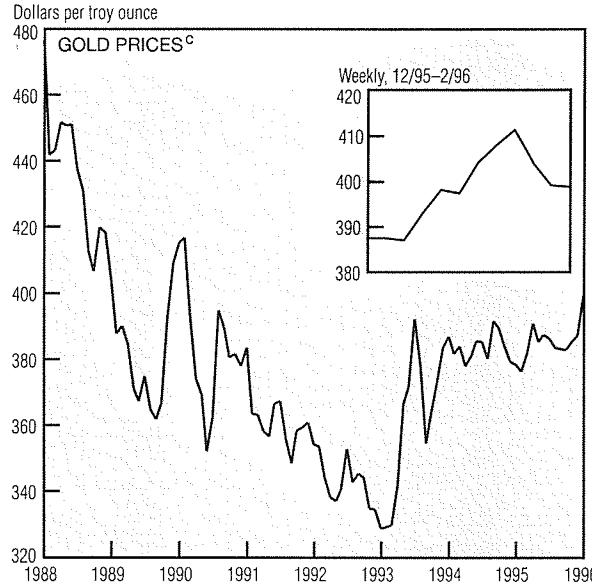
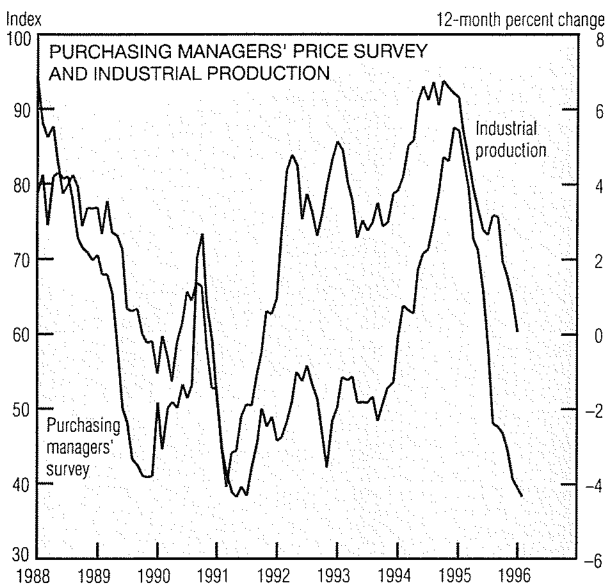
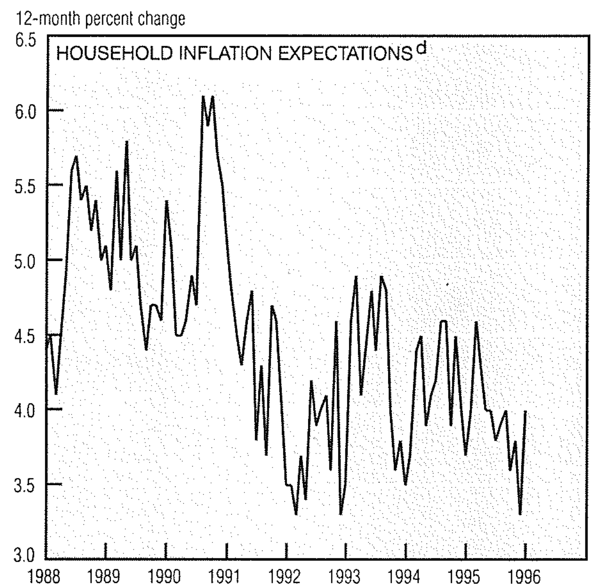
Inflation and Prices

January Price Statistics

	Annualized percent change, last: 1 mo.	12 mo.	5 yr.	1995 average
Consumer Prices				
All items	4.8	2.7	2.8	2.6
Less food and energy	3.7	3.0	3.2	3.0
Median[a]	4.3	3.4	3.1	3.4
Producer Prices				
Finished goods	3.8	2.3	1.2	2.1
Less food and energy	−0.8	2.2	1.8	2.5
Commodity futures prices[b]	−5.2	3.5	2.2	5.4







a. Calculated by the Federal Reserve Bank of Cleveland.
b. As measured by the KR-CRB composite futures index, all commodities. Data reprinted with permission of the Commodity Research Bureau, a Knight-Ridder Business Information Service.
c. Handy and Harman base price, New York.
d. Mean expected 12-month 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; the Federal Reserve Bank of Cleveland; the Commodity Research Bureau; Board of Governors of the Federal Reserve System; the National Association of Purchasing Management; *Metals Week;* and the University of Michigan.

The CPI made an unexpected jump in January (4.8% at an annualized rate), following a string of very moderate increases leading back to mid-1995. Although energy items accounted for a share of January's cost-of-living rise, the core inflation measures—the CPI excluding food and energy goods and the median CPI—also rose sharply, by 3.7% and 4.3%, respectively.

The monthly price data are extremely volatile, and it is unlikely that the January retail price increase marks the beginning of a higher inflationary trend. Still, the recent price jump has certainly dampened hopes that inflation was on the verge of moving to a substantially lower trajectory.

The behavior of the leading inflation indicators has been less ominous and is generally suggestive of continuing low inflation. Gold prices, which were rising at year's end and crossed the $400 per ounce threshold early this year, have very recently begun to moderate once again. Moreover, as industrial production growth slowed last year, so did the cost pressures noted by purchasing managers. In fact, the net proportion of purchasing managers reporting price increases set a recent low in January, dropping past this group's previous low inflation reading during the 1990–91 recession. Interpreting the inflationary expectations of households is more difficult, but these projections have generally been more favorable recently than they were earlier in the expansion.

The inflation projections of policymakers were presented by Federal Reserve Chairman Greenspan in his semiannual report to Congress in February. The central-

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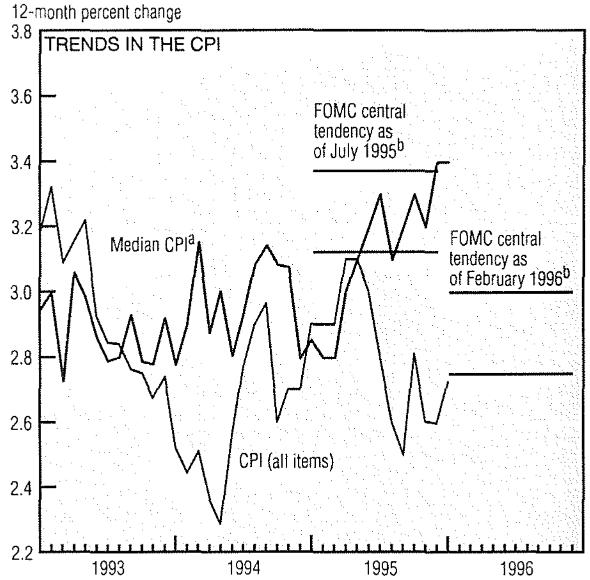
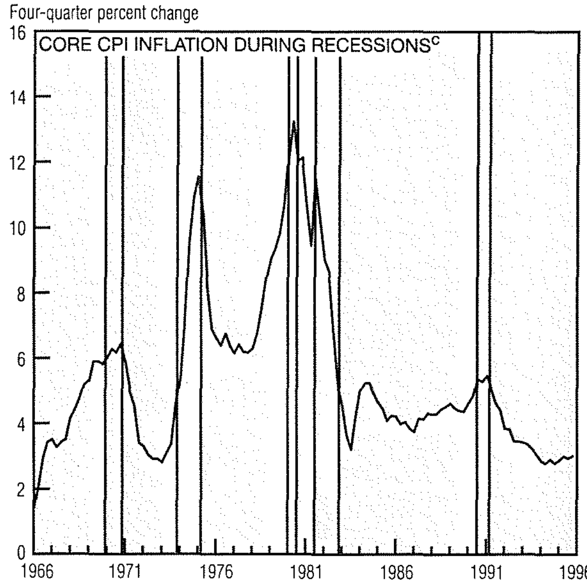
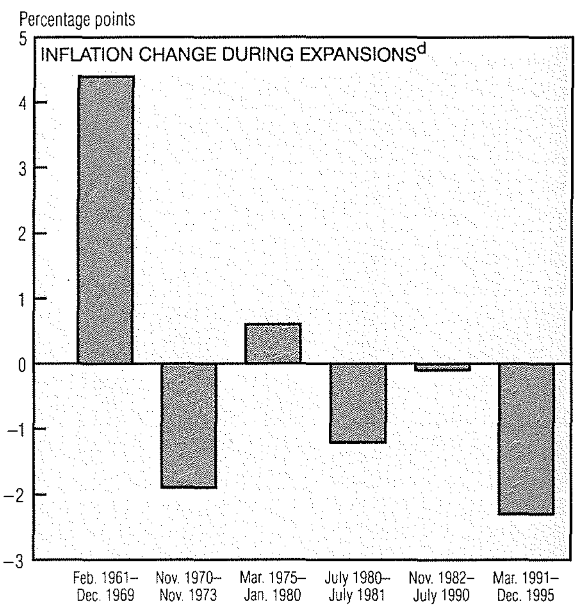
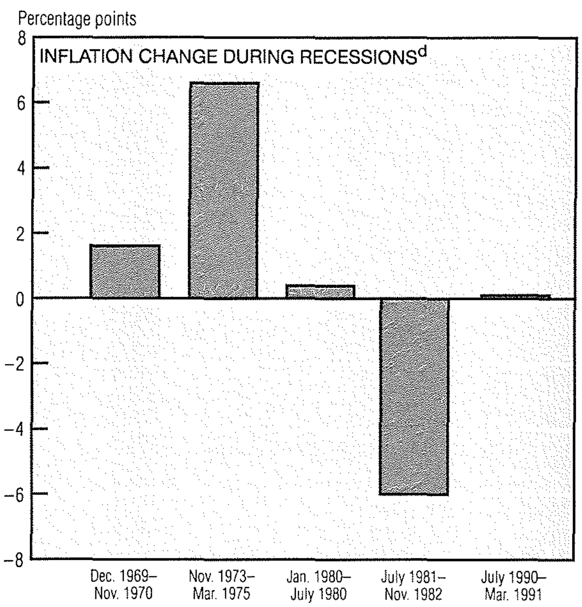
Inflation and Prices (cont.)









a. Calculated by the Federal Reserve Bank of Cleveland.

b. Upper and lower bounds for CPI inflation path as implied by the central tendency growth ranges issued by the FOMC and nonvoting Reserve Bank presidents. As of July, the stated range (fourth-quarter to fourth-quarter percent change) was 3.125 to 3.375 for 1995 and 2.875 to 3.25 for 1996. In February, the range for 1996 was revised to 2.75 to 3.0.

c. Shaded bars indicate recessions.

d. Change in the 12-month inflation trend, as measured by the CPI less food and energy items.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; the Federal Reserve Bank of Cleveland; and Board of Governors of the Federal Reserve System.

tendency CPI projection by members of the Federal Open Market Committee and nonvoting Federal Reserve Bank presidents was 2.75% to 3.0% for 1996. This is nearly half a percentage point lower than the group's inflation projection for last year, but just slightly above the actual 2.6% CPI rise. Chairman Greenspan noted that 1995 was the fifth consecutive year with a CPI increase below 3%, illustrating that "an extended period of growth with low inflation is possible." However, he also cautioned that price stability has yet to be achieved.

He suggested a strategy for attaining price stability, whereby policymakers restrain inflation during economic expansions to permit a gradual ratcheting down of inflation over the course of successive business cycles. Presumably, progress toward price stability is made during contractions in business activity. Indeed, one dramatic downward "adjustment" in inflation occurred during the 1981–82 recession, when the trend in the core CPI fell 6 percentage points from business cycle peak to trough. Moreover, in none of the recent expansions has the inflation trend been substantially higher at the peak than it was at the previous trough. It is surprising, though, when viewed strictly from a business cycle perspective, that in only one expansion of the past 35 years (1961–69) was the inflation trend much higher at the end of the expansion than it was at the beginning. In two recessions (1969–70 and 1973–75), the inflation trend actually rose significantly between the business cycle peak and its subsequent trough.