

CPI: Drivin' To Distraction

U.S. consumer prices rose an expected 0.2% in September, led by a surprising increase in auto prices. New vehicle prices rose 0.4%, a partial bounce-back from the cash-for-clunkers related decline in August. Meantime, used vehicle prices jumped for the second straight month (1.6%), likely due to less supply amid the widespread scrapping of older vehicles. Given the post-clunkers hangover and generally soft demand, auto prices are likely to downshift quickly in coming months. Unfortunately, the same can't be said for health care costs, which have picked up recently (for both prescription drugs and hospital services). They rose 0.4% in September, and the three-month annualized rate is running slightly above the 3.5% y/y rate. As a result, the core CPI rose a larger-than-expected 0.2% in the month. However, beyond health care, most prices remain subdued. Clothing prices have changed little in the past two months. Most importantly, rents, which make up almost 40% of the core index, are falling for the first time in 17 years due to a near quarter-century high apartment vacancy rate. Though not in the core measure, food costs also eased in the month and remain slightly below year-ago levels.

The yearly rate of decline in headline inflation slowed a bit to -1.3%, and will almost certainly turn positive by November as last year's big declines in energy prices drop out of the calculation. Meantime, the annual core rate edged up for the first time in five months, to 1.5%, but remains a full percentage point below last year's cyclical high.

(seasonally adjusted)	(month/month % change)			(% change : a.r.)	
	Sep	Aug	Jul	6-month	12-month
All Items	0.2	0.4	0.0	2.9	-1.3
Ex. Food & Energy	0.2	0.1	0.1	1.9	1.5
Food	-0.1	0.1	-0.3	-1.3	-0.2
Energy	0.6	4.6	-0.4	21.6	-21.6
Clothing	0.1	-0.1	0.6	2.0	1.1
Transportation	0.8	2.3	0.2	16.9	-9.8
New Vehicles	0.4	-1.3	0.5	2.3	1.6
Gasoline	1.0	9.1	-0.8	65.4	-29.7
Medical Care	0.4	0.3	0.2	3.6	3.5
Recreation	-0.1	0.1	0.0	0.1	0.5
Education	0.0	0.5	0.5	4.9	5.1
Owners' Equiv. Rent	-0.1	0.1	0.0	0.5	1.3

The Bottom Line: The core rate is still below the Fed's long-run inflation forecast of 1.7% to 2.0%, and will likely move lower due to the massive slack in the U.S. and global economies. As Vice-Chair Kohn said earlier this week, disinflation is more of a risk than rising inflation, which explains why some Federal Open Market Committee members considered expanding the mortgage purchase program at the September meeting. Sal Guatieri, 416-359-5295