



Economics Group

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CPI Inflation Rises Modestly in March

CPI came in softer than expected in March with both the headline and core indices rising 0.1 percent. Even with the softer figures, the trend remains upward and could test the Fed's stance on data dependency in June.

Headline Rising Again, Core Index Gets Some Payback

Consumer price inflation rose 0.1 percent in March, slightly below market expectations for a 0.2 percent gain. The CPI was the third inflation report this week to come in softer than expected (import prices and producer prices also missed) and highlights that while inflation is picking up, the overall price environment remains soft.

The March report marks the first gain in the headline CPI since last November. As expected, the headline was boosted by a rebound in energy prices, which rose 0.9 percent. Higher gasoline prices, up 2.2 percent after seasonal adjustment, helped boost the energy index to its largest monthly increase since last May, while energy services rose a more modest 0.2 percent. Food prices, on the other hand, were a drag on the headline. The food at home index fell 0.5 percent on broad declines among major grocery categories, including the largest monthly decline in the particularly volatile fruits and vegetables category in more than a decade.

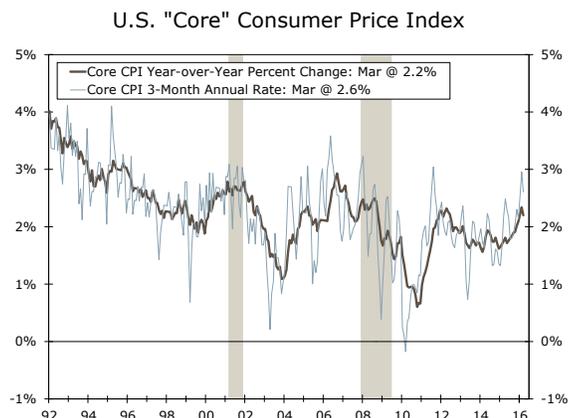
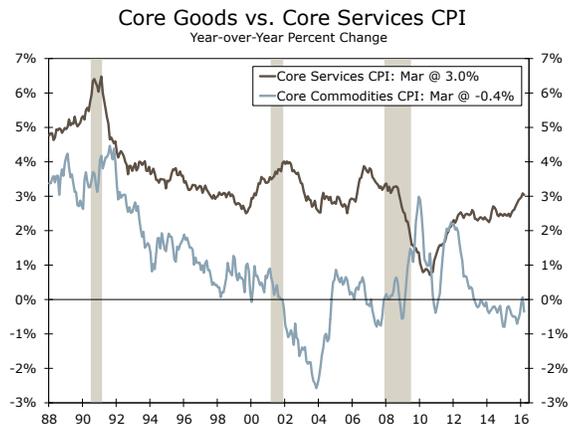
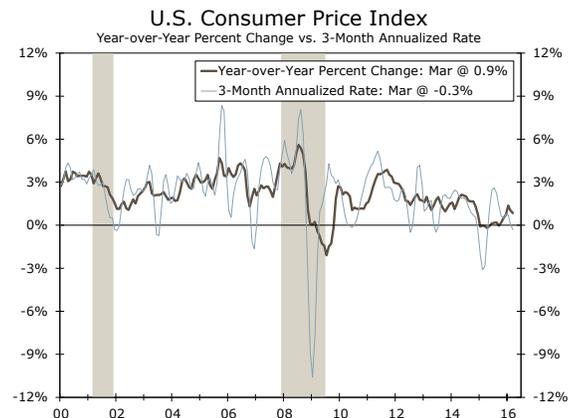
After posting the strongest two-month performance since mid-2006, the core CPI rose 0.1 percent in March. Even with the payback, the index has risen at a 2.6 percent annualized pace over the past three months. The divergence between core goods and core services inflation resumed last month, with core goods slipping 0.2 percent on lower prices for apparel, household furnishings and used vehicles. Core services edged up 0.2 percent with continued gains in shelter, medical care, transportation, education and personal care services.

Upward Trend Could Test the Fed's Mantra of Data Dependency

While the March rise in core CPI was more modest than the previous two months, the trend in core inflation is still strengthening. On a year-over-year basis, core CPI is up 2.2 percent compared to 1.8 percent last March. Moreover, the three month annualized rate of change has been running above the 12-month change for six months now, indicating a further rise in the year-over-year figure is ahead.

Although the Fed prefers the PCE deflator, the core CPI's upward trend is another sign of inflation quickly moving back to levels more consistent with the Fed's goals. The March PCE inflation figures will not be released for another two weeks, but core PCE through February was up 1.7 percent year over year versus a 1.3 percent rate as recently as October.

With the labor market continuing to make solid strides, a June rate rise looks increasingly viable if the Fed sticks to its stance of data dependence. However, with global considerations appearing to take on greater importance in FOMC policy deliberations, we also see a possibility of the Fed tolerating a further pickup in inflation before moving ahead with normalization.



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