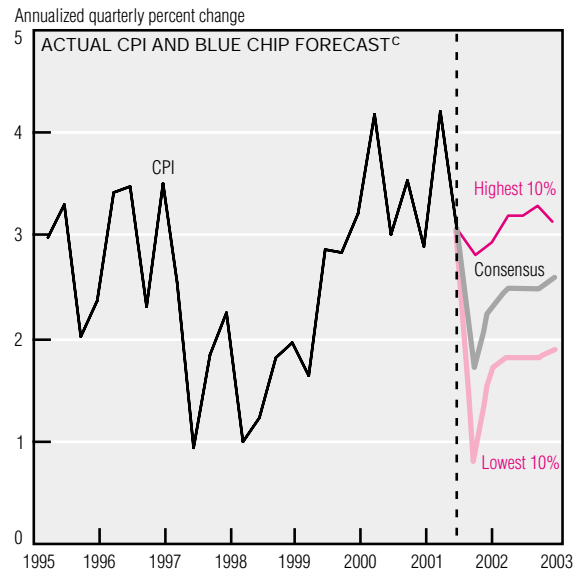
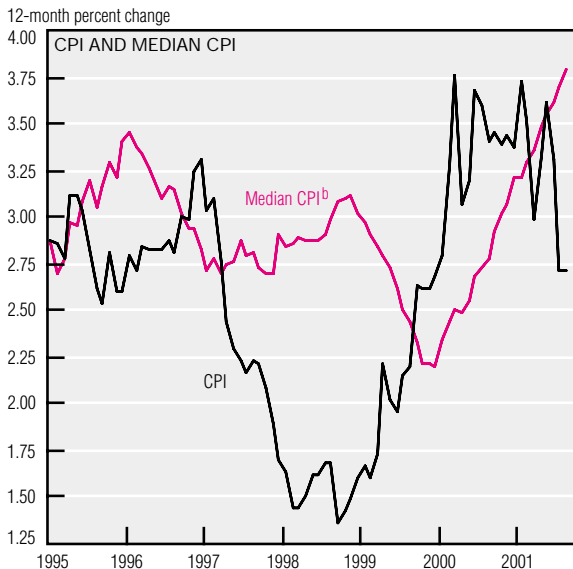
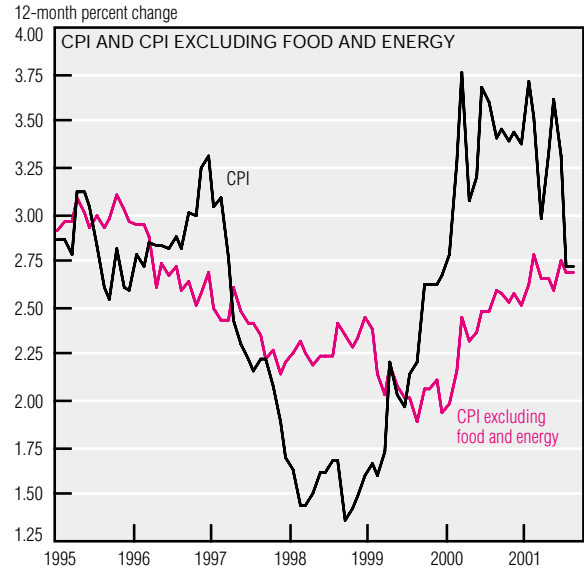


Inflation and Prices

| | Percent change, last: | | | | |
|------------------------|-----------------------|--------------------|--------|--------------------|-----------|
| | 1 mo. ^a | 3 mo. ^a | 12 mo. | 5 yr. ^a | 2000 avg. |
| Consumer prices | | | | | |
| All items | 0.7 | 0 | 2.7 | 2.4 | 3.4 |
| Less food and energy | 2.6 | 2.8 | 2.7 | 2.4 | 2.5 |
| Median ^b | 4.2 | 4.1 | 3.8 | 3.0 | 3.2 |
| Producer prices | | | | | |
| Finished goods | 4.4 | -3.6 | 2.1 | 1.4 | 3.6 |
| Less food and energy | -0.8 | 0.8 | 1.3 | 1.1 | 1.3 |



a. Annualized
 b. Calculated by the Federal Reserve Bank of Cleveland.
 c. Blue Chip panel of economists.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; Federal Reserve Bank of Cleveland; and *Blue Chip Economic Indicators*, September 10, 2001.

The overall cost of the consumer market basket, as measured by the Consumer Price Index (CPI), rose negligibly in August and has shown no net increase over the past three months. This is primarily the result of a sharp drop in energy prices. Consumer energy costs, which comprise about 8% of the CPI market basket, fell 29% (annualized) between June and August, more than offsetting the strong upward pattern of the March-May period (11.5% annualized).

If food and energy are excluded, the CPI paints a less optimistic

picture of recent retail price behavior. This "core" CPI increased 2.6% in August, slightly below its 3-month and 12-month averages of 2.8% and 2.7%, respectively. Looking deeper into the price data, there are hints of even greater inflationary pressure. Consider the median CPI, which identifies the price increase of each CPI component so that half the consumer market basket is rising more and half is rising less. By this measure, retail prices rose 4.2% in August and have been trending steadily

upward since they bottomed out at about 2.5% nearly two years ago.

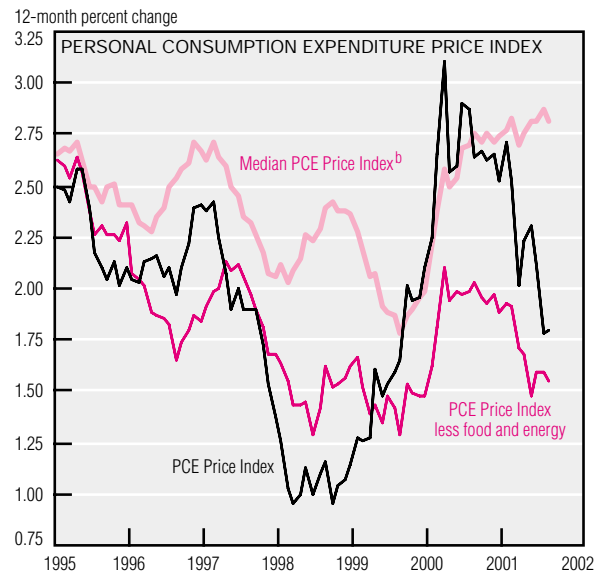
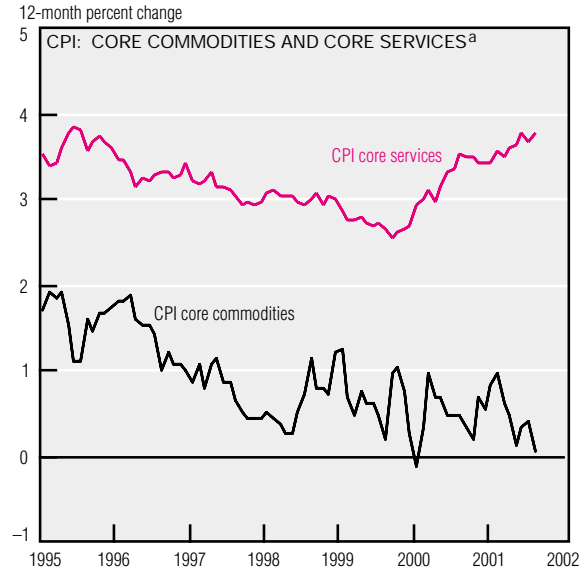
In the months ahead, economists expect the inflation trend to track recent readings of the core CPI more closely than either the CPI or the median CPI.

Mixed interpretations of the pace at which retail prices are rising are not unusual for any particular month, as wide variations in market behavior can temporarily cause different prices to move at very different rates. Such large deviations in the trend

(continued on next page)

Inflation and Prices (cont.)

| CPI Component Data | | |
|---|---|-------------------------------|
| | Annualized percent change since Feb. 2000 | Relative importance Aug. 2001 |
| Fuel oil and other fuels | -6.8 | 0.3 |
| Men's and boys' apparel | -4.1 | 1.2 |
| Infants' and toddlers' apparel | -3.4 | 0.2 |
| Women's and girls' apparel | -2.8 | 1.7 |
| Miscellaneous personal goods | -2.3 | 0.2 |
| Motor fuel | -1.4 | 3.2 |
| Car and truck rental | -1.1 | 0.1 |
| Jewelry and watches | -1.0 | 0.4 |
| Communication | -0.8 | 2.5 |
| New vehicles | -0.4 | 4.6 |
| Footwear | -0.2 | 0.8 |
| Personal care products | 0.9 | 0.7 |
| Household furnishings and operations | 0.9 | 4.5 |
| Nonalcoholic beverages and beverage materials | 1.5 | 1.0 |
| Motor vehicle fees | 1.7 | 0.6 |
| Recreation | 1.8 | 5.9 |
| Used cars and trucks | 1.8 | 1.9 |
| Fresh fruits and vegetables | 2.6 | 1.1 |
| Other food at home | 2.7 | 1.9 |
| Tenants' and household insurance | 2.7 | 0.4 |
| Food away from home | 2.8 | 5.7 |
| Water and sewer and trash collection services | 2.8 | 0.9 |
| Alcoholic beverages | 2.9 | 1.0 |
| Motor vehicle parts and equipment | 2.9 | 0.5 |
| Public transportation | 3.0 | 1.4 |
| Cereals and bakery products | 3.1 | 1.5 |
| Processed fruits and vegetables | 3.1 | 0.3 |
| Dairy and related products | 3.3 | 1.1 |
| Motor vehicle maintenance and repair | 3.4 | 1.6 |
| Lodging away from home | 3.5 | 2.3 |
| Personal care services | 3.6 | 1.0 |
| Medical care commodities | 3.7 | 1.3 |
| Owners' equivalent rent of primary residence | 3.7 | 20.7 |
| Motor vehicle insurance | 3.8 | 2.5 |
| Rent of primary residence | 4.3 | 7.2 |
| Miscellaneous personal services | 4.5 | 1.5 |
| Meats, poultry, fish and eggs | 4.6 | 2.6 |
| Medical care services | 4.7 | 4.6 |
| Education | 5.5 | 2.8 |
| Tobacco and smoking products | 7.1 | 1.4 |
| Gas (piped) and electricity | 10.6 | 4.1 |



a. Excluding food and energy.

b. Calculated by the Federal Reserve Bank of Cleveland.

SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; U.S. Department of Commerce, Bureau of Economic Analysis; and Federal Reserve Bank of Cleveland.

growth rates of the inflation measures, however, are peculiar; market-specific changes in consumer prices tend to be obscured by the longer-term inflationary rise that is common to all prices.

The table above reports the average annualized increase for 42 CPI components between February 2000 and August 2001, a period when the three CPI measures diverged. Energy, auto, and apparel goods represent a disproportionate share of the CPI components that fell during the period. On the other hand, a large

number of service-related costs showed rather ominous increases over the 18-month span. About 57% of the CPI market basket posted an average increase of 3% or more (annualized) over this time. Rents, miscellaneous personal services, medical care services, and education (which, combined, represent about 16% of the CPI market basket) all have shown average annualized price increases in excess of 4% since February 2000.

The widening gap between the cost of goods and the cost of services

has an important influence on how one views the recent retail-price performance. Consider the Price Index for Personal Consumption Expenditures (PCE), which has shown a moderating tendency on both a total and "core" basis over the past year or so. This measure gives less weight to some key retail components, such as medical care and owners' equivalent rent. Still, the median price change in these data, like the median CPI, has been moving steadily higher for more than two years.