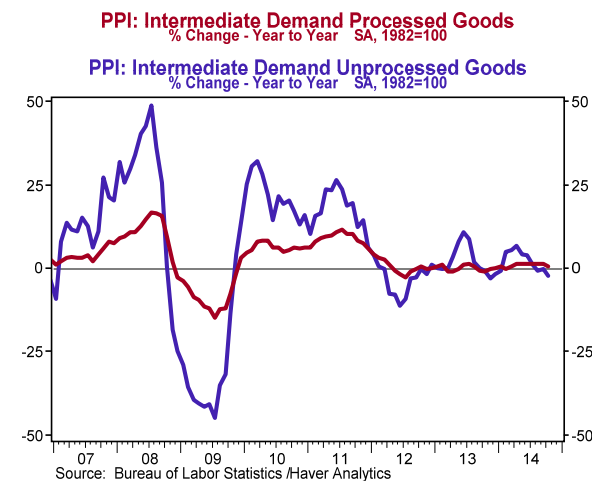
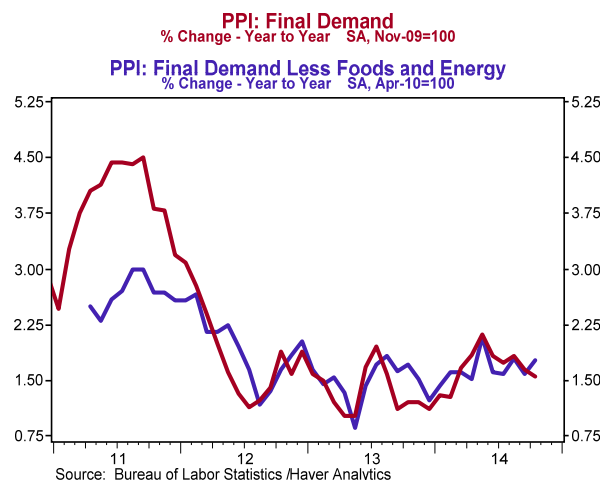


October PPI

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- The Producer Price Index (PPI) rose 0.2% in October, coming in well above the consensus expected decline of 0.1%. Producer prices are up 1.5% versus a year ago.
- Final demand services, up 0.5% in October, led the index higher, more than offsetting a 3.0% decline in final demand energy costs. Producer prices excluding food and energy rose 0.4% in October.
- In the past year, prices for services are up 1.8%, while prices for goods are up 1.1%. Private capital equipment prices rose 0.4% in October and are up 1.4% in the past year.
- Prices for intermediate processed goods declined 0.9% in October, but are up 0.4% versus a year ago. Prices for intermediate unprocessed goods fell 2.4% in October, and are down 2.0% versus a year ago.

Implications: Producer prices surprised to the upside in October versus consensus expectations for a slight decline due to falling energy prices. The gain in overall producer prices was all due to the services sector, where prices rose 0.5%. Oddly, about half of the gain in service prices was due to refiners generating fatter margins while the energy prices fell. In other words, the drop in energy prices did not get fully passed on to users. Meanwhile, it's the same old story for prices of energy goods, which fell 3% in October and are down 3.7% in the past year, a testament to fracking and horizontal drilling. Overall, today's report is consistent with our forecast that the US isn't going to suffer either hyperinflation or deflation. Instead, it's going to be a slow slog upward for inflation. Prices further back in the production pipeline (intermediate demand) show that it will take a while for inflation to move up high enough for the Federal Reserve to take notice. Prices for intermediate processed goods are up only 0.4% in the past year and unprocessed goods are down 2% in the past year. Regardless, with the labor market improving more rapidly now that extended unemployment benefits are done, the Fed is still on track to start raising rates around the middle of next year. These rate hikes will not hurt the economy; monetary policy will still be loose. The problems that ail the economy are fiscal and regulatory in nature, which can't be addressed by the Fed. In other news this morning, the NAHB index, which measures confidence among home builders, rose to 58 in November from 54 in October, with largest gain for current single-family sales. The housing recovery remains on track.



Producer Price Index <i>All Data Seasonally Adjusted</i>	Oct-14	Sep-14	Aug-14	3-mo % Ch. <i>annualized</i>	6-mo % Ch. <i>annualized</i>	Yr to Yr <i>% Change</i>
Final Demand	0.2%	-0.1%	0.0%	0.4%	1.3%	1.5%
Goods	-0.4%	-0.2%	-0.3%	-3.8%	-1.0%	1.1%
- Ex Food & Energy	-0.1%	0.2%	0.0%	0.4%	0.9%	1.7%
Services	0.5%	-0.1%	0.3%	2.6%	2.4%	1.8%
Private Capital Equipment	0.4%	0.3%	0.0%	2.6%	0.7%	1.4%
Intermediate Demand						
Processed Goods	-0.9%	0.1%	-0.3%	-4.4%	-1.4%	0.4%
- Ex Food & Energy	-0.2%	0.2%	0.2%	1.0%	1.0%	1.4%
Unprocessed Goods	-2.4%	0.6%	-3.3%	-19.1%	-16.4%	-2.0%
- Ex Food & Energy	-2.9%	0.5%	-0.7%	-12.0%	-9.2%	-1.0%
Services	0.1%	0.0%	0.2%	1.1%	1.7%	1.5%

Source: Bureau of Labor Statistics