

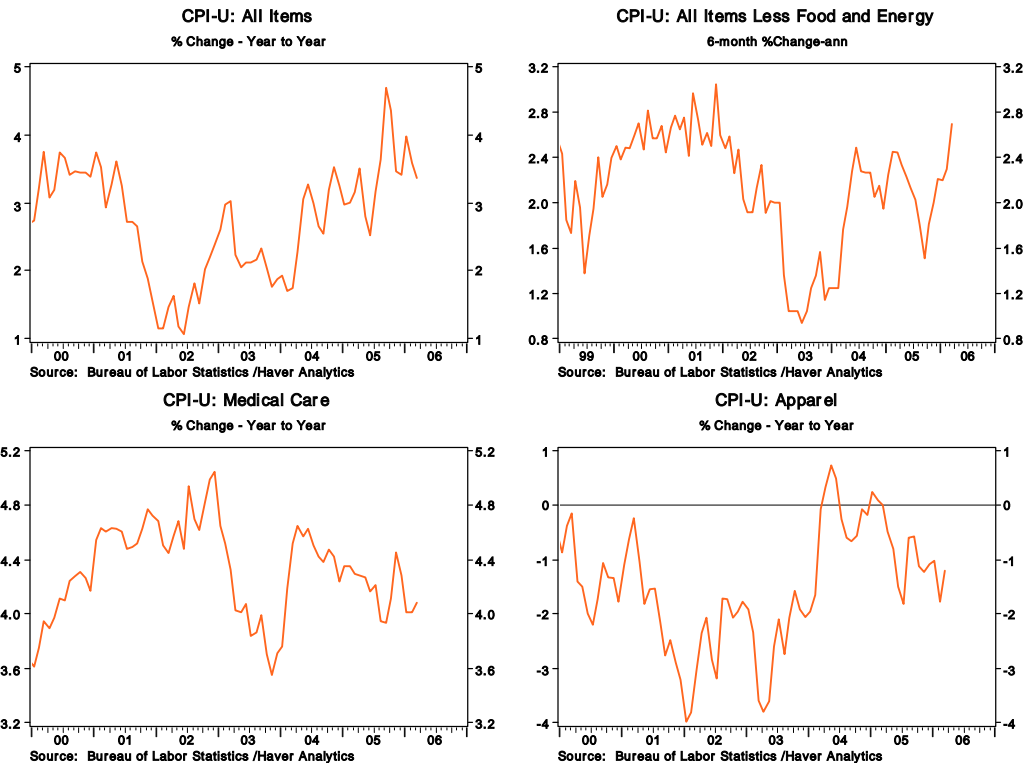
**Brian S. Wesbury**  
*Chief Economist*  
**Bill Mulvihill**  
*Senior Economist*

## MARCH CPI

- The Consumer Price Index (CPI) rose 0.4% in March versus a 0.1% increase in February. The gain was in-line with consensus expectations. The 12-month change in the CPI decelerated to 3.4% last month from 3.6% in February.
- Energy prices rose 1.3% in March after falling 1.2% in February. Food and beverage prices rose 0.1%. Excluding food and energy, the “core” CPI in March was up 0.3% (0.34% unrounded), above consensus estimates and the largest one-month gain since November 2001. “Core” consumer prices are up 2.1% in the past year.

**Implications:** “Core” consumer prices surprised on the up-side in March – increasing at the fastest rate in over four years. This comes after yesterday’s release of the minutes

from the Fed’s March 28 meeting that suggested future Fed rate hikes were becoming increasingly data dependent. Since that meeting, data has shown strong job growth, accelerating wage pressures, rising capacity utilization, and surging commodity prices (gold and silver are at 25-year highs). Now, the six-month annualized change in the “core” CPI is at a 52-month high of 2.7%. At this level, the “core” CPI is rising faster than in 1999 (when the Fed was worried about inflation). Then, as recently released transcripts show, Fed models suggested that the fed funds rate might need to rise to 8% in order to combat the inflationary threat. We are in no way suggesting that the Fed will hike the funds rate to 8% in this tightening cycle, but investors need to understand that a data dependent Fed will likely stay in a tightening mode longer than is currently expected. Given our forecast of 4% real GDP growth in 2006 and continued increases in inflation, a federal funds rate of 5.75 or 6.0% by year-end is not out of the question.



<b>CPI - U</b> <i>all data seasonally adjusted</i>	<b>Mar-06</b>	<b>Feb-06</b>	<b>Jan-06</b>	<b>3-mo % Ch.</b> <b>annualized</b>	<b>6-mo % Ch.</b> <b>annualized</b>	<b>Yr over Yr</b> <b>% Ch.</b>
<b>Consumer Price Index</b>	<b>0.4%</b>	0.1%	0.7%	4.3%	1.2%	3.4%
<b>X Food &amp; Energy</b>	<b>0.3%</b>	0.1%	0.2%	2.8%	2.7%	2.1%
<b>X Energy</b>	<b>0.2%</b>	0.2%	0.2%	2.6%	2.7%	2.2%
<b>Energy</b>	<b>1.3%</b>	-1.2%	5.0%	21.8%	-10.8%	17.3%
<b>Food and Beverages</b>	<b>0.1%</b>	0.2%	0.5%	2.7%	2.5%	2.6%
<b>Housing</b>	<b>0.2%</b>	0.1%	0.5%	3.2%	4.6%	3.7%
<b>Apparel</b>	<b>1.0%</b>	-1.0%	0.3%	1.4%	-0.3%	-1.2%
<b>Transportation</b>	<b>0.9%</b>	-0.2%	1.8%	10.5%	-8.5%	5.1%
<b>- New Vehicles</b>	<b>-0.1%</b>	0.1%	0.6%	2.3%	1.8%	-0.2%
<b>Medical Care</b>	<b>0.4%</b>	0.5%	0.1%	4.2%	4.7%	4.1%
<b>Recreation</b>	<b>0.4%</b>	0.1%	0.0%	1.8%	1.3%	1.5%
<b>Education &amp; Communication</b>	<b>0.2%</b>	0.2%	0.4%	3.2%	2.8%	2.6%
<b>Commodities</b>	<b>0.6%</b>	-0.1%	0.9%	5.3%	-3.2%	2.9%
<b>Commodities x Food &amp; Beverages</b>	<b>0.8%</b>	-0.3%	1.1%	6.9%	-6.6%	3.1%
<b>Services</b>	<b>0.2%</b>	0.2%	0.5%	3.6%	4.5%	3.8%
<b>Services x Energy Services</b>	<b>0.3%</b>	0.3%	0.2%	3.4%	3.7%	2.8%
<b>Other Goods &amp; Services</b>	<b>0.2%</b>	0.1%	0.3%	2.3%	2.7%	2.8%

Source: U.S. Department of Labor

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