

The future of inflation targeting and the present at the Riksbank

Lars E.O. Svensson
Sveriges Riksbank

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Flexible inflation targeting

- Stabilize both inflation around target and resource utilization
- “Forecast targeting:” Choose an instrument-rate path such that the forecast of inflation and resource utilization “looks good”
- “Looks good:” Inflation goes to target and resource utilization goes to normal at an appropriate pace
- Publish and motivate instrument-rate path and forecast of inflation and real economy
- “Management of expectations” par excellence



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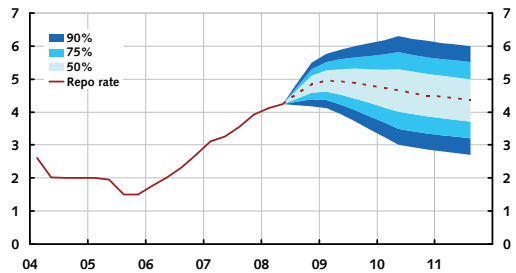
Publishing the repo-rate path

- Repo-rate path “integral part of the monetary policy stance,” necessary for inflation and output-gap forecast
- Policy discussion more about path than current repo rate
- Six-member committee can easily agree on path
- “Forecast, not commitment”
- Mean forecast with uncertainty intervals



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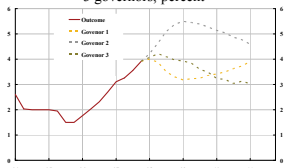
Repo rate with uncertainty bands, July 2008
Per cent



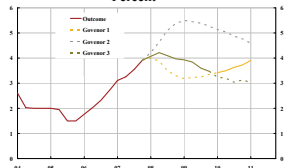
Source: The Riksbank

Deciding on a repo-rate path: Median path?

Individual repo-rate paths
3 governors, percent

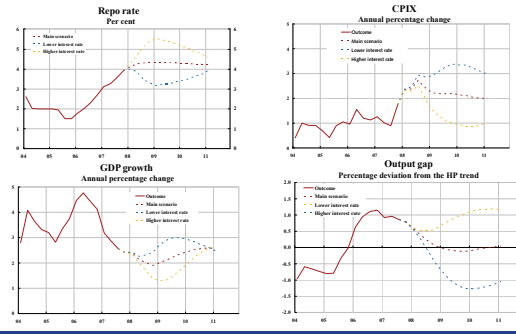


New repo-rate path
Percent



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Deciding on a repo-rate path: Just vote among a few alternatives



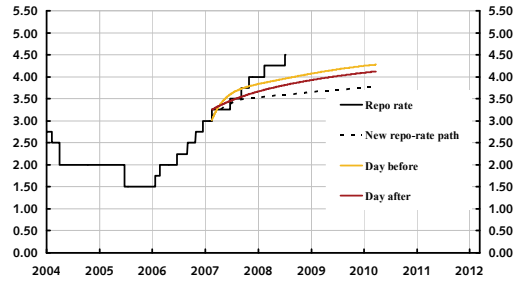
Management of interest-rate expectations

- Publish and motivate inflation, real-economy, and repo-rate forecast
- Compare repo-rate path and market forward rates before and after announcement



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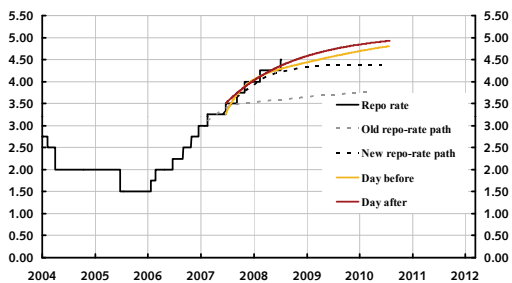
Repo-rate path and market forward rates February 2007



Note:

Source:

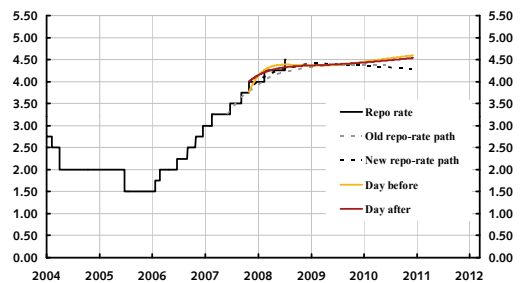
Repo-rate path and market forward rates June 2007



Note:

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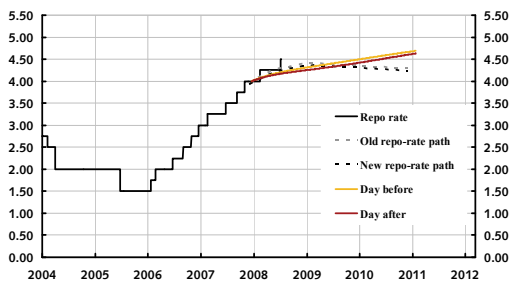
Repo-rate path and market forward rates October 2007



Note:

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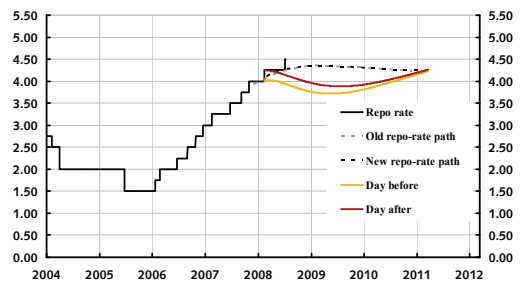
Repo-rate path and market forward rates December 2007



Note:

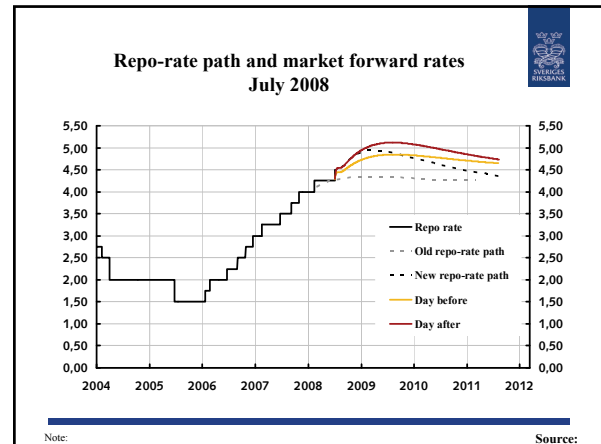
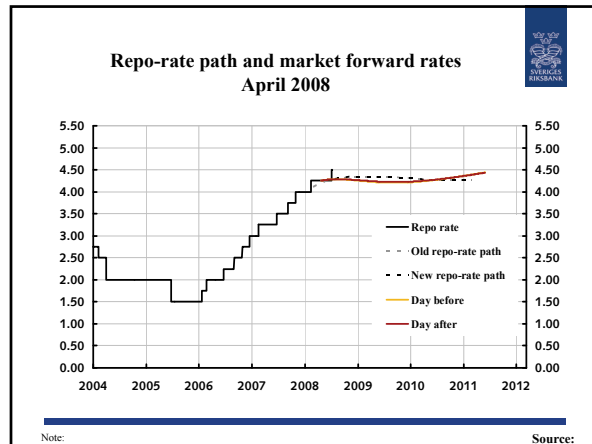
Source:

Repo-rate path and market forward rates February 2008



Note:

Source:



Decision process at the Riksbank

- 6-member Executive Board
- 6 policy decisions per year (3 reports, 3 updates)
- Interaction between staff and EB results in main and alternative combinations of forecasts of repo rate, inflation, and real economy
- At final policy meeting EB discusses and votes on decision and report/update
- Majority decision published day after policy decision
- Attributed minutes, including any dissenting views, published 2 weeks after policy decision

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Individualistic committee

- Individual accountability
- Members appointed by Parliamentary committee
- Regular hearings in Parliament, expert evaluation every 4th year (Giavazzi-Mishkin 2006)
- Attributed minutes, dissenting views
- No free riding/social loafing; better preparation
- Less free discussion?
- Less group-think?

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Individualistic committee: Cacophony problem?

- No:
- After decision, before minutes: Majority view
- After minutes: Individual members clarify their individual views and position at last decision
- No info about future decisions beyond published repo-rate path and Monetary Policy Report/Update
- Except some comments on new data relative to previous forecast and possible policy tradeoffs

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To be done: The near future

- Better measures of resource utilization, output gap, potential output
- Potential output, not HP: Flexprice, conditional or unconditional, relation to Pareto-efficient output
- Optimal policy, minimize quadratic loss function, commitment: Main and alternative repo-rate paths
- Alternative repo-rate paths: Simulate as anticipated, not unanticipated (not Leeper-Zha modest interventions)
- DSGE models w/ better financial sector, labor market

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To be done:**The not so near future**

- Price-level targeting

$$L_t = (p_t - p_t^*)^2 + \lambda(y_t - \bar{y}_t)^2$$

$$p_t^* = p_{t-1}^* + \pi^*$$

- Less long-run price-level uncertainty than inflation targeting
- If credible, inherent stabilization of inflation expectations:

$$p_t \uparrow \Rightarrow \pi_t^e \downarrow$$