

## Strong goal independence and inflation targets

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### Abstract

Inflation targeting has become the monetary policy framework of the nineties. At the other extreme, several central banks have recently adopted key elements of the inflation targeter's toolkit, but at the same time they have made formal declarations that they are not inflation targeters. Such a position may appear surprising. It indirectly suggests that a reneging strategy is beneficial for some. The paper considers reasons why it may be advantageous for some central banks to distinguish themselves from the inflation-targeting strategy. Most importantly, we argue that explicit inflation targets can potentially undermine the goal independence of a central bank.

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### 1. Introduction

Inflation targeting has become the dominant framework for monetary policy in the nineties. The return to a 'nominal anchor with drift' represents a new way of thinking about the monetary objectives for many countries. The global acceptance of inflation targeting has come quickly after only a decade in practice. It is the declared policy of many central banks and has been actively promoted by international organizations such as the IMF and the OECD.

Despite its wide appeal, no universal definition exists. [Bermanke et al. \(1999\)](#) offer a broad interpretation. They characterize inflation targeting as 'constrained discretion', which combines some of the advantages traditionally ascribed to rules with those credited to discretion. A narrower

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Table 1

Toolkit approach to inflation targeting: goal independence and official inflation targeters

Central bank	Official inflation targeter	Inflation forecast published	Voting patterns published/minutes	Policy decisions discussed in publications
<i>Exchange rate floaters</i>				
Bank of England	Yes	Yes	Yes	Yes
Reserve Bank of New Zealand	Yes	Yes	No	Yes
Reserve Bank of Australia	Yes	No	No	Yes
Riksbank	Yes	Yes	Yes	Yes
Bank of Canada	Yes	Yes	No	Yes
Bank of Chile	Yes	No	No	Yes
Bank of Israel	Yes	No	No	Yes
Federal Reserve	No	Yes	Yes	Yes
ECB/Bundesbank	No	Yes	No	Yes
Bank of Japan	No	Yes	Yes	Yes
Swiss National Bank	No	Yes	No	Yes
<i>Exchange rate targeters</i>				
Norges Bank	No	Yes	No	Yes
Bank of Iceland	No	No	No	Yes
Danish National Bank	No	No	No	Yes

Notes: Information from Mahadeva and Sterne (2000).

interpretation advanced by Mishkin and Schmidt-Hebbel (2001) defines inflation targeting as a package of specific elements: an institutional commitment to price stability, absence of fiscal dominance, absence of other nominal anchors, policy instrument independence and policy transparency and accountability. Kuttner and Posen (1999) provide an operational definition in terms of an inflation target over a specific timeframe, an inflation report, and the ability to react to short-term economic shocks. The IMF (2005) defines inflation targeters simply as institutions that have a formal inflation target and publish their inflation forecasts.

Even among central banks, inflation targeting does not enjoy a universal interpretation. At the one extreme, many central banks have jumped on the inflation-targeting bandwagon by proclaiming adherence without the essentials. Table 1 provides a simple checklist of self-proclaimed inflation targeters. It also shows that a few do not publish inflation forecasts, the minimum requirement of an inflation targeter.<sup>1</sup>

At the other extreme, several central banks have recently adopted key elements of the inflation targeter's toolkit, but they also have made formal declarations that they are not inflation targeters. We call these central banks the *abstainers*. Such a declaration may appear surprising at first. It indirectly suggests that a renege strategy is advantageous for some central banks. While comparative studies by Almeida and Goodhart (1998), Corbo et al. (2000), Dueker and Fischer (1996, 2006), Groenevald et al. (1998), and Levin et al. (2004) do not find significant differences between inflation targeters and (successful) non-inflation targeters in terms of inflation and output performance; no empirical study claims there are benefits in abstaining from inflation targets.

<sup>1</sup> The Reserve Bank of Australia, the Bank of Chile and the Bank of Israel are examples. The Bank of Chile has recently begun to publish inflation forecasts after a decade of self-proclamation of being an inflation targeter.

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