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January CPI

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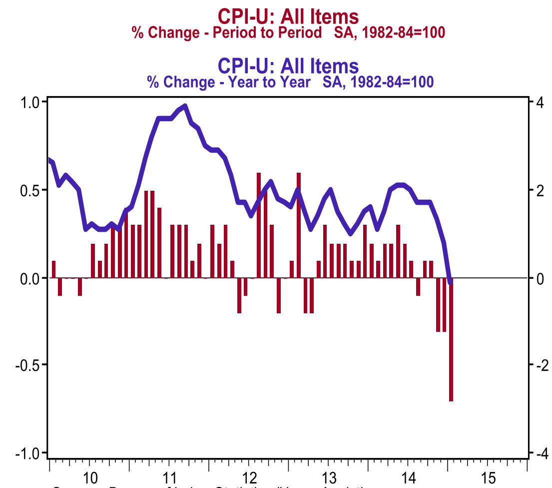
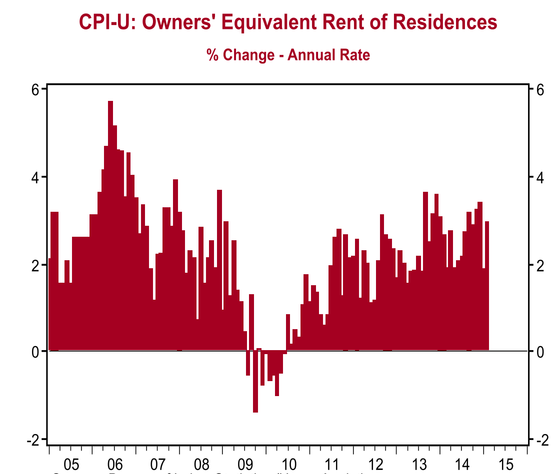
- The Consumer Price Index (CPI) declined 0.7% in January, coming in slightly below consensus expectations of -0.6%. The CPI is down 0.1% versus a year ago.
- "Cash" inflation (which excludes the government's estimate of what homeowners would charge themselves for rent) declined 1.0% in January, and is down 1.0% in the past year.
- The drop in the CPI in January was all due to energy, which fell 9.7%. Food prices were unchanged. The "core" CPI, which excludes food and energy, increased 0.2% in January versus a consensus expected gain of 0.1%. Core prices are up 1.6% versus a year ago.
- Real average hourly earnings – the cash earnings of all workers, adjusted for inflation – rose 1.2% in January and are up 2.4% in the past year. Real *weekly* earnings are up 3.0% in the past year.



Source: Bureau of Labor Statistics /Haver Analytics



Source: Bureau of Labor Statistics /Haver Analytics

Implications: With the exception of the Panic in late 2008, consumer prices fell in January at the fastest pace since 1949. As a result, the CPI is now lower than it was a year ago. Some analysts are going to use these data to warn about "Deflation" and say the Federal Reserve should hold off on raising rates. But the details of the report show we are not in the grips of deflation and the Fed should stay on track to start raising rates in June. True deflation – of the kind we ought to be concerned about – is caused by overly tight monetary policy and price declines that are widespread, not isolated to one sector of the economy. Think of the Great Depression. But we are not experiencing widespread declines in prices. The drop in consumer prices in January was all due to energy. Excluding energy, prices rose 0.1% in January and are up 1.9% from a year ago, very close to the Fed's 2% inflation target. "Core" prices, which exclude food and energy, increased 0.2% in January and are up 1.6% from a year ago. Moreover, energy prices have turned higher in February, so this sector will soon be pushing the CPI up rather than holding it down. And, there are sectors where prices are rising faster. Food prices have risen 3.2% in the past 12 months, so if you only use the supermarket to gauge inflation, we understand thinking the headline reports are too low and that "true" inflation is higher. If you love eating steak, you've been out of luck, with prices up almost 15% from a year ago. In addition, housing costs are going up. Owners' equivalent rent, which makes up about ¼ of the CPI, rose 0.2% in January, is up 2.6% in the past year, and will be a key source of higher inflation in the year ahead. The best pieces of news in today's report was that "real" (inflation-adjusted) average hourly earnings rose 1.2% in January, the fourth consecutive month of gains and the largest monthly rise since 2008. These earnings are up 2.4% from a year ago and up at a faster 4.9% annualized rate over the past six months, signaling that consumer purchasing power continues to grow.

CPI - U *All Data Seasonally Adjusted*	Jan-15	Dec-14	Nov-14	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	**-0.7%**	-0.3%	-0.3%	-5.1%	-2.4%	-0.1%
Ex Food & Energy	**0.2%**	0.1%	0.1%	1.3%	1.4%	1.6%
Ex Energy	**0.1%**	0.1%	0.1%	1.3%	1.6%	1.9%
Energy	**-9.7%**	-4.7%	-4.1%	-53.7%	-36.7%	-19.6%
Food and Beverages	**-0.1%**	0.2%	0.2%	1.6%	2.4%	3.1%
Housing	**0.1%**	0.2%	0.1%	1.9%	2.0%	2.3%
Owners Equivalent Rent	**0.2%**	0.2%	0.2%	2.5%	2.6%	2.6%
New Vehicles	**-0.1%**	0.0%	0.0%	-0.8%	0.2%	0.5%
Medical Care	**0.0%**	0.4%	0.4%	3.4%	2.6%	2.6%
Services (Excluding Energy Services)	**0.3%**	0.2%	0.2%	2.6%	2.3%	2.5%
Real Average Hourly Earnings	**1.2%**	0.1%	0.7%	8.4%	4.9%	2.4%

Source: U.S. Department of Labor