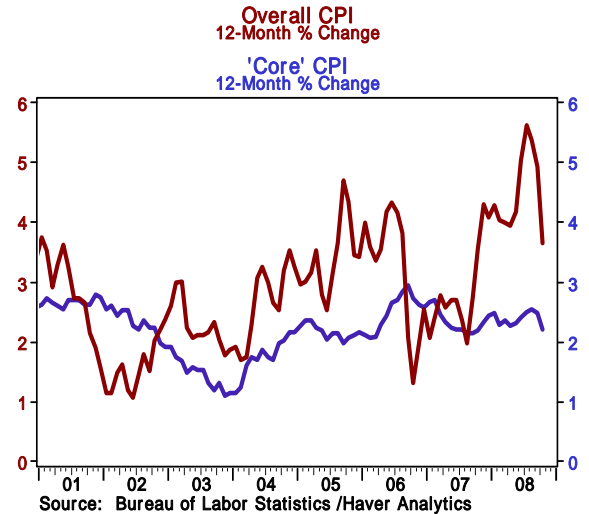


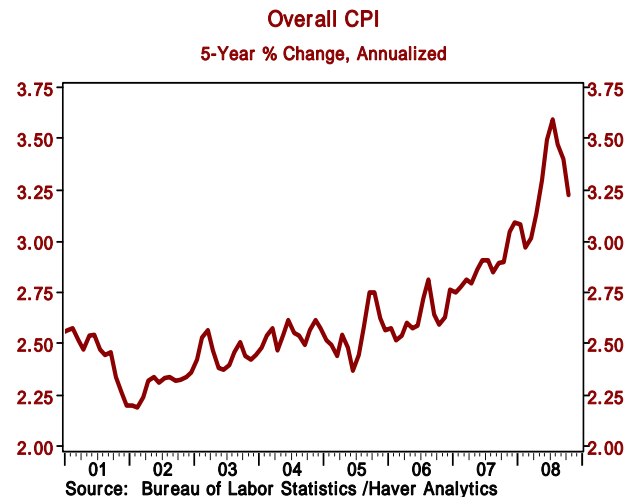
OCTOBER CPI

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- The Consumer Price Index (CPI) dropped 1.0% in October versus a consensus expected decline of 0.8%. The CPI is up 3.7% versus a year ago.
- Energy prices, which fell 8.6%, were the main reason for the decline in the CPI in October. Food and beverage prices were up 0.3% in October and are up 6.1% versus a year ago.
- Excluding food and energy, the “core” CPI was down 0.1% in October and is up 2.2% versus a year ago. Excluding energy, the CPI was unchanged in October and is up 2.8% versus a year ago.
- Real average hourly earnings – the cash earnings of production workers, adjusted for inflation – were up 1.5% in October and are up at a 9.7% annual rate in the past three months, but are still down 0.4% versus a year ago.



Implications: Consumer prices dropped 1% in October, the fastest decline since at least 1947. Although energy prices were the main reason for the drop, even “core” prices fell 0.1%, the largest monthly decline since 1982. Core prices fell due to clothing and autos. The reason for the price declines is the risk aversion hysteria which is causing a huge slowdown in the velocity of money – the speed with which money makes its way through the economy. The 12-month percentage change in consumer price inflation peaked at 5.6% in July and is now 3.7%. We expect further large declines in this measure in the months ahead. However, inflation is not dead; inflation is hibernating. Once the risk aversion hysteria passes – and loan data suggest this is starting to happen – monthly measures of inflation will pick back up. Due to the massive liquidity the Federal Reserve has injected into the financial system, inflation will again be a problem in 2010 and beyond. Meanwhile, largely as a result of falling consumer prices over the past few months, inflation-adjusted measures of worker earnings have turned around, growing at the fastest pace since the early 1970s.



CPI - U <i>All Data Seasonally Adjusted</i>	Oct-08	Sep-08	Aug-08	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	-1.0%	0.0%	-0.1%	-4.4%	2.8%	3.7%
Ex Food & Energy	-0.1%	0.1%	0.2%	1.1%	2.3%	2.2%
Ex Energy	0.0%	0.2%	0.3%	1.8%	3.0%	2.8%
Energy	-8.6%	-1.9%	-3.1%	-43.1%	1.1%	11.5%
Food and Beverages	0.3%	0.6%	0.6%	5.7%	6.9%	6.1%
Housing	0.0%	-0.1%	-0.1%	-0.9%	2.8%	3.2%
Owners Equivalent Rent	0.1%	0.2%	0.1%	2.0%	1.9%	2.3%
New Vehicles	-0.5%	-0.7%	-0.6%	-6.9%	-2.8%	-2.3%
Medical Care	0.2%	0.3%	0.2%	2.9%	2.3%	2.8%
Services (Excluding Energy Services)	0.0%	0.3%	0.2%	2.2%	3.2%	3.0%
Real Average Hourly Earnings	1.5%	0.2%	0.6%	9.7%	1.0%	-0.4%

Source: U.S. Department of Labor

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