

Christoph Grosse Steffen, Banque de France

Departmental Seminar June 24, 2024

Host: Zeno Enders

Anchoring of Inflation Expectations: Do Inflation Target Formulations Matter?

Abstract:

Inflation target formulations differ across countries and over time. Most widespread are point targets, target ranges, hybrid combinations of the two, or mere definitions of price stability. This paper proposes a novel empirical measure of expectations anchoring based on the cross-sectional distribution of private sector inflation point forecasts. Applying this to a panel of 29 countries, it finds three main results. First, a numerical target definition per se does not improve anchoring compared to a definition of price stability, while the formulation of a numerical reference point increases the degree of anchoring. Second, point targets and hybrid target formulations are associated with better anchoring than target ranges. Third, periods of persistent target deviations lead to an increase in tail risks to the inflation outlook. Conditional on such periods, point targets and hybrid targets attenuate tail risks to the inflation outlook, with a stronger quantitative effect for point targets. The results are consistent with models suggesting that target ranges are interpreted as zones where monetary policy is less active.