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January PPI

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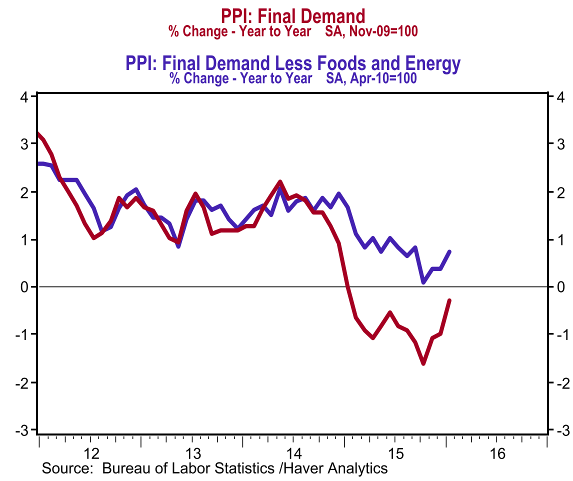
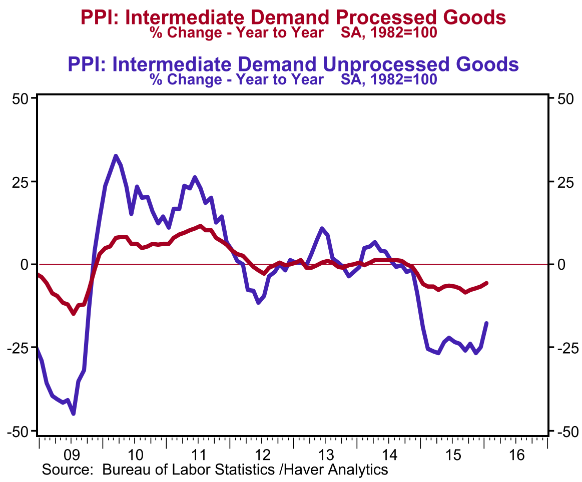
- The Producer Price Index (PPI) rose 0.1% in January, coming in above consensus expectations for a decline of 0.2%. Producer prices are down 0.2% versus a year ago.
- The rise in producer prices in January was led by final demand services, up 0.5%. Energy prices fell 5.0% in January while food prices increased 1.0%. Producer prices excluding food and energy rose 0.4%.
- In the past year, prices for services are up 0.9%, while prices for goods are down 2.6%. Private capital equipment prices rose 0.6% in January and are up 0.7% in the past year.
- Prices for intermediate processed goods declined 1.2% in January and are down 5.4% versus a year ago. Prices for intermediate unprocessed goods dropped 0.7% in January and are down 17.8% versus a year ago.





Implications: A surprise to the upside in January, as rising margins for wholesalers offset the continued decline in energy prices. Final demand services rose for a third consecutive month in January, led by machinery and equipment wholesaling. The rising pace of inflation from the service sector, up 1.3% at an annual rate in the past six months and up 4.8% at an annual rate in the past three months, comes in sharp contrast to the goods sector, where energy continues to dominate. Good prices declined 0.7% in January, as an 8.8% decline in gasoline prices pushed energy prices lower for the sixth time in seven months. Exclude just energy, and goods prices rose 0.2% in January. In the past year, goods prices are down 2.6%, but are down a more modest 0.6% excluding energy. The "core" measure of producer prices, which excludes both the volatile food and energy components, rose 0.4% in January and is up 0.6% in the past twelve months. In other words, inflation is extremely low, but the U.S. is *not* experiencing deflation. Some will argue that low headline readings on inflation are reason for the Fed to hold off further rate hikes, but we think that is a mistake. Oil prices will eventually stabilize, and when they do, inflation will move quickly towards the Feds 2% inflation target. The Fed knows that the impact from energy is temporary - they have made this abundantly clear in Fed statements and in speeches by many of the Governors – and continued strength in employment and earnings should give them confidence to keep further rate hikes on the table for the first half of 2016.

Producer Price Index *All Data Seasonally Adjusted*	Jan-16	Dec-15	Nov-15	3-mo % Ch. *annualized*	6-mo % Ch. *annualized*	Yr to Yr *% Change*
Final Demand	**0.1%**	-0.2%	0.4%	1.1%	-1.3%	-0.2%
Goods	**-0.7%**	-0.7%	0.1%	-5.1%	-6.1%	-2.6%
- Ex Food & Energy	**0.0%**	0.1%	0.0%	0.4%	-0.7%	0.0%
Services	**0.5%**	0.1%	0.5%	4.8%	1.3%	0.9%
Private Capital Equipment	**0.6%**	0.5%	0.2%	5.3%	2.2%	0.7%
Intermediate Demand						
Processed Goods	**-1.2%**	-1.0%	-0.4%	-10.2%	-9.6%	-5.4%
- Ex Food & Energy	**-0.5%**	-0.3%	-0.4%	-4.6%	-4.4%	-3.1%
Unprocessed Goods	**-0.7%**	-3.4%	-4.9%	-30.5%	-27.1%	-17.8%
- Ex Food & Energy	**0.0%**	-1.4%	-3.4%	-17.7%	-20.3%	-17.8%
Services	**1.1%**	0.1%	0.1%	5.2%	1.3%	1.5%

Source: Bureau of Labor Statistics