



TD Economics

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Data Release: Consumer Prices Flat in December

- U.S. consumer prices were flat in December, falling short of market expectations for a 0.1% M/M gain. Core inflation, which excludes volatile food and energy prices, came in as expected at 0.1% M/M.
- On an annual basis, headline inflation was 2.98% in December; core inflation was 2.23%.
- Energy prices fell 1.3% on the month, its third straight month of decline. Prices for apparel (-0.1%), transportation (-0.7%), and other commodities (-0.3%) also contracted.
- The price of housing, including owner's equivalent rent, rose 0.1%, medical care 0.4%, and recreation goods and services 0.5%.

Key Implications

- Inflation continues to moderate thanks to falling energy prices and more muted food price pressures. Food and energy prices account for nearly one-quarter of the consumer price basket since they are critical inputs to economic production. Thus, when pressures on food and energy prices begin to lessen, the overall price level in the economy tends to follow suit.
- Excluding energy and food, core prices continued to rise in December. That isn't too concerning at this point. A little inflation is actually good in the context of the current economic recovery since it helps reduce nominal debt loads and greases income growth. It is when inflation runs too high and begins to influence expectations that it becomes problematic. But there is little evidence of that happening at the moment.
- The Fed has an implicit core inflation target of between 2-2.5% consistent with what it feels is a "healthy" level of inflation. So far, price growth remains squarely within that range. Given the persistent slack in the labor market, slow credit growth, easing commodity pressures, and potential recession in Europe, we feel that the threat of run-away inflation remains remote. Consistent with that view, we expect core inflation to average around 1.9% through 2012.

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