

Economic Trends

March 1986

In late 1985, the rate of price increase accelerated, but recent reductions in oil prices have improved the near-term outlook for prices. From September 1985 to January 1986, the consumer price index (CPI) rose at a 5.0 percent annual rate, up sharply from the 2.5 percent rate over the previous four months. For the same periods, producer prices of finished goods (PPI) increased at a 4.9 percent rate, after declining at a 2.6 percent rate. In February, however, the CPI declined at a 4.6 percent rate, while the PPI fell at a 17.1 percent rate.

The current and prospective slowing is due to oil price developments. The average price of oil has fallen sharply since December 1985 when refiners paid an average of \$26.82 per barrel. The price for West Texas Intermediate Crude in mid-March was down to about \$13 per barrel in the spot market.

A decline in oil and other energy prices affects various measures of price increase differently. Broader measures of prices are for diverse groups of goods and services, so oil purchases have relatively more effect on some measures (PPI) than others (CPI and GNP deflator). The share of oil or energy purchases in the group of goods is an incomplete measure of its importance because the prices for nonenergy goods and services are also influenced by the relative importance of oil and energy in their production.

In the table below, the rates of change of the broad measures and PPI for energy (fuel, related products and power) are shown for several periods when the latter changed sharply relative to prices generally. When such changes occur, broad measures of prices generally are affected in the same direction, though some relatively more than others. The recent decline in oil prices will reduce the PPI relatively more than the CPI, which, in turn, is affected more than the GNP deflator. The timing of price effects also differs, with the PPI tending to adjust more quickly than the CPI and the GNP deflator adjusting more slowly (about five quarters).

Annual Rates of Increase of Price Measures

Periods	PPI-energy	PPI	CPI	GNP deflator
IV/1973-III/1974	78.8%	18.3%	11.8%	9.5%
IV/1978-II/1981	35.6	12.2	12.1	9.2
II/1981-IV/1985	-2.4	2.1	4.4	4.5
Dec. 1985-Feb. 1986	-49.7	-12.6	-0.4	N.A.

—John A. Tatom

