

Assessing the Gap between Observed and Perceived Inflation in the Euro Area: Is the Credibility of the HICP at Stake?

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Discussion by B. Mojon, FRB Chicago
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Outline

- Semantics
- What the paper does
- Overview of the results
- Did the Gap between perceived and observed inflation have an impact?
 - On real wages
 - On consumption
- Issues

Semantics

Teuro

Teuer (expensive in German)



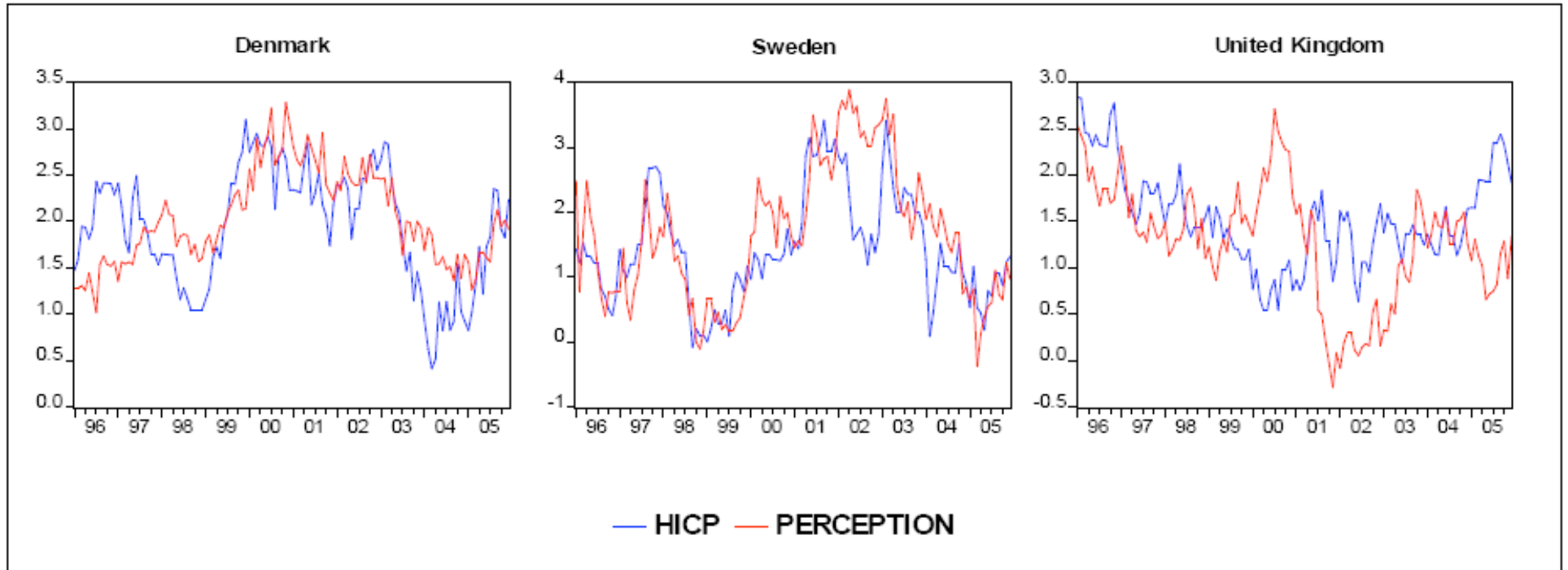
What the paper does?

- Re-scales a qualitative indicator of inflation perception

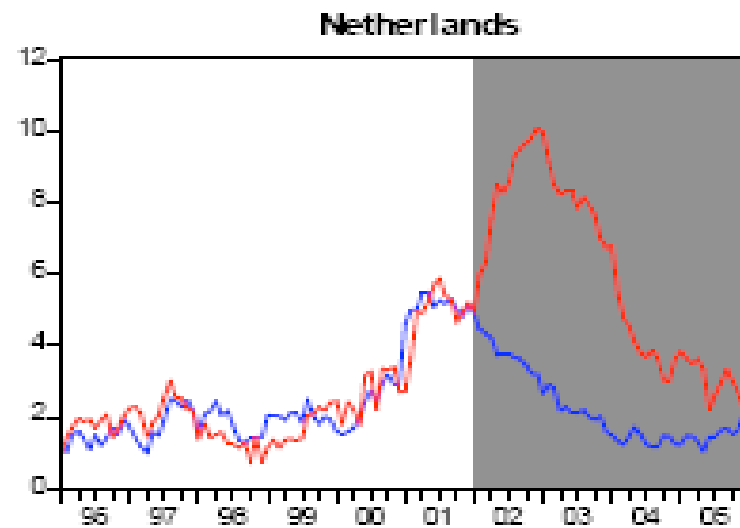
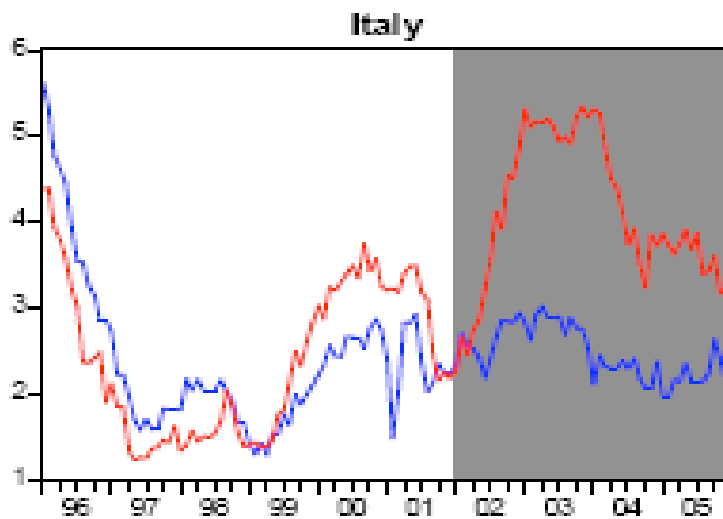
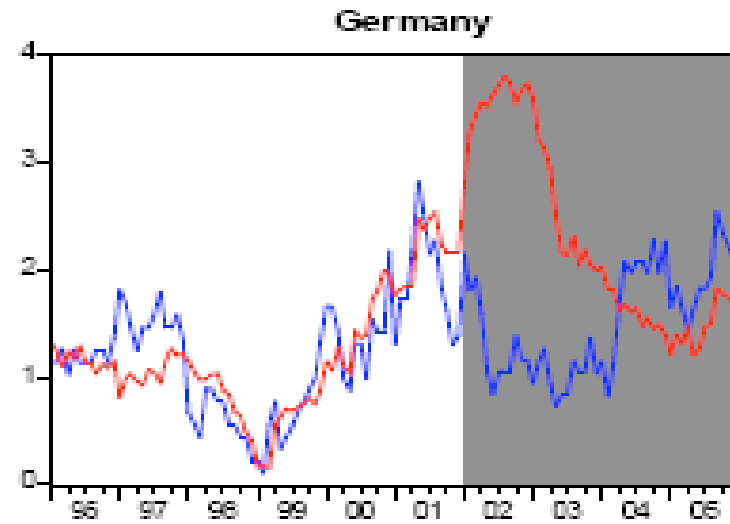
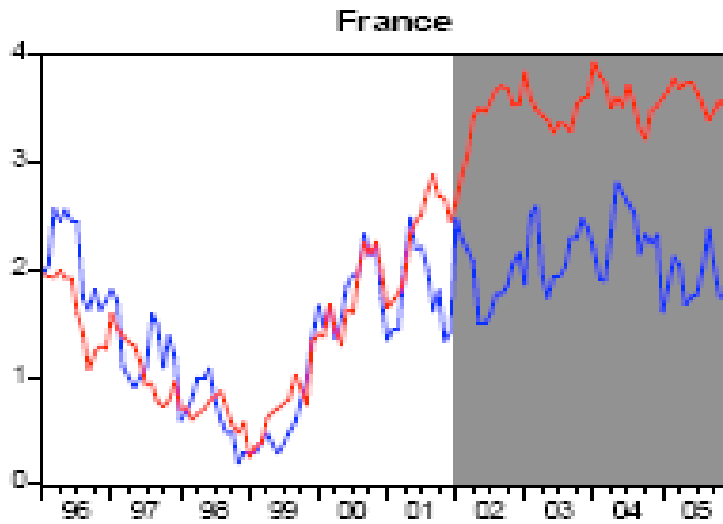
$$GAP_t = \frac{(Bal_t - \overline{Bal})}{S_{BAL}} \times S_{\pi} + \overline{\pi} - \pi_t$$

- Analyzes
 - the persistence of this GAP before and after 2002, i.e. the change over, taking non euro-area countries as point comparison
 - the role of respondents socio-economic characteristics, frequently purchased goods, owner-occupied housing costs
- Robustness exercises

Results of the paper



Results of the paper



Results of the paper

- Econometrics confirm a sustained Gap between perceived and official inflation series, from 2002 on
 - The gap is as large in Germany and in Italy
 - As large across socio-economic groups
- Issues for monetary economics and central bankers
 - The ECB mandate and independence did not bring about confidence for all constituencies spontaneously
 - Inflation expectations as SPF or bond prices did not jump in 2002.
 - Should central bank try to please every constituencies?
 - Causality between “opinion” and economic conditions?



Any implication on wages?

- We can expect real wages to increase sharply following the change over.

=> Is there any evidence of this in the data?

Estimate VAR models with

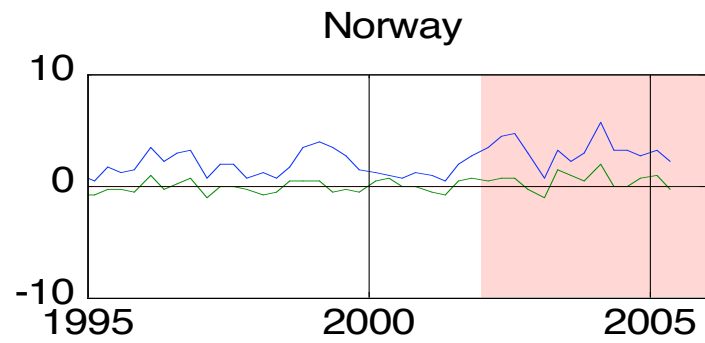
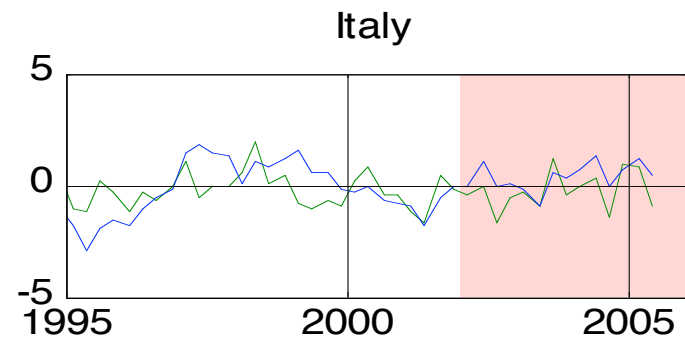
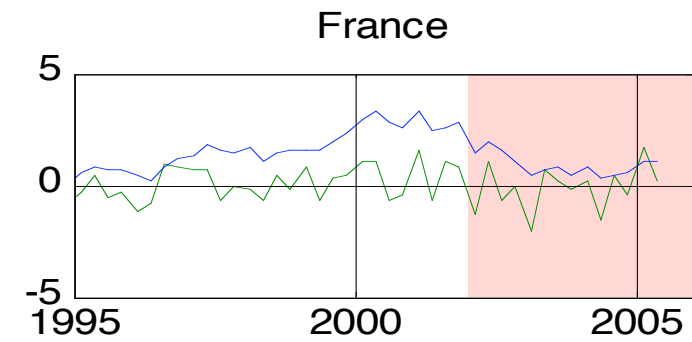
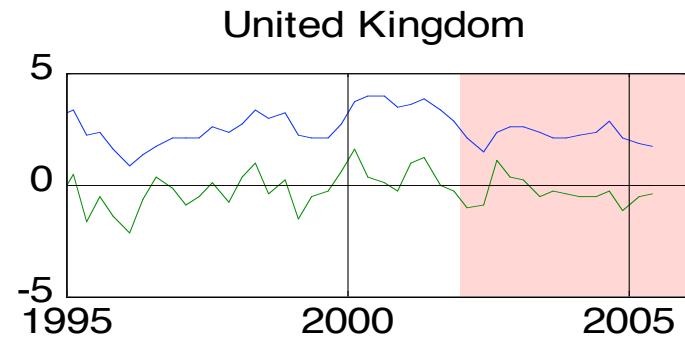
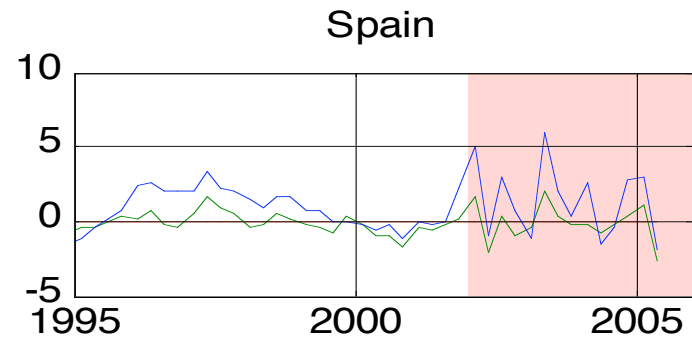
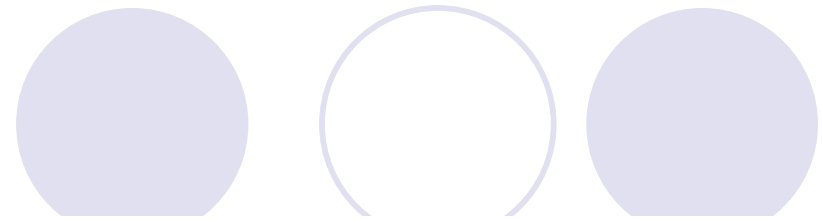
Output

Productivity

Real wages

1980 to 2005

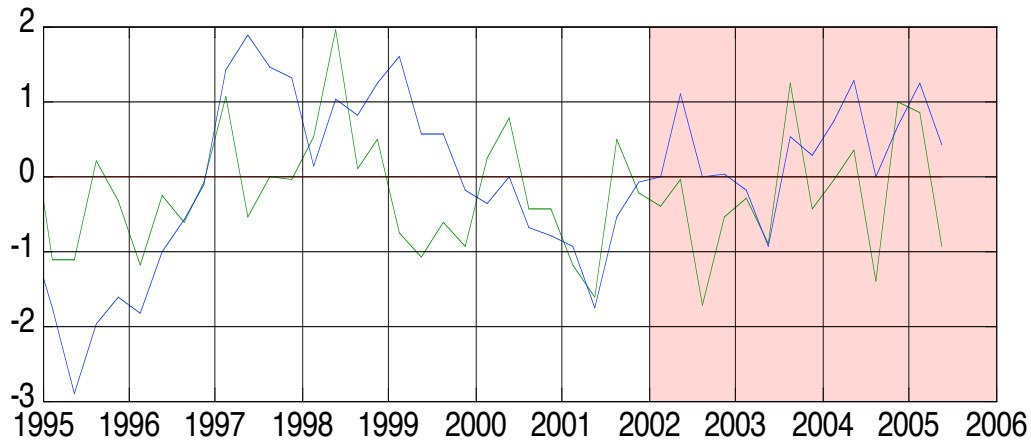
$d\log(w/p)$
 $d\log(w/p)$ shock in the VAR



ZOOM

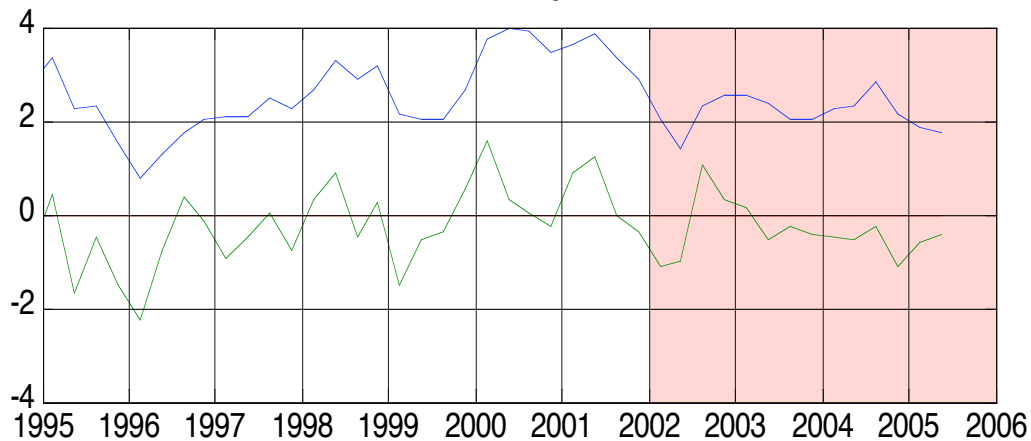
Results:

Italy



No persistent positive real wage shock in 2002-2004

United Kingdom





Any implication on consumption?

- We can expect that, as the perceived purchasing power of consumers has declined substantially and for a prolonged period of time

=> Is there any evidence of this in the data?

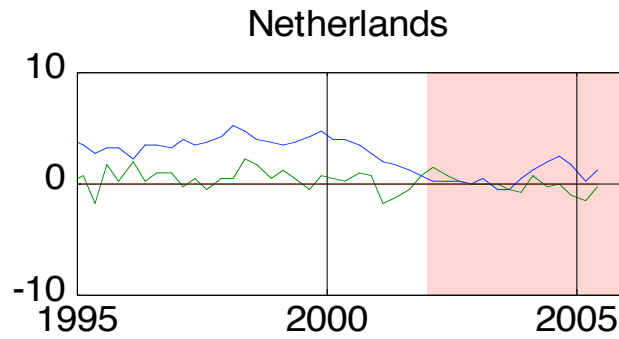
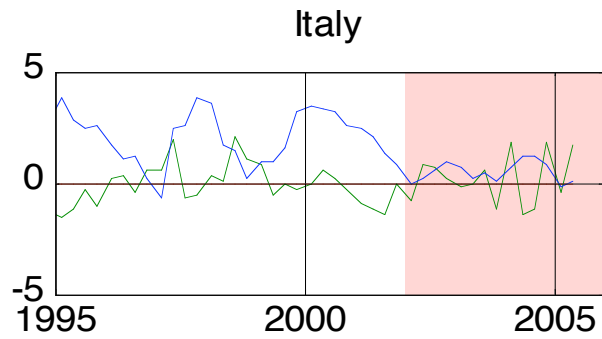
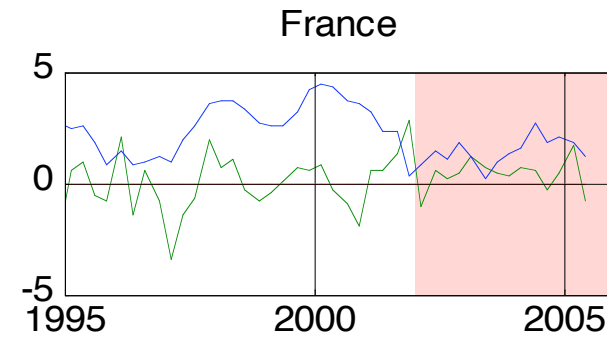
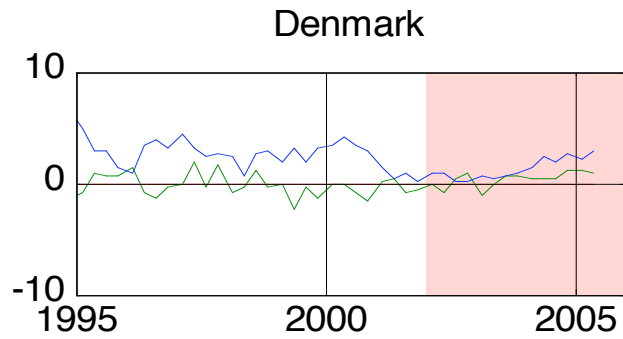
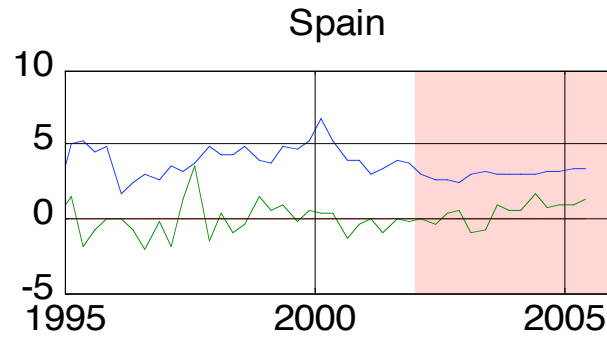
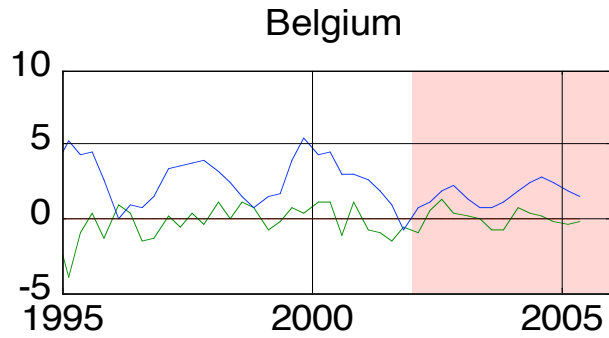
Estimate VAR models with

Consumption

Output

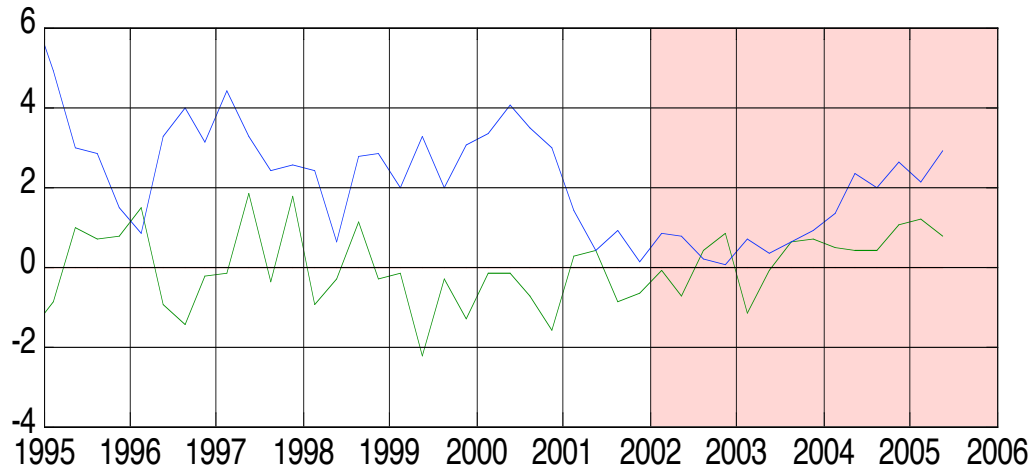
1980 to 2005

dlog(consumption)
dlog(consumption) shock in the VAR

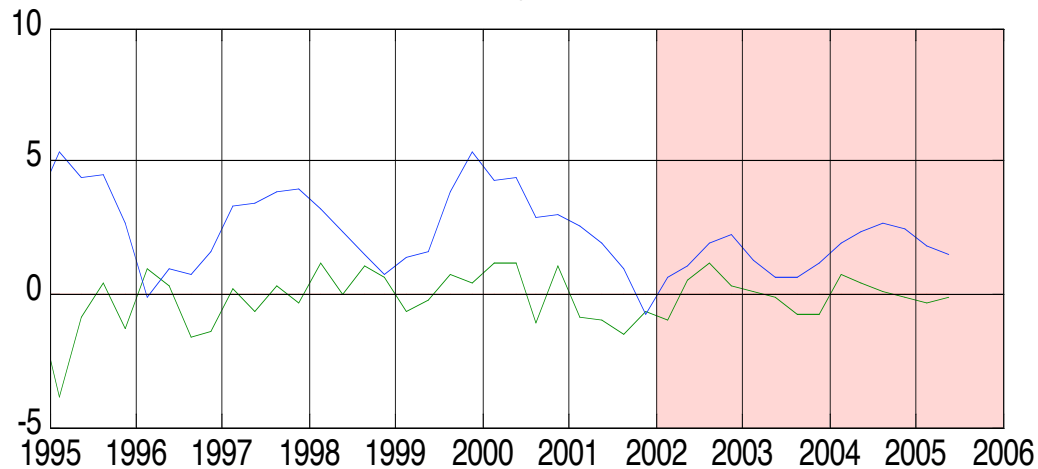


ZOOM

Denmark



Belgium



Results:

For countries in and out

- Slow down starts before the changeover
- No persistent negative consumption shock in 2002-2004



Issues

- No macro effects the inflation gap on wages nor on consumption
nor on Money demand (Angelini-Lippi)

Issue 1: Are Europeans rational homini-economici?

Issue 2: Accuracy and usefulness of this survey and more generally of “soft” data

Issue 1: Rationality/Cognitive limits

- Cesari- Del Giovane and Rossi-Arnaud survey

What was the price of cinema tickets in 2001?

Mean and mode answer on the pre-euro price of cinema tickets are 9000 and 7000 lira

Issue 1: Rationality/Cognitive limits

- Cesari- Del Giovane and Rossi-Arnaud survey

What was the price of cinema tickets in 2001?

Mean and mode answer on the pre-euro price of cinema tickets are 9000 and 7000 lira

Truth was 13000 lira

Issue 1: Rationality/Cognitive limits

- Giovane and Sabbatini

Perception of aggregate inflation influenced by

Most frequently purchased goods
(Potatoes/Ipod)

Highest increases print more easily in
memories

Media coverage (causality?)

Coincidence of changeover and slowdown
(causality?)



Issue 2: Usefulness of Surveys

- Several reasons why perceived inflation can differ from real inflation
- The survey help us understand important trends in the opinion (e.g. the anti euro sentiment- Del Giovane and Sabatini)
- However little macroeconomic impact and usefulness for forecasting and business cycle analysis