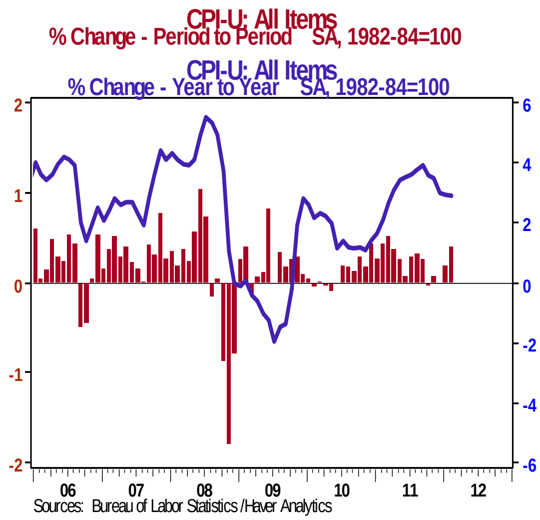
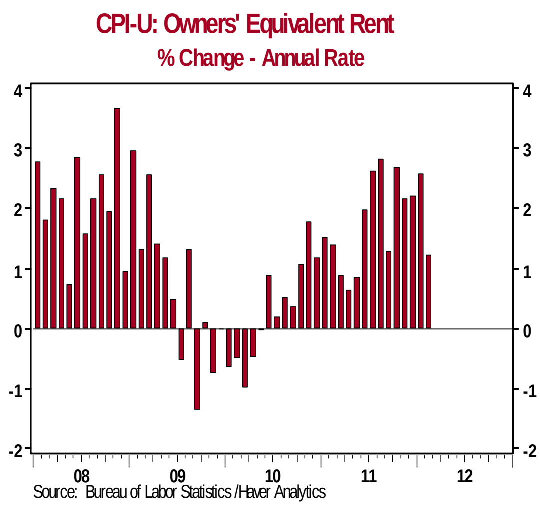
First Trust DATAWATCH
March 16, 2012 • 630.517.7756 • www.ftportfolios.com

February CPI

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

- The Consumer Price Index (CPI) increased 0.4% in February exactly as consensus expected. The CPI is up 2.9% versus a year ago.
- "Cash" inflation (which excludes the government's estimate of what homeowners would charge themselves for rent) was up 0.5% in February, and is up 3.2% in the past year.
- The increase in the CPI was mainly due to a 3.2% gain in energy. Most other categories also rose. The "core" CPI, which excludes food and energy, was up 0.1%, coming in below consensus expectations, but is up 2.2% versus last year.
- Real average hourly earnings – the cash earnings of all employees, adjusted for inflation – were down 0.3% in February and are down 1.1% in the past year. Real *weekly* earnings are down 0.4% in the past year.





Implications: Consumer prices rose 0.4 percent in February, matching consensus expectations and the most in ten months. Energy led the way as the big jump in gas prices accounted for about 80% of the increase in February's report. In the past three months, energy prices have risen at a 8.1% annual rate while overall consumer prices are up at a 2.5% annual rate. This is a stark contrast to the same three months a year ago, when energy prices were rising at a 32.8% annual rate and consumer prices were rising at a 4.8% rate. As a result, year-ago price comparisons have been decelerating. Back in October, consumer prices were up 3.6% from a year ago; now prices are up 2.9% from a year ago. This deceleration is likely to continue into the Spring, which means prices will still be rising, but not as quickly as they were the same time a year ago. However, do not expect the respite from higher inflation to last. Monetary policy is very loose and we are already seeing oil and gas prices continue to move higher. In addition, housing costs (which are measured by rents, not asset values) are rising as well. Owners' equivalent rent, was up 0.1% in February and is up at a 2.0% annual rate in the past six months. The ongoing shift from home ownership toward rental occupancy should boost this inflation measure even more in the year ahead. Meanwhile, "core" inflation, at 2.2% in the past year, is above the Federal Reserve's target. With loose monetary policy and housing costs accelerating, it's hard to see core inflation getting back down to the Fed's 2% target anytime soon. On the earnings front, "real" (inflation-adjusted) wages per hour were down 0.3% in February. Although these earnings are down 1.1% from a year ago, the number of hours worked is up 2.7%, giving consumers more purchasing power. No justification here for a third round of quantitative easing.

CPI - U *All Data Seasonally Adjusted*	Feb-12	Jan-12	Dec-11	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	**0.4%**	0.2%	0.0%	2.5%	1.9%	2.9%
Ex Food & Energy	**0.1%**	0.2%	0.1%	1.9%	1.8%	2.2%
Ex Energy	**0.1%**	0.2%	0.2%	1.8%	1.9%	2.4%
Energy	**3.2%**	0.2%	-1.3%	8.1%	2.1%	7.0%
Food and Beverages	**0.1%**	0.2%	0.2%	1.9%	2.3%	3.8%
Housing	**0.1%**	0.1%	0.1%	1.5%	1.7%	1.8%
Owners Equivalent Rent	**0.1%**	0.2%	0.2%	2.0%	2.0%	1.8%
New Vehicles	**0.6%**	0.0%	-0.2%	1.6%	-0.2%	3.0%
Medical Care	**0.2%**	0.3%	0.3%	3.4%	3.7%	3.4%
Services (Excluding Energy Services)	**0.1%**	0.2%	0.2%	2.3%	2.4%	2.2%
Real Average Hourly Earnings	**-0.3%**	-0.1%	0.1%	-1.2%	-0.4%	-1.1%

Source: U.S. Department of Labor