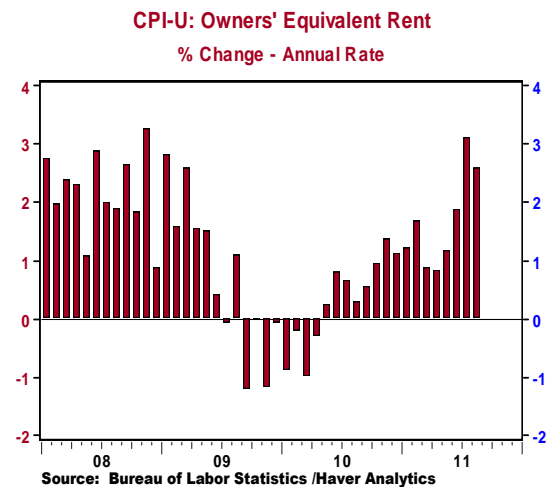
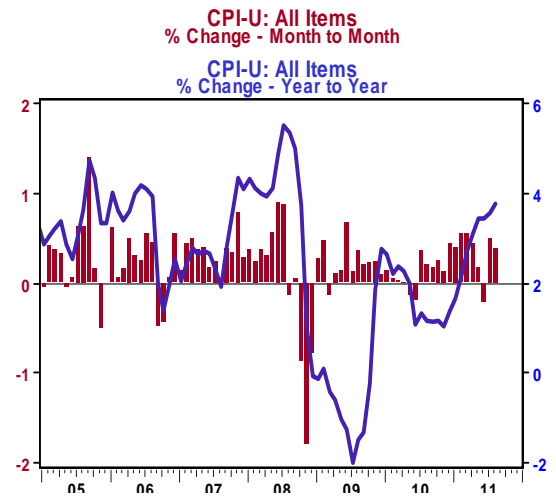


Brian S. Wesbury – Chief Economist
Robert Stein, CFA – Senior Economist
Strider Elass – Economic Analyst
Andrew Hull – Economic Analyst

August CPI

- The Consumer Price Index (CPI) rose 0.4% in August versus a consensus expected increase of 0.2%. The CPI is up 3.8% versus a year ago.
- “Cash” inflation (which excludes the government’s estimate of what homeowners would charge themselves for rent) also rose 0.4% in August and is up 4.5% in the past year.
- Gains in consumer prices were widespread. Energy prices increased 1.2%, food prices were up 0.5% and the “core” CPI, which excludes food and energy, was up 0.2%, matching consensus expectations. Core prices are up 2.0% versus last year.
- Real average hourly earnings – the cash earnings of all employees, adjusted for inflation – fell 0.6% in August and are down 1.9% in the past year. Real *weekly* earnings are down 1.8% in the past year.

Implications: Consumer price inflation came in well above consensus expectations for August, the second month of hot readings. Consumer prices are now up 3.8% versus a year ago. This should make it clear to the Federal Reserve that an easy monetary policy is taking a toll on the US economy in the form of higher inflation. It should also give them great pause before embarking on any measures to ease monetary policy further. The Fed is likely to discuss these measures at its meeting next week. Before today’s data, the Fed appeared to be moving toward a program of buying more longer-maturity treasury securities. We believe this would be a mistake. The Fed has hidden behind relatively low readings for “core” inflation, which excludes food and energy, to justify its accommodative policy. But that dog will no longer hunt. Core prices are up 2.0% from a year ago (at the top of the Fed’s so-called target range), at a 2.7% annual rate in the past six months and a 2.9% annual rate in the past three months. “Cash” inflation, which excludes the government’s estimate of what homeowners would pay themselves in rent, is up 4.5% in the past year. Cash inflation is more indicative of the inflation actually being felt by consumers. In other news this morning, new claims for unemployment benefits rose 11,000 last week to 428,000. The four-week moving average is 420,000 versus 440,000 in May. Continuing claims for regular state benefits fell 12,000 to 3.73 million. High-frequency indicators, like claims, provide real-time data on economic activity. The increase in claims reflects the same problems with employment we have seen in the past two years, not a double-dip in economic activity.



Source: Bureau of Labor Statistics /Haver Analytics

CPI - U <i>All Data Seasonally Adjusted</i>	Aug-11	Jul-11	Jun-11	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	0.4%	0.5%	-0.2%	2.6%	3.6%	3.8%
Ex Food & Energy	0.2%	0.2%	0.3%	2.9%	2.7%	2.0%
Ex Energy	0.3%	0.3%	0.2%	3.2%	3.1%	2.3%
Energy	1.2%	2.8%	-4.4%	-2.3%	8.4%	18.4%
Food and Beverages	0.5%	0.4%	0.2%	4.4%	5.3%	4.4%
Housing	0.2%	0.2%	0.1%	2.1%	2.1%	1.6%
Owners Equivalent Rent	0.2%	0.3%	0.2%	2.5%	1.7%	1.4%
New Vehicles	0.0%	0.0%	0.6%	2.6%	6.6%	3.8%
Medical Care	0.2%	0.2%	0.2%	2.7%	3.0%	3.2%
Services (Excluding Energy Services)	0.2%	0.2%	0.1%	2.2%	2.1%	1.9%
Real Average Hourly Earnings	-0.6%	0.0%	0.2%	-1.6%	-1.7%	-1.9%

Source: U.S. Department of Labor