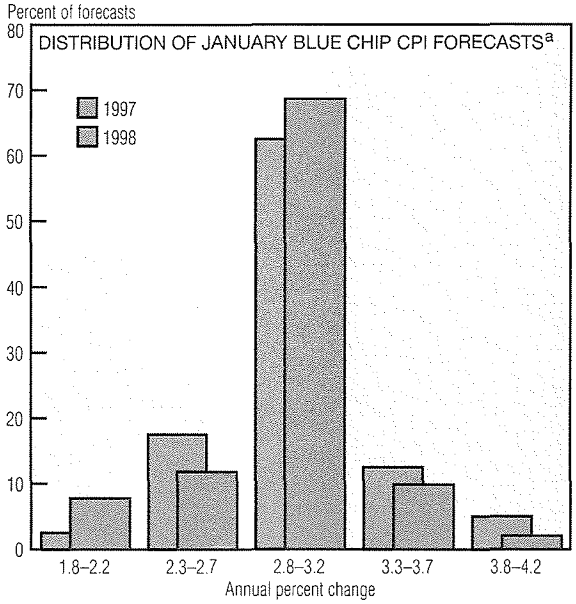
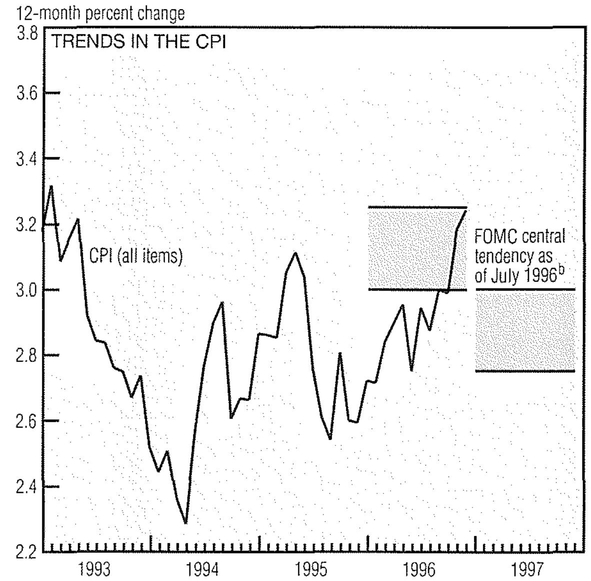
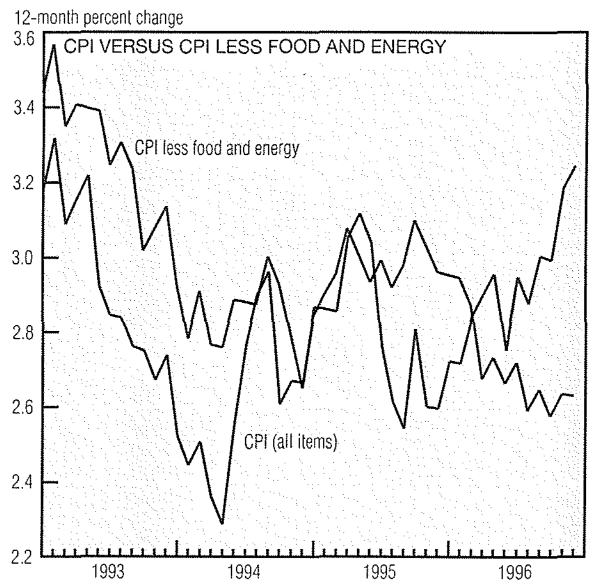
Inflation and Prices





December Price Statistics

	Annualized percent change, last:				1995
	1 mo.	6 mo.	12 mo.	5 yr.	avg.
Consumer Prices					
All items	3.1	3.0	3.2	2.8	2.6
Less food and energy	1.4	2.4	2.6	3.0	3.0
Median[c]	2.1	2.8	2.9	2.9	3.2
Producer Prices					
Finished goods	6.5	3.7	3.0	1.8	2.1
Less food and energy	1.7	0.6	0.6	1.5	2.6
Commodity futures prices[d]	3.0	−5.6	−0.7	2.9	5.4



a. Forecast of the Blue Chip panel of economists.
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.
c. Calculated by the Federal Reserve Bank of Cleveland.
d. 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.
SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; the Federal Reserve Bank of Cleveland; the Commodity Research Bureau; and *Blue Chip Economic Indicators,* January 10, 1997.

Economists' 1997 projections for retail price inflation are narrowly distributed. Nearly 70% of those polled in January's Blue Chip survey expected the Consumer Price Index (CPI) to rise between 2.8% and 3.2% this year, very close to its average increase for the past five years (2.8%). More than 60% of the Blue Chip economists expected the CPI to remain in this narrow range in 1998, and less than 10% saw inflation falling below 2.3% or rising above 3.7%.

After trending beneath the central tendency projection of the Federal Open Market Committee (FOMC) during most of 1996, the CPI's growth rate was pushed to the projection's extreme upper limit (3.2%) by a surge in consumer prices at year's end. In fact, the CPI's 12-month growth rate has been trending upward ever since reaching its recent low of about 2.6% at the end of 1995.

Much of the recent acceleration in retail prices seems centered in only a handful of components, particularly food and energy items—two areas that had a moderating influence on the CPI for most of the past five years. If we exclude these components, the CPI appears to have been trending downward over the past year or so: After reaching about 3% in mid-1995, its 12-month growth rate fell to only 2.6% by the end of 1996. This matches 1994's record as

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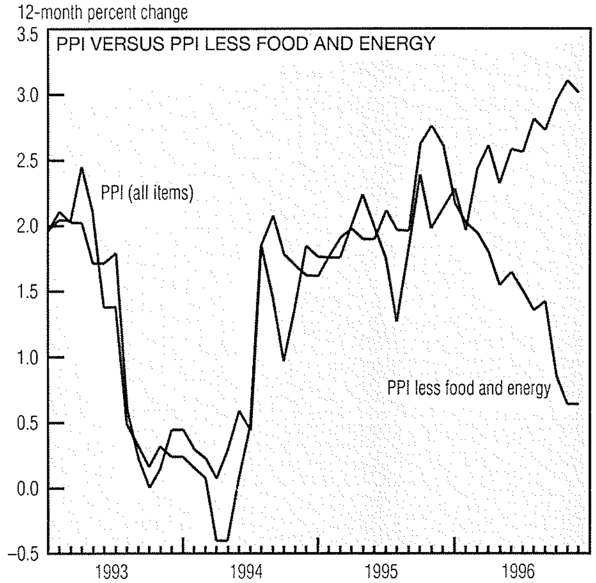
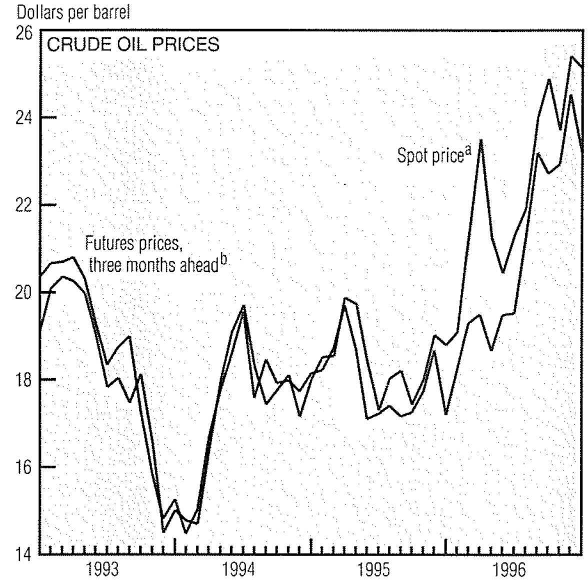
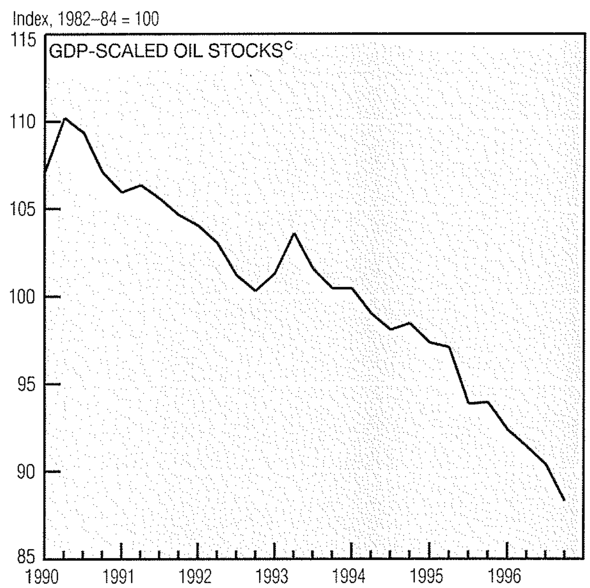
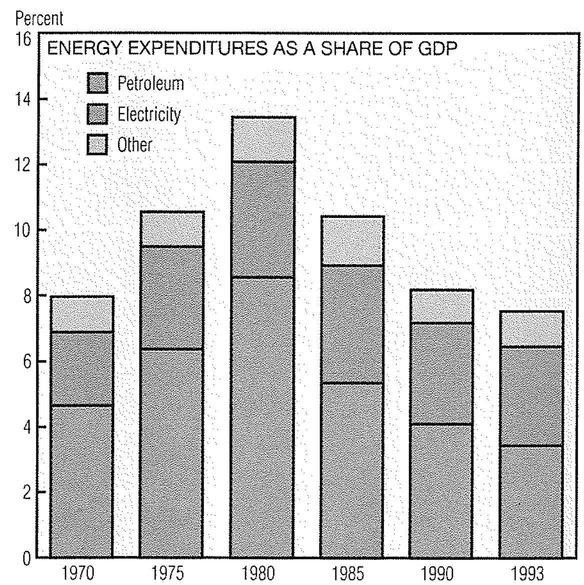
Inflation and Prices (cont.)









a. West Texas intermediate.
b. As measured by the KR–CRB composite futures index. Data reprinted with permission of the Commodity Research Bureau, a Knight-Ridder Business Information Service.
c. Ratio of barrels of oil to dollars of real GDP.
SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; U.S. Department of Commerce, Bureau of Economic Analysis; the Commodity Research Bureau; DRI/McGraw-Hill; and U.S. Energy Information Administration, *State Energy Price and Expenditure Report*.

the smallest annual increase in the index for more than 30 years.

Wide swings in food and energy prices were also major contributors to last year's jump in producer prices. The Producer Price Index for finished goods (PPI) increased 3% over the 12 months ending in December, about a percentage point higher than in 1995 and the strongest rise in six years. Nonetheless, after adjusting for changes in food and energy prices, the PPI was a substantial two percentage points lower in 1996 than in 1995, and nearly one percentage point below its five-year average increase.

The 1996 rise in energy prices broke a string of generally moderate increases for this important commodity dating back to the Gulf War. Several factors, including severe winter weather in Europe, contributed to the price surge and accelerated the downward trend in U.S. crude oil stocks that began in 1990. Commodity market participants apparently do not expect these effects to linger very long. A reading of oil futures suggests that oil prices could come down by the end of spring.

Moreover, improved energy efficiency appears to have reduced the role of oil in the economy. Expenditures on petroleum accounted for less than 4% of GDP in 1993—nearly a full percentage point less than in 1970.