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Producer Price Index (6/09) rises more than forecast, largely but not entirely due to energy



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The Producer Price Index, released by the Bureau of Labor Statistics, rose significantly more than expected in June. While a sharp rise in energy was a major part of the increase, the core index also rose more than expected. Price indices for intermediate and crude goods also increased, both on a headline and on a core basis. This increase is not in my view alarming because it is more likely to represent a one-time catch up in commodity prices rather than the start of a new episode of commodity-based inflation. The energy price increases in the report have in any event been largely reversed in recent weeks.

- The headline, finished-goods PPI rose 1.8% in June, following increases of 0.2% and 0.3% in May and April, respectively. Prior to April, it had fallen for seven of the previous eight months. The June increase was the largest monthly increase in the PPI since November 2007. The consensus forecast had called for a smaller 0.9% increase, with individual forecasts ranging from zero to 1.8%. Excluding food and energy, the finished goods index rose 0.5% in June, compared with a 0.1% consensus forecast and with individual forecasts ranging from -0.2% to +0.3%. June's figure was thus at or above the high end of expectations on both a headline and a core basis. Before seasonal adjustment, the headline finished goods index rose 1.9% and the core index rose 0.2%.
- Energy accounted for two-thirds of the increase in the headline index, with finished energy prices up 6.6% after a 2.9% increase in May. Wholesale gasoline prices rose 18.5%, home heating oil rose 15.4% and natural gas for residential use rose 2.5%. These prices rose by broadly similar amounts both before and after seasonal adjustment. However, these increases have largely reversed since the June 9 reference date for last month's PPI. Between June 9 and today (the July PPI reference date), WTI has fallen 14% from \$70 to \$60 per barrel, wholesale gasoline has fallen 16%, home heating oil has fallen 16.5% and natural gas has fallen 8.5%. These declines suggest that the July PPI should show a significant reversal in the energy component, which makes up 18% of the finished goods index.
- Prices for finished food prices rose 1.1% in June following a 1.6% decline in May. Vegetables and eggs both rose substantially (22% and 12%, respectively), partially reversing sharp drops in May. Prices for several other types of food moved lower, including fish, rice, several meats and cooking oil. Year-over-year, finished food products were down 2.2%. Prices for intermediate and crude food goods were mixed, with intermediate food prices rising 1.3%, largely as a result of an increase in flour prices (which were down nearly 20% year-on-year) but crude food goods prices down 0.5%. There is thus little evidence from crude and intermediate food prices of earlier-stage upward price pressures on food.
- Core finished goods prices rose 0.5%, the largest increase since last October. Automobile prices rose 2.0% and light truck prices rose 3.4%, although both these increases were lower before seasonal adjustment. Wholesale apparel prices fell and wholesale prices for household durable goods were mixed. Capital goods prices rose 0.5% as the increase in light truck prices offset declines in IT equipment, aircraft, tools and dies, and oilfield service equipment. Prices for most other classes of capital goods were little changed.
- Intermediate goods prices rose 1.9%, spurred largely by a 9% increase in intermediate energy products. Core intermediate goods rose 0.4%, the first increase since September 2008. Prices rose for several types of metal products, including a 2.4% increase for foundry products, a 6.2% increase for non-ferrous wire and cable, and a 4.2% increase for primary non-ferrous metals. Prices for most machinery and capital

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equipment components were little changed or down slightly. Chemicals prices were mixed, with inorganic chemicals falling but organic chemicals up 7%. Fertilizer prices fell.

- Crude goods rose 4.6%, with much of the increase again a result of energy. Nevertheless, crude goods excluding food and energy rose 2.6%, reflecting increases in metals other than iron ore, animal hides and skins, and wastepaper. Construction materials prices were mixed..

Source: U.S. Department of Labor

This report is not as alarming as it might first appear, particularly since the bulk of the energy price increases underlying the headline numbers has subsequently been reversed. Nevertheless, there remain broad-based global trends toward higher prices for industrial raw materials, as have also been seen in the price data from the ISM reports (where deflation in business inputs has now come to an end). Since final demand remains weak in the U.S. and Europe in particular, manufacturers may have difficulty passing on raw materials increases to ultimate consumers. If these raw materials price increases continue, then, their impact may be felt more in margins than in broader consumer price inflation. ■