First Trust DATAWATCH

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January PPI

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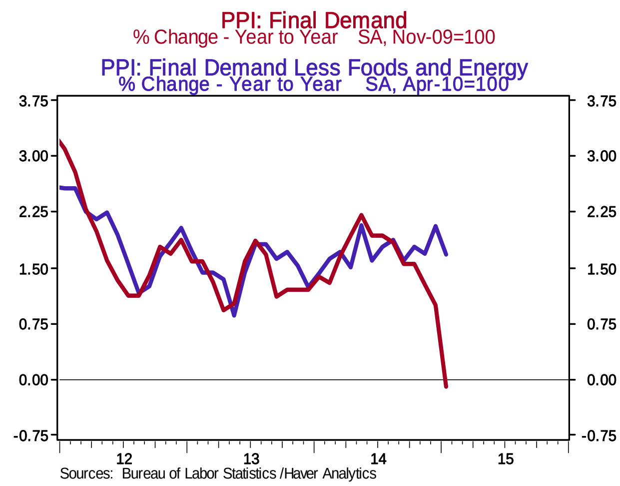
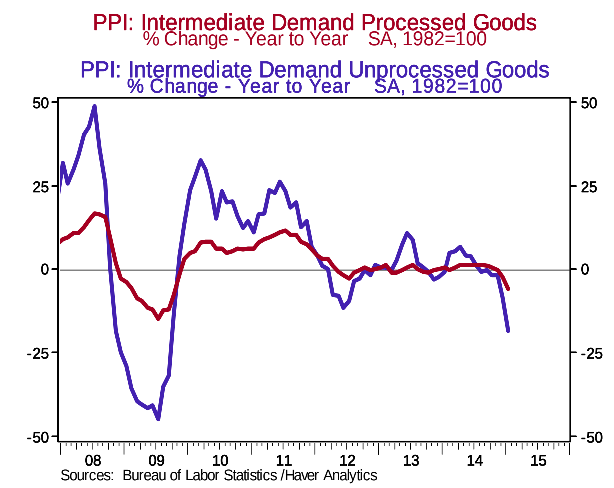
- The Producer Price Index (PPI) dropped 0.8% in January, coming in below the consensus expected decline of 0.4%. Producer prices are down 0.1% versus a year ago.
- Energy prices led the index lower, down 10.3%. Food prices fell 1.1%. Producer prices excluding food and energy slipped 0.1% in January (-0.2% among just goods).
- In the past year, prices for services are up 1.9%, while prices for goods are down 3.9%. Private capital equipment prices rose 0.1% in January and are up 1.3% in the past year.
- Prices for intermediate processed goods declined 2.8% in January, and are down 5.7% versus a year ago. Prices for intermediate unprocessed goods fell 9.4% in January, and are down 18.4% versus a year ago.





Implications: Absolutely no sign of inflation in January, with price declines led by energy but also showing up in food and other products as well. Prices for final demand goods fell for a seventh consecutive month. That's no surprise given the big drop in oil prices. But prices in the service sector fell for the first time since September 2014. The decline in overall producer prices can be primarily attributed to energy, which fell 10.3% in January and is down 22.8% versus a year ago, a testament to fracking and horizontal drilling. That trend won't last forever; in fact crude prices in February are currently up more than 15% from their January lows. As a result, our forecast remains that that the US suffers neither hyperinflation nor deflation. Instead, it's going to be a slow slog upward for inflation. "Core" prices, which exclude food and energy, show deflation is not setting in. Although they slipped 0.1% in January, they're up 1.6% in the past year. However, prices further up the production pipeline remain subdued. Prices for intermediate processed goods are down 5.7% in the past year while prices for unprocessed goods are down 18.4%. Regardless, with the labor market improving, we still believe the Fed is on track to start raising rates in June. These rate hikes will not hurt the economy; monetary policy will still be loose and will likely remain that way for the first couple of years of higher short-term rates. Counterintuitively, higher short term rates may boost lending as potential borrowers hurry up their plans to avoid even higher interest rates further down the road. In other words, the Plow Horse economy won't stop when the Fed shifts gears. In other recent news, a strengthened US dollar continues to impact trade. Import prices fell 2.8% in January, and were down 8% from a year ago. Most of the drop is due to lower oil prices, but import prices are still down 1.2% from a year ago even when petroleum is excluded. Export prices fell 2% in January and are down 5.4% from a year ago. So, like producer prices, no sign of inflation in the trade sector.

Producer Price Index *All Data Seasonally Adjusted*	Jan-15	Dec-14	Nov-14	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Final Demand	**-0.8%**	-0.2%	-0.2%	-4.6%	-2.5%	-0.1%
Goods	**-2.1%**	-1.1%	-0.7%	-14.9%	-9.2%	-3.9%
- Ex Food & Energy	**-0.2%**	0.1%	0.0%	-0.4%	0.0%	0.6%
Services	**-0.2%**	0.3%	0.2%	1.1%	0.9%	1.9%
Private Capital Equipment	**0.1%**	0.0%	0.2%	1.1%	0.7%	1.3%
Intermediate Demand						
Processed Goods	**-2.8%**	-1.6%	-1.0%	-19.6%	-12.2%	-5.7%
- Ex Food & Energy	**-1.3%**	-0.6%	-0.5%	-8.9%	-4.2%	-1.4%
Unprocessed Goods	**-9.4%**	-4.6%	-1.4%	-47.4%	-36.0%	-18.4%
- Ex Food & Energy	**-0.7%**	-0.4%	-1.7%	-10.8%	-11.3%	-7.6%
Services	**-0.2%**	0.1%	0.2%	0.4%	0.4%	1.2%

Source: Bureau of Labor Statistics

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