



# Inflation Observatory

October 15, 2009

## Headline inflation slows

- Energy prices rose less than 1%
- Core inflation stable; downward pressures persist
- Rent and owners' equivalent rent price indexes decreased

## Core inflation continues downward trend

September's headline inflation rose 0.2% after a 0.4% increase in August. The difference can be attributed to lower growth in energy prices. Energy prices rose 0.6% in September, compared with 4.6% in August. Consistent with the average 2009 monthly growth rate, food prices declined at 0.1%. On a year-over-year (yoy) basis, the decline in headline prices eased to -1.3%; this is primarily because energy prices are 21.2% below Sept 2008.

Core inflation (less food and energy) rose at the same rate as headline inflation, 0.2%. This change is consistent with the average monthly growth rate for 2009. Most of its primary components registered slight positive increases; notably, used vehicle prices climbed 1.6% and medical commodities were up 0.6%, well above their 2009 average monthly changes. The August and September increases in used vehicles (1.9%, 1.6%) were perhaps due to secondary effects of the Cash for Clunkers program. Core prices are 1.5% above last year, which is consistent with our baseline scenario of below average, but positive inflation. In the past decade, core inflation averaged 2.2%.

Perhaps the most interesting detail in September's report is the decrease in *both* the rent and owners' equivalent rent price indexes. For the first time in the past 17 years, these indexes registered small, but significant monthly declines. Historically, these indexes have averaged 0.3% monthly growth; in September, both indexes registered 0.1% declines. Growth in these indexes slowed in February and eventually ceased in June before turning negative this past month. The declines reflect the ongoing adjustments in the housing market; as housing prices decreased through 2009, rental prices now decline in response to the lower housing asset values.

## Inflation is expected to remain low but positive

Core inflation over the past twelve months has remained below its historical average, and we expect it to remain low due to weak demand and the weak labor market. The high unemployment rate exerts downward pressure on wages, as employers have a larger applicant pool for their posted job vacancies. Furthermore, with weak demand in a competitive environment, many firms choose not to raise their prices. The current economic conditions help to buffer inflationary pressures from the fiscal stimulus and monetary easing; thus, we maintain our forecast of positive, low inflation into 2010.

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Date	CPI Forecasts		Core	
	Headline			
	mom	yoy	mom	yoy
Jan 09	0.3	0.0	0.2	1.7
Feb 09	0.4	0.2	0.2	1.8
Mar 09	-0.1	-0.4	0.2	1.7
Apr 09	0.0	-0.7	0.3	1.9
May 09	0.1	-1.3	0.1	1.8
Jun 09	0.7	-1.4	0.2	1.7
Jul 09	0.0	-2.1	0.1	1.6
Aug 09	0.4	-1.5	0.1	1.4
Sep 09	0.2	-1.3	0.2	1.5
<b>Oct 09</b>	<b>0.1</b>	<b>-0.4</b>	<b>0.2</b>	<b>1.7</b>
<b>Nov 09</b>	<b>0.2</b>	<b>1.5</b>	<b>0.2</b>	<b>1.8</b>
<b>Dec 09</b>	<b>0.2</b>	<b>2.6</b>	<b>0.2</b>	<b>2.0</b>
2008		3.8		2.3
<b>2009</b>		<b>-0.4</b>		<b>1.7</b>
<b>2010</b>		<b>1.3</b>		<b>1.1</b>

\*Forecasts are in bold

