

U.S. Inflation Flash

Inflation Up Slightly in December As Fed Begins Tapering

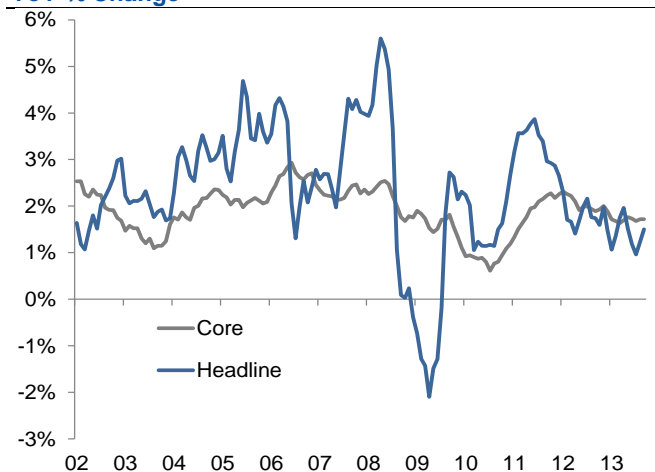
- **Headline inflation in line with forecasts, posts increase of 0.3% MoM**
- **Prices accelerate to 1.5% YoY but hold steady at 1.7% YoY excluding food and energy**
- **Inflation discussion expected to intensify in upcoming FOMC meetings**

The headline consumer price index for December increased by 0.3%, largely due to a surge in energy prices, specifically gasoline. Energy prices were up 2.1% MoM propelled by prices at the pump, which rose 3.1% in December. However, year-over-year rates showed that energy prices were mostly unchanged from a year ago, up a modest 0.5%. Even with the jump in December, gasoline prices were down 1.0% YoY in December, marking the fifth consecutive month for YoY price declines.

Excluding food and energy, the core consumer price index increased 0.1% in December. Transportation services saw a decline of 0.4% MoM driven by a fall in airline fares, which plummeted 4.7% during the month. The transportation services decline was neutralized by an uptick in medical care services and a 0.9% increase in apparel. Electricity prices also jumped up in December, as prices were 0.4% higher than the previous month as a result of the cold weather felt around the country during the latter weeks of the year. Overall, the majority of core categories remained relatively flat or experienced only modest increases from November.

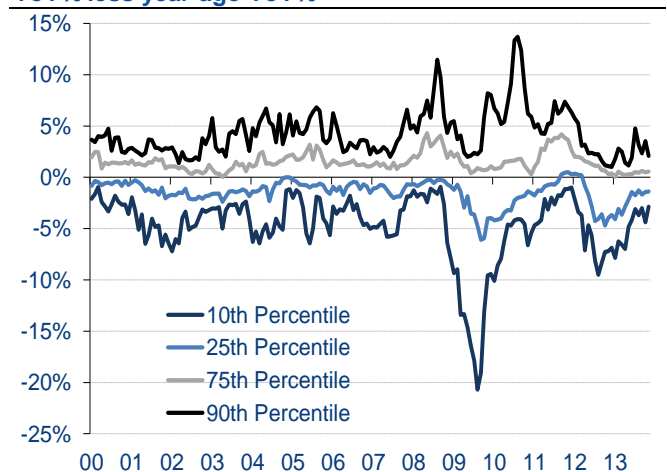
On a yearly basis, headline prices are up 1.5% and core prices are up 1.7% as inflation continues to hold below the Fed's target of 2.0%. The Federal Reserve has been cautious with regards to inflation and we expect the board to closely monitor the inflation rate as they continue on with tapering. The Fed has stated its intention to scale back the pace of asset purchases as the employment picture becomes brighter, so it will be interesting to see how they handle the balance with low inflation. Although we expect inflation to rise hand-in-hand with the economy as growth accelerates, tapering too quickly could put downward pressure on prices and increase the risk of low inflation or potential deflation. While the Fed looks more closely at the PCE inflation measure (which tends to run a bit lower than CPI), upcoming CPI data will remain an important indicator to watch.

Chart 1
Consumer Price Inflation
YoY % Change



Source: Bureau of Labor Statistics & BBVA Research

Chart 2
12M YoY Relative Consumer Price Distribution
YoY% less year-ago YoY%



Source: Bureau of Labor Statistics & BBVA Research

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