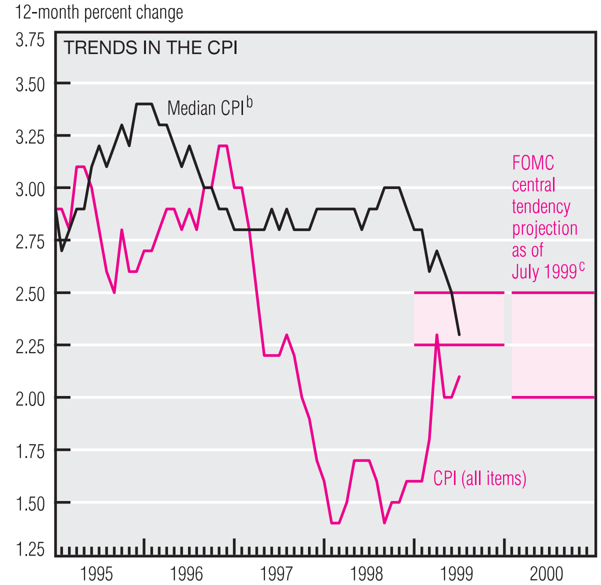
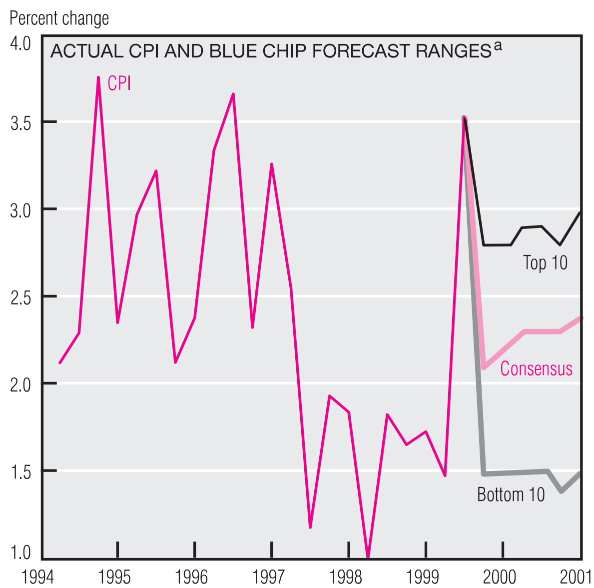
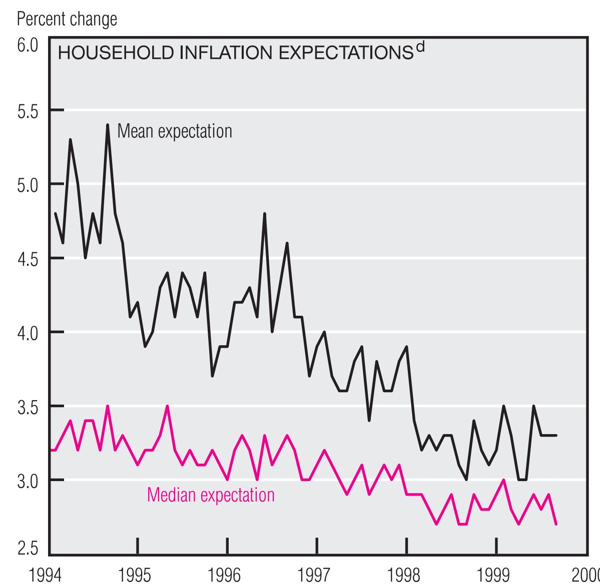
Inflation and Prices

July Price Statistics

	Percent change, last: 1 mo.[a]	3 mo.[a]	12 mo.	5 yr.[a]	1998 avg.
Consumer prices					
All items	3.7	1.2	2.1	2.3	1.6
Less food and energy	2.1	1.4	2.0	2.5	2.5
Median[b]	1.3	1.7	2.3	2.9	2.9
Producer prices					
Finished goods	2.8	1.2	1.5	1.1	−0.1
Less food and energy	0.0	−0.5	1.4	1.2	2.5







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. Expected 12-months-ahead 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; University of Michigan, Survey Research Center; and *Blue Chip Economic Indicators*, August 1999.

Prices in July were subdued on the whole, although anxiety about a reignition of inflation reportedly remains the focal point of any further adjustment to Federal Reserve policy. The CPI jumped an annualized 3.7% during the month, mostly as the result of an upward spike in energy prices. Excluding food and energy, the CPI rose 2.1% in July.

Another measure of core inflation, the Federal Reserve Bank of Cleveland's median CPI, posted only a 1.3% July gain, identical to its June advance. In fact, as the CPI trend has accelerated over the past six months or so, the median CPI has been moving lower, and the 0.2-percentage-point difference separating the 12-month growth rates of these two inflation indicators is the smallest in more than two years.

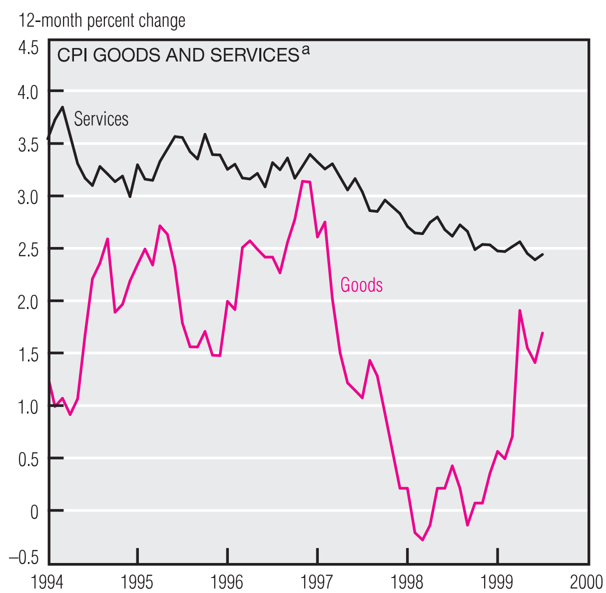
Economists seem unusually divided in their projections for retail prices over the rest of this year and next. The consensus forecast (as compiled by *Blue Chip Economic Indicators*) shows the CPI falling to a 2% pace this quarter and gradually rising to about a 2½% growth rate by the end of 2000. Inflation pessimists, however, see retail price increases remaining in the 2¾% to 3% range over the coming year, while inflation optimists expect retail price growth to fall back to the 1½% level—similar to the low inflation readings for 1998. Survey data reveal that U.S. households' year-ahead inflationary expectations have held relatively steady in the past year, generally in the range of 2¾% to 3¼%, depending on the measure used.

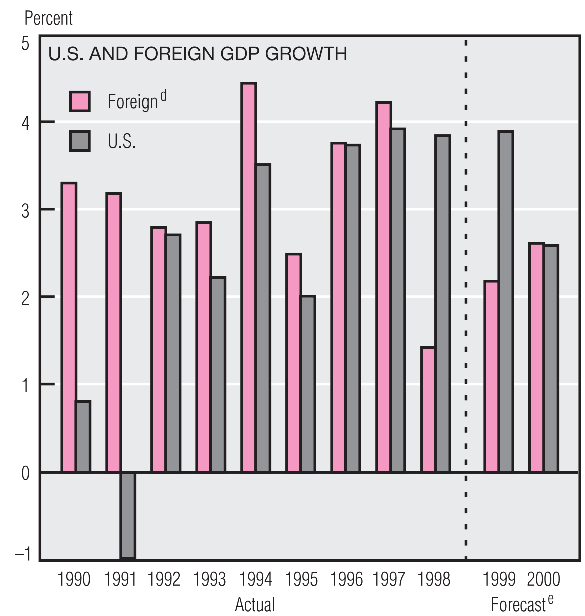
(continued on next page)

Inflation and Prices (cont.)

Consumer Prices and Imports

	Percent of CPI	Percent of imports[a]	Percent change in prices (past 24 months)[b]
CPI (all items)	—	—	1.88
Autos	5.53	42.9	–0.63
Apparel	3.57	14.9	–1.20
Footwear	0.88	2.7	–0.28
Jewelry[c]	0.32	4.5	–1.59





a. Consumer goods imports plus autos (excluding food), January–June 1999.
b. Annualized.
c. Excluding watches.
d. Trade-weighted average of the top 15 U.S. trading partners.
e. *Blue Chip Economic Indicators,* August 1999.
SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; U.S. Department of Commerce, Bureau of Economic Analysis; International Monetary Fund, *International Financial Statistics;* Organisation for Economic Co-operation and Development, *World Economic Outlook;* and *Blue Chip Economic Indicators*, August 1999.

Among the factors that could quickly turn a favorable inflation outlook unfavorable is the volatile and largely unpredictable international environment. Clearly, a strong dollar and falling import prices have helped keep U.S. retail prices flat.

The impact of falling import prices on the CPI is difficult to judge precisely, but there are indications that it is substantial. For example, four categories that account for a large share of U.S. consumer goods imports—autos and auto parts, apparel, footwear, and jewelry—have all posted price declines, on average, over the past two years. Cumulatively, these goods represent more than 60% of consumer goods imports into the U.S. and about 10% of all retail prices. Similarly, goods prices in the CPI for 1998 showed essentially no increase on average, while services prices were rising at about a 2¾% pace. One likely explanation for this divergence is that a large proportion of goods are either imported or compete directly with imports, whereas services are predominantly domestic in origin.

The key uncertainty is the impact of a strengthening world economy on U.S. retail prices. As foreign economies gain momentum and greater demands are placed on their resources, downward pressure could be felt on the U.S. dollar and import price pressure could grow. Indeed, a strengthening world economy may already have begun to push foreign goods prices upward, and this effect could intensify as we move into 2000, when many nations' economies are expected to expand at a pace similar to that of the U.S.