

A New Test for the Success of Inflation Targeting

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Revised April, 2003

Abstract

We propose a new test, derived from a set of variance decompositions of a structural VAR, for the success of inflation targeting. In contrast to standard sacrifice ratios this test considers changes in the structure of real and nominal shocks; second moment effects. We find strong support for IT with 7 of the 9 countries in our sample having negative “sacrifices” and many countries with “benefits”. However, we also find very different performances across IT countries. We find that “IT success” depends on the size of the real shocks suffered but controlling for this there are differences in country performance.

JEL Categories: E42, E52

Keywords: Inflation targeting, Structural Vector Auto-Regression (VAR)

¹We are grateful to Ricardo Hausmann, Leonardo Leiderman, Klaus Schmidt Hebbel and Ted Truman for comments. Naturally all errors remain are own. Please address comments to Andrew Powell at apowell@utdt.edu