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December 14, 2012 • 630.517.7756 • www.ftportfolios.com

November CPI

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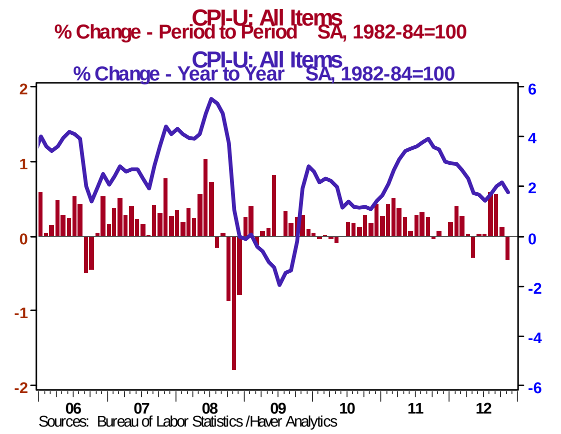
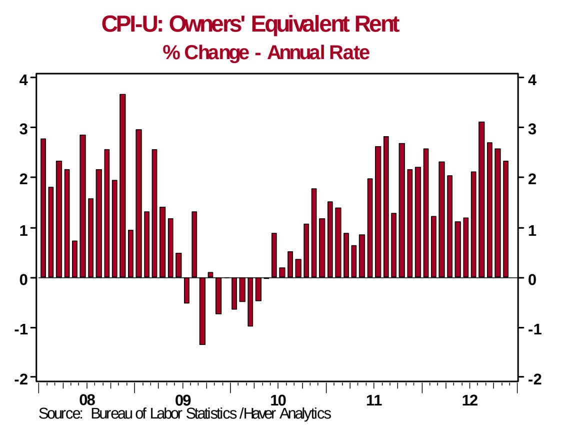
- The Consumer Price Index (CPI) declined 0.3% in November, coming in slightly below the consensus expected -0.2%. The CPI is up 1.8% versus a year ago.
- "Cash" inflation (which excludes the government's estimate of what homeowners would charge themselves for rent) fell 0.5% in November but is up 1.7% in the past year.
- All of the decline in the CPI in November can be attributed to energy prices, which fell 4.1%. Food prices rose 0.2%. The "core" CPI, which excludes food and energy, was up 0.1% in November and is up 1.9% versus a year ago. The consensus expected gain of 0.2% in November.
- Real average hourly earnings – the cash earnings of all employees, adjusted for inflation – were up 0.5% in November but are unchanged in the past year. Real *weekly* earnings are down 0.1% in the past year.





Implications: For now, Ben Bernanke is smiling because all is quiet on the inflation front. Consumer prices fell 0.3% in November, falling short of consensus expectations and are up only 1.8% from a year ago. "Core" prices, which exclude food and energy, were up only 0.1% in November, also coming in lower than consensus expectations, and are up 1.9% from a year ago. Neither figure sets off alarm bells. Instead, they suggest the Federal Reserve's preferred measure of inflation, the PCE deflator (which usually runs a ¼ point below the CPI) remains below the Fed's target of 2%. We don't expect this to last. With nominal GDP growth – real GDP growth plus inflation – running at 4%+, a federal funds rate at essentially zero will generate higher rates of inflation in the year ahead. Look for housing, which makes up about 30% of the CPI, to be a large contributor to higher inflation in the next few years. It's important to recognize that the Fed will not start raising rates just because inflation gets above its target of 2%. For the Fed, the key measure of inflation is its own forecast of future inflation. So even if inflation goes to roughly 3% next year, as long as the Fed projects the rise to be temporary it will not react by raising short-term interest rates. The Fed is more focused on the labor market and, we believe, is willing to let inflation exceed its long-term target of 2% for a prolonged period of time. The best news in today's report was that real average hourly earnings rose 0.5% in November, the largest rise since December 2008. This, as well as job growth and low financial obligations by households, will help support growth in consumer spending in the year ahead.

CPI - U *All Data Seasonally Adjusted*	Nov-12	Oct-12	Sep-12	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	**-0.3%**	0.1%	0.6%	1.6%	2.2%	1.8%
Ex Food & Energy	**0.1%**	0.2%	0.1%	1.8%	1.6%	1.9%
Ex Energy	**0.1%**	0.2%	0.1%	1.8%	1.6%	1.9%
Energy	**-4.1%**	-0.2%	4.5%	-0.2%	7.4%	0.3%
Food and Beverages	**0.2%**	0.2%	0.1%	2.0%	1.8%	1.8%
Housing	**0.3%**	0.2%	0.3%	3.1%	2.3%	1.7%
Owners Equivalent Rent	**0.2%**	0.2%	0.2%	2.6%	2.4%	2.1%
New Vehicles	**0.2%**	-0.1%	-0.1%	-0.3%	0.4%	1.4%
Medical Care	**0.1%**	0.0%	0.3%	1.5%	3.1%	3.4%
Services (Excluding Energy Services)	**0.2%**	0.3%	0.3%	2.9%	2.4%	2.5%
Real Average Hourly Earnings	**0.5%**	-0.2%	-0.2%	0.4%	-0.4%	0.0%

Source: U.S. Department of Labor