Producer price highlights, 1997

Producer Price Indexes for finished goods, finished energy goods, and foods all fell during 1997, the first decline in 11 years for the finished-goods category; only the index for finished goods other than foods and energy remained stable throughout the year

William D. Thomas

William D. Thomas is an economist in the Office of Prices and Living Conditions, Bureau of Labor Statistics. Joseph Kowal, an economist in the same office, assisted in the preparation of this article.

Prices received by domestic producers of finished goods fell 1.2 percent in 1997, following a 2.8-percent rise in 1996 and a 2.3-percent advance in 1995. The last calendar-year decline for finished goods was in 1986, when the index dropped 2.3 percent due to falling energy prices. The index for finished energy goods moved down 6.4 percent from December 1996 to December 1997, after an increase of 11.7 percent a year earlier. Prices for foods, such as pork and fresh fruits and melons, fell 0.8 percent in 1997, following a 3.4-percent increase in 1996. However, prices for finished goods other than foods and energy, a category that includes consumer goods such as passenger cars and apparel, were unchanged in 1997, after a 0.6-percent rise in 1996. (See table 1.)

At the earlier stages of processing, the directions in price changes for intermediate goods were the same as those for crude goods. The index for intermediate goods declined 0.8 percent in 1997, after a 0.7-percent rise in 1996. This index measures the price movements of goods such as flour, steel, lumber, industrial chemicals, diesel fuel, and paper boxes. Prices for crude goods fell 11.3 percent in 1997 after rising 14.7 percent in 1996. Crude goods include wheat, scrap metals, logs, crude petroleum, and cotton. Prices for food-related materials at the intermediate stage of processing also fell from 1996 to 1997; at the crude level, price declines accelerated for foodstuffs and feedstuffs. However, when the effects of price changes for energy and food-related materials are excluded, the core indexes for both intermediate and crude goods turned up somewhat in 1997 after decreasing in 1996.

Economic background

The past year saw the Nation's economy turn in its best performance in a generation. Over the course of 1997, output growth and job creation remained vigorous, while inflation declined. Real (inflation-adjusted) gross domestic product grew 3.9 percent, and employment rose by 3.4 million, for an average rate of 284,000 jobs created per month. The unemployment rate dropped below 5 percent for the first time in 24 years, yet core inflation (as measured by the Consumer Price Index, excluding its volatile food and energy components) averaged only 2.2 percent, its lowest rate in more than 30 years. A principal force behind the current expansion has been private fixed investment. One benefit of this burst of investment has been a rapid expansion of industrial capacity.

Economic growth exceeded expectations in 1997, and the unemployment rate declined to a 24-year low. Households and firms increased their spending at robust rates as continued low inflation, low unemployment, declining costs of business equipment, and lower long-term interest rates contributed to a favorable economic environment for both consumers and producers. Net exports continued to be a restraining influence on growth.

Strong investment in new productive capacity in the past few years has helped the economy accommodate higher spending without rising inflation. Chief among the factors that have combined to hold back inflation have been the rise in the value of the dollar on foreign exchange markets (which makes imports cheaper), unusually steep declines in prices for computers, and continued moderation in employer costs of health insurance.

Household income, consumer sentiment, and household net worth were all favorable in 1997: real disposable personal income grew over the four quarters of the year, and yearend stock market values were up about 30 percent from a year earlier. Outlays grew even faster than income, and as a result, the personal saving rate edged down.

Although consumption was robust over the past year, it was not smooth. Real consumption grew in excess of a 5-percent annual rate in the first and third quarters, but at only a modest yearly rate in the second. Most of the volatility was in goods consumption; services consumption grew at around a 4- to 5-percent annual rate in each quarter. Durable goods, which rose at double-digit annual rates in the first and third quarters, but fell at a 5-percent yearly rate in the second, accounted for much of the quarter-to-quarter fluctuations in growth. The roughly 15 million units of light motor vehicles sold in 1997 were about the same number sold in each of the previous 3 years; over this 4-year period, sales of light motor vehicles were just shy of the record 4-year pace set in the mid-1980s.

The signals for the traditional determinants of business investment were strongly favorable throughout 1997. Business equipment grew 12 percent over the four quarters of the year, with strong demand for most types of equipment. Industrial equipment grew a healthy 7 percent over the year, and transportation equipment advanced 10 percent, with particularly rapid growth in aircraft purchases.

The standout categories of business equipment investment in 1997 were office and computing equipment and telecommunications equipment. Growth in real computer spending was fueled in part by price declines that were even sharper than normal. One factor possibly boosting sales in this industry is the rapidly expanding capacity and availability of cellular telephone and other wireless services.

Investment in nonresidential structures was about flat in 1997, following solid gains in 1996. Construction of new office buildings made substantial gains, as the strength of the economy allowed the sector to grow out from under an overhang of empty office buildings at the beginning of the decade. These gains were offset by small declines in the construction of industrial, utility, and mining structures.

Table 1. Annual percent changes for major categories of the Producer Price Index, by stage of processing, 1993–97

Index	1993	1994	1995	1996	1997
Finished goods	0.2	1.7	2.3	2.8	–1.2
Foods	2.4	1.1	1.9	3.4	–.8
Energy	–4.1	3.5	1.1	11.7	–6.4
Other	.4	1.6	2.6	.6	.0
Intermediate materials, supplies, and components	1.0	4.4	3.3	.7	–.8
Foods and feeds	5.5	–4.5	10.3	2.1	–1.7
Energy	–4.2	2.9	1.1	11.2	–7.0
Other	1.6	5.2	3.2	–.9	.3
Crude materials for further processing	.1	–.5	5.5	14.7	–11.3
Foodstuffs and feedstuffs	7.2	–9.4	12.9	–1.0	–4.0
Energy	–12.3	–.1	3.7	51.2	–23.1
Other	10.7	17.3	–4.2	–5.5	.0

The demand for inventories was probably a result of strong final sales, which increased faster than inventories over the first three quarters of 1997. As a result, stocks remained lean in relation to sales.

Residential construction increased about 6 percent in 1997, with much of the growth occurring in the fourth quarter. The pickup toward the end of the year reflected in part the pattern of mortgage rates, which, after rising through April, fell more than 1 percentage point later in the year. Falling mortgage rates, together with strong real-income growth, resulted in an increase in the affordability of housing in the second half of the year. In addition to rising new-home construction, real-estate commissions moved up over the year, as sales of existing homes grew by 3 percent during 1997 as a whole, to their highest level ever.

The impact of the surge of private spending was muted, however, by an erosion in net exports, a continuing decline in real Federal Government spending, and slow growth in spending by State and local governments.

Short-term interest rates fluctuated within a narrow range over the course of the year, whereas long-term rates rose slightly early in the year, but then declined, finishing the year roughly 50 basis points (half a percentage point) lower. Long-term interest rates remained very low, largely reflecting both continued progress in reducing the deficit and market participants' expectations of low future inflation. (The former lowers nominal interest rates by reducing expected future real rates, while the latter acts directly to reduce nominal rates.) In addition, turmoil in foreign asset markets in the second half of the year helped make U.S. securities more attractive to investors.

On October 27, the Dow-Jones Index fell 554 points, the 12th-largest decline in its history, in percentage terms. The drop was steep enough to cause the New York Stock Exchange's system of "circuit breakers" to suspend trading temporarily for the first time ever. The day after the plunge saw the volume of shares traded on the exchange reach a record high of 1.2 billion. (The market made up much of its previous day's decline that day.) The stock market rebounded quickly following its October losses. Nonetheless, turmoil in East Asia apparently continued to be a source of downward pressure on stock prices for the remainder of the year. The rise in stock prices in 1997 represents the continuation of a trend that has seen major indexes more than double over the past 3 years.

Inflation remained remarkably subdued in 1997. Core CPI inflation slowed over the course of the year, continuing a decline that began in 1995. Surprisingly, this deceleration in price increases occurred in an economic environment that was characterized by extremely low unemployment.

The pace of job creation was quite swift. Among the service-producing industries, growth was particularly rapid in computers and data processing and in engineering and management services. These hiring gains were matched by large increases in industrial capacity. Nevertheless, labor markets were tight and wages accelerated continuously during the year. Hourly wages, as measured by the employment cost index, rose by 3.9 percent in 1997, 0.5 percentage point faster than in 1996.

Growth in output per hour worked picked up in 1997: over the year, the official measure of productivity in the nonfarm business sector rose at an average annual rate of 1.7 percent.

Finished goods other than foods and energy

As mentioned earlier, the index for finished goods other than foods and energy—the "core" index—was unchanged in 1997, following a 0.6-percent advance in 1996. This slowdown in price increases was broadly based. The index for consumer goods other than foods and energy rose 0.3 percent in 1997, following a 0.8-percent increase in 1996. Prices for capital equipment turned down 0.6 percent in 1997 after rising 0.4 percent a year earlier. (See table 2.)

Table 2. Annual percent changes in Producer Price Indexes for selected finished goods other than foods and energy, 1993–97

Index	1993	1994	1995	1996	1997
Finished goods other than foods and energy	0.4	1.6	2.6	0.6	0.0
Consumer goods	–.2	1.6	2.3	3.6	–1.4
Passenger cars	3.3	2.1	1.7	–.8	–2.6
Light trucks	4.2	3.3	1.5	.2	–3.6
Prescription drugs	3.2	3.1	4.2	2.0	3.6
Over-the-counter drugs	2.7	1.7	1.7	–1.7	.3
Tobacco products	–21.4	.4	3.6	2.6	7.7
Books	.6	5.4	6.5	3.2	3.3
Periodicals	2.5	3.6	4.8	2.0	4.0
Newspapers	2.4	3.3	8.8	4.2	.1
Household furniture	3.7	2.7	2.7	1.4	1.1
Capital equipment	1.8	2.0	2.2	.4	–.6
Heavy trucks	3.1	3.0	4.1	–4.5	.6
Truck trailers	3.3	7.7	2.2	–1.4	2.0
Metal-cutting machine tools	.6	1.8	4.1	3.1	2.1
Metal-forming machine tools	1.6	3.5	2.2	2.6	3.2
Computers	–12.5	–6.8	–12.7	–22.3	–21.6
Agricultural machinery	2.9	2.7	4.7	1.4	1.4
Construction machinery	1.1	2.0	2.5	1.8	1.9

Among consumer goods other than foods and energy, indexes fell in 1997 after moving up in 1996 for sanitary papers, passenger cars, over-the-counter drugs, tires and tubes, cosmetics, and household appliances. Price increases slowed for light trucks, prescription drugs, newspapers, alcoholic beverages, periodicals, books, household furniture, tobacco products, mobile homes, sporting goods, soaps and detergents, girls' apparel, footwear, floor coverings, toys, and lawn and garden equipment. Prices continued to rise modestly for men's and boys' apparel. By contrast, the index for women's apparel rose after falling the previous year. Price increases accelerated for textile housefurnishings, costume jewelry, gold jewelry, and household glassware. Prices for home electronic equipment continued to move down.

The Producer Price Index for capital equipment fell 0.6 percent in 1997, following a 0.4-percent advance in 1996. Prices for light motor trucks turned down 3.6 percent after moving up 0.2 percent the year before. Price increases slowed markedly for civilian aircraft, commercial furniture, tools and dies, communications equipment, printing trades machinery, railroad equipment, ships, and metal-cutting machine tools. Prices increases also slowed, but only slightly, for construction machinery, industrial material-handling equipment, and agricultural machinery. By contrast, prices rose in 1997 after falling in 1996 for heavy motor trucks and for office and store machinery. Prices fell less than in the previous year for x-ray equipment, truck trailers, and transformers. Price increases accelerated for pumps and compressors, oil field machinery, textile machinery, and mining machinery. Prices continued to rise for metal-forming machine tools and paper industry machinery.

Transportation equipment. The index for motor vehicles declined significantly in 1997 as prices fell for both passenger cars and light trucks; however, prices for heavy trucks increased 0.6 percent. Prices for passenger cars decreased throughout 1997, partly a result of higher incentives offered by manufacturers to dealers to liquidate inventories. Prices also were held down by lower increases in the introduction of the new model-year cars and fewer interim price increases during the year. The market for domestic automobiles struggled all year and required higher incentives to keep it moving. In addition, sales of new automobiles in 1997 in the United States were dampened by large gains made by foreign manufacturers. Several foreign manufacturers even experienced double-digit gains in sales. Domestic manufacturers of automobiles also faced stiff competition from the light-truck segment, which has grown immensely in market share in recent years. Domestic manufacturers continued to pare down product lines in 1997 by cutting down on duplication of models within the company (under different brand names), thereby giving each line a unique appearance. As in the recent past, motor vehicle manufacturers relied on the highly profitable light-truck segment to bolster their net profits. The market for light trucks has undergone numerous changes over the past few years. Consumers have come to expect the same incentives and discounts offered by automobile manufacturers. In addition, in 1997, competition heated up from foreign manufacturers who entered the light-truck market, offering luxury sports utility models. By yearend, much discussion and debate had taken place over emissions and fuel economy for the sports utility segment, whose vehicles generally have larger and more powerful engines than cars. The combination of marketing programs and a strong economy boosted the market for heavy trucks in 1997.

The index for aircraft and aircraft parts inched up slightly in 1997. Aircraft demand was fairly high; however, prices were held down due to competition. The aircraft parts industry also experienced growth over the year; however, lower costs for materials and fierce competition among manufacturers kept prices down. The index for ships increased 3.0 percent in 1997, reflecting increased production costs, especially for labor. The industry continued to be plagued by a shortage of highly skilled workers. The index for railroad equipment fell 1.5 percent in 1997, with prices for locomotive parts moving down as a result of burdensome inventories accumulated in late 1996 in anticipation of a boost in demand for these products that never materialized.

Paper products. Prices declined again in 1997 for a wide variety of paper goods, particularly sanitary household paper products. Prices for both tissue and towel stock were 6.4 percent lower than they had been in 1996. Declines for paper products reflected earlier decreases in prices for woodpulp and wastepaper. In 1997, two major producers of sanitary paper products merged and were able to take the lead in pricing.

Drugs and pharmaceuticals. Price increases for drugs and pharmaceuticals accelerated somewhat from 1996 to 1997. The index for prescription drugs rose 3.6 percent after increasing 2.0 percent the year before. Prices for over-the-counter drugs turned up 0.3 percent in 1997, following a 1.7-percent decline in the previous year. Price changes were not confined to any particular class of drug or buyer; small increases were registered for most categories of products. As in earlier years, health insurance providers, as well as managed care providers, used their purchasing power to induce pharmaceutical manufacturers to negotiate lower prices and limit increases. In contradistinction to prices for prescription drugs, prices for over-the-counter drugs behave more like those of other consumer finished goods: manufacturers compete directly for consumer dollars using coupons and other special promotions.

Computers. The index for electronic computers fell more than 20 percent for the second straight year. Prices declined sharply in 1997 for personal computers and workstations (30.7 percent), portable computers (35.1 percent), and midrange computers (25.4 percent). The multiplicity of different types of microprocessors and disk drives in the marketplace contributed greatly to these declines. The economic crisis in Asia also drove computer prices lower, by guaranteeing a flow of cheap components. As in other recent years, fierce price competition was prevalent throughout the industry.

Tobacco products and alcohol. Increases for tobacco products accelerated from 2.6 percent in 1996 to 7.7 percent in 1997. Most of the acceleration was due to the index for cigarettes, which advanced 10.0 percent in 1997, following an increase of 3.4 percent in 1996. In 1997, prices for cigars rose almost 6 percent, about the same as the year before. Cigarette manufacturers engaged in fierce competition for market share as the domestic market for cigarettes continued to shrink. As in recent times, the manufacturers expanded their presence abroad, with foreign markets having fewer age and advertising restrictions. Producers continued to increase exports through joint ventures abroad. By yearend, the possibility of multibillion-dollar settlements in class-action liability suits loomed over the cigarette-manufacturing industry. The previous year's upsurge in demand for cigars continued into 1997; in evidence of this trend were the proliferation of cigar manufacturers, more bars and restaurants catering to cigar smokers, and Web sites on the Internet devoted exclusively to cigar aficionados. The index for alcoholic beverages turned down 0.5 percent in 1997 after increasing 3.8 percent in 1996. In 1997, beermakers benefited from lower costs for grain and aluminum cans. Stiff competition among breweries for market share resulted in aggressive price discounting.

Energy

Following a rise of more than 50 percent in 1996, the index for crude energy materials fell 23.1 percent in 1997. Prices declined markedly for both natural gas and crude petroleum after advancing sharply in 1996. By contrast, the index for coal increased (4.9 percent) after decreasing (1.1 percent) the year before. (See table 3.)

Prices for intermediate energy goods dropped 7.0 percent in 1997, following an increase of 11.2 percent in 1996. After rising a year earlier, prices decreased in 1997 for liquefied petroleum gas, number 2 diesel fuel, jet fuels, and residual fuel. Price increases slowed markedly over the same period for utility, commercial, and industrial natural gas. By contrast, prices turned up after showing no change a year earlier for electric power. Price increases accelerated for natural gas sold to electric utilities.

The Producer Price Index for finished energy materials declined 6.4 percent in 1997, following an 11.7-percent rise in 1996. Gasoline prices fell 15 percent in 1997 after advancing 27.1 percent a year earlier. The index for home heating oil dropped 21.7 percent after advancing 25.0 percent in 1996. Price increases for residential gas slowed to 2.4 percent from 11.2 percent in the previous year. By contrast, the index for residential power fell in 1997 after increasing in 1996.

Foods and related products

Farm prices, as measured by the Producer Price Index for crude foodstuffs and feedstuffs, declined 4.0 percent in 1997, following a 1.0-percent drop in 1996. (See table 4.) After advancing substantially in 1996, prices moved down markedly in 1997 for slaughter hogs, slaughter broilers and fryers, wheat, fresh fruits and melons, and unprocessed finfish. Price increases slowed from 1996 to 1997 for alfalfa hay and unprocessed shellfish. Prices fell even more in 1997 than in the previous year for slaughter turkeys and raw cane sugar. By contrast, indexes rose after falling a year earlier for corn, slaughter cattle, fresh and dry vegetables, Irish potatoes for processing, soybeans, and vegetables (except potatoes). Price increases accelerated somewhat for fluid milk.

The index for intermediate foods and feeds fell 1.7 percent, following a 2.1-percent advance a year earlier. Prices dropped after increasing in 1996 for prepared animal feed, pork, confectionery materials, beef and veal, refined sugar, liquid milk products, and condensed and evaporated milk. Price increases slowed somewhat for fluid milk products and liquid beverage base. By contrast, prices increased in 1997, following declines in 1996, for crude vegetable oils and natural and processed cheese. Price increases accelerated for butter and dry mix preparations. Prices fell less in 1997 than they had fallen in the previous year for flour and dry milk products.

Table 3. Annual percent changes in Producer Price Indexes for selected energy items, 1993–97

Index	1993	1994	1995	1996	1997
Finished energy goods	–4.1	3.5	1.1	11.7	–6.4
Gasoline	–16.8	11.2	2.4	27.1	–15.0
Home heating oil	–10.1	6.9	11.9	25.0	–21.7
Residential electric power	.8	1.5	.9	.6	–.2
Residential natural gas	5.4	–2.6	–2.4	11.2	2.4
Intermediate energy goods	–4.2	2.9	1.1	11.2	–7.0
Residual fuels	–17.8	10.2	–4.7	32.8	–7.6
Natural gas to electric utilities	–13.0	3.4	–1.4	6.1	9.3
Diesel fuels	–15.9	5.9	11.1	26.2	–22.5
Jet fuels	–11.7	4.3	6.1	26.1	–22.3
Commercial power	3.2	2.3	.6	–.1	.0
Liquefied petroleum gas	–15.4	13.0	3.9	71.4	–29.3
Crude energy materials	–12.3	–.1	3.7	51.2	–23.1
Natural gas	–3.8	–14.0	–.3	92.0	–27.9
Crude petroleum	–27.7	21.1	10.8	35.8	–28.3
Coal	1.0	–2.1	–.8	–1.1	4.9

Prices received by domestic producers of finished consumer foods moved down 0.8 percent in 1997 after rising 3.4 percent in 1996. This reversal was led by a downturn in prices for pork, fresh fruits and melons, beef and veal, processed young chickens, processed fruits and vegetables, eggs for fresh use, soft drinks, and pasta. Price increases slowed for bakery products, confectionery end products, dairy products, and fish. By contrast, the index for fresh and dry vegetables turned up sharply in 1997 after a marked decline in 1996. Similarly, prices rose after falling a year earlier for roasted coffee, shortening and cooking oils, and milled rice. Price declines for processed turkeys slowed over the same period.

Grains and feeds. From December 1996 to December 1997, grain prices fell 2.0 percent, following a 20.3-percent drop over the previous 12 months. Contributing to the 1997 decline was lackluster growth in U.S. exports, due to large world crops and the Asian crisis. Wheat prices decreased 11.3 percent in 1997 after declining 19.3 percent in 1996, continuing the fall from their historically high levels reached in the summer of 1996. High wheat prices induced both domestic and foreign growers to plant more wheat. In addition, the U.S. Department of Agriculture's Conservation Reserve Program policy, which for years had eliminated millions of acres of wheat production, was replaced with a new policy in 1996 that gave growers much broader latitude in deciding which crops to plant. Corn prices rose 2.2 percent in 1997 after declining 21.0 percent in 1996. Like wheat prices, corn prices had reached historically high levels in the summer of 1996, causing more worldwide acreage to be planted. Generally favorable weather in growing areas resulted in record harvests.

Soybean prices increased 1.8 percent in 1997 after falling 3.7 percent in 1996. Adverse weather that delayed planting or ruined crops in many growing areas resulted in higher prices. During the summer, prices generally fell, as considerably more soybean acreage had been planted, leading to a worldwide glut in supplies. In the latter part of the year, high crop harvests were balanced by even higher domestic and foreign demand, and prices fluctuated somewhat as users replenished their stocks.

Slaughter livestock and meats. The year 1996 was very profitable for hog farmers; the bubble burst, however, in the third quarter of 1997. Export demand dropped due to a strong dollar after economic woes began to plague Asian markets and also partly because of Asian preference for Asian rather than North American varieties of pork. Together with increased pork production at home and cheaper chicken prices, the lackluster export demand pushed hog prices lower in 1997. Lower prices for both barrows and gilts, as well as for slaughter sows, contributed to the aggregate decrease. Barrows and gilts are sources of the highly promoted lean pork products, and sows are the source for pork bellies and bacon.

The index for slaughter cattle turned up in 1997 after moving down in 1996. Drought resulted in sharply reduced grazing prospects, and higher hay prices forced cattle ranchers to cull herds sharply and retain fewer stocker cattle. Most of the impetus behind this reversal in the direction of price change came from the slaughter cows and bulls component. Slaughter cows and bulls are either excess animals culled from the dairy herd or excess mature breeding stock culled from the beef-type cattle herd. Prices dropped significantly in 1996 due to supply pressure as producers culled their herds of these types of animals. To some extent, culling of the herds continued on into early 1997, but prices did rebound from the 1996 level as the remaining stocks of the mature cattle herd began to enable ranchers to recoup the previous year's losses.

As with pork producers, producers of slaughter broilers and fryers had enjoyed positive returns a year earlier, despite feed costs. In 1997, production of such poultry began to outstrip demand, and at the same time, competing meats became cheaper. During the fourth quarter of 1997, producer prices for broilers plummeted as production increased.

Dairy products. Prices for dairy products rose almost 5 percent in 1997, about twice as much as they had risen in 1996. At yearend, fluid milk prices were higher due to seasonally higher prices during the colder winter months and an increase in demand from butter and cheese manufacturers. Skyrocketing demand for butter during the holiday season also helped to drive prices higher. Creamery butter prices increased 82.2 percent in 1997. Higher prices for fluid milk and butter caused prices for many manufactured dairy products, such as ice cream and cheese, to increase throughout much of the year.

Table 4. Annual percent changes in Producer Price Indexes for selected food items, 1993–97

Index	1993	1994	1995	1996	1997
Finished consumer foods	2.4	1.1	1.9	3.4	–0.8
Pork	4.3	–11.1	15.3	21.9	–13.6
Dairy products	3.1	–2.0	5.4	2.4	4.7
Fresh fruits and melons	11.8	–11.2	2.5	37.2	–8.2
Fresh and dry vegetables	27.7	25.6	–36.0	–24.3	21.6
Roasted coffee	5.5	49.8	–8.2	–8.4	18.1
Beef and veal	–6.0	–4.8	–1.4	7.4	–5.4
Processed poultry	4.0	–3.7	8.4	2.6	–6.3
Intermediate foods and feeds	5.5	–4.5	10.3	2.1	–1.7
Prepared animal feeds	6.0	–10.6	20.6	5.4	–3.1
Crude vegetable oils	34.3	4.1	–14.1	–9.3	13.9
Flour	8.6	–1.1	20.1	–9.0	–8.2
Confectionery materials	10.4	2.2	1.5	2.2	–15.8
Refined sugar	–.6	.8	.8	4.2	–4.5
Crude foodstuffs and feedstuffs	7.2	–9.4	12.9	–1.0	–4.0
Slaughter hogs	–5.0	–21.3	40.6	23.2	–21.7
Soybeans	20.1	–18.1	26.7	–3.7	1.8
Wheat	18.6	–5.6	29.9	–19.3	–11.3
Corn	34.7	–22.4	49.4	–21.0	2.2
Fluid milk	6.7	–5.2	8.4	1.1	2.8
Slaughter cattle	–7.1	–5.3	–5.2	–2.5	2.0

Intermediate industrial materials

Prices for intermediate materials other than foods and energy increased 0.3 percent in 1997 after falling 0.9 percent in 1996. Prices for nondurable manufacturing materials moved up after declining the previous year. Prices for durable manufacturing materials were unchanged in 1997 after falling the year before. However, price increases slowed from 1996 to 1997 for construction materials.

Nondurable manufacturing materials. The index for nondurable manufacturing materials increased 0.3 percent in 1997, following a 3.3-percent decline in 1996. (See table 5.) Much of the 1997 reversal was due to an upturn in prices for paper and paperboard. Prices also rose after falling a year before for woodpulp, alkalies and chlorine, paint materials, and leather. Prices fell less than in the previous year for intermediate basic organic chemicals, phosphates, and synthetic rubber. Price increases accelerated for medicinal and botanical chemicals, inedible fats and oils, and gray fabrics. By contrast, prices turned down in 1997 after rising in 1996 for primary basic organic chemicals, plastic resins, nitrogenates, processed yarns and threads, and synthetic fibers.

Following 2 years of declines, prices for pulp and paper products turned up in 1997, as an improved economy and dwindling customer inventories gave rise to price hikes for most grades of paper. Woodpulp prices rose 4.1 percent in 1997, catapulted by sharp increases in the third quarter. Woodpulp prices moved down in the first 4 months of the year, only to rise when demand increased as customers rebuilt depleted inventories. Export demand to Asia—particularly, South Korea—dropped off significantly as a result of upheaval in financial markets in that country. Demand for woodpulp was dampened somewhat by the rapid rate of recovered paper consumption.

Paper prices increased 3.8 percent in 1997, following a 14.2-percent decline in 1996. After beginning 1997 with 3 straight months of price declines, the paper market rebounded, finishing the year with nine consecutive modest increases. The two driving forces behind this recovery were uncoated groundwood (up 24.5 percent) and newsprint (up 16.0 percent). Despite some pockets of discounting, especially in cut-size stock, prices for uncoated free-sheet were relatively stable at yearend. Mills were successful in holding transaction pricing in the last months of this year and did not have to resort to discounting. Overall U.S. demand growth for uncoated free-sheet averaged slightly more than 5 percent for 1997, buoyed by a booming economy and increased sales of computers and printers. Future expansion of capacity was expected to come from productivity gains on existing papermaking machines. Newsprint consumption in 1997 by U.S. dailies outpaced the level of a year ago. At yearend, there was much concern about the effect on supply of the 5-month old work stoppage at a major Canadian newsprint mill. North American producers also were concerned about the dropoff in newsprint demand to Asia, which accounts for 42 percent of offshore exports.

As usual, price changes for paperboard mirrored those for paper. In 1997, paperboard prices rose 5.8 percent after falling 19.0 percent in 1996. All grades of paperboard showed increases in 1997, led by the unbleached linerboard category, which rose 8.0 percent. Paperboard capacity, which includes linerboard and corrugating medium made from virgin and recovered fiber, grew by 2.9 percent in 1997, compared with 5.8 percent in 1996. The increased capacity in 1996 and 1997 reflected the startup of seven new recycled linerboard machines and one recycled medium machine.

Prices for basic organic chemicals dropped 1.7 percent in 1997 after rising 3.6 percent in 1996. Primary basic organic chemicals, which are petrochemically derived and which include such products as ethylene, fell 3.9 percent in 1997. Earlier declines in prices for crude petroleum and gasoline, along with record imports, combined to increase inventories of primary basic organic chemicals and to lower prices. Demand for these chemicals was fairly strong in 1997 despite excess supplies. The domestic producing sector for such chemicals continues to grapple with lower prices due to expanded European production, a phenomenon that has greatly increased world supplies.

Construction materials. The Producer Price Index for construction materials increased 1.2 percent in 1997 after rising 1.8 percent in 1996. The slowdown in price increases was led by a downturn in prices for softwood lumber. Prices also turned down in 1997 after increasing in 1996 for air-conditioning and refrigeration. Price increases slowed for millwork, gypsum products, plumbing fixtures, heating equipment, cement, other metal products, metal valves, and switchgear. By contrast, price increases accelerated for fabricated structural metal products, wiring devices, and fabricated ferrous wire products. Prices declined, but less than a year earlier, for nonferrous wire and cable, plastic construction products, asphalt felts and coatings, and plywood. The index for steel wire advanced 1.3 percent, the same as its decline in 1996.

Softwood lumber prices fell in 1997. Prices fluctuated throughout the year in response to construction activity, weather, and demand. During 1997, railcar shortages and a slowdown in rail service hampered shipments from many wood products operations in western states. Several logistical problems resulted from the highly touted merger of the Union Pacific and Southern Pacific railroads. Prices also moved down in 1997 for softwood plywood. However, the year ended with much optimism by plywood producers, particularly manufacturers of treated plywood. Uses for such products increased substantially as demand expanded for applications such as home subflooring encased with fiberglass, roofing sheathing, flooring in portable buildings, and siding for beach homes. Prices increased again in 1997 for hardwood lumber, which is used mostly for furniture manufacturing; however, some is used for construction, particularly flooring. In 1997, prices also advanced somewhat for general millwork, such as cabinets, vanities, doorframes, and sashes. The market for millwork is one of the most stable for the various lumber products. Strong demand from the home improvement market helps to hold down price increases, even when there are swings in new-home construction.

Prices for gypsum products increased 7.1 percent in 1997 after rising 6.6 percent in 1996. Much of the increase was on the strength of robust activity in the home improvement sector. Most (uncalcined) gypsum is used to manufacture prefabricated products such as gypsum board. Price increases for insulation materials, such as building batts, accelerated in 1997 after rising modestly in 1996. Cement prices increased

Table 5. Annual percent changes in Producer Price Indexes for selected inetermediate and crude materials other than foods and energy, 1993–97

Index	1993	1994	1995	1996	1997
Intermediate goods other than foods and energy	1.6	5.2	3.2	–0.9	0.3
Nondurable manufacturing materials	–.6	10.4	5.9	–3.3	.3
Inedible fats and oils	–6.1	48.0	–3.9	2.1	3.8
Woodpulp	–14.0	38.1	40.7	–33.0	4.1
Basic organic chemicals	–.7	15.7	.4	3.6	–1.7
Durable manufacturing materials	2.5	9.8	1.1	–1.4	.0
Copper	–19.7	68.2	–.1	–22.9	–22.8
Aluminum	–11.1	64.4	–7.3	–12.8	12.4
Lead	.0	37.5	9.1	4.2	–4.0
Zinc	–3.8	13.1	–5.7	–1.4	2.7
Construction materials	5.0	3.9	1.9	1.8	1.2
Gypsum products	12.8	30.8	1.0	6.6	7.1
Nonferrous wire and cable	–3.1	13.8	1.6	–3.1	–2.2
Softwood lumber	30.8	–9.6	–10.3	19.6	–3.8
Crude nonfood materials less energy	10.7	17.3	–4.2	–5.5	.0
Wastepaper	–12.3	179.6	–50.9	–1.3	11.6
Nonferrous scrap	–14.0	70.3	–10.3	–7.9	–.6
Raw cotton	12.9	34.9	4.2	–13.0	–11.2
Sand and gravel	3.1	2.2	3.6	1.9	1.8

3.5 percent, following a 5.0-percent rise the year before. Prices also advanced for concrete and concrete products, on the strength of increases for their chief ingredient, cement.

Durable manufacturing materials. In 1997, the index for durable manufacturing materials showed no change, following a 1.4-percent decline the year before. Prices rose after falling in 1996 for aluminum mill shapes, semifinished steel mill products, hot rolled bars, building paper and building board mill products, silver, zinc, and platinum. Prices fell, but less than in the previous year, for primary nonferrous metals, copper and brass mill shapes, cold finished bars, cold rolled sheets, flat glass, copper, and plywood. By contrast, prices turned down after rising the year before for hot rolled sheets and lead. Price increases slowed for prepared paint, cement, other metal products, and other miscellaneous metal. Prices for gold fell much more in 1997 than in 1996.

Copper prices declined 22.8 percent in 1997, about the same as in 1996. In 1997, prices declined steadily in the second half of the year. As in 1996, there was much concern that projected increases in capacity would have a dampening effect on prices. Warehouse stocks built up during the year, and supplies, coming to market from new mines, greatly exceeded demand. There were hopes in the marketplace that new demand from Japan or China would materialize. The index for copper last increased from May to June 1997, when London Metal Exchange warehouse stocks declined about 10 percent. Declines were restrained by threats of a work stoppage at Chilean mines and production snarls at a major domestic smelter.

The index for aluminum increased 12.4 percent in 1997 after falling 12.8 percent in 1996. Prices fluctuated throughout the year, nosediving in the fourth quarter. Consistent rises in London Metal Exchange inventories and periodic reports of increased production dampened prices for primary aluminum. Throughout the year, there were supply-demand imbalances that also helped to erode prices. Prices did rebound somewhat at yearend as producers worked down excessive inventories and warehouse inventories dropped at the metal exchange. Demand for primary aluminum was favorable in 1997; stock levels moved down consistently, almost without interruption. Prices were expected to respond more propitiously to what had been viewed as favorable market fundamentals. Although Southeast Asia is not a major consumer of primary aluminum, the region was blamed for some of the pricing predicament.

Domestic prices for gold fell 21.9 percent in 1997 as a robust stock market made the metal less attractive as an investment. However, prices for silver and platinum, which are both used in specialty manufacturing, increased in 1997 on the strength of steady demand.

Basic industrial materials

The Producer Price Index for basic industrial materials—crude nonfood materials other than energy—showed no change in 1997 after falling 5.5 percent in 1996. Prices turned up after falling the year before for iron and steel scrap, aluminum base scrap, wastepaper, pulpwood logs, and hardwood logs. Prices fell less in 1997 than in 1996 for copper base scrap, raw cotton, and phosphates. By contrast, price declines were steeper than in the previous year for gold ores, nonferrous metal ores, and softwood logs. The indexes for cattle hides and leaf tobacco both declined after advancing in 1996. Price increases slowed for other roundwood products. Sand and gravel prices rose 1.8 percent in 1997, only slightly less than they had risen the year before. (See table 5.)

Price movements for wastepaper, generally considered an early barometer of future manufacturing activity in the economy, were volatile in 1997. Wastepaper prices rose in the first quarter of the year, only to dip in the second quarter. Prices then advanced sharply in the third quarter and finally plummeted in the last quarter of the year. At its high marks, export prices rose 31.0 percent in May and 25.7 percent in August. Exports took a tumble in the latter part of the year, ending the fourth quarter 26.1 percent lower in price. At yearend, recovered-paper consumption continued to grow modestly; demand for old corrugated containers was steady to strong, with most mills using up all the product they bought. Demand for mixed papers was mostly in a holding pattern at the end of 1997, and paper stock dealers were optimistic that prices would strengthen in the near future. Demand for old newsprint dropped in the latter months of the year after showing improvement earlier in the fall. Demand softened, in particular, for standard newsprint, due to a steep drop in shipments to South Korea. By contrast, the strength of the Mexican market was a factor that bolstered prices of high-grade newsprint in the Southwest.

Prices for iron and steel scrap increased 14.5 percent in 1997, after falling 11.1 percent in 1996. Prices surged moderately at the start of 1997, lost some of that gain in March and April, and then steadily moved up for the rest of the year. Domestic steel mills operated at very high capacity, which bode well for scrap metal demand. Startups and ram-ups (restarts of idle plants) at various new scrap-fed minimills and the resumption of production at a major steel mill all supported demand. Export shipments were relatively low during 1997, not only largely because the domestic market was so vibrant, but also because the world market was a bit more sluggish than the U.S. market. High-grade scrap is now being purchased more on a contract basis, and this new phenomenon has led to more stable pricing than in years past. The year 1997 was also one in which the industry experienced considerable consolidation. This industry, once composed of old family-owned businesses that usually operated three or four yards has evolved into one of giant publicly traded corporations. Scrap substitutes such as pig iron, iron carbide, and direct-reduced iron were increasingly available in 1997. A ready supply of pig iron from Russia and Brazil and the possibility of increased domestic pig iron output combined to keep prices in check. After falling in 1996, prices for aluminum base scrap increased 9.7 percent in 1997, as inventories of stock were drawn down and supplies became more balanced with demand.

Prices for raw cotton declined 11.2 percent in 1997, following a 13.0-percent decline the previous year. An excellent harvest kept supplies of cotton abundant in 1997. However, competition from foreign cotton farmers continued to be fierce, and U.S. farmers were still not able to be competitive with the lower foreign prices. In spite of this situation, certain grades of high-quality specialty cotton held their own. The index for leaf tobacco inched down 0.5 percent in 1997. With strong demand for exports of tobacco products, the outlook for increased tobacco production was optimistic. Prices for flue-cured leaf at auction were 11.3 cents per pound below those of the previous season. At yearend, during the first few weeks of the burley auctions, prices were slightly less than in the previous season. The 1997 flue-cured auction sales averaged $1.724 per pound, compared with $1.837 the year before.

Selected industries

Mining. The Producer Price Index for the net output of total mining industries declined 20.2 percent in 1997 after advancing 40.6 percent in 1996. Prices for the oil- and gas-extracting industry group decreased about 25 percent, following a 57.9-percent advance the year before. Prices for the metal-mining industry group fell 14.3 percent in 1997 after declining 12.7 percent in 1996. Prices increased 2 percent for nonmetallic minerals mining, the same as in 1996. However, the index for the coal-mining industry group rose 2.8 percent after moving down 0.7 percent the year before. (See table 6.)

Manufacturing. The Producer Price Index for the net output of the domestic manufacturing sector moved down 0.8 percent in 1997 after increasing 2.2 percent in 1996. Prices fell after rising a year earlier for the industry groups of food and kindred products, petroleum refining and related products, rubber and plastic products, and transportation equipment. Price increases slowed from 1996 to 1997 for textile mill products, apparel, lumber and wood products, furniture and fixtures, chemicals and allied products, and nonmetallic mineral products. Prices fell more in 1997 than in 1996 for electrical and electronic machinery. As in 1996, the index for nonelectrical machinery continued to fall. By contrast, prices increased after falling in the previous year for paper products and primary metal industries. Price increases accelerated for tobacco manufactures and fabricated metal products. The indexes for the industry groups of printing and publishing, leather and leather products, and measuring and controlling instruments, etc., continued to rise.

Table 6. Annual percent changes in Producer Price Indexes for the net output of major industry groups, 1993–97

Index	1993	1994	1995	1996	1997
Mining industries	–7.9	–1.0	2.9	40.6	–20.2
Metal mining	–6.8	35.5	6.2	–12.7	–14.3
Coal mining	–.1	–2.1	–.8	–.7	2.8
Oil and gas extraction	–10.7	–3.2	3.5	57.9	–24.6
Mining and quarrying of nonmettalic minerals, except fuels	1.0	1.4	2.9	2.2	2.2
Manufacturing industries	.8	2.4	3.0	2.2	–.8
Food and kindred products	2.2	–.3	4.0	3.2	–.9
Tobacco manufacturers	–21.7	.3	3.8	3.2	9.0
Textile mill products	–.1	.7	2.6	1.1	.5
Apparel and other finished products made from fabrics and similar materials	.5	.4	.8	2.0	.9
Lumber and wood products, except furniture	13.6	1.3	–2.6	3.0	1.3
Furniture and fixtures	2.9	3.0	3.0	1.9	1.1
Paper and allied products	–.9	10.7	13.1	–10.3	1.9
Printing, publishing, and allied industries	3.1	3.8	7.0	2.4	2.6
Chemicals and allied products	.1	7.4	6.0	1.5	.6
Petroleum refining and related products	–12.9	8.9	2.6	22.7	–14.5
Rubber and miscellaneous plastic products	1.0	3.6	2.6	.1	–.4
Leather and leather products	1.3	2.5	1.5	1.1	1.0
Stone, clay, glass, and concrete products	2.9	4.3	2.7	1.3	.9
Primary metal industries	1.6	9.3	3.2	–3.0	.7
Fabricated metal products, except machinery and transportation equipment	1.1	2.4	3.4	.6	1.2
Machinery, except electrical	.1	.9	1.4	–.6	–.6
Electrical and electronic machinery, equipment, and supplies	1.2	.3	.7	–.7	–1.7
Transportation equipment	3.0	2.4	2.1	.5	–1.0
Measuring and controlling instruments; photographic, medical, and optical goods; watches and clocks	1.2	1.2	1.5	.6	.5
Miscellaneous manufacturing industries	1.8	1.6	2.0	1.4	.6
Service industries:					
Railroad transportation	.9	.4	–.3	.0	1.0
Motor freight transportation and warehousing	–	2.7	1.7	2.4	2.1
U. S. postal service	.0	.0	10.4	.0	.0
Water transportation	–.9	2.5	2.4	.2	–.9
Transportation by air	8.2	–.3	7.4	5.9	.5
Pipelines, except natural gas	.6	10.2	3.4	–8.8	–2.2
Health services	–	–	3.5	1.7	1.0
Legal services	–	–	–	–	4.1

NOTE: Dash indicates data not available.

Services. The index for railroad line haul operations increased 1.0 percent in 1997 after showing no change in 1996. The modest price rise resulted from increased charges for some of the industry's lucrative commodities, such as coal, chemicals, and petroleum. 1997 was a mixed year for the railroad industry. Both passenger and freight operations experienced declining capacity and capability in meeting demand during the year. However, the two key measures of freight traffic—intermodal volume and total freight volume—both set records in 1997. Intermodal volume totaled 8.7 million trailers and containers, an increase of 6.8 percent over the previous year. Total freight volume reached nearly 1,375 billion ton-miles (shipment weight times travel distance), an increase of 0.9 percent from the 1996 figure. Overall, price movements for the index for line haul operations resulted from several factors: weather, the continued concentration of the rail freight industry, fuel prices, competitive market forces, and a robust economy. Inflationary pressures, such as rising fuel costs, the imposition of mandatory rail safety measures, and expanded services, were all held in check by increased operating efficiencies, wage concessions, increased productivity, industry restructuring, low interest rates, and competitive market forces.

From December 1996 to December 1997, the index for trucking (except local) rose 1.9 percent, following a 3.6-percent rise in 1996. During 1997, strong demand allowed the trucking industry to remain relatively stable, with steady, but small, price increases throughout the year. Less-than-truckload carriers, the category that showed the largest increase over the year, benefited from the rise in demand and posted profits during each of the four calendar quarters of 1997. Fuel prices remained stable at relatively low levels. Wages for drivers rose in response to driver shortages; however, carriers showed restraint and did not pass along all increased labor costs.

The index for air transportation moved up 0.5 percent in 1997 after advancing 5.9 percent the year before. In 1997, an increase in the index for scheduled air passenger transportation more than offset a decrease for scheduled air cargo transportation. Airlines were generally profitable in 1997, on the strength of a robust economy and high load factors (the percentages of seats filled on a plane). The elimination of the Federal excise tax on January 1 caused the index for scheduled air transportation to rise in the first quarter. The increase occurred because the airlines failed to pass on this tax savings to consumers. Since the Producer Price Index captures price changes excluding taxes, eliminating the tax resulted in an increase in the index when the airlines failed to lower ticket prices. After the airlines experienced strong profits and 2 months of a tax-free windfall, the 10-percent Federal excise tax was reinstated on March 7; the airlines passed along only a portion of the tax to consumers, thereby causing the index to decline for March. The Federal excise ticket tax was restructured again on October 1. The new tax became 9 percent, with the addition of a fee of $1 per segment. (A segment begins with a takeoff and ends with a landing.) The year also was characterized by labor unrest, particularly from pilots, and airlines were faced with making concessions to avoid shutdowns.

The index for airports, flying fields, and airport services rose 4.2 percent in 1997, following a 5.3-percent increase in 1996. Leased space for concessions moved up 13.7 percent over the year. This index is subject to large swings; leases for concessions are often based on a percentage of gross revenue and are highly indicative of passenger traffic and the spending habits of passengers. As in 1996, airport managers chose to raise prices for services rendered to air passenger and air cargo carriers during 1997 in order to fund airport improvements. The index for other commercial airport services decreased 2.6 percent in 1997; unlike other operations, the aviation side of the airport is not expected to generate a profit. Airports used passenger facility charges, as well as airline ticket taxes, to help fund costly improvements.

Although the index for commissions for airline arrangements declined 4.7 percent in 1997, a 19.0-percent advance in the index for nonairline arrangements caused the overall index for travel agencies to rise 0.9 percent from December 1996 to December 1997. The system of capping commissions to travel agencies has greatly restricted compensation to agents since 1995. Among nonairline arrangements, bookings for cruises showed the largest increase (35 percent).

The radio broadcasting index moved up 4.9 percent in 1997 after increasing 8.7 percent in 1996. The higher rise in 1996 resulted from two stellar events: the summer Olympics in Atlanta and the presidential election in November. The increased demand associated with these events permitted radio broadcasters to raise their rates more quickly than usual; previously, these companies could increase their rates only in response to changes in programming costs. In addition, the Telecommunications Act of 1996 ignited a merger frenzy within the industry. The consolidation of radio-broadcasting stations allowed broadcasters to pass along higher rates to advertisers at all levels. Radio broadcasters benefited from three market advantages. First was the greater ease of purchasing advertising, compared with the other media. Second, there arose a greater awareness of radio's cost-effectiveness. Finally, the medium benefited from a greater awareness of its ability to target key demographic groups.

From 1996 to 1997, the index for cable and other pay television services rose 4.3 percent. This hike resulted primarily from rising cable rates, reflected in a 4.1-percent increase in the price of subscriber services. In addition, charges for advertising services increased 8.2 percent, and charges for network affiliate services advanced 2.7 percent. Throughout 1997, there was much concern across the country over rapidly rising cable rates. Many consumer groups complained that rates were rising at the fastest pace ever, with some even increasing at twice the rate of inflation in the overall economy. As the year drew to a close, these same groups demanded that the Federal Communications Commission put a freeze on cable rates.

From December 1996 to December 1997, the index for operators and lessors of nonresidential buildings increased 1.9 percent, compared with a decrease of 0.9 percent a year earlier. The index for operators and lessors of office property rose 2.9 percent in 1997, mostly due to the lack of new office property development, which palls in the 1990s in comparison to the excess buildup in the 1980s. In the 1990s, nationwide vacancies were in the 8- to 10-percent range. The index for operators and lessors of retail property rose 1.3 percent in 1997, and the index for operators and lessors of industrial property increased 0.9 percent.

The hotel and motel index advanced 4.2 percent from December 1996 to December 1997, compared with an increase of 4.5 percent over the previous 12 months. In 1997, charges for guest room rentals moved up 5.7 percent; prices for food and beverages rose 2.9 percent; rates for other guest room rentals, including casino hotels, increased 11.4 percent; and the index for limited-service hotels and motels advanced 7.8 percent. The industry as a whole experienced a year of high occupancy rates as a result of a booming economy, with robust demand from both the business travel and leisure travel sectors.

As in 1996, revenues for help supply services were robust in 1997. The index for the industry increased 1.7 percent in 1997. The unemployment rate was relatively low for most of the year, and fierce competition among agencies prevented charges from rising higher.

The index for passenger car rentals, without drivers, advanced 15.0 percent in 1997 after falling 9.3 percent in 1996. The 1997 increase was largely the result of a 17.3-percent rise in the index for passenger car rental, except replacement. During 1997, the passenger car rental industry was plagued with legislative proposals to increase taxes at both the State and local level, ongoing class-action discrimination suits, industry restructuring, and increased competition for market share.

Price increases for health care services slowed from 1.7 percent in 1996 to 1.0 percent in 1997. The index for general medical and surgical hospitals mirrored this slowdown; however, the index for offices and clinics of doctors rose somewhat more in 1997 than in 1996. Prices for home health care services moved up 7.9 percent in 1997, with charges for home health aides increasing the most of all types of payors. In 1997, pressures by managed care companies on the health care industry continued to help lower prices and keep inflation at a minimum. There was a growing trend of physicians consolidating into larger organizations. Doctors increasingly had to compete for managed care dollars in this new environment by creating their own networks, which enhanced their bargaining power. Physician networks bring together partners with management skills, managed care expertise, information systems, and capital. With the increasing presence of health maintenance organizations in the health care industry, physicians have continually moved away from traditional fee-for-service arrangements into capitation arrangements, or fixed periodic prepayments per member. While the Producer Price Index does not capture changes in capitation rates, this type of payment is becoming increasingly popular and contributes to the reasons physicians experienced smaller increases in revenue.

The newly introduced index for legal services increased 4.1 percent in 1997. This index was rather stable throughout the year, except in January, when most law firms make changes in their fee schedules that become effective with the new calendar year. Also introduced in 1997 were indexes for engineering and architectural services. The index for engineering design, analysis, and consulting services moved up 3.2 percent in 1997; the index for architectural design, analysis, and consulting services increased 3.0 percent from December 1996 to December 1997.

The index for accounting, auditing, and bookkeeping services increased 2.3 percent in 1997, reflecting semiannual adjustments in January and July to such firms' billing rates and pricing strategies. In addition to being affected by a strong economy, 1997 prices changed because the proposed mergers of the big six accounting firms in the industry resulted in intense competition among these top firms, which were willing to grant deep discounts to clients in order to land big accounts. □