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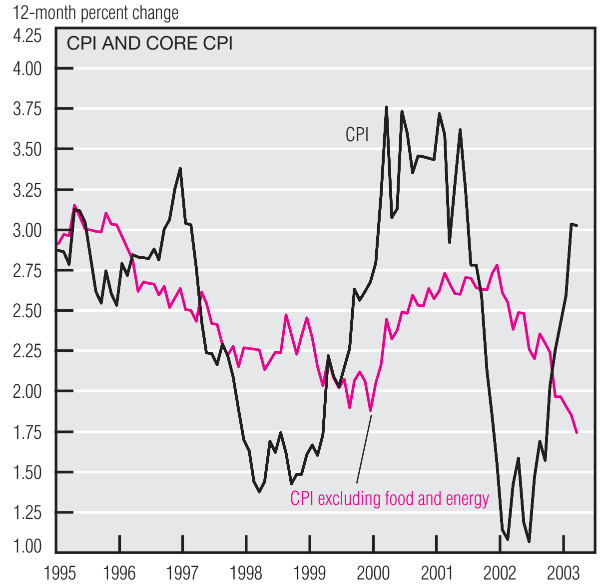
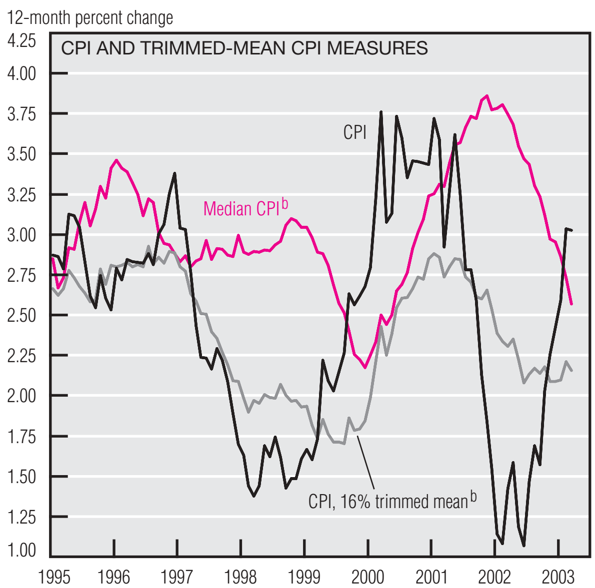
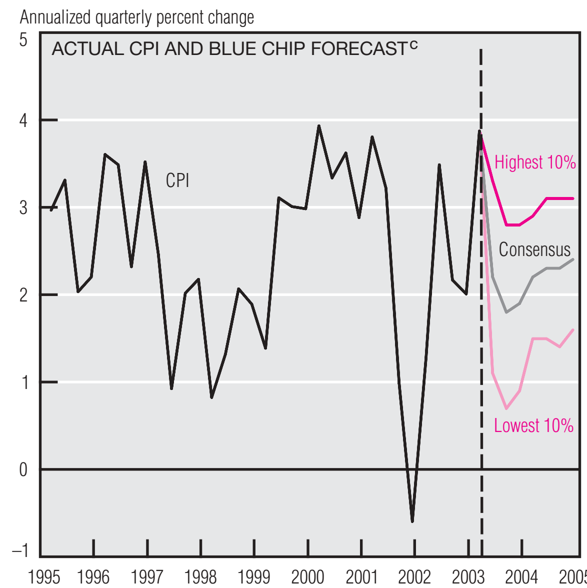
Inflation and Prices

March Price Statistics

	Percent change, last: 1 mo.[a]	3 mo.[a]	12 mo.	5 yr.[a]	2002 avg.
Consumer prices					
All items	4.0	5.2	3.0	2.6	2.4
Less food and energy	0.0	0.8	1.7	2.3	2.0
Median[b]	1.1	2.0	2.6	3.0	3.0
Producer prices					
Finished goods	19.1	17.4	4.2	2.1	1.2
Less food and energy	9.1	4.6	0.9	1.1	–0.5







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*, April 10, 2003.

The Consumer Price Index (CPI) jumped an annualized 4% in March and has risen 5.2% over the first three months of 2003. Outsized increases in energy costs were again responsible for its rapid rise; the energy sector has been an aggravating influence on the accelerating increase (on a year-over-year basis) in the cost of the representative consumer's market basket. After excluding food and energy, however, the market basket's cost increases have been mostly flat this year and have shown only a modest 1.7% increase from last year, a sign that there has been little underlying inflationary pressure outside the energy sector. Indeed, the median CPI, an alternative measure of the general rise in consumer prices, has been moderating over the past 18 months, and its current 12-month reading of 2.6% is the lowest since mid-2000.

Whether the inflation trend will continue its downward course is unclear, of course, but even the most pessimistic economists do not expect the CPI's behavior to worsen. In fact, the highest 10% of inflation forecasts from the Blue Chip panel of economists predict a CPI growth trend of around 3%, the current 12-month rate. The panel's consensus forecast puts the inflation trend down around $2\frac{1}{2}$% over the next 18 months, while the optimists see inflation moving down to $1\frac{1}{2}$% over the same horizon.

From an arithmetic perspective, the moderation in the underlying inflation trend has resulted from a downward tilt in the rate of service price increases. Excluding energy-related services, the growth trend in services prices, which seem to have peaked around 4% early last year, has

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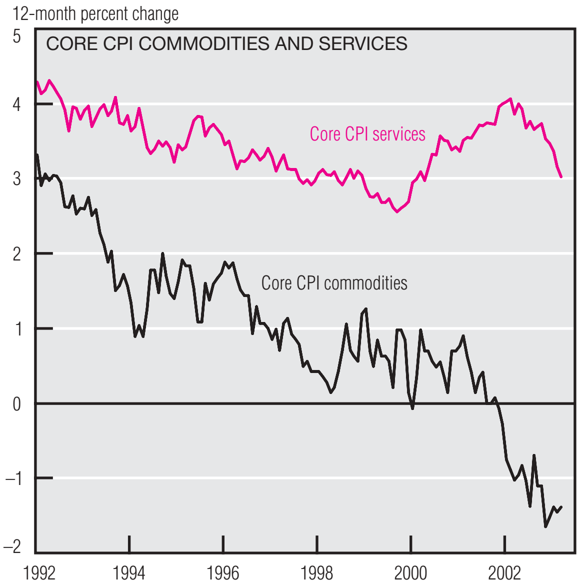
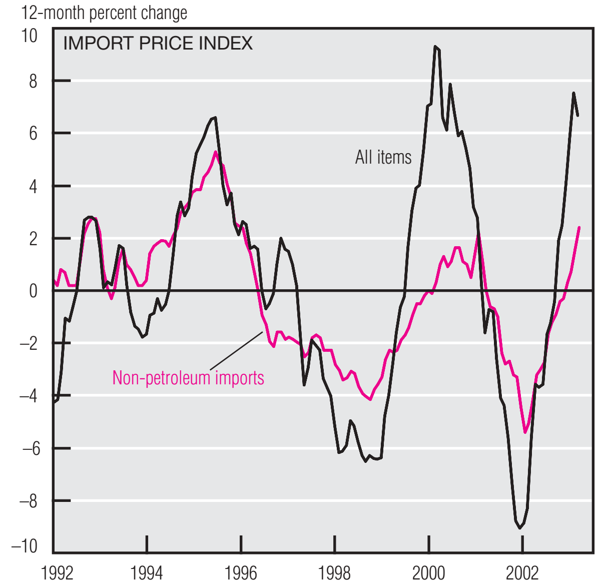
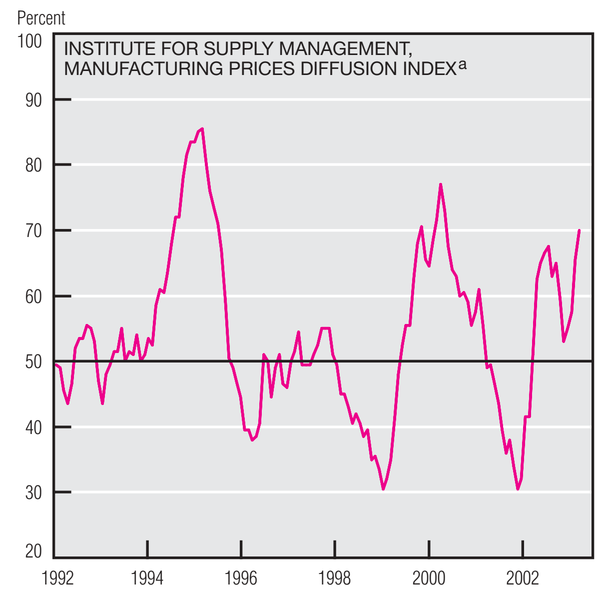
Inflation and Prices *(cont.)*





Producer Price Index, Major Industries[a]

	Annualized percent change			
	3 mos.	12 mos.	5 yrs.	10 yrs.
Total manufacturing industries	15.1	4.6	2.0	1.5
Food and kindred products	5.8	2.0	1.4	1.3
Apparel and other finished products made from fabrics	0.6	0.2	0.2	0.5
Lumber and wood products except furniture	2.9	–0.9	–0.4	0.3
Furniture and fixtures	2.2	1.1	1.1	1.7
Chemicals and allied products	10.7	5.5	1.9	2.6
Petroleum refining and related products	313.2	63.7	17.4	6.2
Rubber and miscellaneous plastic products	8.9	3.0	0.9	1.1
Primary metal industries	–0.3	3.0	–0.8	0.6
Fabricated metal products except machinery and transportation equipment	1.2	1.1	0.6	1.2
Machinery except electrical	–1.4	–1.3	–0.3	–0.1
Transportation equipment	9.1	1.4	0.9	1.1
Electrical and machinery equipment and supplies	–1.5	–2.3	–1.2	–0.7



a. Not seasonally adjusted.
SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; and Institute for Supply Management.

fallen steadily to about 3% since then. Because such costs account for more than half of the consumer's market basket, this downward trend has eased inflation in non-energy household expenses. Meanwhile, the cost of consumer goods (less food and energy) continues to show outright declines—down about 1½% over the past 12 months.

The persistent decline in goods prices has doubtless helped raise the specter of deflation seen by some business analysts. Certainly, outright declines in prices have been occurring for certain goods, like communications equipment, for some time now. But deflation of the sort that usually troubles economists involves more than price declines in a subset of goods. Rather, deflation is a condition in which price declines are seen across a broad range of goods and services. Economists seem somewhat divided as to whether such a deflationary episode is likely in the U.S. Some of them observe that the Federal Reserve has the tools to prevent such an occurrence, but others are less confident.

Still, there may be reason to believe, albeit tentatively, that the downward slide in consumer goods prices is coming to an end. Import prices, which contributed to the drop in consumer goods prices in recent years, are now showing their largest increases in about seven years. In addition, price increases posted by U.S. manufacturers have been increasing strongly this year across a range of industries, a development that is consistent with the price hikes reported by an increasing share of the nation's purchasing managers.