

# Sharp drop in energy prices holds inflation in check during 1986

*Lower prices for petroleum products result in Consumer Price Index rise of 1.1 percent, the smallest advance since the 1960's; producer prices decreased 2.5 percent*

CRAIG HOWELL, ROGER BURNS, AND ANDREW CLEM

Inflation seemed to vanish in 1986. A slight increase in consumer prices was a contrast to the economy of the 1970's, when double-digit price increases appeared. Furthermore, producer prices actually fell across a broad front for the first time since the early 1960's.

The continuing decline in energy prices resulted in the Consumer Price Index (CPI) advancing only 1.1 percent during the 12-month period ended in December. This rise compares with increases of about 4 percent in each of the 4 preceding years and was the smallest annual change since a 0.7-percent rise in 1961.

Falling energy prices had an even larger impact on the Producer Price Index (PPI). The finished goods price index turned lower for the first time since 1963, declining 2.5 percent; it had risen less than 2 percent in each of the 3 preceding years. The intermediate goods price index fell 4.4 percent over the year after rising slowly from 1982 through 1984 and edging down slightly in 1985. The 1986 decreases for both these major stage-of-processing indexes were the largest annual declines since 1949. The drop of 9.7 percent in the crude goods price index was considerably more than the declines recorded in 1984 and 1985 and marked the largest decrease since 1952.

The sharp declines in energy prices and their broad impact

on the CPI are shown in table 1. The 19.7-percent drop in energy prices was almost entirely responsible for the deceleration in the CPI. Excluding energy, the index increased 3.8 percent during 1986, compared with increases of between 4 and 4.5 percent in each of the prior 4 years. The food index advanced 3.8 percent in 1986, largely reflecting an upturn in meat and poultry prices. Shelter costs, however, rose somewhat less in 1986 than in other recent years, increasing 4.6 percent. The index for all items excluding food, shelter, and energy continued to slow. Within this group, however, price movements for commodities and services continued to be different. Charges for these other services remained in the 5- to 6-percent range, while other goods prices rose only 1.4 percent in 1986.

Energy in the PPI for all three stages of processing—crude materials, intermediate goods, and finished goods—registered sharper declines than in the CPI. The 1986 declines in the PPI energy measures were substantially larger than in 1985 and more than offset a moderate acceleration in the prices for nonenergy goods. (See table 1.)

By the end of 1986, the economic expansion had entered its fifth year, with few signs of either an impending recession or a resurgence of double-digit inflation. Labor costs continued to move up at only a modest pace, indicating a lack of pressure on current prices. The Employment Cost Index decelerated steadily after peaking at near double-digit rates in 1980, with total compensation for private industry workers advancing only 3.6 percent for the year. In addition, growth in output was sluggish in 1986, with capacity

---

Craig Howell, Roger Burns, and Andrew Clem are economists in the Office of Prices and Living Conditions, Bureau of Labor Statistics. They were assisted by Mary Lynn Schmidt and Doug Robertson, economists in the same office.

**Table 1. Percentage changes for major categories of the Consumer Price Index and Producer Price Index, 1982-86<sup>1</sup>**

Index	1982	1983	1984	1985	1986
<b>Consumer Price Index</b>					
All Items .....	3.9	3.8	4.0	3.8	1.1
Energy .....	1.3	-5	.2	1.8	-19.7
Energy commodities .....	-5.0	-3.2	-1.9	3.4	-30.5
Energy services .....	14.1	4.1	3.4	-5	-3.3
All items less energy .....	4.2	4.4	4.5	4.0	3.8
Food .....	3.1	2.6	3.8	2.7	3.8
Shelter .....	2.4	4.7	5.2	6.0	4.6
All items less food, shelter, and energy .....	6.1	5.0	4.4	3.7	3.4
Other commodities .....	5.5	5.0	3.1	2.2	1.4
Other services .....	7.3	4.9	6.0	5.4	5.6
<b>Producer Price Index</b>					
Finished goods .....	3.7	.6	1.7	1.8	-2.5
Finished energy goods .....	-1	-9.2	-4.1	-3	-39.1
Finished goods less energy .....	4.2	2.0	2.5	2.1	2.7
Intermediate materials .....	2	1.8	1.3	-3	-4.4
Intermediate energy goods .....	-7	-5.5	-1	-8	-28.9
Intermediate materials less energy .....	5	3.2	1.6	-2	2
Crude materials .....	4	4.7	-1.6	-5.6	-9.7
Crude energy materials .....	2.6	-4.6	-1.3	-4.9	-29.4
Crude materials less energy .....	-7	9.6	-1.7	-6.0	-9

<sup>1</sup> Calculated on a December-to-December basis.

utilization rates below 80 percent and civilian unemployment 6.7 percent at yearend. These factors offered little in the way of cost pressure on prices.

Measures taken by policymakers, designed to stimulate growth by depreciating the dollar and lowering interest rates, had only a minor impact on prices, but could contribute to inflation in the longer term. However, the value of the dollar did not fall uniformly against currencies of all other nations. Thus, price advances for some commodities will continue to be restrained by competition from abroad.

Interest rates generally declined throughout the year, easing the debt burden for many companies; nevertheless, expenditures for capital investments decreased, in part because of the uncertainty associated with changes in business tax policies. Widespread warnings about excessive personal debt went largely unheeded as consumer expenditures continued to play a major role in sustaining the overall expansion. Real residential investment spending climbed strongly early in the year, but then slowed.

In this article, we first examine price changes during 1986 for the CPI. We then focus on price changes for all major components of the PPI.

## Consumer prices

### Energy

The deceleration in the overall CPI in 1986 was almost entirely attributable to the sharp drop in energy prices, down 19.7 percent. Prices for commodities and services within energy, as well as within the overall CPI, continued to diverge. OPEC's decision in late 1985 to formally abandon production quotas led to plunging crude oil prices and resulted in sharp declines in consumer prices for energy com-

modities. Retail gasoline prices dropped 30.7 percent and fuel oil prices decreased 33.4 percent in 1986. While these prices declined more rapidly during the first half of the year, attempts to stabilize markets and increase prices met with only limited success. At yearend, gasoline and fuel oil prices were 38.7 and 40.4 percent, respectively, below their peak levels in early 1981.

The index for energy services—natural gas and electricity—also declined in 1986, but by substantially less than the index for energy commodities. Charges for natural gas and electricity declined 5.8 and 1.5 percent, respectively.

### Food

Retail food prices rose 3.8 percent in 1986, after increasing 2.7 percent in 1985. In 1986, the food at home component increased 3.6 percent, while prices for food away from home rose 4.3 percent. Prices for grocery foods advanced substantially more in the second half of the year, partially due to the severe drought during the late spring in the Southeast. The acceleration in grocery prices during the last 6 months of 1986 was largely concentrated in the meats, poultry, fish, and eggs index and the fruits and vegetables index. After registering declines during the first 6 months, these components increased at double-digit rates during the last half of the year. For the year as a whole, the meats, poultry, fish, and eggs group increased 6.4 percent and accounted for over 55 percent of the increase in the food at home index. All other major grocery food groups rose 3.0 percent or less in 1986.

### Shelter

The 1986 rise in shelter costs, up 4.6 percent, was the smallest increase in this component since the rental equivalence approach to the measurement of homeowners' costs was adopted in 1983. Prior to 1983, the measurement of shelter costs for homeowners included investment costs associated with purchasing a housing asset; these costs were inappropriate for the CPI. Historically, shelter costs, principally reflecting the increase in interest rates, were a major cause of the double-digit inflation during 1979, 1980, and the first part of 1981. Conversely, when mortgage interest rates dropped sharply in 1982, the shelter index was a major factor in the slowdown of the overall CPI. Since the shift to an owners' equivalent rent measure for homeowner shelter costs, the volatility of the shelter component has been dampened. While the rise in shelter costs slowed, both the magnitude and the speed of adjustment were much less than in the overall CPI.

### Other services

Price increases for other services except shelter and energy did not, on average, contribute to the further slowdown in prices in 1986 and have remained in the 5- to 6-percent range over the last 4 years. While considerable variance exists in the magnitude of the service groups increases in

1986, the service component of all major expenditure groups rose more than the commodities portion of these groups. Nevertheless, some individual components in these service groups slowed substantially or even declined; perhaps most dramatic was the sharp drop in automobile finance charges as interest rates generally declined and automobile manufacturers made extensive use of below-market rate financing in order to stimulate car sales. With a 7.3-percent drop in 1986, these charges have declined in 3 of the past 4 years. In addition, substantial price reductions in interstate long distance toll calls have occurred in each year since the AT&T divestiture on January 1, 1984. These declines, however, have been more than offset by the increases in local telephone charges. In each of the last 3 years, the increase in the costs of all telephone services—local, intrastate, and interstate—exceeded the increases in the overall CPI.

Most services, however, continued to post substantial price increases in 1986 and some even accelerated. The cost of medical care services, which increased at double-digit rates during the 1973–82 period, slowed during 1983–85, advancing about 6 percent a year. In 1986, these charges rose 7.9 percent. Other service components that registered large increases in 1986 included automobile insurance costs, up 11.8 percent, and charges for tuition and other school fees, up 7.9 percent.

### **Other commodities**

Even excluding the sharp drop in the energy index and lower prices for used cars, prices for commodities rose at a much slower rate than those for nonenergy services. This divergence in commodity and service prices suggests that commodity prices in this country may have been affected by lower priced imports resulting from the high value of the dollar relative to the currencies of other countries.

When the dollar appreciated from 1981 to March 1985, foreign suppliers of imports received the same income in their own currency by selling the same quantity of imports at lower dollar prices, as each dollar received by them commanded a greater amount of their own currency. After the dollar began depreciating, several factors still existed that helped to delay any inflationary impact. The effects of the changing value of the dollar on import prices can be delayed or reduced substantially as a result of changing profit margins of suppliers, the necessity to revise dollar-denominated contracts, and specific trade restrictions such as import quotas. Also, changes in the rates of exchange between the dollar and the currencies of the Nation's various trading partners have not been uniform. While the dollar has depreciated significantly against the yen and a number of major European currencies, there has been little change against the currencies of many less developed countries that are significant trading partners. Further, the relative price level of imports may be strongly affected by the growth rate of the domestic economy. Although U.S. economic growth has

been quite modest, it still exceeds that of many of the country's principal trading partners. Thus, a large number of factors may have intervened to minimize the price-reducing effect of the 1981–85 dollar appreciation, and these same factors may vitiate or delay any inflationary impact of the post-March 1985 devaluation.

From June 1982 through March 1985, as the dollar was appreciating, prices paid by *importers* for consumer commodities (other than energy, food, and used cars) edged up at an annual rate of only 0.7 percent, while prices paid by *consumers* for the same set of commodities rose at an annual rate of 3.0 percent.

In the 21 months following the March 1985 peak value of the dollar, these import prices accelerated sharply, rising at an annual rate of 8.1 percent, while the corresponding retail prices rose at a much slower rate, only 2.6 percent. Prices charged by importers did not show any obvious impact of the dollar devaluation until December 1985. At the end of 1986, however, prices paid by consumers had advanced 10.3 percent.

Comprehensive analysis relating import prices to changes in consumer prices is difficult. There has been, however, some recent evidence of larger consumer price increases for import-affected items. In 1986, new car prices rose 5.8 percent, their largest increase since 1981. In addition, prices for apparel commodities, housefurnishings, and housekeeping supplies—components which contain commodities with higher than average import proportions—accelerated in the second half of 1986. The largest increases in other commodity prices in 1986, however, occurred in areas with little import penetration: medical care commodities and tobacco products. These components have not accelerated, but rather continued to advance at rates well above most other commodities.

## **Producer prices**

### **Crude goods**

Following decreases of 1.6 percent in 1984 and 5.6 percent in 1985, the PPI for crude materials for further processing fell 9.7 percent during 1986. Price indexes for crude petroleum and natural gas plummeted after showing much smaller declines in 1985, but price decreases for nonenergy materials were not as large as in the previous year.

*Energy.* The crude energy materials index fell 29.4 percent following a drop of 4.9 percent in 1985. In response to the breakdown in the pricing discipline of the Organization of Petroleum Exporting Countries (OPEC), Saudi Arabia in late 1985 reversed its previous policy of restraining its oil production. Competitive underbidding by certain oil producing countries accelerated during early 1986 as prices for crude oil began to plummet. However, crude petroleum prices rebounded somewhat during the third quarter, following an August OPEC announcement of production cutbacks.

The war-related financial burdens of Iran and Iraq and the debt-servicing needs of certain other oil producing nations both contributed to the ending of OPEC's pricing discipline before 1986. In the longer term, a number of factors have contributed to the fundamental transformation of the global petroleum market. Expanded production by non-OPEC nations has gradually taken a larger share of the world market in the 1980's. In the United States, the cumulative effect on demand of the 1973 and 1979 energy price increases was reflected by the 17-percent decline in petroleum consumption between 1978 and 1985.

Domestic prices for crude petroleum and most refined products fell by nearly 50 percent in 1986. This decrease represented an unprecedented disinflationary advantage to the American economy, helping to maintain the momentum of growth despite the problem of the trade imbalance.

After falling 7.8 percent in 1985, the natural gas index plunged a record 21.6 percent. Natural gas producers lowered their prices during most of the year to remain competitive with falling prices for petroleum-derived heating fuels. This index climbed in the early 1980's, but fell 31.1 percent from its March 1983 peak by December 1986. Coal prices edged down over the year.

**Foodstuffs.** The index for crude foodstuffs and feedstuffs moved down 1.7 percent, much less than the 6.4-percent drop in 1985. Contributing to this slowdown of price decreases was an advance in fluid milk prices that contrasted with a substantial decrease the previous year. For several years, the dairy industry has experienced low milk prices, resulting from milk overproduction; therefore, the Government created the Dairy Termination Program, which pays farmers to sell or slaughter their dairy cows, reducing milk production and raising prices in 1986.

After dropping in 1985, hog prices advanced strongly in mid-1986, reflecting restricted supplies after several years of stock reductions. Price decreases slowed for cattle; although slaughter rates remained high, low feed prices enabled some farmers to hold their cows off the market during the second half of the year. Raw cane sugar prices moved up after falling in 1985, in response to the lowering of the Government ceiling on import shipments for that commodity.

Increased domestic and world supplies of grains and feedstuffs, along with reduced U.S. Government price supports for grains, put downward pressure on their prices. Domestic corn prices dropped more than 30 percent because of good harvests, larger carryover stocks, and limited storage facilities that compelled farmers to sell off their holdings to make room for new harvests. Record carryover stocks for wheat contributed to a price decline of more than 18 percent. Prices for hay and soybeans dropped at double-digit rates for the third consecutive year. Hay demand was down because of improved pasturing, while soybean stocks were high and exports were off.

**Industrial materials.** The index for crude nonfood materials other than energy turned up 1.6 percent, after declining in both of the 2 preceding years. Prices were particularly active in the latter half of 1986, with the index falling at a simple seasonally adjusted rate of 6.7 percent during the third quarter and then rising 1.9 percent in the fourth quarter. In large part, this pattern was due to volatile prices for raw cotton. A new Government program, instituted in August 1986 to make American cotton competitive on international markets, initially caused domestic prices to drop almost 60 percent (thereby matching the world price level). However, by the end of the year, the world price for raw cotton (adjusted to U.S. quality and specifications) had jumped over 70 percent, partly reflecting poor weather in growing regions abroad; in addition, the U.S. price climbed above the world price level as a result of stronger demand from domestic cotton mills, tight supplies of quality cotton due to crop damage, and increased export demand. Despite this late surge, the December 1986 price for domestic raw cotton was still below its December 1985 level, although the price decrease was less than those registered in 1985 or 1984.

Several factors contributed to the upturn in raw material prices in 1986. Ferrous scrap prices advanced after declining in the preceding 2 years. Following 2 years of decreases, aluminum base scrap prices rose with the expectation of an improving market for aluminum during the spring. However, these scrap prices remained unchanged during light trading in the second half, when the market for primary aluminum proved to be weak. After falling in 1985, prices for heavy yellow brass scrap turned up in accord with strongly advancing prices for primary zinc. Wastepaper prices soared 52 percent after plummeting in 1985, as paper mill demand increased sharply and exports moved up. Prices also advanced for cattle hides and domestic apparel wool. Price declines slowed for leaf tobacco.

However, prices turned down for logs and timber as falling fuel prices reduced business costs. Construction sand and gravel showed smaller price increases, as transportation costs fell with decreasing fuel prices.

### **Intermediate goods**

Contrasting with the mild pattern of movements experienced since the early 1980's, the PPI for intermediate materials, supplies and components dropped 4.4 percent during 1986. However, virtually all of the impetus behind this downturn came from the energy sector. The index for intermediate goods excluding foods and energy remained nearly unchanged for the second year in a row. One unusual feature of 1986 index changes for this category and its main stage-of-processing components is the close similarity to corresponding changes of a year earlier.

**Energy.** The index for intermediate energy goods plunged 28.9 percent during the year, following relatively small

declines in recent years. Prices for diesel fuel, residual fuel, and jet fuel each fell nearly 50 percent. Less uniformity was shown in 1985, when residual fuel declined 15.6 percent, jet fuel moved down moderately, and diesel fuel rose nearly 6 percent. Liquefied petroleum gas prices fell 52.4 percent during 1986, closely paralleling refined product movements during the year. Reduced fuel generation costs likewise affected electric power prices. The index for industrial and commercial electric power recorded a 1.0-percent decline, the first decrease for this category in over 2 decades. Electric power rates are typically rather stable, because of the regulatory environment in which utilities operate. These prices did not fall as much as other energy products for that reason, and because petroleum is not used for power generation as much as in the 1970's.

*Manufacturing materials.* The index for intermediate goods other than foods and energy edged up 0.1 percent over the year, after a 0.1-percent decline in 1985. As in the previous year, declines for manufacturing materials were offset by small advances for manufacturing components and products used in the construction sector.

The index for materials for nondurable manufacturing fell 1.8 percent, slightly less than in the year before. The overwhelming influence was the precipitous fall in petroleum costs, which led to lower prices for industrial chemicals (down 6.0 percent), plastic resins and materials (down 3.6 percent), and synthetic rubber (down 8.8 percent). The rate of capacity utilization in the chemicals industry remained at about 80 percent for most of the year, further depressing pricing. Another commodity whose price fell because of energy developments was nitrogenate fertilizer materials, which registered a 21-percent drop for the year. Most anhydrous ammonia is derived from natural gas, prices of which were negatively affected by the oil price collapse.

In sharp contrast, however, prices jumped for many paper-related goods. Woodpulp prices advanced 16.9 percent, recovering virtually all of the losses experienced the year before. Upturns of a similar but less-pronounced nature occurred in prices for paper and paperboard (both rose between 4 and 5 percent). Growth in the paper sector was centered in the business and computer paper markets, where demand continued to be fairly strong. Woodpulp and paperboard producers benefited from the reduced level of foreign competition due to the decline in the U.S. dollar. Finally, leather prices surged 11.4 percent, the most in several years. This upturn reflected the strong overseas demand (and hence higher costs) for U.S. cattle hides.

The durable manufacturing materials index moved down 1.2 percent, about the same as in 1985. A good portion of this decline was related to the January drop in the steel mill products index. This reflected a broad cut in list prices to bring them into alignment with actual transaction prices, which had been falling for some time. Among nonferrous metals, considerable diversity existed in price movement.

Copper and silver prices declined, as did certain types of aluminum. Expectations early in the year of higher prices for copper and aluminum were not fulfilled because demand for both stagnated, and labor disputes in the aluminum industry were settled.

The most dramatic activity was found in the markets for lead, zinc, and platinum. Lead prices began to climb sharply during the spring months, contrary to expectations. Short-term tight inventories due to various technical factors (such as refinery shutdowns and strikes) prevailed over the long-term perception of weakness in demand, and prices ended the year 47.7 percent over the December 1985 level. Zinc prices followed lead prices closely; the two metals are produced together, and both experienced supply problems because of labor disagreements. In the precious metals markets, political unrest in South Africa sparked increased interest in platinum by speculators. Over 90 percent of the world's supply of platinum comes from South Africa and the Soviet Union. Prices began to surge in mid-1985 and continued to increase until the final quarter of 1986, when profit-taking set in. The platinum index was still nearly 50 percent higher at the end of 1986 than it was a year earlier.

*Construction materials.* In spite of the continued downward trend of mortgage interest rates during the year, the housing construction market began to show signs of weakness in the second quarter. Beginning the year around the 2-million unit level, the annual rate of new private housing starts retreated to about 1.7 million units by the end of the year. In the commercial construction sector, activity remained generally subdued because of the continued oversupply of office space in certain cities.

The PPI for construction materials and components edged up only 0.4 percent, less than in any other year since the early 1960's. Substantial declines were noted for products derived from petroleum: asphalt paving materials fell nearly 12 percent, and asphalt roofing materials dropped almost 9 percent. Plastic plumbing products registered a decline of 6.3 percent, likewise reflecting lower costs of petrochemically derived resins. Prices for gypsum products moved down 2.5 percent, after a strong year (up 7.8 percent) in 1985. The gypsum industry raised prices during the spring, but the slack market failed to support the move; prices slid back for most of the remainder of the year.

The lumber and wood products industries were unusually influenced by governmental actions during the year. A trade dispute with Canada had arisen after 2 years of sagging prices in the midst of strong residential construction activity. Domestic lumber producers filed a countervailing duty petition against Canadian producers in May, alleging that unfair subsidies by provincial governments in Canada permitted below-cost sales. The International Trade Commission ruled that U.S. producers were being injured by the subsidies, and in October an interim 15-percent tariff was imposed on softwood lumber imports from Canada.

Prices for lumber rose during the third quarter, when they normally decline sharply. Over the year, the PPI for softwood lumber advanced 6.5 percent. Prices for millwork and plywood each moved up less than 2 percent.

The cement industry was another source of trade friction in 1986. However, the U.S. producers lost their bid for countervailing duties on imports of eight nations that allegedly guarantee their own firms a minimum rate of return. In spite of substantial transportation costs for such a bulky product (and minimal differences in production technology), cement imports accounted for 10 percent of the American market in dollar terms and 15 percent in tonnage terms. Under such pressure, prices for Portland cement fell 4.5 percent between December 1985 and December 1986.

*Foods.* The intermediate foods and feeds index continued on a downward path over the past year, but the 0.4-percent decline was less than in 1984 or 1985. Crude vegetable oil prices fell 25.5 percent, reaching their lowest level since the late 1960's. After showing little change over the previous 4 years, flour prices dropped 10.5 percent, reflecting burgeoning world grain supplies. However, refined sugar prices (which are kept above prevailing world levels by a Government support mechanism) rose moderately after declining in recent years.

### Finished goods

Among major categories within the finished goods price index in 1986, the index for energy goods fell 39.1 percent, dwarfing the declines registered in other recent years. Consumer food prices climbed 2.9 percent, continuing the moderate increases registered for this index in each year after 1980. As in 1985, the increase in the index for consumer goods other than foods and energy was just under 3 percent. Capital equipment prices rose less in 1986 (2.1 percent) than they had in 1985 (2.7 percent).

*Energy.* The dramatic decline in the index for finished energy goods followed decreases of just 0.3 percent in 1985 and 4.1 percent in 1984. This decline occurred largely in response to the precipitous drop in world crude oil prices attributable to the breakdown of OPEC's production control system at the end of 1985. Prices received by refineries for both gasoline and home heating oil were nearly cut in half over the year, following much smaller declines in 1984 and moderate increases in 1985. The natural gas index also fell far more than it had a year earlier.

*Foods.* The 1986 rise in the index for finished consumer foods was well within the range of moderate increases registered for this index each year after 1980; for example, food prices inched up only 0.5 percent in 1985, following a 3.5-percent climb a year earlier. A drought in the summer of 1986 had a limited and relatively short-lived impact on food prices, primarily through heat-related deaths of chick-

ens in the Southeast. Weather conditions during the growing season were generally much more favorable in the Midwest, California, and other major farming regions than in the Southeast. Exports of American agricultural products were seriously hampered by excess supplies in many other countries.

After a rise of less than 1 percent a year earlier, pork prices climbed 13.4 percent in 1986; a 5-percent drop in production was largely responsible for this climb. Processed poultry prices quickly retreated from the high levels attained in the immediate aftermath of the summer drought and ended the year 1.8 percent lower than their December 1985 values, as higher prices for chickens offset a sharp drop in turkey prices. Beef and veal prices fell sharply through the first half of the year, reflecting increased output and the continuing decline in feed grain costs, but recovered somewhat in the second half for a net decrease of 6.3 percent.

Roasted coffee prices climbed 18.2 percent, mostly because of unusually dry weather in Brazil's growing areas for much of the year. The index for fresh and dried vegetables advanced 2.9 percent, far less than the double-digit climb a year before. Prices also rose in 1986 for fish, confectionery end products, dairy products, and refined sugar. In contrast, the index for shortening and cooking oils fell almost 10 percent, partly because of the continued drop in soybean quotations.

*Other consumer goods.* The index for consumer goods other than foods and energy moved up 2.9 percent, about the same as a year earlier. However, the composition of the 1986 advance was the reverse of the 1985 pattern. Consumer durable price increases accelerated from 2.1 to 3.5 percent, while nondurables slowed to 2.4 percent after a 3.2-percent rise the year before.

Much of the acceleration in the index for consumer durable goods was due to the 6.6-percent increase in the index for passenger cars, far larger than in any other year since 1981. The falling value of the dollar against the yen, coupled with continued Japanese limitations on car shipments into this country, led to higher prices for some Japanese models and allowed room for domestic manufacturers to raise their prices as well. While imported autos still commanded a substantial share (more than one-quarter) of the total American market, sales of domestic cars also enjoyed another strong, if erratic, year. Intermittent discounting, especially evident in cut-rate loans subsidized by producers, again characterized the marketing of domestic models during 1986. New car sales were further stimulated at the end of the year, before tax law changes effective for 1987 would end deductions for State sales taxes on Federal income tax returns. In contrast with the accelerated price increases for new passenger cars, however, prices for light trucks rose less than half as much as in 1985 (3.7 versus 7.9 percent).

Among other consumer durables, prices for gold jewelry

rose following several years of decline, reflecting the parallel upturn in gold quotations. By contrast, lower stainless steel prices were a major influence in the 6.5-percent decline in the flatware index, which showed almost no change in 1985. Prices for books, floor coverings, toys and games, sporting goods, glassware, household furniture, and mobile homes rose moderately, while appliance prices decreased for the first time since 1965.

Within the category for consumer nondurable goods other than foods and energy, the effect of substantially higher prices for some items was eased by modest advances for others. Prescription drug prices climbed nearly 10 percent, marking the seventh consecutive year that this index rose between 8 and 12 percent. Prices for tobacco products and over-the-counter drugs also increased about as sharply (7.8 and 6.2 percent) as in other recent years. In contrast, the index for tires and tubes fell for the fourth consecutive year, reflecting lower costs for synthetic rubber and relatively sluggish demand in both the original equipment and replacement markets. Prices for luggage and soaps decreased after increasing in 1985. Prices for apparel, newspapers, period-

icals, sanitary paper, alcoholic beverages, cosmetics, and footwear rose somewhat less than they had a year earlier.

*Capital equipment.* The index for capital equipment moved up 2.1 percent in 1986, following advances of 2.7 percent in 1985 and 1.8 percent in 1984. Business spending on investment goods declined over the year, with capital expenditures in the energy-production sector especially hard hit. Capacity expansion projects in many other industries were postponed pending the outcome of political debates on elimination of the investment tax credit and similar tax policies. Spending on some projects was accelerated, however, to take advantage of favorable tax treatments that would be scaled back or eliminated in 1987. The scarcely abated influx of imports kept most domestic manufacturing industries at output levels well below any capacity constraints and thus diverted pressure for new capital construction. Prices for only a handful of major types of capital equipment rose more than 3 percent in 1986, while the index for oil field and gas field machinery dropped 3.5 percent, a symptom of the depression in the energy-production sector. □

---

#### A note on communications

The *Monthly Labor Review* welcomes communications that supplement, challenge, or expand on research published in its pages. To be considered for publication, communications should be factual and analytical, not polemical in tone. Communications should be addressed to the Editor-in-Chief, *Monthly Labor Review*, Bureau of Labor Statistics, U.S. Department of Labor, Washington, DC 20212.

---