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Discussion of Andrew Filardo and Hans Genberg,
Targeting inflation in Asia and the Pacific:
Lessons from the recent past

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In general a very nice discussion of Asian experience, with useful comparisons of formal and informal inflation targeters plus some interesting speculation in final section that a less formal commitment to IT allows more scope for responding to diverse shocks.

- inflation targeting and inflation performance
- inflation targeting and inflation forecasts/expectations
- multiple pillars?

- useful presentation of central bank monetary policy frameworks in 12 Asian-Pacific countries
 - very varied group, Australia and New Zealand, Japan, Korea, India, China, Malaysia, and other smaller
 - turns out that all these CBs have price stability as (the or a) main objective of policy, except Hong Kong (currency board)
 - all have high/recently increased independence, and transparency
 - Australia, Indonesia, Korea, New Zealand, Philippines, Taiwan are formal inflation targeters (ITers); China, Hong Kong, India, Japan, Malaysia and Singapore are not (NITers)

- previous work by Ball & Sheridan failed to identify significant contribution of formal inflation targeting to reductions in inflation and in inflation volatility, but Schmidt-Hebbel, Pétursson and others have found some effects
- F&G do not replicate these studies on their smaller sample but they show that ITers and NITers alike have been broadly successful in achieving better inflation performance, especially since 2000
- they also estimate inflation persistence and find no clear difference between the two groups (but some tendency for developed countries to have lower persistence than emerging)

- F&G then examine dispersion of inflation forecasts using a novel statistic (Kullback-Leibler divergence statistic): in general there is some reduction in the dispersion and some reduction in the level around which forecasts are centred
- in their econometric analysis of the causes of these movements, initially it seems that formal inflation targeting reduces the dispersion, but the introduction of a variable that summarises the region-wide use of IT dominates individual IT dummies
- F&G argue that a common regional trend rather than adoption of formal IT may be responsible for narrowing of divergence of forecasts, and they present this finding as in line with Ball & Sheridan's view that formal IT has little effect

- interesting, could be rationalised as result of process by which over time forecasters develop their understanding of and focus on Asian-Pacific countries and they produce more model-based forecasts which tend to converge
- would merit further investigation in other country samples
- would merit further investigation in later sample periods including financial crisis where presumably forecasting harder and divergence more likely

- F&G also present informal evidence that ITers and NITers differ little in short run behaviour of inflation or inflation expectations (forecasts) in response to 2006-8 commodity price cycle
- not clear how consistent this is with findings of Roger or Schmidt-Hebbel, but should be investigated

- final section of paper: discussion of role of alternative/additional objectives such as exchange rate stability or non-misalignment, and of course financial stability
- F&G acknowledge the Tinbergen principle, that each (independent) objective needs separate instrument, but suggest that the additional objectives may not be independent of price stability [in 1970s the changing perception of link between inflation and output due to introduction of expectations into the Phillips curve went along with Friedmanite insistence on primacy of single, monetary, instrument]
- they also point out that some Asian-Pacific CBs have succeeded in pursuing two objectives, typically price and exchange rate stability [and of course many European CBs managed to pursue – compatible – monetary and exchange rate targets in much of 1980s-1990s]

- in Europe and maybe US, the issue is whether CBs should respond to asset prices as well as inflation
- Lucas Papademos has recently argued that the ECB's definition of price stability would allow it to pursue a 'leaning against the wind' policy in some circumstances, and that the ECB's longer term analysis of monetary and credit developments could provide signals of financial imbalances
- more broadly we can suggest that a CB which has goal independence and a solid reputation (inherited partly from the Bundesbank) can afford to consider multiple objectives/perspectives, whereas a CB which has a poor historical record on inflation may have little alternative but to concentrate on one simple goal (adopt formal IT)

- that then enables us to return to the vexed issue of whether formal IT adoption has or has not led to improved inflation performance
- Ball & Sheridan emphasised regression to the mean as an explanation for improved performance, in other words the poor historical record of IT-adopters
- Mishkin and Schmidt-Hebbel have then considered why countries have chosen IT (and still found some effect from formal IT adoption)
- we can widen this out to include also social and political attitudes to central banking (given the arguments about causation):

- CBs in the countries that took the Keynesian revolution as it was understood in the 1950s most seriously were those which came to be most deeply subordinated to their ministries of finance, and which most needed the break involved in explicit inflation targeting
- on the other hand CBs in countries where the old tradition of sound money persisted, and that tradition served to protect the CB to some extent from the politicians, did not need such a dramatic break and are not now so circumscribed by the formal IT framework in their responses to other state-dependent objectives
- with respect to F&G and the Asia-Pacific, what sort of background these CBs have? what sort of social-political attitudes prevail(ed) in the environments in which they developed? how much did they ‘need’ or not need to adopt IT for the above reasons?

- lastly, I want to emphasise another factor which underlies the different performance of different CBs: as economists we always find it easier to talk about the choice of monetary policy rules or frameworks, but careful examination of the historical record of individual CBs make clear that performance is also heavily affected by the – undefinable and unmeasurable – elements of the degree of commitment and competence of the specific individuals and groups making policy in different CBs at different times
- differences here are surely an important part of the explanation of why formal IT sometimes seems, and sometimes doesn't seem, to improve inflation performance, and suggest we should not be too concerned about which way our findings go in this respect – just be pleased that inflation and monetary policy performance are generally much better than they were 2-3 decades (or more) ago