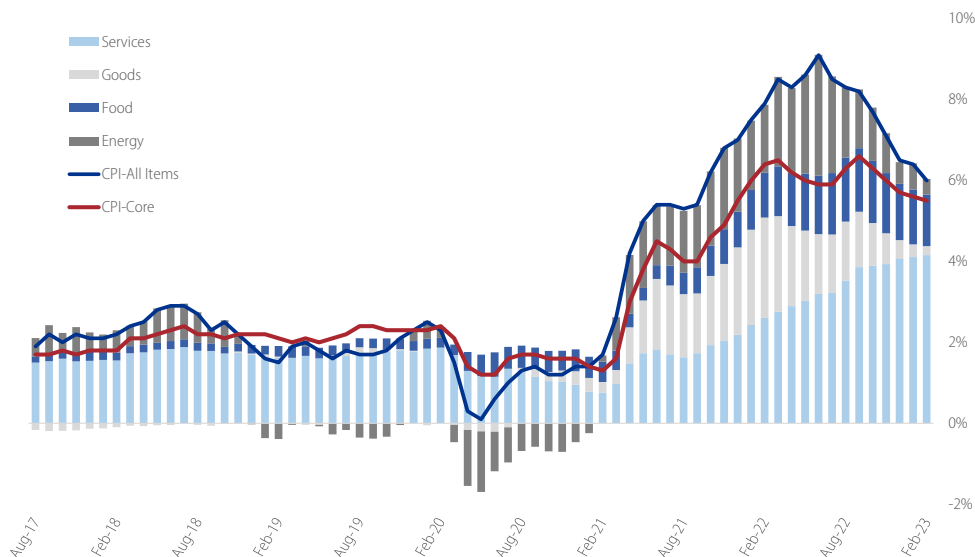


Yields Move Higher on Stubborn CPI

Any significant cooling in the monthly CPI data might have given the Fed the latitude to pause rate hikes to further assess damage to bank balance sheets, but this morning's release was still a bit too hot. The headline consumer price index (CPI) rose +0.4% in February, as expected, while core CPI came in above forecast at +0.5%.

Consumer Price Index (Year-over-Year Percent Change)



Source: Bureau of Labor Statistics

Overall energy prices were down -0.6% in February, although the energy sub-indexes were mixed. Natural gas prices fell -8.0%, the biggest single month decline in over 16 years, while gasoline prices climbed +1.0% following a +2.4% January gain.

The cost of food rose +0.4% in February, continuing a gradual deceleration, and is now up "just" +9.5% on an annual basis.

Shelter costs were up +0.8% in February, after climbing +0.7% in January, and are now rising at a +8.1% annual pace. Shelter costs seem to have peaked and are expected to gradually decline over the remainder of the year, but still accounted for 70% of the headline increase and 60% of the core.

New vehicle prices rose +0.2% for the month and +5.8% year-over-year, while used vehicle prices fell -2.8% for the month and -13.6% over the past 12 months.

The annual pace of headline CPI, as expected, slipped from +6.4% to +6.0%. Although it was the slowest year-over-year increase since September 2021, it was also the 17th straight month that CPI has been at or above 6%. The annual rate of core CPI decreased from +5.6% to +5.5%, also matching the median forecast.

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Core goods prices were *unchanged* in February after rising a scant +0.1% in January, but core services stepped-up from +0.5% to +0.6%. There is little question that service inflation is the Fed's most pressing issue. The service sector is labor-intensive, and labor is in short supply. The worker/job mismatch is still pressuring wages. If the number of workers can't increase to match available jobs, economic growth will have to weaken enough to destroy some of the job openings.

Just a week ago, Chair Powell testified to Congress that the Fed may need to increase rates at a faster pace to slow demand and curb persistently high inflation. At the time, this solidified the likelihood of a 50 basis point increase at next week's FOMC meeting. Yesterday, in the midst of the SVB fallout, the bond market had extinguished the half point possibility and was chipping away at the remaining quarter-point.

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Analysts at *Bloomberg Economics*, after sifting through this morning's CPI data, believe core PCE, the Fed's preferred inflation measure, may actually move higher in February. Assuming this comes to pass when the data is released on March 31st, the Fed's job will be a little tougher in May.

Market Indications as of 9:25 A.M. Central Time

DOW	Up 402 to 32,221 (HIGH: 36,800)
NASDAQ	Up 228 to 11,417 (HIGH: 16,057)
S&P 500	Up 62 to 3,917 (HIGH: 4,797)
1-Yr T-bill	current yield 4.56%; opening yield 4.17%
2-Yr T-note	current yield 4.35%; opening yield 4.02%
3-Yr T-note	current yield 4.15%; opening yield 3.90%
5-Yr T-note	current yield 3.87%; opening yield 3.69%
10-Yr T-note	current yield 3.66%; opening yield 3.56%
30-Yr T-bond	current yield 3.78%; opening yield 3.70%

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