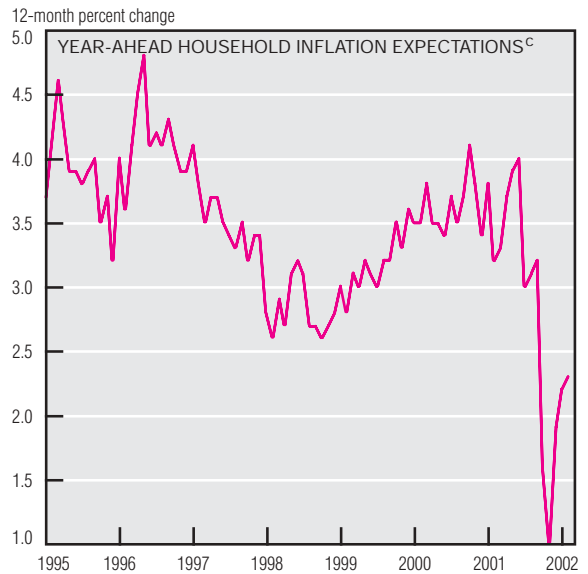
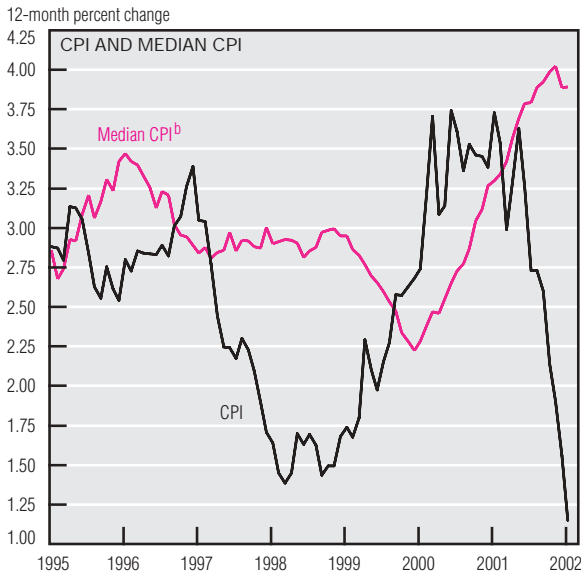
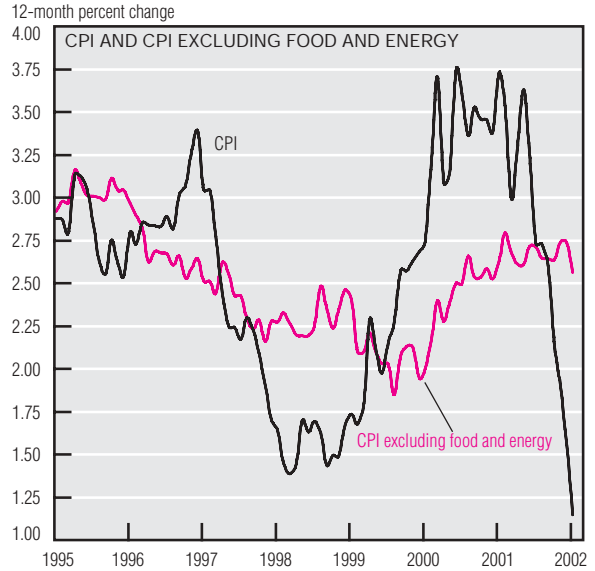


Inflation and Prices

January Price Statistics	Percent change, last:				
	1 mo. ^a	3 mo. ^a	12 mo.	5 yr. ^a	2001 avg.
Consumer prices					
All items	2.0	0.0	1.1	2.2	1.5
Less food and energy	1.9	2.6	2.6	2.4	2.7
Median ^b	3.7	3.1	3.9	3.1	3.9
Producer prices					
Finished goods	1.8	-3.7	-2.8	0.7	-1.9
Less food and energy	-0.8	0.3	0.3	1.0	0.7



a. Annualized.
 b. Calculated by the Federal Reserve Bank of Cleveland.
 c. Mean expected change in consumer prices as measured by the University of Michigan's *Survey of Consumers*.
 SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; Federal Reserve Bank of Cleveland; and University of Michigan.

The consumer price index continues to bounce around, rising an annualized 2% in January after falling 2% in December. Over the past three months, the CPI remained unchanged (on average) because a sharp drop in energy prices offset modest price increases in other components of the consumer market basket.

How close is the central bank to achieving its stated objective of price stability? Looking only at the evidence of the CPI, we seem to be coming exceptionally close. Given the biases that are thought to make the CPI over-

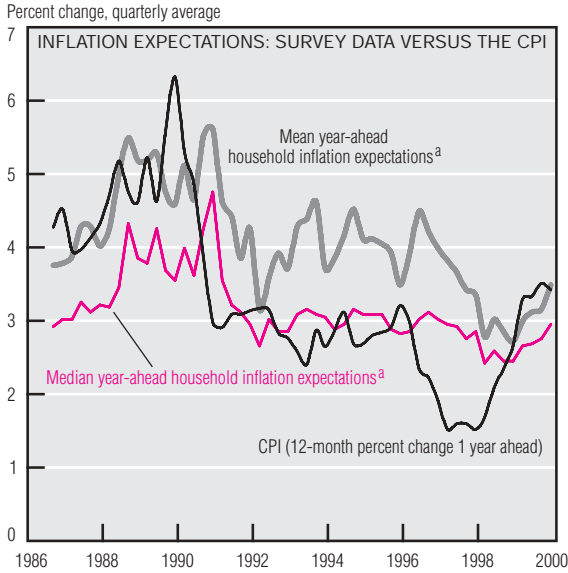
state actual inflation, the 1.1% rise in this measure over the past 12 months may put us within 1/2 percentage point of zero inflation. But price stability entails more than simply holding the CPI down for a time. A sustained environment of price stability requires that inflation expectations do not materially affect the behavior of households and businesses. Because much of the recent moderation in the rate of price increase was limited to the energy area, it is unlikely that the public is now ignoring the potential for inflation. Excluding food and energy

items, the CPI rose at a rate just shy of 2% in January and has hovered between 2% and 3% per year for several years now. Meanwhile, the median CPI continues to record a much more rapid advance, fueled by a continued surge in consumer services prices.

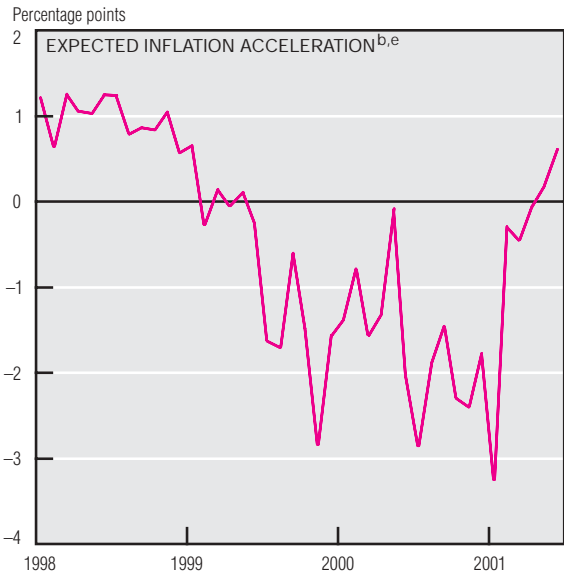
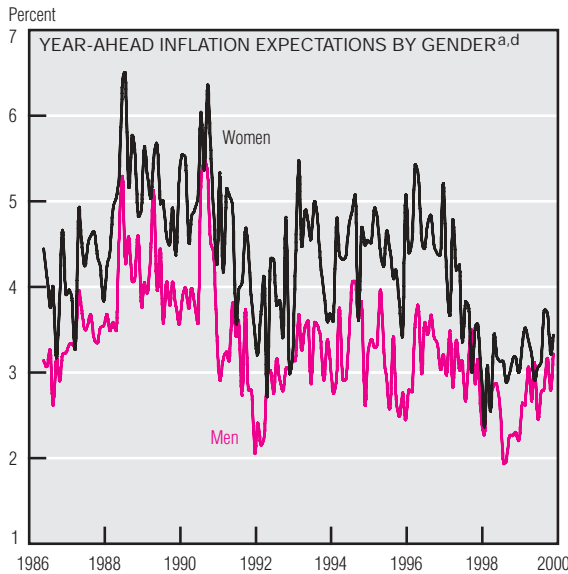
What do opinion polls say about the public's inflationary sentiment? According to the University of Michigan's Survey Research Center, the public's expectation for inflation over the next 12 months plunged amid the economic turmoil that followed the events of September 11.

(continued on next page)

Inflation and Prices (cont.)



	Perceptions	Expectations
Full sample	5.9	5.3
Male	4.5	3.9
Female	6.9	6.4
White	5.6	5.0
Nonwhite	7.8	7.7
Single	6.6	6.0
Married	5.3	4.9
High school or less	7.5	6.6
More than high school	4.7	4.4
Low income	9.2	8.3
Low-middle income	7.3	6.3
Middle income	5.9	5.3
High-middle income	4.7	4.4
High income	4.7	4.3



a. University of Michigan, *Survey of Consumers*, June 1986–December 1999.
 b. Federal Reserve Bank of Cleveland and the Ohio State University, *Inflation Psychology Survey*
 c. Michael F. Bryan and Guhan Venkatu, "The Demographics of Inflation Opinion Surveys," Federal Reserve Bank of Cleveland, *Economic Commentary*, October 15, 2001.
 d. Michael F. Bryan and Guhan Venkatu, "The Curiously Different Inflation Perspectives of Men and Women," Federal Reserve Bank of Cleveland, *Economic Commentary*, November 2001.
 e. Defined as the difference between the average of survey participants' inflation expectations and the average of their inflation perceptions in a given month.
 SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; Federal Reserve Bank of Cleveland and the Ohio State University, *Inflation Psychology Survey*; and University of Michigan, *Survey of Consumers*.

And the survey's estimates of inflation expectations—though reviving a bit in the past two months—have remained modest even as the economy recovers from the disaster.

Still, many economists tend to be skeptical about survey-based measures of the public's inflationary sentiment, which are often wide of the mark when compared to official inflation estimates. Moreover, the survey data indicate public inflation sentiment that often seems to be overly

pessimistic. A recent investigation of survey-based inflation expectations data, conducted jointly by the Federal Reserve Bank of Cleveland and the Ohio State University, has shown that the public's inflation expectations—and their perceptions of past price increases—are strongly correlated with respondents' demographic characteristics. Specifically, poorer respondents see prices rising more rapidly than wealthier respondents, single people more than married people,

and women more than men. This finding, though still unexplained, may be an important clue in interpreting the curious responses on inflationary perceptions that appear in survey data. Nevertheless, what we can say is that the public apparently expects no acceleration in inflation over the next 12 months. That is, they expect prices to rise at a rate that is about the same as (or perhaps slightly higher than) the rate at which they perceive it to have risen over the past 12 months.