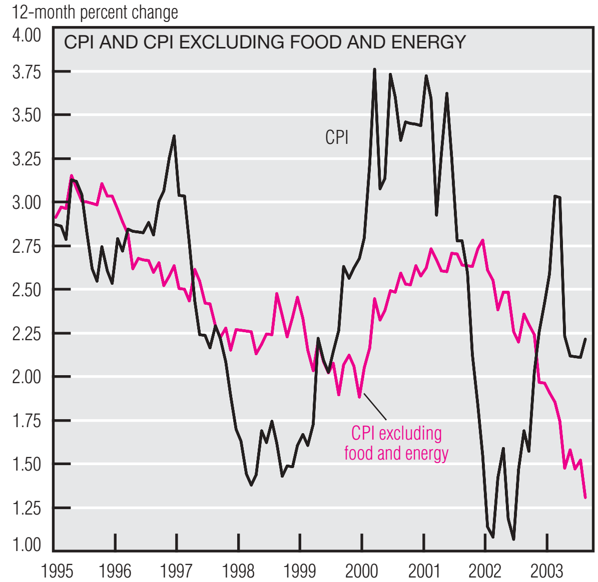
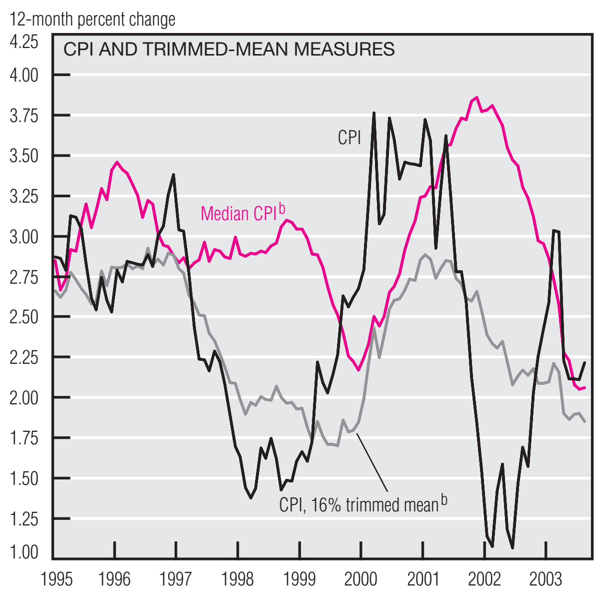
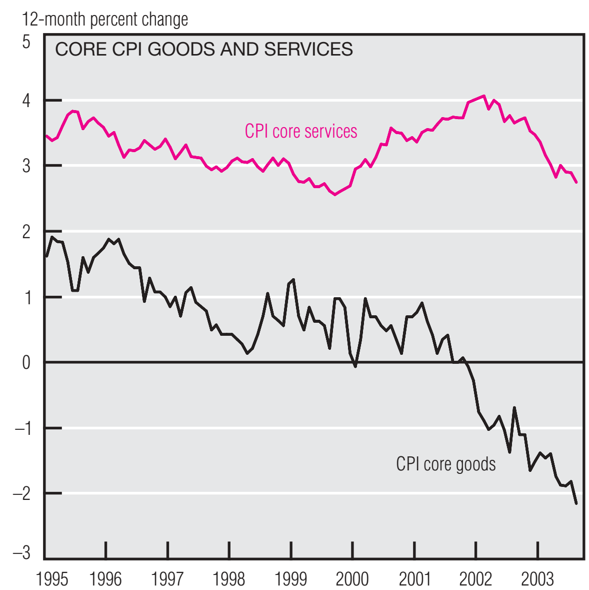
Inflation and Prices

August Price Statistics

	Percent change, last: 1 mo.[a]	3 mo.[a]	12 mo.	5 yr.[a]	2002 avg.
Consumer prices					
All items	4.0	2.6	2.2	2.5	2.4
Less food and energy	1.2	1.2	1.3	2.2	2.0
Median[b]	2.8	2.2	2.1	2.9	3.0
Producer prices					
Finished goods	5.2	4.3	3.5	1.9	1.2
Less food and energy	1.6	0.8	0.5	0.9	–0.5







a. Annualized.
b. Calculated by the Federal Reserve Bank of Cleveland.
SOURCES: U.S. Department of Labor, Bureau of Labor Statistics; and Federal Reserve Bank of Cleveland.

The Consumer Price Index (CPI) rose 0.3% in August (4.0% at an annual rate), compared with increases of 0.2% (2.0% annualized) in the previous two months. Part of the CPI's acceleration resulted from a sharp increase in its energy index, which rose 2.7% in August after far more modest monthly increases (0.8% in June and 0.4% in July). The primary reason for energy's abrupt jump was an outsize increase in the gasoline index, which rose more than 6% (an annualized rate exceeding 100%), the component's largest monthly increase since February.

Excluding energy prices, as well as the often-volatile food component, yields a less pronounced increase in inflation. According to the CPI excluding food and energy, sometimes called the core CPI, prices rose 0.1% in August (1.2% annualized). The median CPI and the 16% trimmed-mean CPI, other inflation measures intended to be less influenced by volatile items, also showed smaller August increases than the unadjusted CPI. Each of these trimmed-mean measures rose about 0.2%.

For the 12 months ending in August, the CPI rose 2.2%. If food and energy are excluded, inflation according to the core CPI increased 1.3%. Clearly, removing some components from the CPI changes the price trend picture significantly. Breaking down the core CPI further shows a growing price gap between core goods and core services. Underlying inflation in the economy's service sector seems to have settled at around 3%. In the goods-producing portion of the

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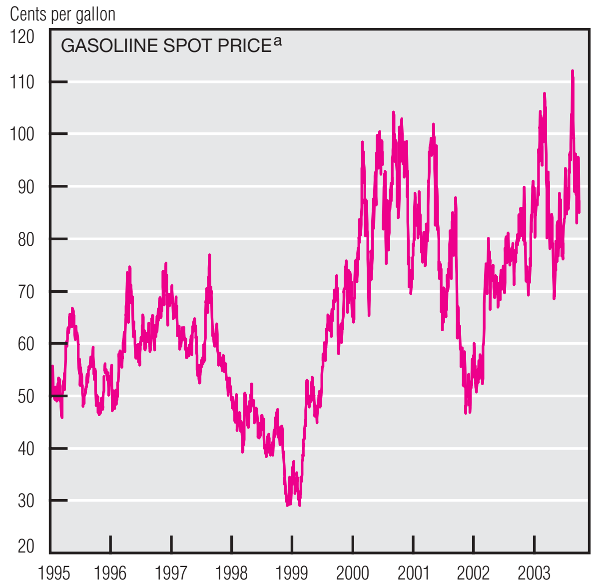
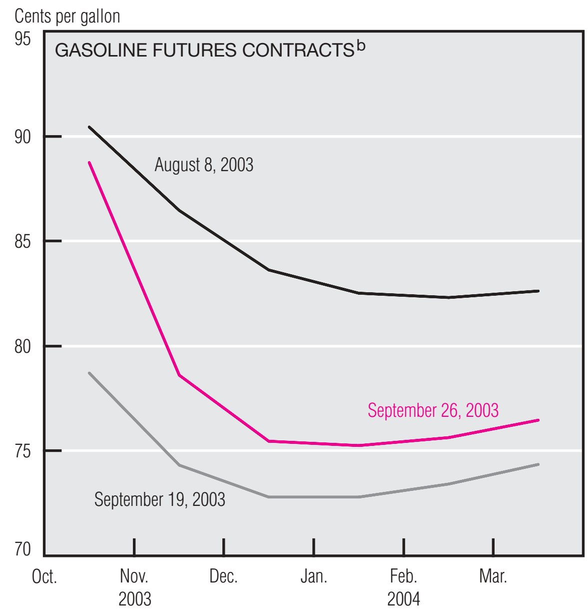
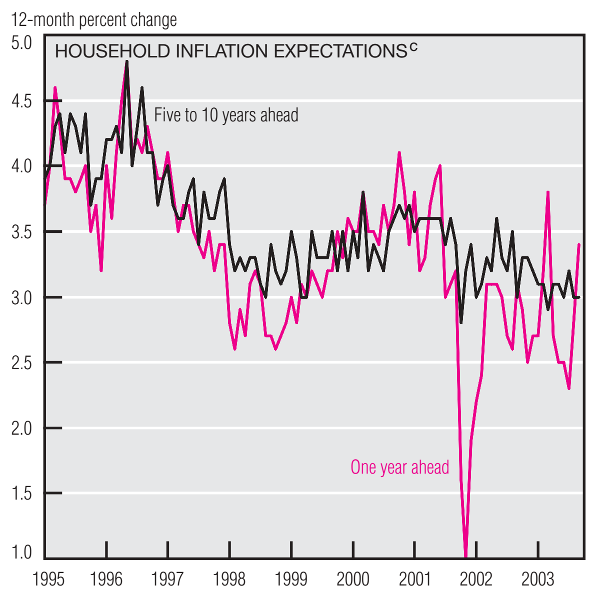
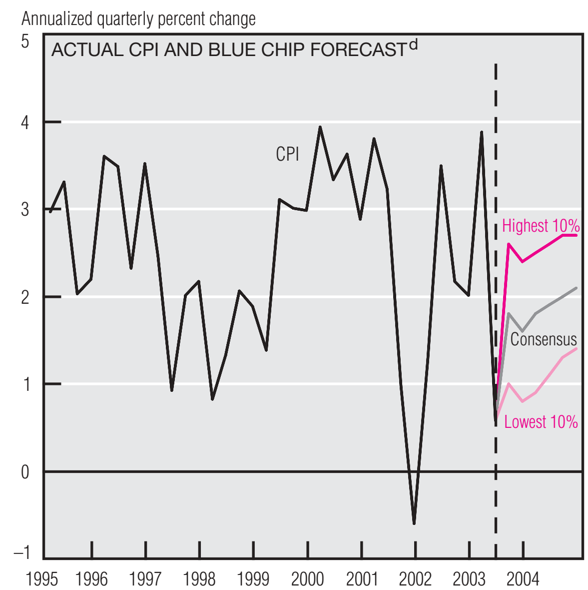
Inflation and Prices *(cont.)*









a. New York Gasoline Conventional Regular Spot Price.
b. New York Phase II Complex Model Reformulated Gasoline.
c. Mean expected change in consumer prices as measured by the University of Michigan's *Survey of Consumers*.
d. Blue Chip panel of economists.
SOURCES: U.S. Department of Energy, Energy Information Administration; University of Michigan; Bloomberg Financial Information Services; and *Blue Chip Economic Indicators*, September 10, 2003.

economy, however, an underlying deflation continues.

While the advance in gasoline prices accounted for much of August's CPI acceleration, spot gasoline prices have since fallen significantly, more than 10% during September. Prices did spike upward late in the month, after the Organization of Petroleum Exporting Countries (OPEC) announced its intention to curtail crude oil supplies. But this increase was short-lived, and prices have since fallen below pre-announcement levels.

The prices of gasoline futures contracts were also affected by OPEC's announcement. But aside from the October contract, prices for future delivery of gasoline into the first quarter of next year remain well below the levels of early August. And the trend in prices into the future is still decidedly downward.

Nevertheless, August's pronounced increase in gasoline prices may have affected households' short-run expectations of inflation. Year-ahead household inflation expectations rose 0.6% in September and are up 1.1% since July. By contrast, households' longer-run inflation expectations have stayed reasonably well anchored at around 3%. Professional forecasters, attempting to predict the CPI's path, expect the index to register an annualized increase of about 2% over the next 18 months. The range of their opinions is rather wide, however, with about 1.5 percentage points separating inflation pessimists from inflation optimists.