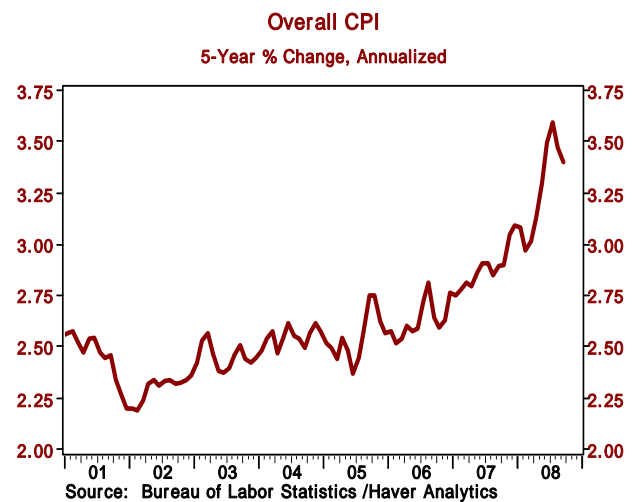
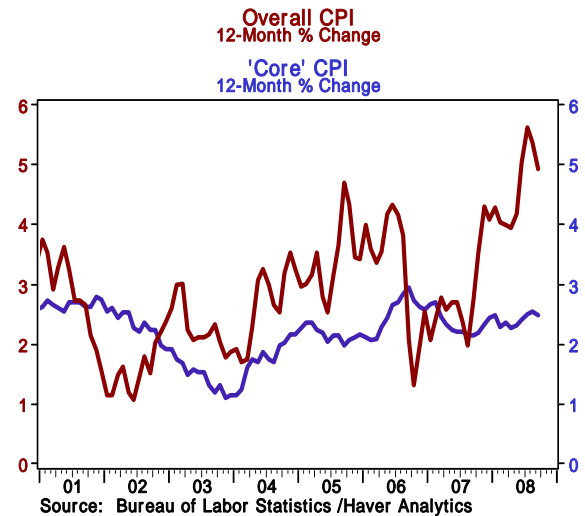


SEPTEMBER CPI

Chief Economist – Brian S. Wesbury
Senior Economist – Robert Stein, CFA

- The Consumer Price Index (CPI) was unchanged in September versus a consensus expected increase of 0.1%. The CPI is up 4.9% versus a year ago.
- Energy prices, which fell 1.9%, were the main reason for the decline in the CPI in September. Food and beverage prices were up 0.6% in September and are up 6.0% versus a year ago.
- Excluding food and energy, the “core” CPI was up 0.1% in September (0.141% unrounded) and is up 2.5% versus a year ago. Excluding energy, the CPI was up 0.2% in September and is up 3.0% versus a year ago.
- Real average hourly earnings – the cash earnings of production workers – were up 0.2% in September but are down 1.9% versus a year ago.

Implications: The 12-month percentage change in consumer price inflation peaked at 5.6% in July. Now the year-ago comparison is 4.9% and headed lower over the next few months. It is important to recognize that the underlying trend in inflation was never as high as 5.6%; we believe the underlying trend in inflation was, and still is, 3.5%+. Now, after spending the past year above the trend, CPI inflation is on the verge of spending some time below the trend. The US economy and financial system is suffering from a panic-induced sudden decline in the speed with which money makes its way through the economy (the velocity of money). The slowdown in velocity will result in both a temporary contraction in real GDP and a slowdown in inflation. However, we believe recent government actions will help unfreeze the credit markets and that once the flow of credit returns to normal, we will experience a return to both faster economic growth and higher inflation. In other news this morning, new claims for unemployment insurance dropped 16,000 last week to 461,000. Continuing claims increased 40,000 to 3.711 million, the highest since mid-2003. These data suggest further payroll declines in October.



CPI - U <i>All Data Seasonally Adjusted</i>	Sep-08	Aug-08	Jul-08	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	0.0%	-0.1%	0.8%	2.6%	5.2%	4.9%
Ex Food & Energy	0.1%	0.2%	0.3%	2.7%	2.6%	2.5%
Ex Energy	0.2%	0.3%	0.4%	3.6%	3.5%	3.0%
Energy	-1.9%	-3.1%	4.0%	-4.9%	20.9%	23.1%
Food and Beverages	0.6%	0.6%	0.9%	8.5%	8.3%	6.0%
Housing	-0.1%	-0.1%	0.6%	1.8%	3.5%	3.5%
Owners Equivalent Rent	0.2%	0.1%	0.1%	1.9%	2.0%	2.4%
New Vehicles	-0.7%	-0.6%	0.2%	-4.2%	-2.1%	-1.9%
Medical Care	0.3%	0.2%	0.1%	2.5%	2.3%	3.2%
Services (Excluding Energy Services)	0.3%	0.2%	0.3%	3.2%	3.4%	3.2%
Real Average Hourly Earnings	0.2%	0.6%	-0.6%	1.0%	-2.2%	-1.9%

Source: U.S. Department of Labor