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By Martin Crutsinger
The Associated Press

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Wednesday 20 April 2005

Washington - Consumer prices jumped 0.6 percent in March, the biggest inflation surge in five months, as the costs of energy, clothing and airline fares all rose sharply.

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The Labor Department said last month's increase in the Consumer Price Index, the most closely watched inflation gauge, followed a 0.4 percent rise in February and left consumer inflation rising at an annual rate of 4.3 percent in the first three months of this year. That was a full percentage point above the 3.3 percent rise in prices for all of 2004.

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The new report showed that even outside of food and energy, there were significant price pressures last month. The so-called core rate of inflation rose by a worrisome 0.4 percent in March, double what economists had expected, reflecting higher prices for clothing, hotel rooms and airline tickets.

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Energy Prices Lead to Jump in March Inflation
By Dean Baker

The Center for Economic Policy Research

Wednesday 20 April 2005

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Inflation is more of a threat today than in 1994-95.

The overall CPI rose by 0.6 percent in March driven largely by a 4.0 percent jump in energy prices. The core (excluding food and energy) CPI also showed evidence of rising inflation, increasing by 0.4 percent for the second consecutive month. This brings the annual rate of inflation in the core index to 3.3 percent over the last quarter. This is up from a 2.3 percent rate over the last year.

This inflation rate in the overall CPI over the last three months has been 4.3 percent, well above the 3.1 percent rate for the last year. Both the inflation rate of the last quarter and the last year are running far above the rate of hourly wage growth, which has been approximately 2.5 percent over both periods. The amount of income lost to falling real wages over the last year is equal to the gains from job growth, which means that real wage income has been virtually flat for the last year.

While inflation has been on a persistent upward path for the last two years, many observers have failed to appreciate the amount of inflationary pressure in the economy. There is little danger of runaway inflation, but virtually all measures, inflation poses more of a threat today than it did in 1994-95 period, when the Fed raised the federal funds rate from 3.0 percent to 6.0 percent.

Table 1 below compares the inflation rate shown in various indices in the year from January 1994 to January 1995 to the inflation rate from March of 2004 to March of 2005. In virtually every index, the inflation rate is higher at present than it was in 1994-95. (The sole exception is the core GDP consumption deflator.)

TABLE 1

	Jan. 94- Jan. 95	**Mar. 04 – Mar 05**
CPI	2.4%	3.1%

CPI (core)	2.3%	2.3%
Finished goods index (core)	1.5%	2.6%
Intermediate goods index (core)	6.3%	7.6%
Crude goods index (core)	-1.6%	3.3%
	94(Q1)-95(Q1)	**03 (Q4)-04 (Q4)**
GDP deflator	2.2%	2.4%
PCE deflator	2.4%	2.6%
PCE deflator (core)	2.5%	1.6%

Not only is the current inflation rate higher by most measures than in the 94-95 period, there is more evidence of acceleration. By every measure inflation has been higher in the last year than in the prior year. This was not true in the 1994-95 period.

There is also good reason to believe that there will be more inflationary pressures in the near future. The most recent data suggest that productivity growth is slowing from its extraordinary pace over the years from 2001 to 2004, with the first quarter rate likely to be less than 2.0 percent. In addition, real wages have been falling for the last year and a half, there will almost certainly be some catch up wage growth in the not distant future. And, the dollar will have to decline to correct an unsustainable trade deficit that is now running at more than 6 percent of GDP (it was just over 1.0 percent of GDP in 1994).

While it is difficult to know how the Fed will respond to any particular economic situation, the evidence clearly shows that inflation is more of a threat today than it was in the 1994-95 period. If the Fed were to respond similarly, then interest rates will go much higher.

Dean Baker is Co-Director of the Center for Economic and Policy Research in Washington, DC.

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