CONGRESS OF THE UNITED STATES
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For Immediate Release *November 18, 1997*

Continued Disinflation Sparks Prospect of a Future Federal Reserve Rate Cut

--CPI and PPI Show No Inflation Threat--

Washington, DC – Joint Economic Committee (JEC) Chairman Jim Saxton (R-NJ) today pointed to the release of **Consumer Price Index (CPI)** data as confirming the lack of inflation in the U.S. economy. The October core CPI climbed only 0.2 percent, while the core **Producer Price Index (PPI)** was flat in October. Furthermore, the forward-looking market price indicators monitored by the JEC – commodity prices, bond yields and the dollar exchange rate – suggest that falling prices are a future possibility. These market price indicators have proven to be a reliable gauge of future inflation pressures. Saxton's statement follows:

"The CPI, PPI, and market price indicators have shown no inflation threat over the last year. Now the market price indicators monitored by the JEC indicate continued disinflation. Should these trends continue, they would suggest that falling prices may be in the pipeline. This potential for falling prices indicates that the Federal Reserve should balance its stance by being as ready to cut interest rates as to tighten policy. The key goal of price stability shared by the Federal Reserve and the JEC is inconsistent with rising or falling prices. Furthermore, there is an agreement that monetary policy must move preemptively to head off price changes before they occur. Consequently, the Federal Reserve, guided by the goal of price stability, should be prepared for the option of an interest rate cut in the future."

The forward-looking market price indicators monitored by the JEC, have proven to be reliable leading indicators of price changes, up or down. While the recent focus has been on a lack of inflation, the latest evidence from these indicators suggests, if these trends continue, a potential modest decline in prices is possible in the near future. If this proves to be the case, then an interest rate cut and easing of monetary policy would be appropriate and consistent with price stability. This approach would be codified under recently introduced legislation.

The Price Stability Act of 1997, H.R. 2360, introduced by Saxton, would establish inflation targets as a means of maintaining price stability by the Federal Reserve. Inflation targets would be set within a narrow band of about a 0-2.5 percent increase in a broad price index. The inflation targeting approach would prevent the occurrence of significant inflation or deflation. This approach has been successfully applied in a number of nations, including the United Kingdom and Canada. A number of Federal Reserve officials have voiced their support for this approach. At a recent JEC hearing, Fed Chairman Alan Greenspan testified that he was sympathetic with inflation targeting and agreed that it was consistent with recent Federal Reserve policy.

The JEC's research on inflation targeting, market price indicators and other issues in monetary policy are available in the special studies on monetary policy. The six JEC studies in this series are:

(1) *Lessons From Inflation Targeting Experience*, February 1997
(2) *The Importance of the Federal Reserve*, March 1997
(3) *Establishing Federal Reserve Inflation Goals*, April 1997

(4) *The Roots of the Current Expansion*, April 1997
(5) *A Response to Criticisms of Price Stability*, September 1997
(6) *Transparency and Federal Reserve Monetary Policy*, November 1997

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Press Release: #105-93

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