

PUBLICATION FACTS

JOURNAL

OPEN ECONOMIES REVIEW

PUBLICATION DATE

2025

VOLUME/ISSUE

36 (1)

PAGES

1-23

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ABSTRACT

We investigate the time-series properties of the price level in advanced and emerging economies. We are motivated by the debate of whether central banks should accommodate past inflation shock under inflation targeting or reverse past inflation shock as with price-level targeting or average inflation targeting. We use time series data for G7 and E7 countries and examine the integration properties of their price level indices using alternative testing procedures. We find the price level dynamics in most countries are consistent with the "bygones are bygone" aspect of inflation targeting, a pattern consistent even in Canada, contrary to previous findings. Evidence of stationary price level is found only in Japan. For emerging countries, the deviation between the actual and implied prices based on the target rates is more extensive and continues to expand rapidly in some emerging markets.

Journal Citation
Indicator

0.38