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After several decades of low and stable inflation rates in most parts of the globe, high inflation has reemerged once again to become probably one of the most pressing macroeconomic issues right now. By the time we are writing this introduction, the search interest for the term “inflation” has reached peak popularity worldwide according to Google Trends. Regardless of the factors behind these recent trends, explaining and forecasting inflation around the world have been two of the most important questions that have traditionally preoccupied academic researchers and policymakers in macroeconomics. And most likely, these two broad issues will continue to be at the top of the agenda even after finally the current bout of inflation subsides.

We are glad to introduce Volume 45 Number 89 of the Journal *Economía* dedicated precisely to these questions. This Special Issue 2022-1 is titled “Recent Developments in Inflation Dynamics”. The issue contains new research presented in seven papers that study inflation dynamics from different angles and using novel techniques and diverse data samples. The content covers a wide range of topics ranging from the hypotheses that link inflation with other key macroeconomic indicators such as money growth, interest rates, and output gaps, to methodological issues related to the measure of the long-run component of inflation, to its forecasting and forecast evaluation under different contexts.

Allow us to summarize the articles. This special issue starts with “Some Long-Run Correlations of Inflation in Developed Countries” by Kenneth D. West (University of Wisconsin) and Tu Cao (University of Wisconsin). The authors provide a correlation analysis of two relevant long-term relationships: the inflation-money growth link as well as the inflation-nominal interest rates link. This empirical study exploits more than a century of data from eighteen advanced economies using a frequency domain technique. By *long-run* the authors mean one decade or more. An interesting feature of the method employed is the robustness of the confidence intervals to the order of integration of the data, namely, stationary, fractionally integrated, or unit root, cointegrated or possibly not cointegrated. The authors find that the estimated long-run

correlation coefficients are mostly positive. Even though the size of the correlation is modest for interest rates, it is relatively significant for money growth. In general, the authors find that post-Global Financial Crisis (GFC) data does not influence these results. Having always in mind that correlation does not imply causality, the article concludes that the well-known macroeconomic propositions of monetary neutrality and the Fisher effect are broadly consistent with the data.

In “Implications of Endogenous Money Growth for Some Tests of Superneutrality and the Fisher Effect,” John Keating (University of Kansas) studies the same hypotheses addressed by West and Cao, but from the perspective of empirical testing. Tests have sometimes been performed by estimating how a variable responds to a permanent shock to inflation. The author observes that the use of permanent shocks to inflation and money growth for testing such hypotheses has declined. One possible reason is that permanent movements in these variables have an endogenous component and, thus, estimates are biased. However, such a bias sign can be determined using credible qualitative assumptions about the effects of structural shocks on variables. These results are used to re-examine cross-country findings from two different structural VAR models that estimate the effects of permanent inflation shocks. The author argues, first, for the rejection of superneutrality for output in favor of a long-run positive output effect from permanently higher money growth. Second, provides reasons for the rejection of the Fisher effect in favor of nominal rates moving less than one-for-one with inflation in the long term. These results are robust to endogenous money growth bias under a wide range of plausible structural assumptions. The article concludes that these results provide evidence in support of structural models that predict the Mundell-Tobin effect. That is, nominal interest rates would rise less than one-for-one with inflation because higher prices would induce individuals to hold lower money balances and more financial assets, which would push interest rates down.

The third article is coauthored by Kristin J. Forbes (MIT Sloan School of Management), Joseph E. Gagnon (Peterson Institute for International Economics), and Christopher G. Collins (Morgan Stanley) and is titled “Low Inflation Bends the Phillips Curve around the World.” The authors tackle a finding sometimes labeled as the *flattening of the Phillips curve*. In turn, this fact is closely related to the so-called “missing deflation” phenomenon observed since the GFC until the COVID pandemic. The authors estimate a non-linear specification for the Phillips curve using a panel of advanced and emerging market economies. They find strong statistical support for a Phillips curve that turns nonlinear when inflation is relatively low (more precisely, below 3 percent). Moreover, this estimated curve is linear and steep when output is above its potential level (i.e., the economy faces a negative output gap) and becomes flat when output is below its potential level. At the latter state, additional increases in the output gap have nil effects on the inflation rate. The authors argue that this nonlinearity is consistent with evidence that supports downward nominal wage and price rigidities. Robustness checks show that the results are not sensitive to different cut-off values such as those between two and four percent—nor to country-specific thresholds based on median inflation rates. In addition, they find that headline—but not core—inflation is mainly related to international drivers, especially during the post-GFC period. The authors conclude that the Phillips curve is well alive and its slope is strongly statistically significant and nonlinear, whether one accounts for global factors or not.

An adequate measure of the long-run component of inflation is crucial for effective monetary policy decisions. In “Is it Time to Reassess the Focal Role of Core PCE Inflation in Assessing the Trend in PCE Inflation?”, Randal Verbrugge (Federal Reserve Bank of Cleveland) convincingly argues that the use of a “Core” Personal Consumption Expenditures (PCE) index—which excludes food and energy prices—to measure trend inflation in the United States is long overdue for replacement. One reason is that the exclusion of those items (with the exception perhaps of gasoline) is not optimal. The excluded items usually contain persistent trends and are highly volatile. Consequently, their exclusion causes a time-varying bias and significant departures from trend inflation. As part of his constructive criticism of core measures that exclude food and energy, the author proposes the use of trimmed mean PCE inflation and median PCE inflation as better alternatives. Even though no one measure is ideal, these two well-known measures deal with the methodological issues abovementioned. The paper provides an ample set of empirical exercises comparing the three alternatives. The author concludes that either trimmed mean PCE inflation or median PCE inflation are superior measures in practice.

In “Flexible Average Inflation Targeting: How Much Is U.S. Monetary Policy Changing?”, Jarod Coulter (Federal Reserve Bank of Dallas), Roberto Duncan (Ohio University), and Enrique Martínez-García (Federal Reserve Bank of Dallas) explore the Federal Reserve’s adoption of flexible average inflation targeting (FAIT) in August 2020 after concluding its first-ever public review of the monetary policy framework. Using synthetic controls, the authors find that the inflation rate increased considerably more than predicted had the strategy not changed (an average of 1.18 percentage points during 2020:M8–2022:M2). The authors then go on to estimate a workhorse open-economy New Keynesian model and run a series of counterfactual exercises feeding the recovered shock innovations from the estimated model under alternative specifications of the Taylor rule that place different weights on past cyclical inflation deviations. On that basis, the authors argue that FAIT is, in practice, much more an incremental change to policy than a major structural break from the preceding regime. They show that the differences in terms of cyclical growth and inflation under FAIT are small over the 1984:Q1–2019:Q4 period unless average inflation puts significant weight on inflation in the distant past, two years or more back. Furthermore, the authors also indicate that the rise in inflation since the pandemic is not necessarily the direct result of targeting average inflation under FAIT. In turn, the authors argue, the shock component of monetary policy—particularly forward guidance—could have contributed more to the observed inflation spike. The authors finally caution that the ability to keep long-run inflation expectations well-anchored under FAIT will be key to determining the new regime’s performance—on that point, the jury is still out there since FAIT has only been tested in the U.S. for a short period of time since being implemented.

As mentioned earlier, accurate inflation forecasting has been another big challenge among scholars and policymakers. To obtain precise forecasts, we need adequate forecast evaluations of the models at hand. In “A Power Booster Factor for Out-of-Sample Tests of Predictability”, Pablo Pincheira Brown (Universidad Adolfo Ibáñez) proposes a method that can be used to improve finite sample properties of several out-of-sample tests of predictability in an environment in which we compare one large nesting model vis-à-vis a small nested model. In particular, the

paper focuses on the widely used Clark-West t-statistic. The new test multiplies this statistic by a factor that equals one under the null hypothesis that the short nested model is the true model, but that should be greater than one under the alternative hypothesis that the larger nesting model is more adequate. Monte Carlo simulations show that the new test is well-sized and powerful. Moreover, it tends to be less undersized and more powerful than the original Clark-West test. Although most of the gains in power are related to size improvements, gains in size-adjusted-power are also observed. In a sample of thirty OECD economies, the method is applied to evaluate two forecasting models of core inflation rates in which one of them uses an international core inflation factor. More rejections of the null hypothesis are obtained with the augmented model, indicating a strong influence of global inflation in the selected group of countries.

In “Searching for the Best Inflation Forecasters within an Employment Survey: Microdata Evidence from Chile”, Carlos Medel (Central Bank of Chile) aims to determine which group of consumers is better at inflation forecasting in Santiago, Chile’s capital city. The study uses a specific survey of consumer perceptions at the individual microdata level that is linked to a survey of employment. The datasets allow linking consumer perceptions and 12-month-ahead inflation forecasts with personal characteristics (namely, gender, age, educational level, county of living, and the economic sector in which they are currently working) without errors. The results suggest that women—in contrast to the international evidence—aged between 35 and 65 years old, with a college degree, living in the North-eastern part of Santiago (that with the highest living standards in the country), and working in the Community and Social Services sector are the best forecasters of total inflation. Men aged between 35 and 65 years old, with a college degree, living in the South-eastern and North-eastern part of the city but working in Retail and Government and Financial Services sectors, respectively, are the second-best at forecasting inflation. All these results are compared to the naïve random walk (RW) forecast, as it assumes no deeper knowledge of the inflation dynamics. These results are relevant because they might allow identifying the most accurate group when forecasting inflation and, thus, may help refine the information provided by the survey for inflation forecasting purposes.

To finish this introduction, we would like to thank the authors and all the anonymous referees for their valuable work to make this special issue possible.

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