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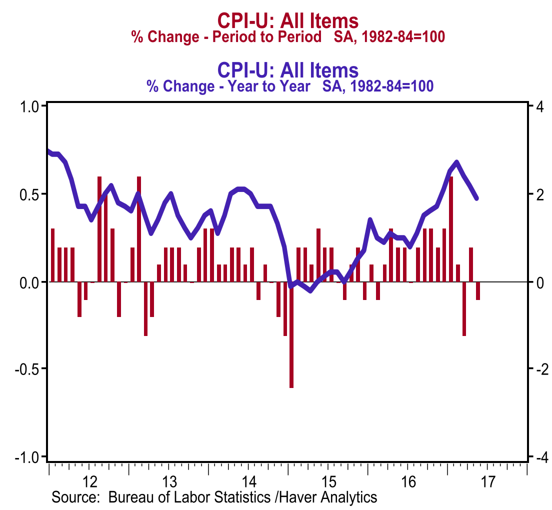
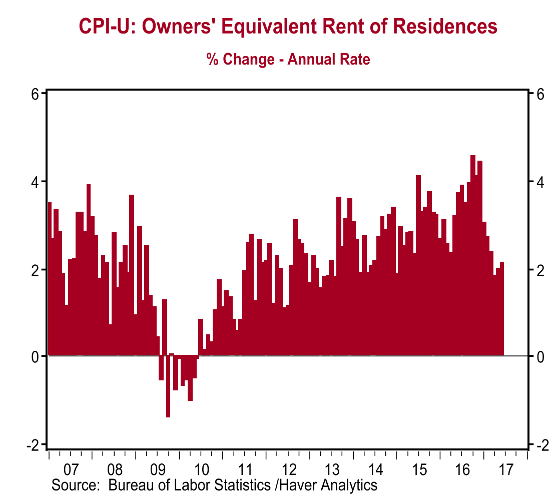
May CPI

Brian S. Wesbury – Chief Economist
Robert Stein, CFA – Dep. Chief Economist
Strider Elass – Economist

- The Consumer Price Index (CPI) declined 0.1% in May, coming in below the consensus expectation of no change. The CPI is up 1.9% from a year ago.
- "Cash" inflation (which excludes the government's estimate of what homeowners would charge themselves for rent) declined 0.2% in May but is up 1.5% in the past year.
- Energy prices fell 2.7% in May, while food prices rose 0.2%. The "core" CPI, which excludes food and energy, increased 0.1% in May, slightly below the consensus expected rise of 0.2%. Core prices are up 1.7% versus a year ago.
- Real average hourly earnings – the cash earnings of all workers, adjusted for inflation – rose 0.3% in May and are up 0.6% in the past year. Real average weekly earnings are also up 0.6% in the past year.



Implications: Consumer prices fell 0.1% in May, but the decline should do little to sway the Fed's decision to raise rates by 0.25% later today. Consumer prices are up 1.9% in the past year, compared to a 1.0% increase in the twelve months ending May 2016 and no change for the period ending May 2015. In other words, inflation is still in a rising trend. Energy prices led the index lower in May, falling 2.7%, while rising costs for nonalcholoic beverages, meats, and poultry pushed food prices up 0.2%. Stripping out the volatile food and energy components, the "core" CPI rose 0.1% in May and is up 1.7% in the past year. Housing led "core" prices higher in May, gaining 0.2%, more than offsetting declines in medical and apparel costs. The best news in today's report is that real average hourly earnings rose 0.3% in May. These earnings are up a modest 0.6% over the past year, but they're up at a 0.9% annual rate over the past six months and a 2.6% annual rate over the past three. This acceleration signals that a loose monetary policy has led to a tighter labor market. Because the Fed believes in the Phillips Curve, the trend of accelerating price and wage gains should have Fed officials focusing more on the potential for inflation to rise faster than desired as the jobless rate continues to fall below their long-term target. That's why we expect the Fed to raise rates twice more in 2017, once today and again in September. Then, in the fourth quarter, we expect the Fed to start unwinding the bloated Fed balance sheet that ballooned during early episodes of quantitative easing.



CPI - U *All Data Seasonally Adjusted Except for Yr to Yr*	May-17	Apr-17	Mar-17	3-mo % Ch. annualized	6-mo % Ch. annualized	Yr to Yr % Change
Consumer Price Index	**-0.1%**	0.2%	-0.3%	-1.0%	1.4%	1.9%
Ex Food & Energy	**0.1%**	0.1%	-0.1%	0.0%	1.5%	1.7%
Ex Energy	**0.1%**	0.1%	-0.1%	0.5%	1.6%	1.6%
Energy	**-2.7%**	1.1%	-3.2%	-17.7%	-1.5%	5.4%
Food	**0.2%**	0.2%	0.3%	2.8%	2.1%	0.9%
Housing	**0.2%**	0.3%	0.1%	2.4%	2.9%	3.1%
Owners Equivalent Rent	**0.2%**	0.2%	0.2%	2.4%	2.8%	3.3%
New Vehicles	**-0.2%**	-0.2%	-0.3%	-2.5%	0.2%	0.3%
Medical Care	**0.0%**	-0.2%	0.1%	-0.1%	1.0%	2.7%
Services (Excluding Energy Services)	**0.2%**	0.1%	-0.1%	1.0%	2.2%	2.6%
Real Average Hourly Earnings	**0.3%**	0.0%	0.4%	2.6%	0.9%	0.6%

Source: U.S. Department of Labor