May PPI

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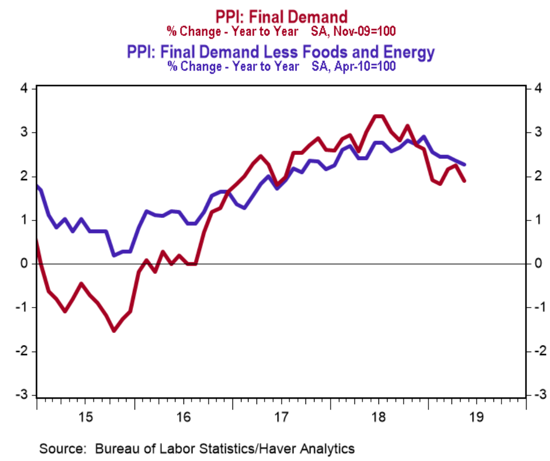
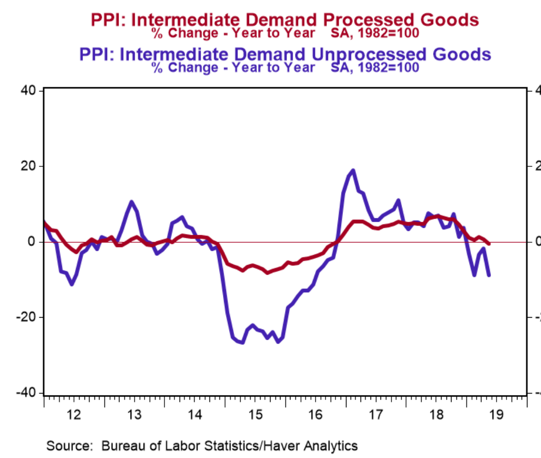
- The Producer Price Index (PPI) increased 0.1% in May, matching consensus expectations. Producer prices are up 1.8% versus a year ago.
- Energy prices fell 1.0% in April, while food prices declined 0.3%. Producer prices excluding food and energy rose 0.2% in May and are up 2.3% in the past year.
- In the past year, prices for goods are up 0.6%, while prices for services are up 2.4%. Private capital equipment prices rose 0.2% in May and are up 2.6% in the past year.
- Prices for intermediate processed goods fell 0.2% in May and are down 0.6% versus a year ago. Prices for intermediate unprocessed goods declined 5.1% in May and are down 8.9% versus a year ago.





Implications: Hold off on the details of the today's PPI report for a moment and let's talk about what today's report should mean to the Fed. Producer prices are up 1.8% in the past year (very near the Fed's 2% inflation target) and are up at a faster 3.5% annualized rate in the past three months. "Core" prices - which strip out the ever-volatile food and energy components and are a better measure of trend inflation - are up 2.3% in the past year, above the Fed's target. And when you add in the 3.6% unemployment rate and average job gains of 196,000 a month over the past year, there is no reason for the Fed to cut rates. That's not to say some dovish Fed members won't alter down their forecasts for rates through 2019 and into 2020, but the data, if anything, suggests higher rates would be the more appropriate path based on economic fundamentals alone. Fed rant over, now to the details of today's PPI report. Following a 0.6% surge in March and 0.2% increase in April, producer prices continued to rise in May, up 0.1%. But unlike the prior two months, where higher energy costs led the way, May's rise came despite a 1.0% drop in energy prices. Striping out food and energy shows core prices rose 0.2% in May, led by prices for services. As noted above, core prices have been rising faster than the Fed's 2% inflation target, and we should note that core prices have now exceeded the 2% target for twenty-two consecutive months. Within core prices, prices for services less trade, transportation, and warehousing (so think costs for things like health care, lodging, and banking) rose 0.5% in May, with guestroom rental prices in particular jumping 10.1% on the month. It's also notable that private capital equipment prices are up 2.6% in the past year, the fastest year-over-year growth of any major category, signaling continued demand for business investment. Given these readings, we think many investors are severely mistaken in their belief that the Fed's path should be lower in the months ahead. The actual data – for employment, wages, inflation, and GDP growth – are not flashing signals of tight monetary policy.

Producer Price Index *All Data Seasonally Adjusted Except for Yr to Yr*	May-19	Apr-19	Mar-19	3-mo % Ch. *annualized*	6-mo % Ch. *annualized*	Yr to Yr *% Change*
Final Demand	**0.1%**	0.2%	0.6%	3.5%	1.4%	1.8%
Goods	**-0.2%**	0.3%	1.0%	4.6%	0.3%	0.6%
- Ex Food & Energy	**0.0%**	0.0%	0.2%	0.7%	0.9%	1.6%
Services	**0.3%**	0.1%	0.3%	2.7%	1.9%	2.4%
Private Capital Equipment	**0.2%**	0.4%	0.1%	2.8%	2.8%	2.6%
Intermediate Demand						
Processed Goods	**-0.2%**	-0.1%	0.8%	1.8%	-3.3%	-0.6%
- Ex Food & Energy	**0.1%**	-0.4%	0.0%	-1.0%	-2.1%	0.3%
Unprocessed Goods	**-5.1%**	2.7%	2.3%	-1.1%	-11.6%	-8.9%
- Ex Food & Energy	**-4.5%**	-1.2%	1.2%	-17.3%	-10.8%	-8.6%
Services	**0.0%**	0.3%	0.4%	3.0%	2.0%	2.5%

Source: Bureau of Labor Statistics