DAILY GLOBAL COMMENTARY

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The Energy Price Index Lifts Consumer Price Index in August

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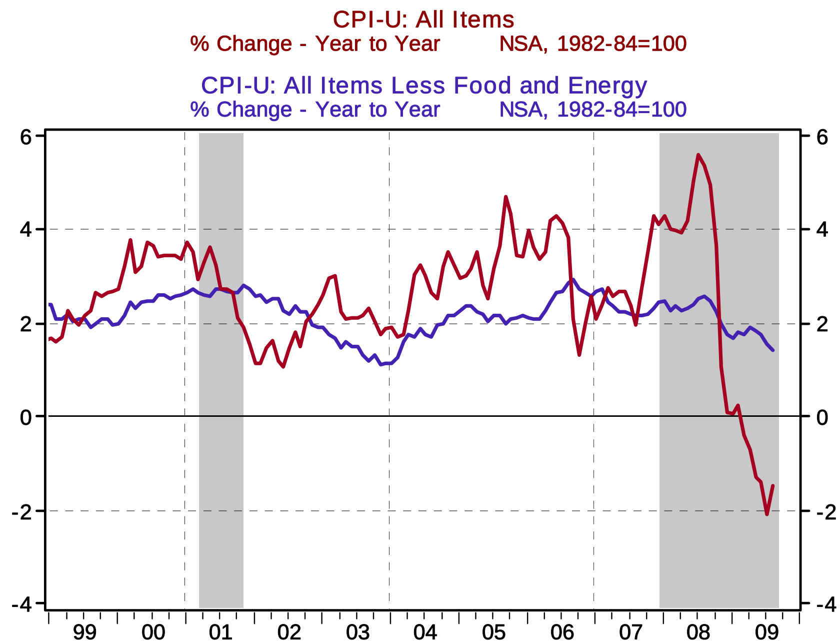
The Consumer Price Index (CPI) moved up 0.4% in August after holding steady in July. The 9.1% increase in gasoline prices accounted for the sharp increase in the headline number. Excluding energy, the CPI increased only 0.1% in August compared with no change in July. Food prices rose 0.1% in August following a 0.3% decline in the prior month. The energy price index recorded a 4.6% gain in August vs. a 0.4% decline in July. The decline in energy prices in the early weeks of September suggests a drop of the energy price index for the month. On a year-to-year basis, the CPI declined 1.5% in August vs. a 2.1% in the twelve months ended July.

Chart 1

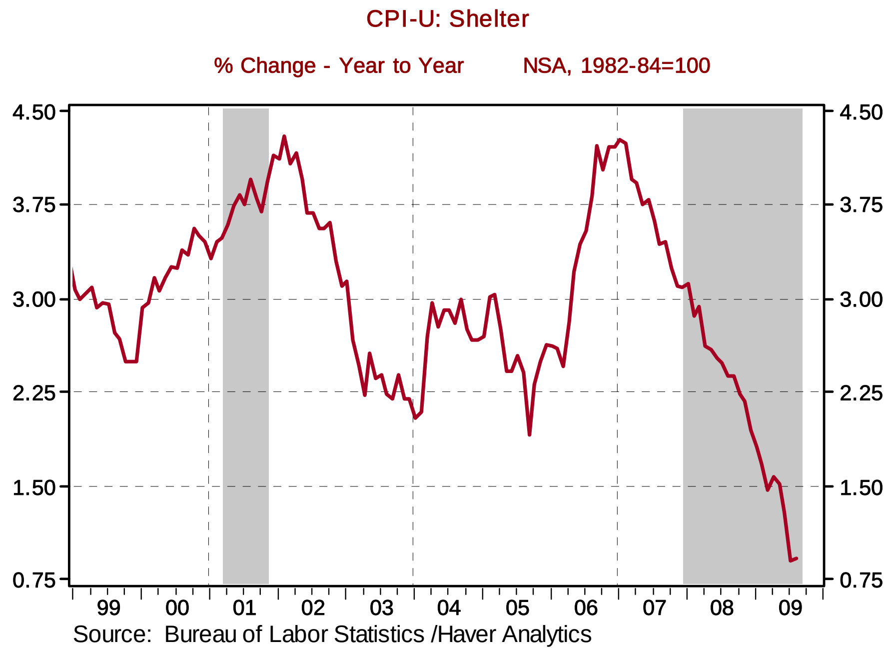


Sources: Bureau of Labor Statistics /Haver Analytics

The core CPI, which excludes food and energy, rose 0.1% in August, putting the year-to-year gain at 1.4%. The deceleration of the core CPI and declining trend of the overall CPI is indicative of inflation being a non-issue for several months.

In August, shelter costs rose 0.1%, inclusive of a steady rent index, a 0.1% increase in owners' equivalent rent, and a 0.5% jump in hotel prices. The year-to-year trend of the shelter index, which is the largest component of the core CPI and accounts for 33% of the CPI, has shown a noticeable deceleration for several months (see chart 2). We will be watching this index closely in the months ahead as it may have established a plateau with the year-to-year increase in August (+0.91%) marginally higher than the July year-to-year gain (+0.9%).

Chart 2



In August, the drop in new car prices (-1.3%) reflects the "cash for clunkers" incentives and should be reversed soon. The apparel price index fell 0.1% and medical care prices advanced 0.3% in August.

Chairman Bernanke indicated yesterday that the recession is most likely a matter of history. Our forecast and the market consensus is that the recovery commenced in the third quarter of 2009. The important question now is that if the Fed will be fortunate to fine tune monetary policy such that it prevents inflationary pressures from gaining a strong hold. Ensuring that the trajectory of economic growth does not slip into negative territory and financial markets remain stable is the Fed's primary goal in the near term. Inflation is not the primary concern, for now.

Highlights of the Consumer Price Index – August 2009

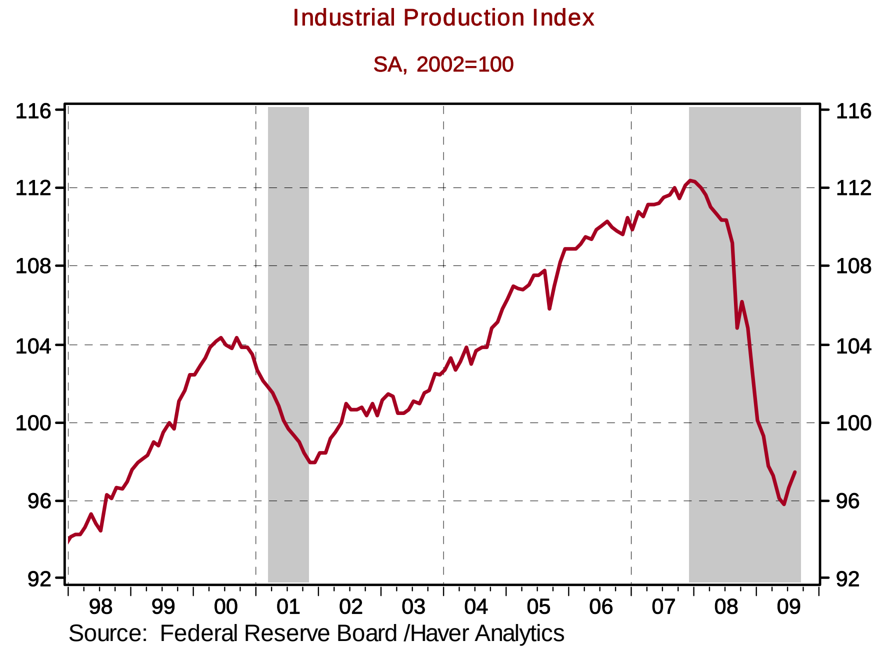
	% change	annualized % change			% change		
	prior month	year-to-date	3 mo. ago	6 mo. ago	Aug-09 yoy	Aug-08 yoy	Dec-08 yoy
CPI - ALL ITEMS	0.4	2.7	4.9	2.3	-1.5	5.4	0.1
CORE - ALL ITEMS LESS FOOD & ENERGY (77.75)*	0.1	1.9	1.4	1.9	1.4	2.5	1.8
CPI ALL ITEMS LESS ENERGY (92.4)	0.1	1.5	1.1	1.4	1.3	3.1	2.4
FOOD (14.63)	0.1	-1.1	-0.5	-1.4	0.4	6.1	5.9
ENERGY (7.62)	4.6	18.0	57.1	12.9	-23.0	27.2	-21.3
SHELTER (33.2)	0.1	0.7	0.0	0.6	0.9	2.4	1.9
COMMODITIES (39.6)	0.8	5.8	10.6	4.9	-4.5	7.3	-4.1
COMMODITIES LESS FOOD & ENERGY (21.5)	-0.3	2.8	1.0	2.7	1.1	0.6	-0.6
SERVICES (60.4)	0.2	0.7	1.1	0.5	0.7	4.1	3.0
SERVICES LESS ENERGY SERVICES (56.3)	0.2	1.6	1.6	1.6	1.6	3.3	2.7
FRB CLEVELAND MEDIAN CPI	0.2	1.6	0.9	1.3	1.8	3.2	2.9

* - Figures in parentheses denote the relative importance of each category in the CPI.

Cars and Many Other Components Account for the Strength in Factory Activity

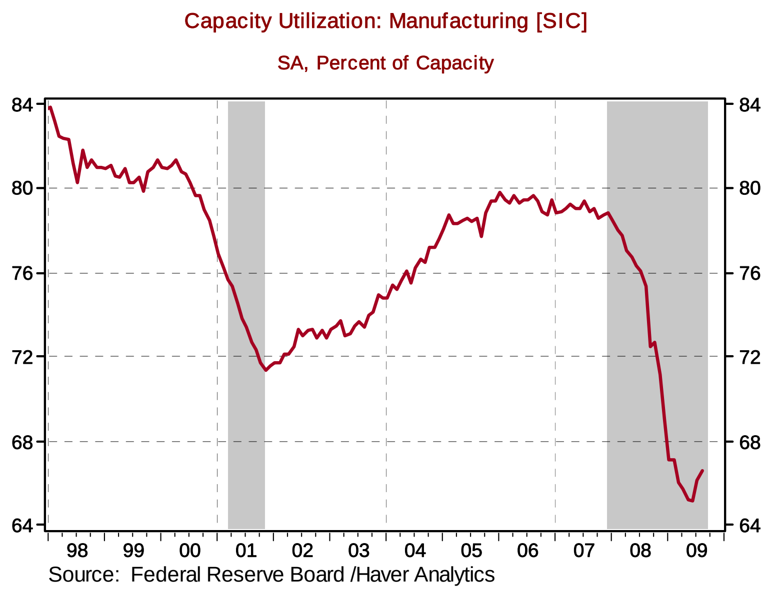
Industrial production increased 0.8% in August after an upwardly revised 1.0% gain in July (previously estimated as a 0.5% increase). The Business Cycle Dating Committee of the National Bureau of Economic Research (NBER) uses four variables -- industrial production, nonfarm payroll employment, real personal income less transfer payments, and real manufacturing and trade sales -- to determine turning points of a business cycle. The important aspect to note is that the trough of industrial production was in June 2009 (see chart 3). Therefore, it is quietly likely that the NBER will date the end of the Great Recession as June 2009/July 2009 once additional information is available.

Chart 3



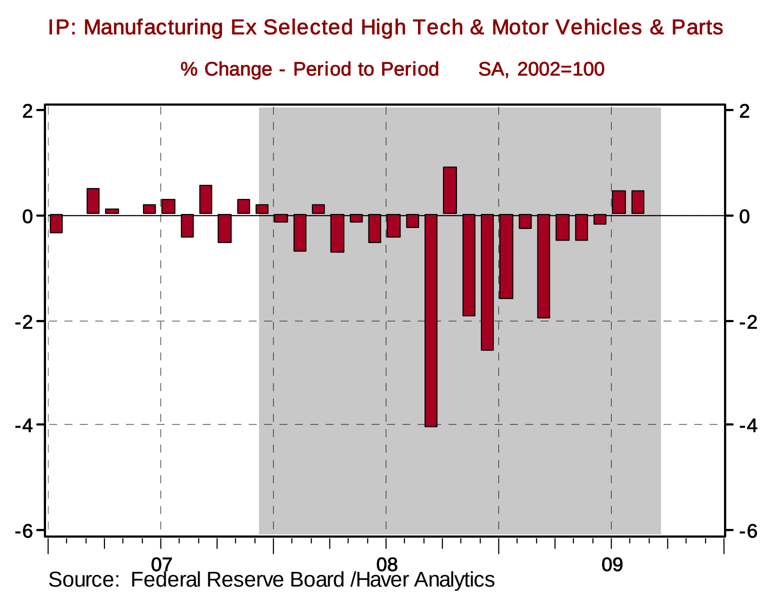
Factory production increased 0.6% in August, after an upwardly revised 1.4% increase in July (previously estimated as a 1.0% gain). Production of autos rose 5.5% in August, following a 20.1% jump in the prior month. Primary metals; machinery; and electrical equipment, appliances, and components all posted gains between 0.5% and 1% during August. The operating rate of the factory sector rose to 66.6% in August, after establishing a record low of 65.1% in June 2009 (see chart 4).

Chart 4



Auto production and sales are both likely to decline in the near term as the temporary effect of the "cash for clunkers" program dies out. In the months ahead it will be crucial for non-auto components to add to industrial production. Preliminary evidence is encouraging because factory production excluding autos and high-tech has risen for two straight months (see chart 5).

Chart 5



Industrial Production – August 2009

	Mar-09	Apr-09	May-09	Jun-09	Jul-09	Aug-09
Industrial Production*	-1.6	-0.6	-1.1	-0.4	1.0	0.8
Total Capacity Utilization	69.5	69.2	68.5	68.3	69.0	69.6
Manufacturing output*	-1.7	-0.5	-0.9	-0.3	1.4	0.6
Man. Capacity Utilization	66.0	65.7	65.2	65.1	66.1	66.6
Capacity Utilization ex. High-tech industries	66.1	65.8	65.3	65.2	66.2	66.8
High-tech industries - output*	0.5	1.9	-2.2	0.8	2.5	-0.5
Manu. Ex autos &high-tech output*	-1.9	-0.6	-0.5	-0.2	0.5	0.4

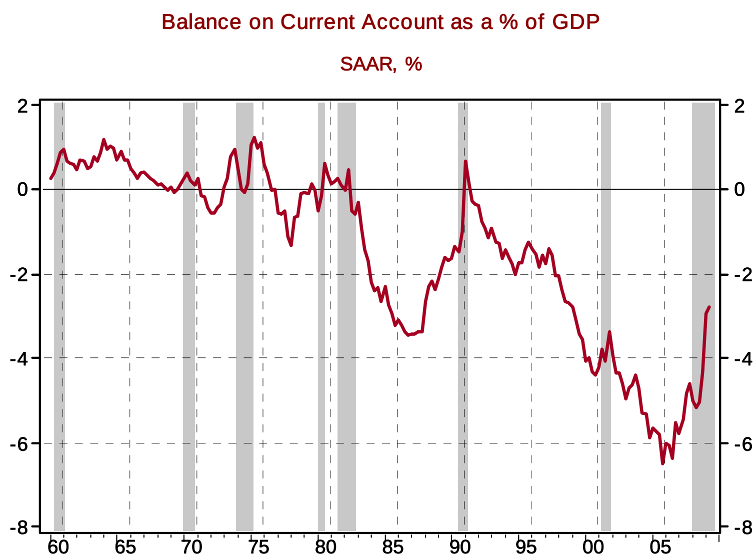
* - percent change from prior month

Current Account Narrows in Q2, but a Small Reversal is Likely in Q3

The current-account deficit of the U.S. economy narrowed to $98.8 billion in the second quarter from $104.5 billion in the first quarter. As a percent of nominal GDP, the current account deficit was 2.8% in the second quarter, down from a 2.9% mark in the first quarter of 2009 and record high of 6.5% in the fourth quarter of 2005. The trade deficit widened in July (-$31.9 billion vs. -$27.5 billion in June) which raises the probability of a wider current account deficit in the third quarter.

In the second quarter, the surplus on income declined, marking the fifth quarterly drop in the last six quarters. Foreign-owned assets in the U.S. rose $16.4 billion in the second quarter after recording declines in the fourth quarter of 2008 (-$11.9 billion) and the first quarter (-$67.8 billion).

Chart 6



Source: Bureau of Economic Analysis/Haver Analytics