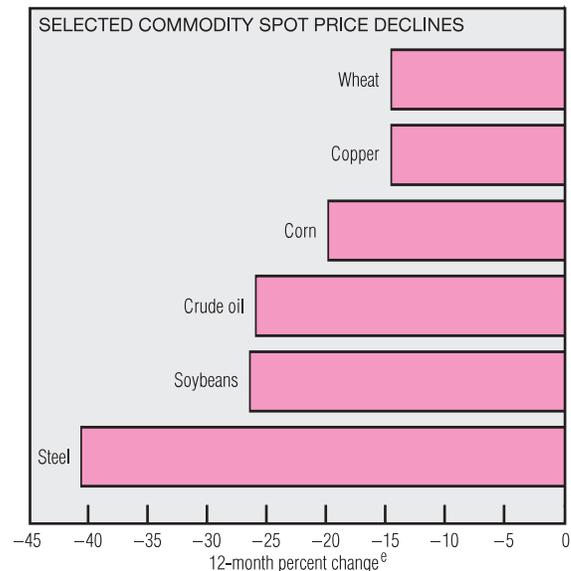
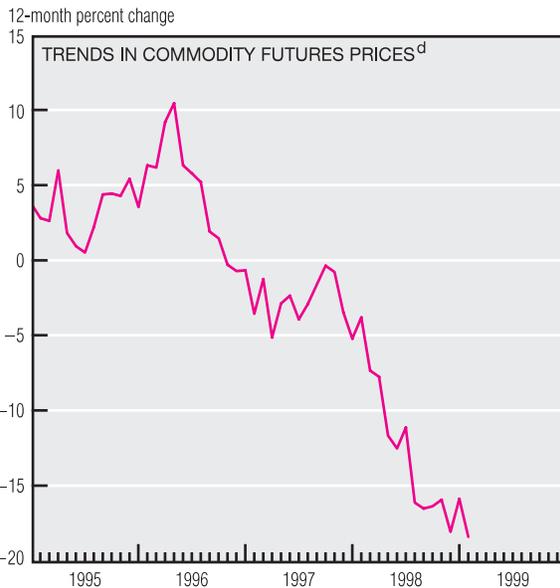
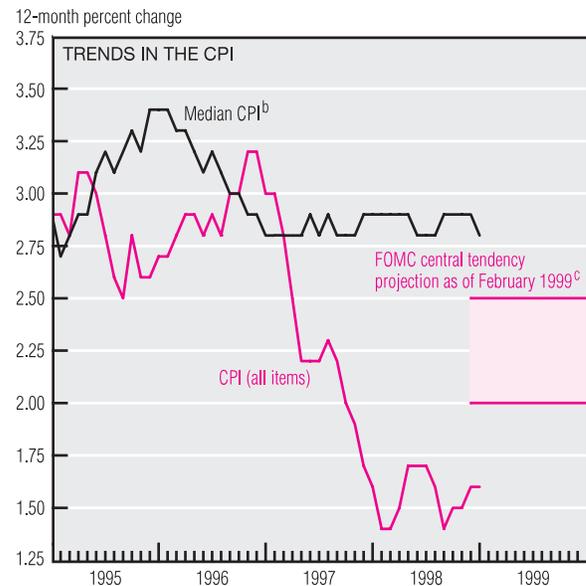


Inflation and Prices

| | Percent change, last: | | | | 1998 avg. |
|---------------------------------|-----------------------|--------------------|--------|--------------------|--------------|
| | 1 mo. ^a | 3 mo. ^a | 12 mo. | 5 yr. ^a | |
| January Price Statistics | | | | | |
| Consumer Prices | | | | | |
| All items | 1.5 | 1.7 | 1.6 | 2.4 | 1.6 |
| Less food and energy | 0.7 | 2.1 | 2.3 | 2.6 | 2.5 |
| Median ^b | 1.3 | 2.2 | 2.8 | 3.0 | 2.9 |
| Producer Prices | | | | | |
| Finished goods | 6.6 | 2.8 | 0.9 | 1.1 | -0.2 |
| Less food and energy | -0.8 | 4.5 | 2.3 | 1.4 | 2.4 |



a. Annualized.

b. Calculated by the Federal Reserve Bank of Cleveland.

c. 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.

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.

e. February 1998–February 1999.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; the Federal Reserve Bank of Cleveland; the Commodity Research Bureau; and DRI/McGraw-Hill.

Consumer prices showed little movement in January, as the Consumer Price Index (CPI) inched up an annualized 1.5%, with much of the increase caused by higher food prices. After exclusion of the volatile food and energy components, the CPI showed even less movement, rising a mere 0.7% (annualized). The median CPI, an alternative measure of inflation, showed little change in January, rising an annualized 1.3%.

At its February meeting, the Federal Open Market Committee (FOMC) left the central tendency

projection for the CPI unchanged at 2%–2.5% for 1999. The CPI is currently tracking nearly ½ percentage point under the lower bound of the central tendency, an indication that the FOMC expects consumer price pressure to increase significantly this year.

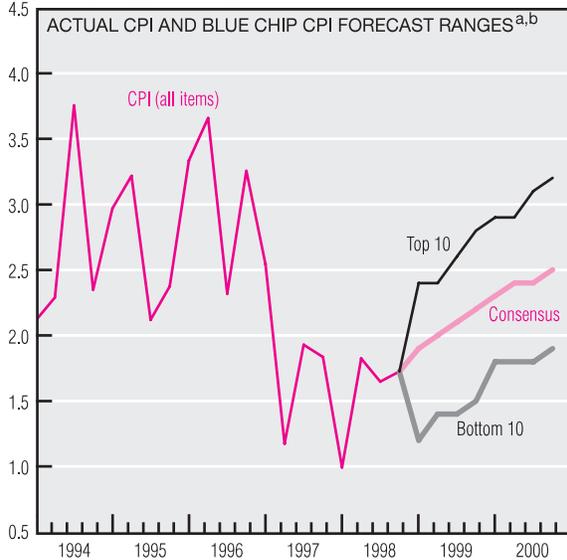
The futures price index of the Commodity Research Bureau (CRB) recently hit lows not seen since February 1975; the 12-month percent change in the index has been negative since November 1996, and its downward trend has accelerated during the past several years.

Economic weakness in Asia and Russia has reduced foreign demand for U.S. products while also creating fierce competition for the U.S. market. Since February 1998, the bushel spot price of soybeans has fallen 25%. Other agricultural products whose prices have dropped include corn (down more than 20%) and wheat (down 15%). Steel spot prices have been hit the hardest, as a flood of imported steel has driven the price down more than 40% in 12 months.

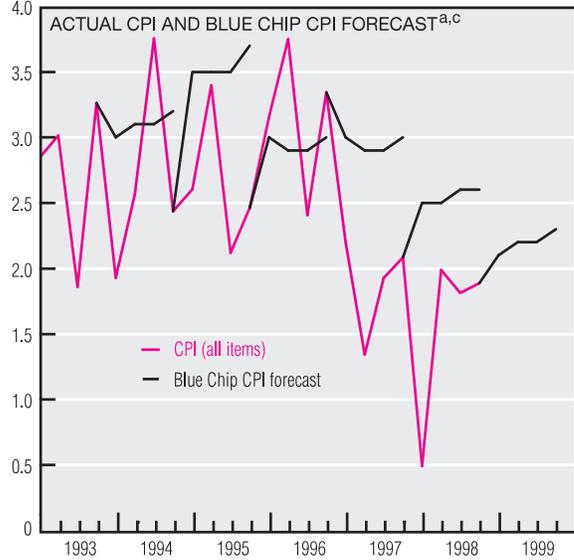
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Inflation and Prices (cont.)

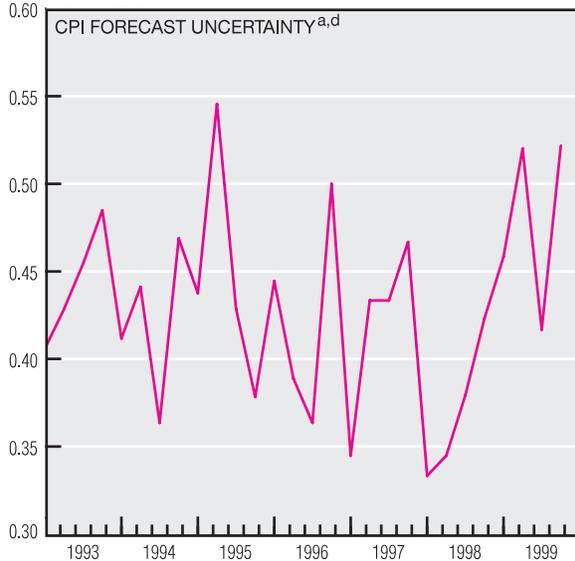
Annualized quarterly percent change



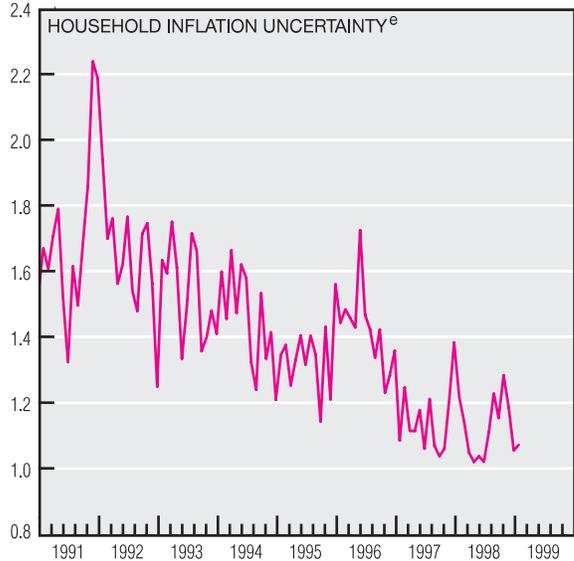
Annualized quarterly percent change



Relative percentage points



Coefficient of variation



- a. Blue Chip panel of economists.
 b. Forecast data represent annualized quarterly percent change.
 c. December 10 forecast.
 d. Top 10 forecast minus bottom 10 forecast, divided by the consensus forecast.
 e. Standard deviation of monthly responses divided by the response mean.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; *Blue Chip Economic Indicators*, various issues; and the University of Michigan's Survey Research Center.

Although the growth trend of the CPI has moderated rather sharply in the past two years, economists are calling for a pickup in CPI increases this year and next. The consensus forecast calls for consumer price increases of 2.2% by the end of 1999 and around 2½% by the middle of 2000.

However, economists have over-predicted the rise in consumer prices a disproportionate number of times in the past six years, and their inflation projections were especially far off the mark for the past two

years. In fact, economists' current inflation projections cover a wide range of opinions, with optimists seeing inflation holding around its current modest level and pessimists anticipating an inflation resurgence above 3% late next year.

The maintenance of price stability requires the central bank to provide for a stable price level *and* the expectation of its continued stability in the future. Economists' uncertainty over the price level has grown in the past year or so, presumably as they attempt to ascertain the staying

power of the recently improved inflation trend.

In contrast to economists' uncertainty, households' expectations about future inflation appear to be narrowing—a positive sign for policymakers. The amplitude of variation in households' inflation expectations (relative to the mean) has decreased markedly with their inflation projections since 1996, indicating that households have increased confidence in the persistence of a moderate inflation trend.