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## Inflation a conundrum for Fed

The December Consumer Price Index (CPI) report did not do the Federal Reserve any favors. Facing a strong economy that is challenging their decision to ease policy in autumn, Fed Chair Jerome Powell and colleagues were in need of decisive numbers—hot or cold—to guide them. On Wednesday, the Labor Department gave them lukewarm data.

Headline CPI rose 0.4% month-over-month (m/m), and 2.9% year-over-year (y/y). Both readings were slightly higher than the prior month's 0.3% and 2.7%, respectively. But this wasn't a strong signal inflation has reaccelerated and that rates need to remain restrictive. Why? Because the increase was largely due to surging gasoline prices. Energy costs are famously volatile, which is why the Fed pays much more attention to the Core CPI. This reductive measure removes items prone to short-term fluctuation, such as food prices, giving policymakers a better sense of what is really happening. Core CPI grew 0.2% m/m and 3.2% y/y, both a tenth of a percent lower than November's numbers of 0.3% and 3.3%. Good news, but not decisively so.

Once certain that they had dealt inflation (including the Producer Price Index, which was also slightly cooler in December than November,) a mortal blow, policymakers now are not sure. With every passing Federal Open Market Committee (FOMC) meeting, they seem to doubt that victory more. Once projecting several additional rate cuts this year, they now expect only two. After the release of the CPI report, the fed funds futures market is essentially betting we will only get one. If Powell tries to goad the markets into a different opinion in his press conference following the FOMC meeting Jan. 29, CPI won't offer much support.

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