June CPI

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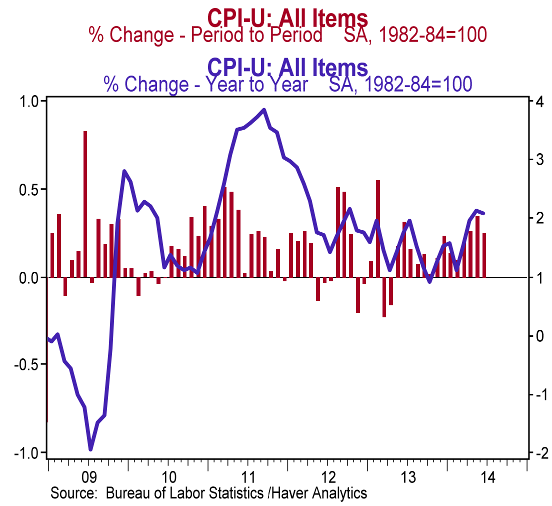
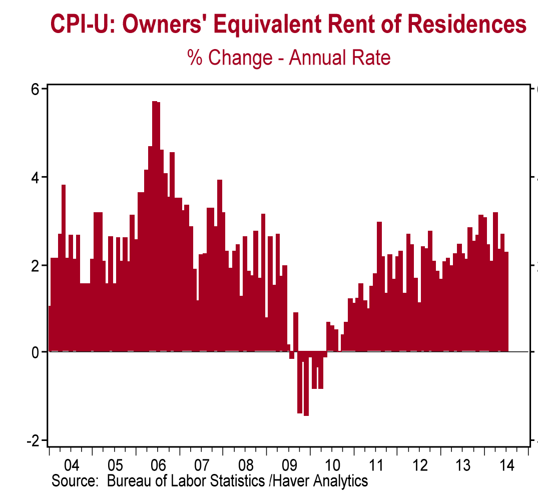
- The Consumer Price Index (CPI) increased 0.3% in June, matching consensus expectations. The CPI is up 2.1% versus a year ago.
- "Cash" inflation (which excludes the government's estimate of what homeowners would charge themselves for rent) rose 0.3% in June and is up 1.9% in the past year.
- Most of the increase in the CPI in June was due to a 1.6% rise in energy prices. Food prices increased 0.1%. The "core" CPI, which excludes food and energy, increased 0.1%, below consensus expectations of a 0.2% rise. The gain in core prices was led by shelter and core prices are up 1.9% versus a year ago.
- Real average hourly earnings – the cash earnings of all employees, adjusted for inflation – were flat in June, and are down 0.1% in the past year. Real *weekly* earnings are also down 0.1% in the past year.





Implications: In her last press conference, Janet Yellen said recent higher inflation readings weren't a problem because the data are "noisy." But, lately, that noise all seems to be coming from the direction of higher inflation. Consumer prices increased 0.3% in June, following a large 0.4% rise in May. Although consumer prices are up a moderate 2.1% from a year ago, this year-over-year number masks a real acceleration. Over the past three months, the CPI is up 3.5% at an annual rate. And if you think three months is just noise, how about the first half of the year? In the first six months of 2014, consumer prices are up 2.7% at an annual rate, a clear acceleration from the 1.5% rate seen through the first six months of 2013. Energy led the way in June, with gasoline prices, up 3.3%, accounting for two-thirds of the increase in the overall index. And while a 0.1% increase in "core" prices in June means core prices are up only 1.9% from a year ago, they are still up an annualized 2.5% in the past three months. In addition, owners' equivalent rent (the government's estimate of what homeowners would charge themselves for rent), which makes up about ¼ of the overall CPI, is up 2.6% over the past 12 months. This measure will be a key source of the acceleration in inflation in the year ahead, in large part fueled by the shift toward renting rather than owning. The worst news in today's report was that "real" (inflation-adjusted) average hourly earnings remained flat in June and are down 0.1% in the past year. Plugging today's CPI data into our models suggests the Fed's preferred measure of inflation, the PCE deflator, probably increased 0.2% in June. If so, it would be up 1.7% from a year ago, barely below the Fed's target of 2%. We expect to hit and cross the 2% target later this year, consistent with our view that the Fed starts raising short-term interest rates in the first half of 2015.

CPI - U *All Data Seasonally Adjusted*	Jun-14	May-14	Apr-14	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	**0.3%**	0.4%	0.3%	3.5%	2.7%	2.1%
Ex Food & Energy	**0.1%**	0.3%	0.2%	2.5%	2.2%	1.9%
Ex Energy	**0.1%**	0.3%	0.3%	2.7%	2.4%	2.0%
Energy	**1.6%**	0.9%	0.3%	11.9%	5.7%	3.2%
Food and Beverages	**0.0%**	0.4%	0.4%	3.4%	3.4%	2.2%
Housing	**0.1%**	0.3%	0.0%	1.6%	3.0%	2.6%
Owners Equivalent Rent	**0.2%**	0.2%	0.2%	2.5%	2.5%	2.6%
New Vehicles	**-0.3%**	0.2%	0.3%	0.6%	0.0%	0.0%
Medical Care	**0.1%**	0.3%	0.3%	3.1%	3.1%	2.6%
Services (Excluding Energy Services)	**0.1%**	0.3%	0.3%	3.1%	2.9%	2.7%
Real Average Hourly Earnings	**0.0%**	-0.1%	-0.2%	-1.2%	-0.2%	-0.1%

Source: U.S. Department of Labor