The Economy in 1993

The economy recorded significant gains in 1993, lifted, as in 1992, by a surge in activity in the latter part of the year. Job creation picked up, and the unemployment rate fell appreciably. Inflation continued to trend lower.

The rise in real gross domestic product over the year amounted to about 3¼ percent, according to preliminary data from the Department of Commerce. For a second year, the growth of activity was propelled chiefly by rapid gains in the investment outlays of households and businesses. Households boosted their purchases of homes and motor vehicles considerably, and spending for household durables also rose rapidly. Business investment in computers continued to grow at an extraordinary pace in 1993, and outlays for other types of capital equipment strengthened. Investment in nonresidential structures, which had gone through a protracted decline in the latter part of the 1980s and early 1990s, rose moderately. Bolstered by the gains in these sectors, the four-quarter rise in the final purchases of households and businesses amounted to 5 percent in real terms in 1993, matching the large 1992 rise. Not since the 1983–84 period had private final purchases exhibited a comparable degree of strength.

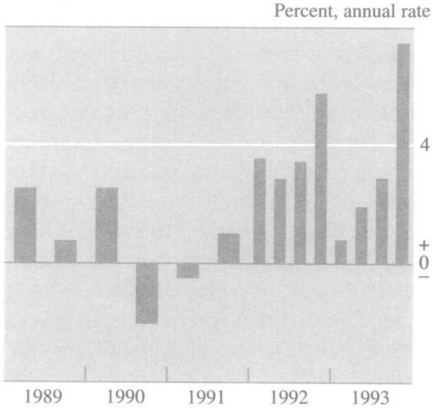
The increase in private spending in 1993 was augmented by a pickup in the spending of state and local governments, especially for construction. By contrast, real federal purchases of goods and services—the part of federal spending that is included in GDP—fell sharply, as outlays for national defense continued to trend lower. The federal budget deficit declined somewhat in fiscal 1993, but the combined deficit in the operating and capital accounts of state and local governments increased further.

Growth of the economy continued to be significantly influenced in 1993 by the changing patterns of transactions with foreign economies. The weakness of activity in a number of foreign countries that are major trading partners of the United States tended to limit the gains in U.S. exports of goods and services. At the same time, a significant portion of the rise in domestic spending in this country continued to translate into rapid increases in imports. Net exports of goods and services thus fell for the second year in a row, after a run of several years in which real export growth had outpaced the growth of real imports by a considerable margin.

The CPI rose 2.7 percent over the four quarters of 1993, after increases of about 3 percent in both 1991 and 1992. Price increases were damped last

Change in Real GDP

Percent, annual rate



The data are seasonally adjusted and come from the Department of Commerce; they are measured in terms of 1987 dollars.

year by falling oil prices, near-stable prices for non-oil imports, and a further rise in labor productivity, which held down production costs in the domestic economy.

The Household Sector

Consumer spending recorded a second year of brisk growth in 1993. Support for the rise in expenditures came from declines in interest rates and moderate increases in real incomes. Household balance sheets continued to strengthen in 1993 and debt servicing burdens diminished, easing the financial strains that had inhibited spending earlier in the 1990s.

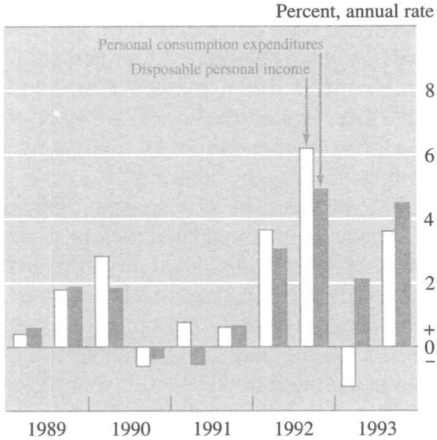
In real terms, the 1993 advance in personal consumption expenditures (fourth quarter to fourth quarter) amounted to about 3¼ percent. After surging in late 1992, growth of real outlays slowed in the first quarter of 1993. Whatever tendency there may have been for a "payback" after a period of unusually rapid growth was reinforced by a severe late-winter storm on the East Coast, which temporarily hurt retail sales. Thereafter, spending proceeded at a relatively strong pace over the remaining three quarters of the year.

Consumer expenditures for motor vehicles increased 6 percent in real terms over the four quarters of 1993, after rising 9 percent the previous year. The advance in expenditures continued to come partly from the replacement needs of individuals who had put off buying vehicles earlier in the 1990s, as well as from growth in consumers' desired stock of vehicles. Increasingly, buyers have opted for vans, light trucks, and other vehicles instead of cars, and annual sales of these vehicles in 1993 reached the highest level on record. Car sales also rose, but they remained well below previous highs.

Expenditures for a number of other types of durable goods also rose rapidly in 1993. Outlays for furniture and appliances scored further hefty gains, in conjunction with sharp increases in sales of new and existing homes. Consumer purchases of home computers and other electronic equipment remained on a steep uptrend. In total, outlays for durable goods other than motor vehicles increased more than 9 percent over the year, after a rise of 10 percent in 1992. Other types of consumer expenditures, which typically exhibit less cyclical variation than do outlays for durables, rose moderately, on balance, during 1993. Consumer purchases of nondurable goods increased about 2 percent, after a jump of more than 3½ percent in 1992. Spending for services rose nearly 3 percent during 1993, an increase of roughly the same magniture as that of the previous year.

Real income continued to advance in 1993, although its trend was masked by tax considerations that caused a sizable volume of bonuses that would have been

Change in Real Income and Consumption



The data are seasonally adjusted and come from the Department of Commerce; they are measured in terms of 1987 dollars.

paid to workers in early 1993 to be shifted into the latter part of 1992. Abstracting from these shifts in timing, the beneficial effects of continued economic expansion showed through in most categories of income, much as they had in 1992. Wage and salary accruals, a measure of income as it is earned rather than as it is disbursed, rose about 4½ percent in nominal terms over the four quarters of 1993, considerably outpacing the rate of inflation for the second year in a row. Further gains also were reported over the course of 1993 in dividends and in the income of proprietors, both farm and nonfarm. Transfer payments, which tend to vary inversely with the state of the economy, slowed in 1993 after rising at rates of 10 percent or more in each of the four previous years. Interest income, which had declined on net in 1991 and 1992, edged up slightly over the four quarters of 1993. Because of the shift in timing of bonuses, growth of real disposable income in 1993 was noticeably less than in 1992. However, the cumulative gain over the two-year period was about 6 percent, a clear step-up from the performance of the three previous years, when real income growth had averaged less than 1 percent per year.

The personal saving rate—measured as the percentage of nominal after-tax income disbursements that are not used for consumption or other outlays—declined nearly 2 percentage points, on net, over the course of 1993. However, the saving rate in late 1992 had been temporarily elevated by the aforementioned speedup of bonus payments. Looking through that blip of late 1992, a downward drift still is evident in the saving rate from mid-1992 to the end of 1993. Such a pattern is not uncommon when economic recovery is taking hold and consumer purchases of durable goods are rising rapidly. In effect, households have been holding part of their saving in the form of consumer durables, which, at the time of purchase, are counted fully as consumption in the national accounts, but which in reality will yield households a flow of services over time.

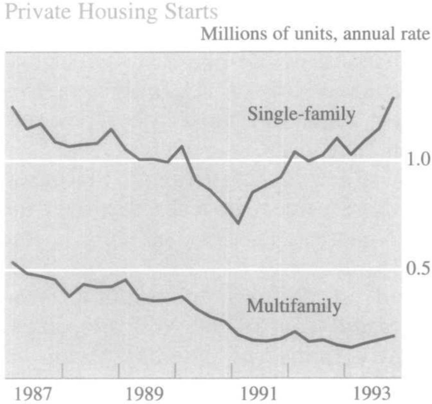
Household wealth rose further in 1993. As in 1992, the total nominal value of household assets increased at a pace moderately faster than the rate of inflation. Large increases in stocks and bonds boosted the nominal holdings of financial assets, more than offsetting a reduction in the aggregate holdings of deposits and credit market instruments. The nominal value of tangible assets was lifted by heavy investment in consumer durables and residential structures and by a rise in the average price of existing residential properties. With a jump in the growth of consumer credit and a slight pickup in the growth of home mortgage debt, household liabilities rose somewhat faster than in 1992. Nonetheless, net worth appears to have increased in both real and nominal terms. The incidence of financial stress among households diminished further in 1993, as delinquency rates on various types of household debt continued to decline, in some cases to the lowest levels since the first half of the 1970s. According to survey data, households' own assessments of their financial situations improved, on net, with some survey readings the most upbeat in more than three years.

Residential investment increased nearly 8 percent in real terms over the four quarters of 1993, building on the 18 percent rise of 1992. As in 1992, most of the advance came from increased construction of new single-family homes. The construction of multifamily housing continued to be adversely affected by a persistent overhang of vacant rental units.

In the single-family market, the impetus for activity continued to come mainly from declines in mortgage interest rates, which by autumn had dropped to their lowest levels in more than two decades. Fairly sharp declines in mortgage interest rates took place early in the year, but the effect on housing activity was apparently short-circuited for a time by a number of influences. A severe blizzard on the East Coast in mid-March temporarily waylaid the start-up of construction in that region, and a huge run-up in lumber prices during late winter also may have discouraged some new construction for a while. Concerns about the possible loss of jobs perhaps continued to deter some potential homebuyers. Other buyers may simply have been holding back, waiting to see how far rates eventually would fall.

In any event, the effects of the drop in mortgage rates began to show through with greater force over the summer and fall, and considerable strength had emerged by year-end in all the major indicators of single-family housing activity. Sales of existing homes rose without interruption from April on. By the fourth quarter they had climbed to the highest level on record (the series goes back to 1968). Although sales of new homes proceeded more erratically from month to month, their increase over the four quarters of the year amounted to nearly 25 percent. Housing construction also strengthened. The number of single-family starts increased about 18 percent over the year, reaching the highest quarterly level since 1979. According to survey data, consumers' assessments of home-buying conditions continued to be very upbeat at year-end, as were builders' ratings of market conditions.

Private Housing Starts



The data are seasonally adjusted and come from the Department of Commerce.

Activity in the multifamily housing market remained depressed in 1993. In the mid-1980s, tax incentives and the relatively easy availability of credit encouraged overbuilding in many locales. The proportion of multifamily rental units that were vacant soared and has remained high even as the construction of multifamily units has dwindled. Starts of these units reached the lowest levels on record early in 1993, and they picked up only slightly thereafter, despite restoration of tax credits for low-income units.

The Business Sector

The year saw appreciable gains in most important barometers of business activity. Output of the nonfarm business sector increased more than 4 percent, slightly more than during 1992. Profits rose further, business balance sheets continued to strengthen, and capital spending surged.

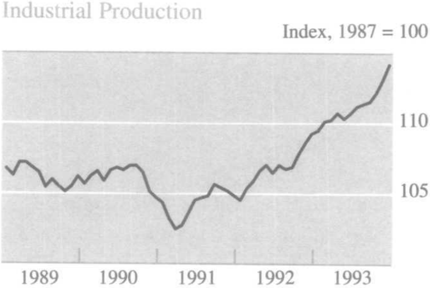
In the industrial sector, production rose 4¼ percent, the largest advance in six years. The production gain was at least moderate in each quarter, and in the final quarter it was quite large—on the order of 6¾ percent at an annual rate. Output of business equipment held to a strong uptrend throughout the year, as did the production of materials that are used as inputs in the durable goods industries. The output of construction supplies rose moderately in the first half of the year and at a stronger pace in the second half. Motor vehicle assemblies also rose appreciably, with strength early in 1993 and in the year's final quarter more than offsetting a stretch of sluggishness through the middle part of the year. By contrast, output of consumer goods other than motor vehicles rose only a small amount, and production of defense and space equipment fell 9½ percent further, extending a downward trend that began in 1987.

The amount of spare capacity in the industrial sector continued to diminish. The utilization rate in December, 83.0 percent, was up more than 2 percentage points from the level of a year earlier and was at the highest level since the summer of 1989. In manufacturing, capacity use in primary-processing industries was above its long-run average throughout 1993, and the rate of utilization in advanced-processing industries had moved up almost into line with its long-run average by year-end.

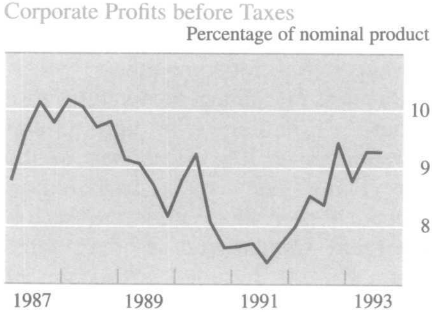
Corporate profits, which had surged in 1992, increased an additional 6½ percent over the first three quarters of 1993 and appear to have risen further in the year's final quarter. Financial institutions in general continued to benefit in 1993 from the persistence of a relatively wide margin between their cost of funds and the interest rates on their assets; insurers' profits suffered less drag from natural disasters than in 1992, the year of hurricane Andrew. The profits of nonfinancial corporations moved up slightly further over the first three quarters, boosted by the rise in the volume of output over that period. Operating profits per unit of output held fairly steady, close to the high level reached in the final quarter of 1992. Although nonfinancial corporations raised their prices by only a small amount over those three quarters, they were able to maintain unit profit margins through continued tight control over costs. Gains in productivity restrained the rise in unit labor costs, and net interest expenses per unit of output continued to edge lower.

Business fixed investment increased 15 percent in real terms over the four quarters of 1993, after a rise of 7½ percent in 1992. A spectacular increase in outlays for office and computing equipment accounted for about half of the 1993 gain. Business expenditures for these items increased more than 25 percent in nominal terms over the year, the steepest annual gain since 1984, and the rise in real terms was greater still. The latest computers are far more powerful than those that were at the forefront only

Industrial Production



Corporate Profits before Taxes



Profits of nonfinancial corporations from domestic operations, with adjustments for inventory valuation and capital consumption, divided by GDP of nonfinancial corporate sector.

a few years ago, and highly competitive market conditions have kept prices on a downward course. The many businesses eager to boost labor productivity and overall operating efficiency provided a huge market for the new products.

Excluding office and computing equipment, outlays for capital equipment increased about 11½ percent in real terms during 1993, the biggest rise in ten years. Business expenditures for motor vehicles advanced about 14 percent, as investment in trucks, which had strengthened considerably in 1992, climbed further. Factories producing heavy trucks were operating at or near full capacity at year-end. Spending for communication equipment also advanced sharply, as did real outlays for many other types of machinery and equipment. Diminished slack in many industries and expectations of continued business expansion were among the chief factors giving rise to the increase in these outlays. Internal cash flow provided a ready source of finance.

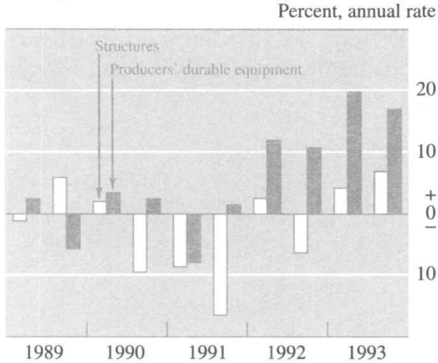
Commercial aircraft was the most notable exception to the general upward trend in equipment spending. Outlays for aircraft plunged in the second half of 1993, and survey data pointed to continued weakness in 1994. The reductions in outlays had been foreshadowed by earlier declines in new orders, and producers of aircraft have been scaling back their operations for some time.

Business investment in structures rose about 5½ percent, the first annual increase since 1989. Declines in the intervening years had cumulated to about 18 percent. Within the sector, divergent trends were evident once again. Outlays for the construction of office buildings fell for the sixth consecutive year, to a level two-thirds below the peak of the mid-1980s. Several indicators suggested, however, that the worst of the decline in office construction might be over. The rate at which real outlays fell in 1993 was much smaller than the declines of the three previous years. In addition, the national vacancy rate for office buildings, while still quite high, moved down somewhat; the improvement was most noticeable in suburban areas, where vacancy rates previously had been the highest. The value of contracts for construction of office buildings firmed over the course of the year.

Investment increased for most other types of structures. Outlays for industrial structures, which had declined sharply in 1991 and 1992, rose about 9½ percent, on net, over the four quarters of 1993. Outlays for commercial structures other than office buildings increased sharply for a second year; by the fourth quarter, they had retraced nearly half of the steep decline that took place during 1990 and 1991. Investment in drilling also rose as incentives from rising prices for natural gas apparently offset the disincentives associated with falling oil prices. Spending for other types of structures rose by a small amount in the aggregate.

Change in Real Business Fixed Investment

Percent, annual rate



The data are seasonally adjusted and come from the Department of Commerce; they are measured in terms of 1987 dollars.

Swings in business inventory investment played only a small role in the 1993 economy. Inventory accumulation in the nonfarm business sector picked up in the early part of the year but slowed thereafter. Accumulation for the year as a whole was of only modest proportions, especially when compared with the rates of buildup seen during previous business expansions. Conceivably, the usual cyclical patterns in inventory change have been tempered to some degree by the more sophisticated inventory control procedures that have become widespread in the business sector in recent years. Toward year-end, inventories appeared to be comfortably aligned with sales in most industries and were lean in some. Most notable among the latter were the stocks of motor vehicles, which were drawn down by production delays through the summer and strength in sales through the latter part of the year. In view of those developments, producers of motor vehicles scheduled a hefty rise in production for the first quarter of 1994.

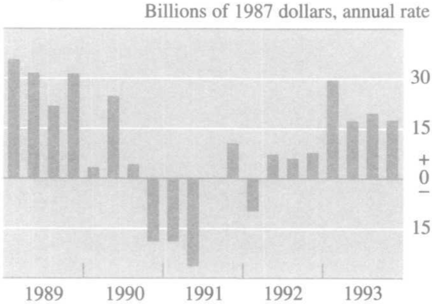
In the farm sector, inventories declined. Stocks were pulled down by weather-related reductions in crop output, especially in parts of the Midwest, where the worst flood of the century took millions of acres out of production and cut deeply into yields of the crops that were planted. Inventories of some major field crops tightened markedly. Farmers whose crops were hurt by weather suffered income losses in 1993, while the producers whose crops were not hurt benefited from rising prices. Total net farm income appears to have held in the range of other recent years, at a level well within the extremes of either boom or bust.

Trends in business finance remained favorable for sustained expansion. Business expenditures for fixed capital and inventories were financed almost entirely with funds generated internally, and, in the aggregate, the relatively little external financing that did take place came partly from positive net issuance of equity. Debt rose slowly, both in absolute terms and relative to the rapid pace seen in the 1980s. With little growth in debt and interest rates down, the portion of business cash flow required for the repayment of principal and interest declined further.

The Government Sector

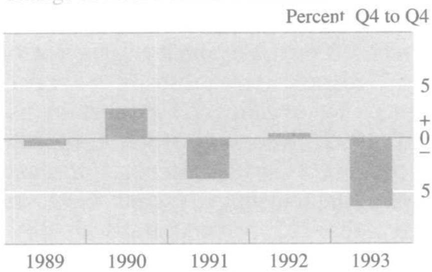
Federal purchases of goods and services, the portion of federal outlays that are included in GDP, fell 6½ percent in real terms over the four quarters of 1993. Real outlays for national defense,

Change in Real Business Inventories



Total nonfarm sector. The data are seasonally adjusted and come from the Department of Commerce.

Change in Real Federal Purchases



The data are from the Department of Commerce.

which have been trending down since 1987, declined nearly 9 percent. Nondefense outlays fell slightly, on net, after rising fairly rapidly in each of the three previous years. The level of real federal purchases in the fourth quarter of 1993 was down more than 10 percent from the peak of six years earlier. Real defense purchases dropped about 20 percent over that six-year stretch.

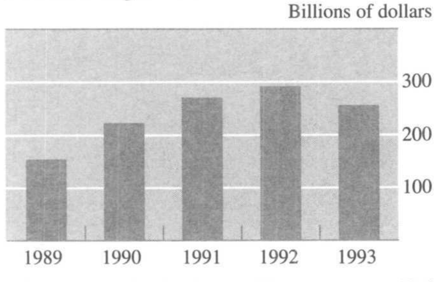
Total federal outlays, measured in nominal terms in the unified budget, rose 2 percent in fiscal 1993, the smallest increase in six years. Outlays for defense fell about 2½ percent in nominal terms, and net interest payments were down slightly—the first decline in that category since 1961. Net expenditures for deposit insurance, which had been slightly positive in 1992, were negative in fiscal 1993, held down in part by delays in funding the activities of the Resolution Trust Corporation. Federal spending for income security slowed from the rapid pace of 1991 and 1992, as economic expansion led to a reduction in outlays for unemployment compensation and a less rapid rate of increase in outlays for food stamps. The growth in federal expenditures for Medicare and other health programs also slowed, but the rate of increase continued to exceed the growth of nominal GDP by a considerable margin.

The growth of federal receipts picked up a bit in fiscal 1993, to a pace roughly matching that of nominal GDP growth. Combined receipts from individual income taxes and social insurance taxes, which account for about 80 percent of total federal receipts, rose about 5½ percent, after a gain of 3 percent in fiscal 1992. Receipts from corporate income taxes, which account for about half of the remaining receipts, increased more than 17 percent in fiscal 1993, after only a small gain in the previous fiscal year.

Taken together, the slowing of federal outlays and the pickup of receipts led to a decline in the size of the federal budget deficit in fiscal 1993, after three years of sharp increases. The 1993 deficit amounted to $255 billion and was equal to 4.0 percent of nominal GDP. The previous year, the deficit had amounted to $290 billion and was equal to 4.9 percent of nominal GDP. In fiscal 1989, toward the end of the last economic expansion, the size of the deficit relative to nominal GDP had reached a cyclical low of 2.9 percent.

In the state and local sector, receipts moved up about in step with the growth of nominal GDP in 1993, but state and local expenditures rose still faster. In nominal terms, the increases in spending cumulated to a rise of about 7 percent over the four quarters of the year. State and local transfer payments to persons slowed from the extraordinary rates of increase seen in the early 1990s, a reflection of improvement in the economy and intensified efforts among state and local governments to tighten control over these types of outlays. Nonetheless, the rate of rise in these payments remained above 10 percent in 1993. Nominal purchases of goods and services rose moderately but at a pace somewhat faster than that of 1992. The

Federal Budget Deficit

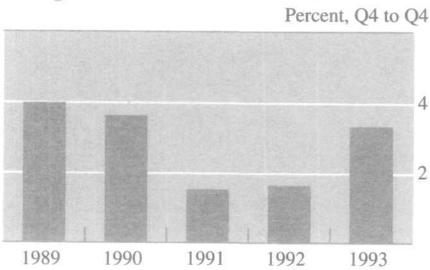


The data are for fiscal years. They are on a unified budget basis and are from the Department of the Treasury.

deficit in the combined operating and capital accounts of state and local governments widened further during the first three quarters of the year, from an end-of-1992 level that already was quite sizable; in the fourth quarter, the deficit apparently shrank, but not by enough to fully retrace the earlier increases.

In real terms, purchases of goods and services by state and local governments increased nearly 3½ percent over the four quarters of 1993, after gains of about 1½ percent per year in both 1991 and 1992. State and local expenditures for structures rose almost 12 percent in real terms over the year, according to preliminary data. Some of the spending went for the repair or replacement of structures that had been damaged in recent natural disasters, such as the summer flooding in the Midwest. In addition, the efforts of state and local governments to cope with the needs of growing populations prompted increased investment in schools, highways, and other state and local facilities. Low interest rates probably convinced state and local officials to undertake more of this new construction in 1993 than they would have otherwise. Growth in other types of state and local purchases continued to be fairly restrained. Employee compensation, which makes up nearly two-thirds of state and local purchases, rose about 1¼ percent in real terms, the same as in 1992. Employment in the state and local sector again grew slowly by historical standards, and increases in hourly compensation were relatively small. State and local purchases of goods rose moderately in real terms.

Change in Real State and Local Purchases



The data are from the Department of Commerce.

Labor Market Developments

The labor market strengthened in 1993, as economic expansion began to translate more forcefully into increased job creation. Payroll employment, a measure of jobs that is derived from a monthly survey of establishments, rose more than 2 million over the twelve months of the year. Although this gain was only moderate when compared with increases in many years of the 1970s and 1980s, it was about twice the increase of 1992.

Hiring picked up in most major sectors in 1993. The number of jobs in retail and wholesale trade increased more than one-half million, the largest annual rise since 1988. The number of jobs in finance, insurance, and real estate picked up a bit, after a five-year period that had encompassed three years of sluggish growth and two years of unprecedented reductions. Construction employment rose 200,000, after three years of sharp declines.

The services industry added about 1.2 million new jobs in 1993. More than one-third of the increase came at firms that supply services to other businesses; in that group, the most rapid growth by far was in personnel supply firms—companies that essentially lease the services of their employees to other businesses, usually on a temporary basis. Many companies requiring additional labor apparently have been attracted by the flexibility of such arrangements, as well as by cost advantages, at least over the short run.

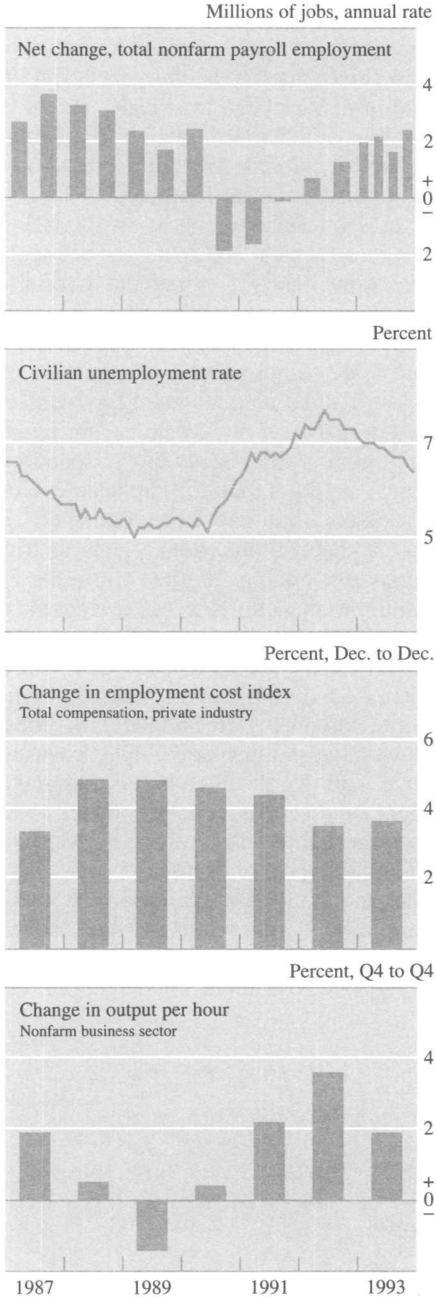
Elsewhere in the services industry, health services continued to generate a substantial number of new job opportunities in 1993, even though the gain was not quite as large as those of other recent years. Small to moderate employment gains also were reported during the year at firms supplying a wide variety of other types of services.

Manufacturing employment continued to decline in 1993, but at a slower pace than in any of the three previous years. Although manufacturers boosted output considerably, the gain was achieved mainly through another sizable rise in factory productivity. Labor input in manufacturing reportedly increased only slightly and only in the form of a lengthened workweek rather than increased hiring. By the latter part of the year, the average workweek in manufacturing had reached 41¾ hours, the longest since World War II. Hiring did pick up late in the year, however. Reliance by manufacturers on workers from personnel supply firms reportedly has increased in recent years; because these workers are carried on the payrolls of the personnel firms, actual labor input in manufacturing in 1993 was greater than the data indicate.

Like the survey of establishments, the monthly survey of households showed significant improvement in labor market conditions in 1993. The measure of employment that is derived from this survey rose 2½ million over the twelve months of 1993, after an increase of about 1½ million during the previous year. At the same time, the number of unemployed persons fell more than 1 million over the course of 1993, and the civilian unemployment rate declined nearly a full percentage point, to a year-end level of 6.4 percent.

Growth of the civilian labor force—the sum of persons who are employed and those who are looking for work—

Labor Market Conditions



The data are from the Department of Labor.

was relatively sluggish again in 1993. The rise over the four quarters of the year was 1.2 percent, only slightly faster than the rate of growth of the working-age population. Over the four years ended in 1993, labor force growth averaged less than 1 percent per year, and the labor force participation rate edged down slightly, on net. The number of individuals who desired work but did not seek it because of a perceived lack of job openings changed little over the course of 1993. In addition, the number of individuals outside the labor force and not wanting a job rose about 0.8 percent during the year, pulled up, in part, by a sharp increase in the number of retirees. Workers whose careers were cut short by business restructurings and defense cutbacks probably augmented the normal flow of workers into retirement. Growth in the number of persons not wanting a job because of attendance in school also increased during 1993. To the extent that these individuals have been building their job skills, their lack of current participation in the labor force could turn into a positive factor for the economy over the longer run.

The slowing of nominal increases in hourly compensation came to a halt in 1993. The employment cost index for private industry—a labor cost measure that includes wages and benefits and covers the entire nonfarm business sector—increased 3.6 percent from December 1992 to December 1993, about the same as the rise of the previous year. Wages rose 3.1 percent over the year, ½ percentage point more than in 1992, and the growth of benefits slowed only a little, to 5.0 percent. Compensation gains picked up for workers in some white-collar occupations, notably sales workers and managers. Slightly bigger gains than in 1992 also were realized by workers in some blue-collar occupations. By contrast, the rate of compensation growth held steady in service occupations and edged down in some blue-collar occupations in which fewer specialized skills are required. The overall rise in hourly compensation during 1993 exceeded the rise in consumer prices by about 1 percentage point. Hourly wage gains more than kept pace with inflation, and the value of benefits provided to workers by their employers continued to rise rapidly in real terms.

Labor productivity continued to increase in 1993, albeit less rapidly than in the earlier stages of the cyclical expansion. According to preliminary data, output per hour in the nonfarm business sector rose 1.9 percent during the year, after increases of 2.2 percent in 1991 and 3.6 percent in 1992. Part of the gain over this three-year period is no doubt a reflection of normal cyclical processes. The data, however, also seem to suggest that the longer-run trend in productivity is tilting up a bit more sharply than in the 1970s and 1980s, a result of heavy investment by business in new information technologies, the rising skill of workers in exploiting those technologies, and, perhaps, the more quiescent inflation environment of recent years. With gains in labor productivity offsetting part of the 1993 increase in compensation per hour, unit labor costs in the nonfarm business sector increased just 0.9 percent, the smallest rise in ten years.

Price Developments

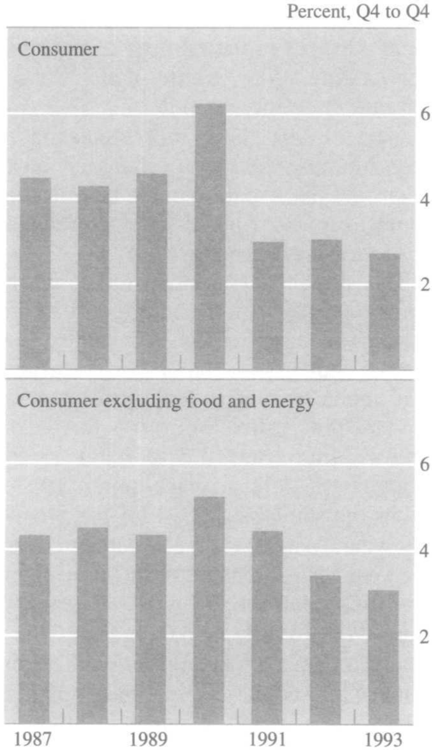
Inflation edged down a bit further in 1993. The 2.7 percent rise in the CPI over the four quarters of the year was the smallest increase since 1986, and the four-quarter rise of 3.1 percent in the CPI excluding food and energy was the smallest increase in that measure in more than twenty years. At the same time, however, progress toward lower inflation was sporadic during the year, and the slowing of price increases was less widespread than it had been in 1992. Scattered upward price pressures showed up in the commodity markets from time to time during 1993; late in the year these increases became more widespread.

The patterns of price change for items other than food and energy were more checkered in 1993 than they had been in 1992, a year when deceleration was widespread among both commodities and services. The CPI for commodities other than food and energy rose only 1.6 percent over the four quarters of 1993, 1 percentage point less than in 1992. Within this category, the CPI for tobacco fell 5 percent, after many years of large increases, and the price of apparel rose less than 1 percent, an even smaller increase than in 1992. By contrast, the prices of motor vehicles moved up somewhat faster than in 1992; the price rise for trucks was the largest in recent years.

The CPI for non-energy services increased 3.8 percent over the four quarters of 1993, about the same as the rise during the previous year. The index for medical care services slowed for the third year in a row, but airfares rose sharply for a second year. Price increases for other services generally were little different from those in 1992, with a small deceleration for some items and a small acceleration for others.

Food prices picked up in 1993. The consumer price index for food increased 2.7 percent over the four quarters of the year, an acceleration of about 1 percentage point from the pace of the two previous years. Because price increases in those two previous years had been held down, in part, by unusually favorable supply developments in agriculture, some pickup of food price inflation might have been in store for 1993 even had weather conditions been no worse than average. In the event, the weather was unusually bad. Severe winter weather disrupted livestock production early in the year; drought in the eastern states hurt crop production in that region during the summer; and flooding of historic severity in the Missouri and Mississippi river basins cut deeply into the production of major field crops. At retail, effects of the various supply disruptions showed through in the prices of meats, poultry, and fresh produce. Price increases for other foods, which represent by far the larger share of total food in the CPI, showed almost no accelera-

Change in Prices



Consumer price index for all urban consumers. The data are seasonally adjusted and are from the Department of Labor.

tion in 1993; most of the value added in production of these other foods comes from nonfarm inputs.

Consumer energy prices declined 0.4 percent over the four quarters of 1993 after rising only moderately in 1992. With world oil production outstripping demand, crude oil prices fell sharply during the last three quarters of 1993, to levels in December that were about 25 percent below those of a year earlier. Gasoline prices, after increasing in the early part of 1993, turned down in March and fell for six additional months thereafter. The string of declines was interrupted in October when federal gasoline taxes were raised, but they resumed in November and continued through year-end. Average pump prices for the fourth quarter were about 4 percent below the level of a year earlier. Fuel oil prices fell about 3 percent over the same period. Prices of the service fuels—electricity and natural gas—increased during 1993. The rise for electricity amounted to 1.7 percent, slightly less than the increase posted in 1992. Natural gas prices rose nearly 5 percent for the second year in a row; consumption of natural gas has picked up in recent years, after trending lower through much of the 1970s and a large part of the 1980s.

The producer price index for finished goods, which includes both consumer goods and capital equipment and covers only the prices received by domestic producers, increased just 0.2 percent over the four quarters of 1993. An identical increase was reported in the PPI for finished goods other than food and energy; the increase in this measure was the smallest in its history, which goes back to 1974. As at retail, price increases for these domestically produced goods were held down, in part, by the sharp drop in prices of tobacco products. More broadly, competition from imports and further increases in labor productivity in manufacturing were important elements in pricing restraint. The prices of intermediate materials excluding food and energy rose 1.5 percent over the four quarters of 1993, a small step-up from the pace of the previous year.

In the markets for raw commodities and other primary inputs, scattered upward price pressures emerged from time to time during the first three quarters of 1993, and fairly widespread increases were reported in the year's final quarter. The producer price index for crude materials excluding food and energy thus moved up sharply over the year, by more than 10 percent in all. The weight of these inputs in GDP is quite small, however, and in the absence of more general cost pressures, increases in their prices usually do not impart much upward thrust to the prices of finished goods.

Inflation expectations, as reported in various surveys of consumers and other respondents, flared up for a time during 1993 but retreated in the latter part of the year. The most pronounced swing in expectations was reported in the survey conducted by the University of Michigan Survey Research Center, in which the rate of price increase expected one year into the future moved up from an average of 3.8 percent in the final quarter of 1992 to an average of 4.7 percent in the third quarter of 1993; the rise was fully reversed in the fourth quarter, however. As in 1992, the surveys continued to show one-year expectations of price change running somewhat higher than the actual increases of recent years. Longer-run expectations of price change remained higher still; for interviews conducted in the second half of 1993, the Survey Research Center's series on average inflation rates that are expected over a five- to ten-year horizon ranged from 4½ percent to 5 percent, down only slightly from the average rates reported earlier in the 1990s. ■