%	1.4%	2.1%	1.9%
Ex Energy	**0.1%**	0.1%	0.2%	1.5%	2.0%	1.9%
Energy	**5.6%**	-0.3%	-1.4%	15.6%	-3.1%	-0.6%
Food and Beverages	**0.2%**	0.1%	0.2%	1.7%	1.6%	2.0%
Housing	**0.3%**	0.0%	0.1%	1.4%	1.2%	1.4%
Owners Equivalent Rent	**0.3%**	0.2%	0.1%	2.1%	2.0%	2.0%
New Vehicles	**0.2%**	-0.1%	0.2%	1.0%	2.2%	1.0%
Medical Care	**0.2%**	0.4%	0.6%	4.6%	4.4%	4.1%
Services (Excluding Energy Services)	**0.1%**	0.1%	0.2%	1.8%	2.3%	2.4%
Real Average Hourly Earnings	**-0.7%**	0.1%	0.3%	-1.2%	0.0%	0.0%

Source: U.S. Department of Labor