USA TODAY

Rising prices crimp consumers' spending power

Paul Davidson, *June 18, 2014*

Consumer prices last month rose at the fastest pace in more than a year, a development that could threaten forecasts for a more robust recovery.

The increase could hurt Americans still struggling with modest wage gains and pose a dilemma for the Federal Reserve, which concludes a two-day meeting Wednesday. The Fed has been trying to spark higher inflation to prevent the economy from slipping back into a malaise — but without dampening consumer spending or economic growth.

The consumer price index jumped 0.4% last month after rising 0.3% in April, the Labor Department said Tuesday. Economists had expected a 0.2% increase.

Over the past 12 months, prices have increased 2.1%.

Core inflation, which excludes the volatile food and energy categories, was up 0.3% last month, the most since August 2011.

The rise in prices was broad-based. Food costs jumped 0.5% from April, the largest monthly increase since August 2011. Year-over-year, prices for meat, poultry, fish and eggs are up 7.7%, and fruits and vegetables are up

3.2%. Those categories have been rising in part because of a drought in California and a virus in the pork population.

Energy costs also surged in May, with gasoline prices rising 0.7% from April and electricity costs increasing 2.3%. The conflict in Iraqi could continue to push up gas prices, says economist Michael Montgomery of IHS Global Insight.

Other prices also were higher. Airline fares jumped 5.8% in May, the largest monthly increase since 1999. Apparel prices and housing costs both rose 0.3%. And an index of medical care costs increased 0.3% for the month and is up 3% the past 12 months.

Independent economist Joel Naroff says the brisker inflation contrasts with still-modest income gains, a disparity that's likely to dampen consumer spending in the near term.

After figuring in inflation, average hourly earnings are down 0.1% the past year, the Bureau of Labor Statistics said Tuesday.

"For the vast number of average workers who have gotten no wage increases, this hurts their spending power," says Naroff, who like many economists, expects wage growth to accelerate later this year.

In the meantime, consumers have fueled their spending with more credit card debt. Higher debt, along with rising prices and interest rates, could prompt consumers to hunker down later this year, says **Bernard Baumohl, chief global economist of The Economic Outlook Group**.

He says the economy "could pivot from healthier growth to one that teeters close to recession in the next six to 18 months."

The sluggish housing market is another cause for concern. The government said Tuesday that housing starts fell 6.5% in May, more than economists had forecast.

Others are more bullish. Lewis Alexander, chief U.S. economist of Nomura, says higher inflation is "being driven by the economy doing really well" and should have only a marginal impact on spending.

Both overall and core inflation are up about 2% the past year — matching the Fed's target. And wholesale prices fell in May, auguring a possible moderation in consumer prices this month.

Still, last month's spike in inflation could help prompt the Fed to begin to raise interest rates earlier in 2015 than expected, says Paul Dales of Capital Economics.

###