Reading the inflation tea leaves
Gauging (dis)inflation pressures: Comparing tools and current findings
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Views expressed are the presenter’s and not necessarily those of the BIS.
A taxonomy of inflation indicators

<table>
<thead>
<tr>
<th></th>
<th>Timeliness</th>
<th>Diagnosis ability</th>
<th>Prognosis ability</th>
<th>Adaptability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Headline, core, trimmed readings</td>
<td>High</td>
<td>None</td>
<td>Often hard-to-beat benchmarks</td>
<td>May reflect regime shift</td>
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<tr>
<td>Granular measures (similarity, spillovers)</td>
<td>Typically high</td>
<td>Suggestive</td>
<td>Unknown</td>
<td>May signal turning points</td>
</tr>
<tr>
<td>Expectations: market-based</td>
<td>Very high</td>
<td>None</td>
<td>Good but beware of risk premia</td>
<td>Full distribution may predict a shift</td>
</tr>
<tr>
<td>Expectations: survey-based</td>
<td>Typically low</td>
<td>Some, esp. when anchor is weak</td>
<td>Good but beware of biases</td>
<td>Full distribution may predict a shift</td>
</tr>
<tr>
<td>Models: time series</td>
<td>Very high</td>
<td>Limited</td>
<td>Typically good</td>
<td>May be unstable in regime shifts</td>
</tr>
<tr>
<td>Models: (semi-) structural</td>
<td>Low</td>
<td>High</td>
<td>Varies</td>
<td>Low</td>
</tr>
</tbody>
</table>
Performance of mean-reverting models deteriorates when inflation picks up, usefulness of full-fledged model insights hinges on correct specification.

Source: BIS Bulletin no 60.
Current indicators give mixed signals on a transition to a high-inflation regime: Sectoral price changing becoming more similar and spillovers increasing...

Source: BIS Bulletin no 60.
...at the same, sensitivity of wages to past inflation only mildly higher while that of prices to past wage growth is stable

Source: BIS Bulletin no 60.
Evolution of forecast errors tells a story: expectations/models have finally caught up to actual readings but not at the same time for all countries

Source: Consensus Economics.
Key takeaways

- When inflation is low, sector-specific price changes explain most of it
  - Core a more accurate signal than headline
  - Little relation to price- and wage-setting decisions
- The opposite holds when inflation is high
  - Synchronicity across sectors become prominent
  - Price changes become more salient to firms and workers
- How useful different indicators are depend on the regime
  - Particularly unreliable during transitions
  - Signals of ongoing transition:
    - Drifting expectations,
    - Increase in sectoral co-movements and spillovers,
    - Rising pass-thru from wages to prices and vice versa
Based on work by numerous BIS colleagues, most notably, Fiorella De Fiore, Marco Lombardi, Dan Rees with support from Burcu Erik and Alexis Maurin

For more:
Inflation indicators amid high uncertainty
Inflation: a look under the hood