ECONOMIC UPDATE

REGIONS

February 21, 2013

January Consumer Price Index: Tame Headline, Hotter Core

- The headline CPI was <u>unchanged</u> (up 0.026 percent unrounded) in January, with the core CPI <u>up</u> 0.3 percent (0.251 percent unrounded).
- On a year-over-year basis, the headline CPI <u>rose</u> by 1.6 percent and the core CPI <u>rose</u> by 1.9 percent.

The total CPI was unchanged in January compared to expectations for a 0.1 percent increase, while the core CPI was up by 0.3 percent, ahead of the expected 0.2 percent gain. On an over-the-year basis, the total CPI is up by 1.6 percent and the core CPI is up by 1.9 percent.

The headline CPI was held down by a 3.0 percent decline in retail gasoline prices. This of course may come as a surprise to those who watched pump prices rise during January, but these higher prices did not map into the January CPI data because January's price increases were confined to the latter stages of the month and also because of what was a favorable seasonal adjustment factor. Okay, we realize that our discussions of seasonal adjustment factors tend to elicit cries for mercy and glazed over eyes but think of it this way – this January's price increase was far smaller than typically occurs in January, so the seasonal adjustment factor basically overcompensated, thus holding down measured inflation. Rest assured, however, that there will be payback in February, particularly as retail gasoline prices to date in February are over nine percent higher than their January average. This alone could add roughly five-tenths of a percent to February's headline CPI. As the final chart in the opposite panel shows, gasoline prices have resumed a long running trend interrupted only by the Great Recession.

On top of the reported decline in gasoline prices, food prices were flat in January, with a modest gain in prices for food consumed away from home negated by flat prices for food consumed at home. Removing the impact of food and energy prices, however, the core CPI posted its largest monthly gain since May 2011. Apparel prices rose by 0.8 percent, costs of lodging away from home rose by 1.2 percent, air fares were up by 0.8 percent, and new car prices rose by 0.4 percent while used car prices rose by 0.2 percent for their first gain since last June.

Rents posted mild gains in January, with rents on primary residences up by 0.2 percent and owners' equivalent rent up by 0.1 percent, translating into over-the-year gains of 2.7 percent and 2.1 percent, respectively. The pace of growth of rents on primary residences has moderated over the past two months, which could reflect the impact of rising numbers of single family homes hitting the rental market. Nonetheless, we expect that rent growth will continue at a healthy clip over the course of 2013, particularly to the extent further improvements in job and income growth help promote a faster rate of household formation. This will remain a source of upward pressure on the core CPI, though the impact of rising rents on the core PCE deflator will not be nearly as large.

January's increase in the core CPI was largely due to one-off factors, such as the increase in lodging costs and prices for tobacco products, while prices for apparel and for motor vehicles are unlikely to continue rising at the pace seen in January. Even accounting for rising gasoline prices, February's headline inflation rate will still come in right around 2.0 percent. The bottom line here is that inflation pressures remain muted, and should there be any changes in the near term to the Fed's path of asset purchases, inflation concerns won't be the main driver.

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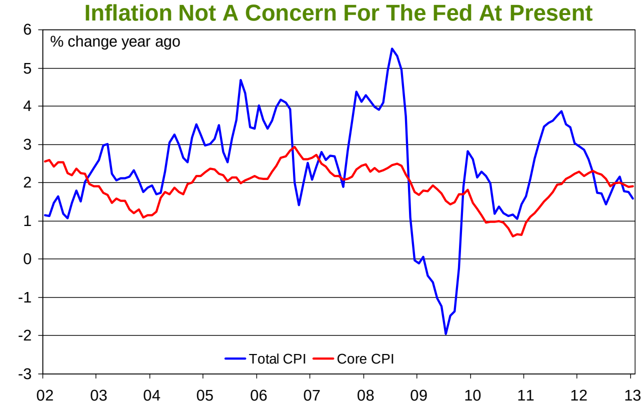
Inflation Not A Concern For The Fed At Present



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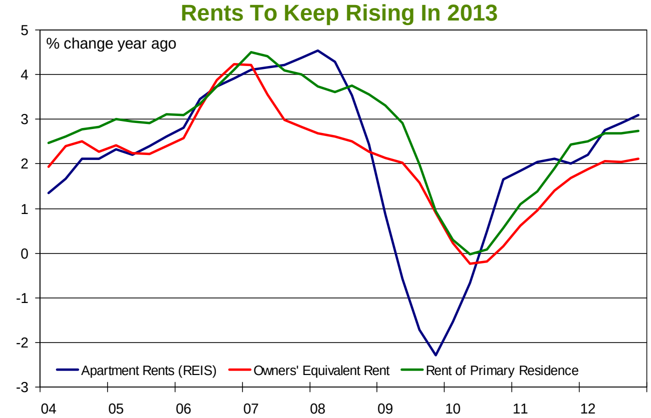
Rents To Keep Rising In 2013



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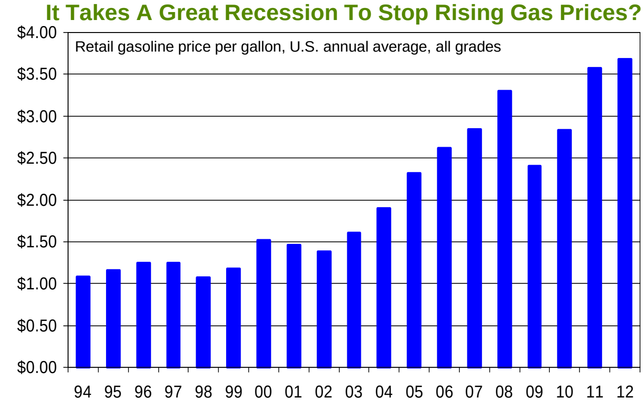
It Takes A Great Recession To Stop Rising Gas Prices?



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