MONETARY AND CAPITAL MARKETS

Are Household Inflation Expectations De-Anchoring?

European Banking Institute

Tobias Adrian
Financial Counsellor and Director
Monetary and Capital Markets Department, IMF

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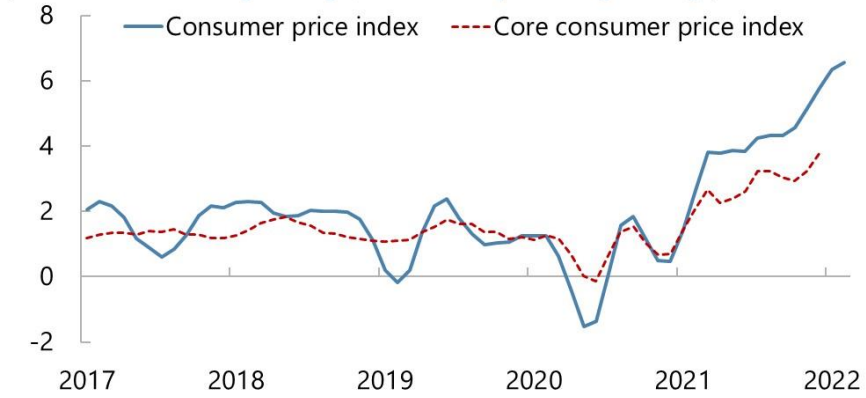
Inflation has risen globally on the heels of strong demand and persistent supply-chain disruptions

Inflation trends - AEs

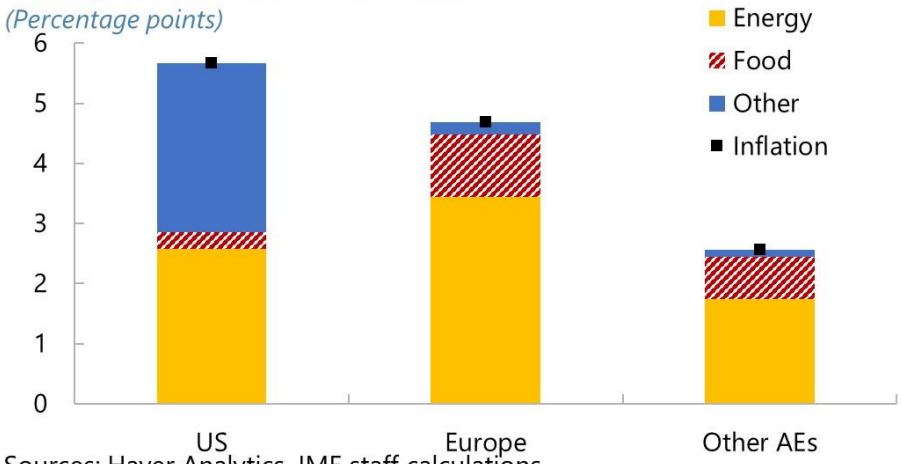
(Three-month moving average; annualized percentage change)



Sources: Haver Analytics, IMF staff calculations.

Changes in inflation drivers

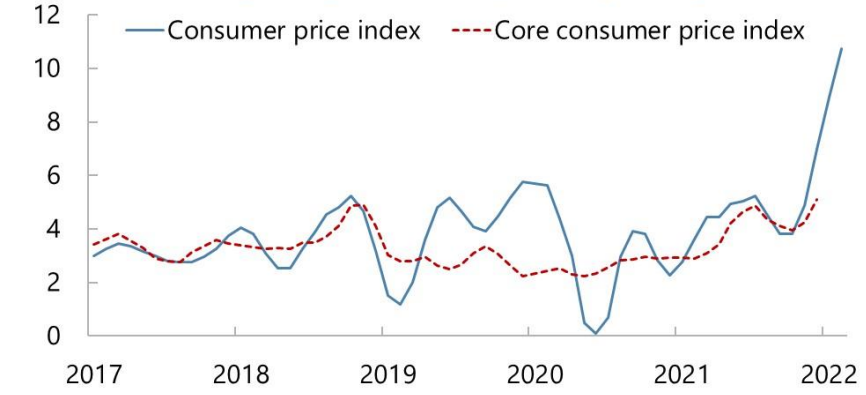
(Percentage points)



Sources: Haver Analytics, IMF staff calculations.

Inflation trends - EMDEs

(Three-month moving average; annualized percentage change)



Sources: Haver Analytics, IMF staff calculations.

Goods and services inflation

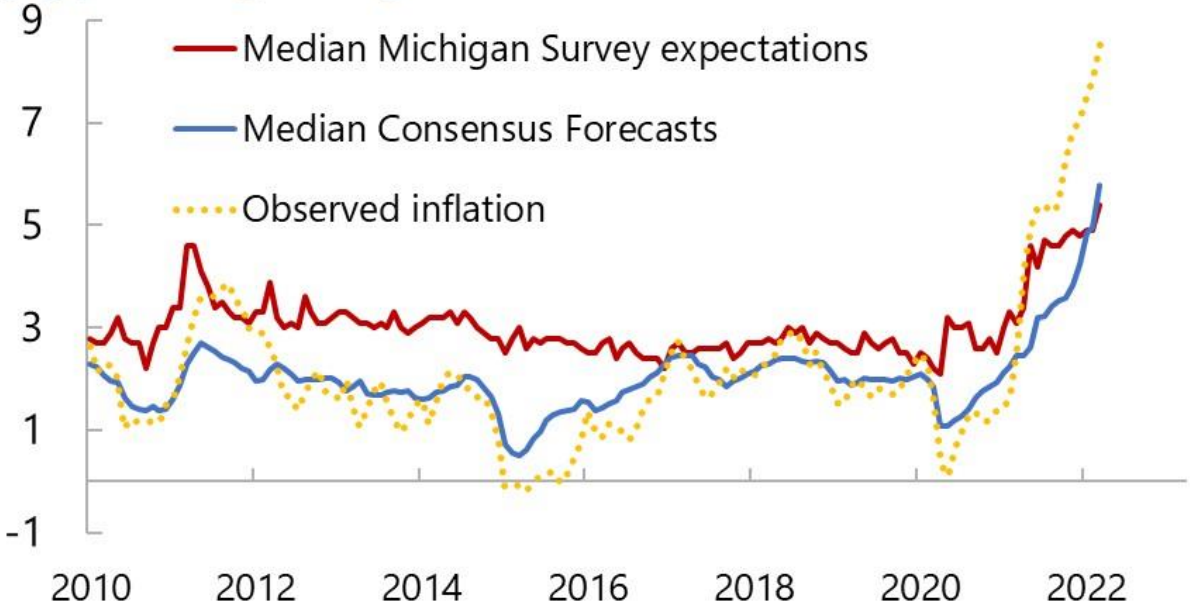
(Deviation from pre-COVID-19 averages, percent)

Sources: Haver Analytics, IMF staff calculations.

Even if shocks are “temporary,” they could have persistent effects if they de-anchor inflation expectations

US: 1-year ahead inflation expectations

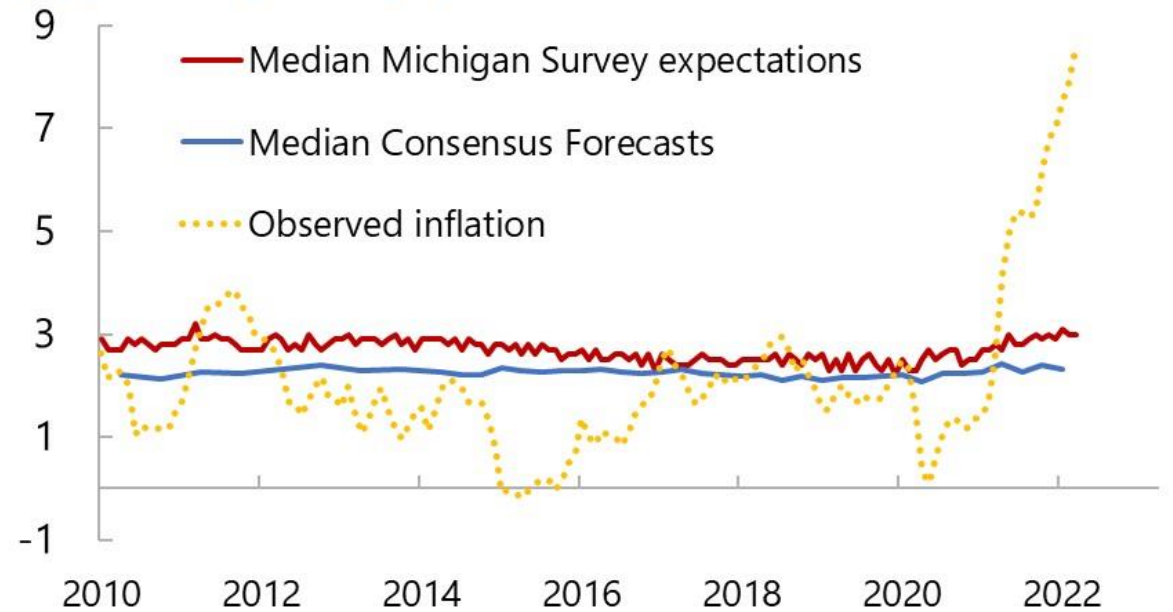
(yoy percentage changes)



Sources: US Bureau of Labor Statistics, Survey of Consumers - University of Michigan, Consensus Forecasts.

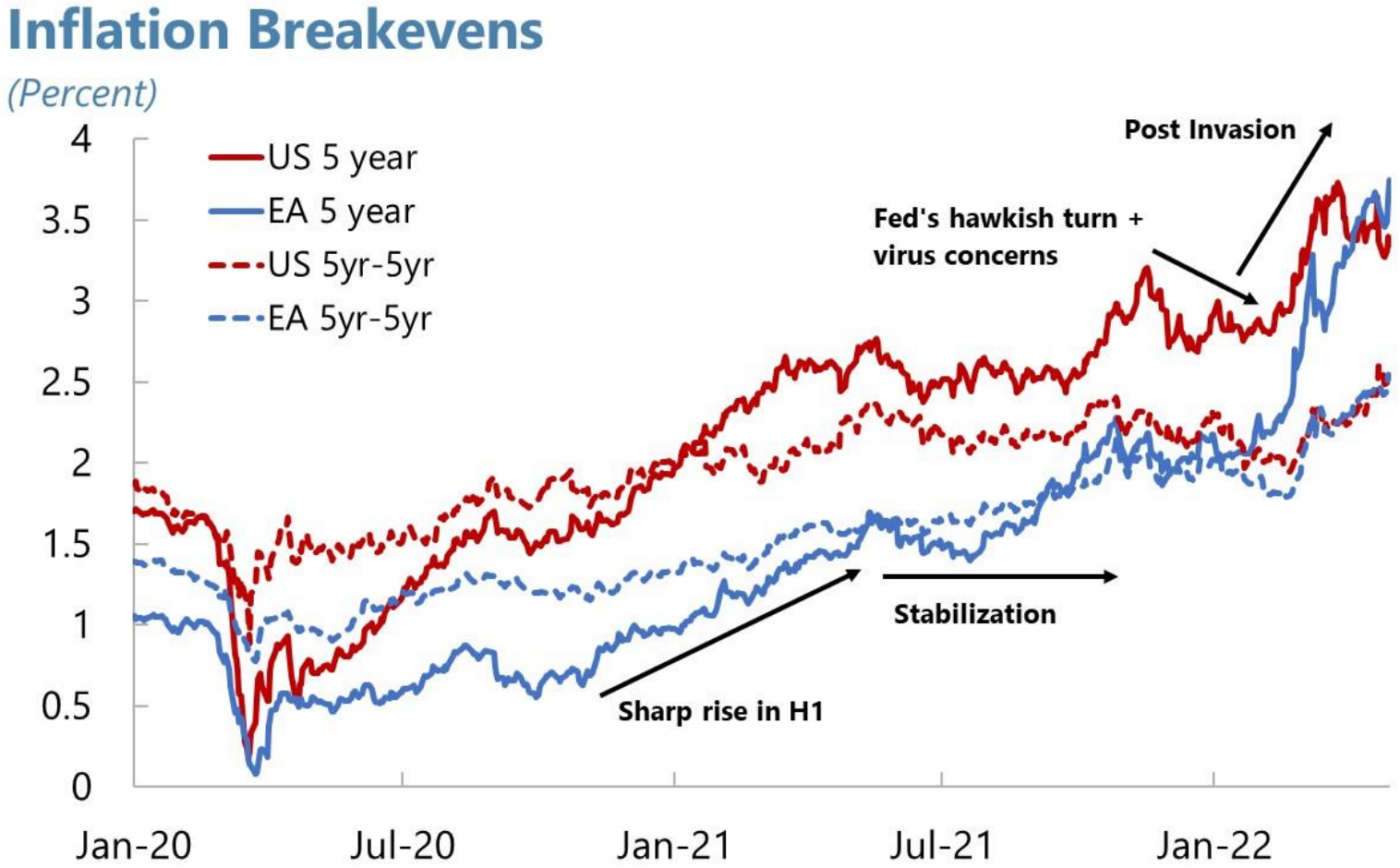
US: 5-year ahead inflation expectations

(yoy percentage change)



Sources: US Bureau of Labor Statistics, Survey of Consumers - University of Michigan, Consensus Forecasts.

Shifts in longer-term expectations are also (and more) evident in market-based measures



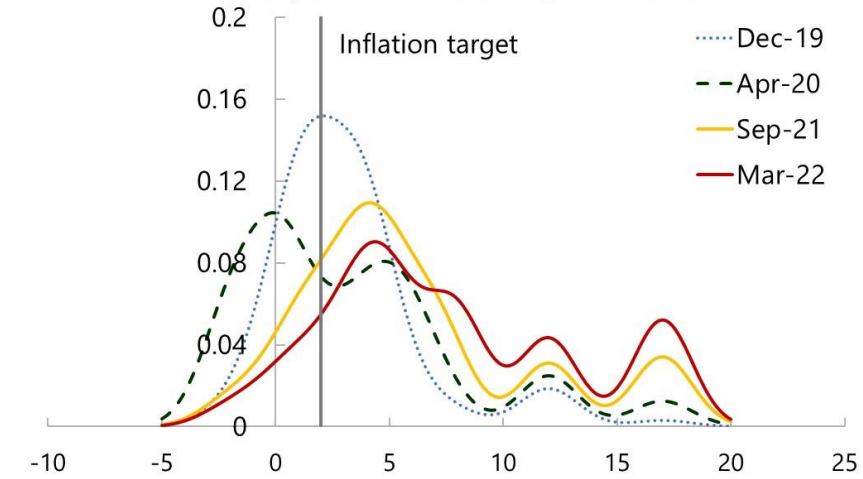
Sources: Bloomberg and IMF staff calculations.

Inflation expectations of households are less often discussed, but may be important

- Financial-market and professional inflation expectations are often cited, while household expectations receive less attention
- Household inflation expectations matter for consumption, saving, financing, and home-ownership decisions, and may impact wage negotiations and labor supply (D'Acunto et al., 2022; Andrade et al., 2020; Duca-Radu et al., 2021)
- Household expectations are closer to firm expectations (especially SMEs), which inform investment, hiring, and price-setting decisions (Gorodnichenko & Coibion, 2018)
- While *median* household expectations tend to have less predictive power than other expectations measures, changes in their distribution can provide important signals (Chang & Gomez-Rodriguez, 2022; Meeks & Monti, 2019; Reis, 2021; Verbrugge & Zaman, 2021)

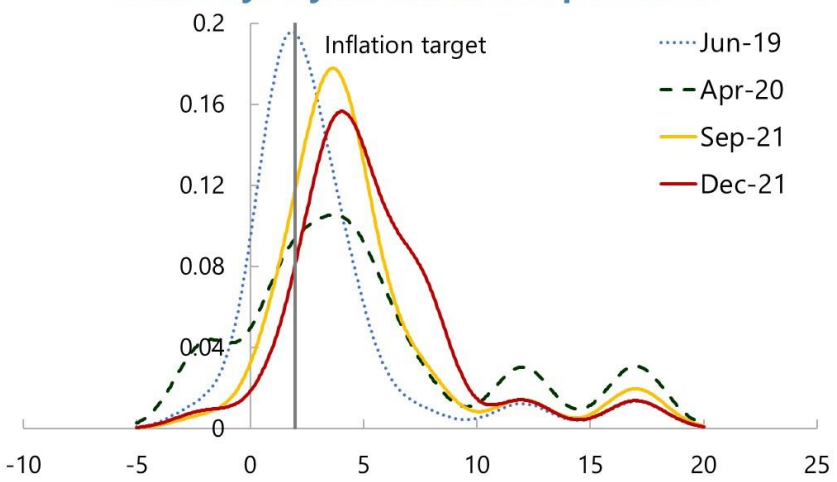
The distribution of near-term inflation expectations has shifted right in a sample of four advanced economies

US: 1-year inflation expectations



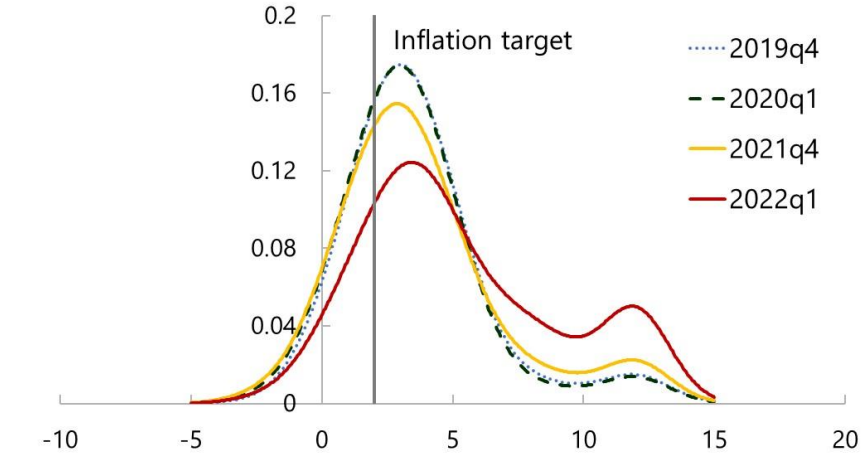
Sources: Survey of Consumers - University of Michigan, IMF staff calculations.

Germany: 1-year inflation expectations



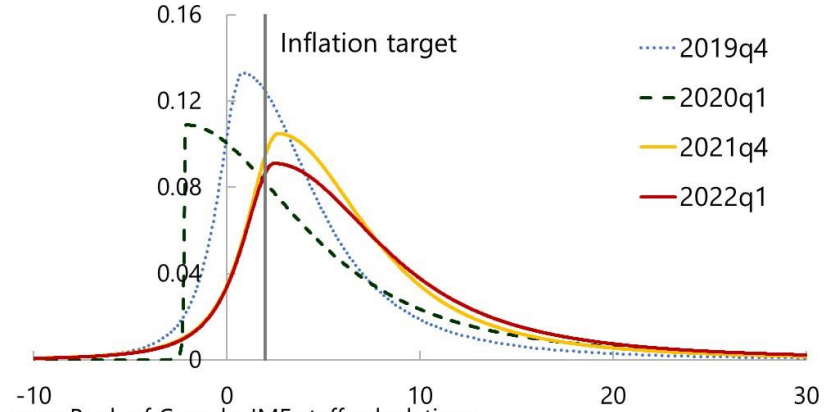
Sources: Bundesbank Online Panel – Households (BOP-HH), IMF staff calculations.

UK: 1-year inflation expectations



Sources: Bank of England, IMF staff calculations.

Canada: 1-year inflation expectations



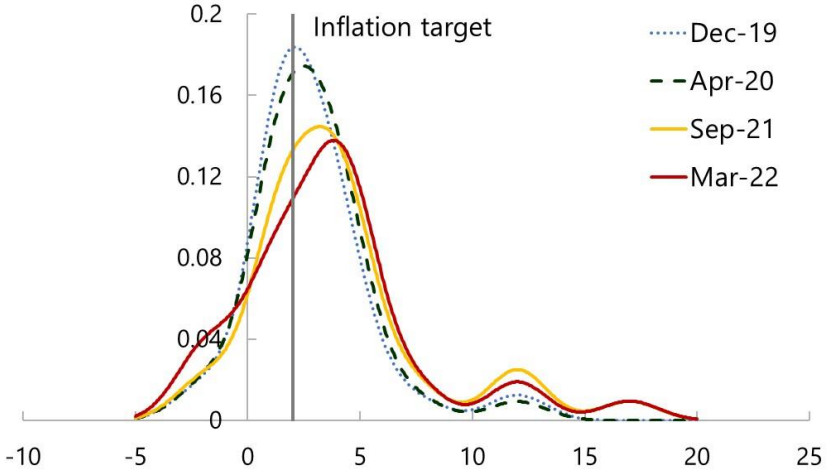
Sources: Bank of Canada, IMF staff calculations.

Note: This chart was constructed by fitting a skewed t distribution to percentiles of point forecasts, unlike the other charts which fit a kernel density.

For medium-term expectations, the picture is more mixed

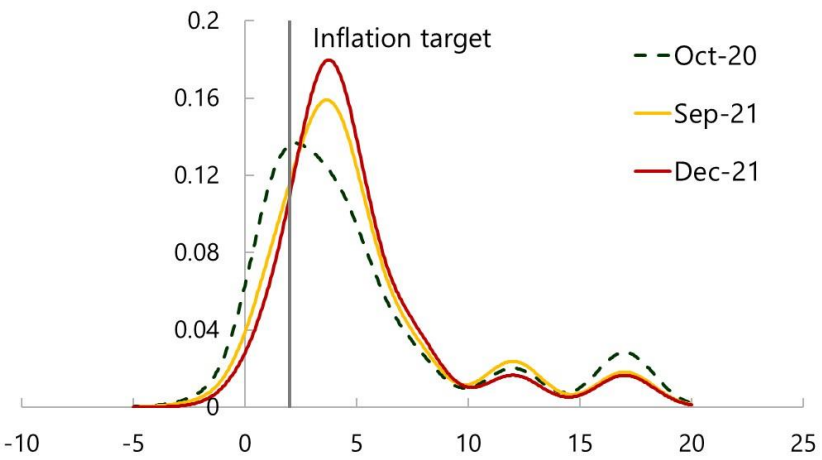
At the 5-year horizon, expectations seem well-anchored in Canada, but less so in the US and UK

US: 5-year inflation expectations



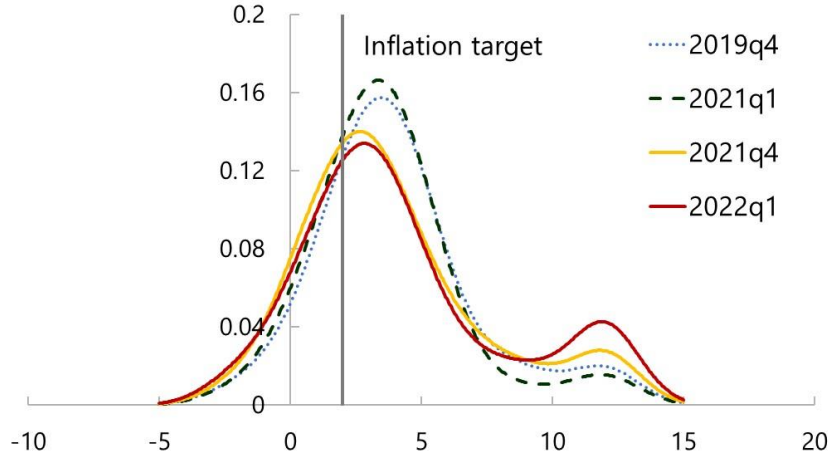
Sources: Survey of Consumers - University of Michigan, IMF staff calculations.

Germany: 5-year inflation expectations



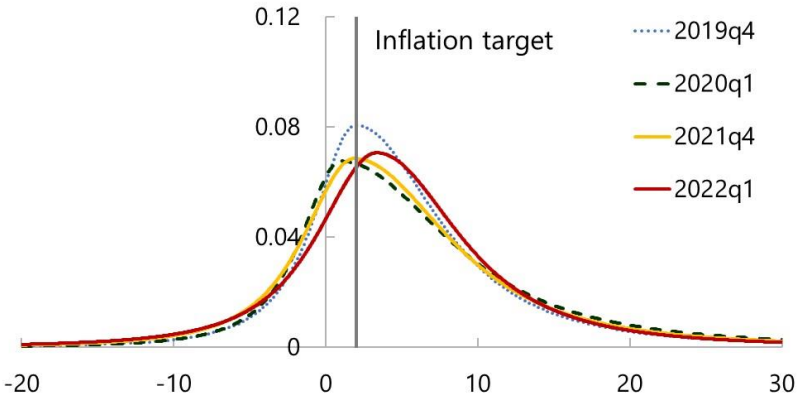
Sources: Bundesbank Online Panel – Households (BOP-HH), IMF staff calculations.

UK: 5-year inflation expectations



Sources: Bank of England, IMF staff calculations.

Canada: 5-year inflation expectations



Sources: Bank of Canada, IMF staff calculations.

Note: This chart was constructed by fitting a skewed t distribution to percentiles of point forecasts, unlike the other charts which fit a kernel density.

Near-term expectations contain important information about future inflation and anchoring of longer-term expectations

- New work finds that distributional changes (shifts in median, variance, skewness, and kurtosis) in US household near-term expectations contain information about future inflation
- Even after controlling for market-based professional forecasts, households' inflation expectations add value
- Higher disagreement among households on near-term inflation also predicts increases in future longer-term expectations

	Headline CPI inflation in t+12		Median 5-year-ahead exp. (MS) in t+24
	I	II	III
Constant	***	***	***
Inflation	***	**	***
Median MS	***	***	***
Variance MS	*	***	***
Skewness MS	*	*	*
Kurtosis MS	**	***	-
Market-based		-	
Median CF		***	
Variance CF		-	
Skewness CF		-	
Kurtosis CF		-	

Notes: The time period is 1989m10-2022m2. *** = significant at 0.01 level, ** = significant at 0.05 level, * = significant at 0.1 level.

Sources: Survey of Consumers - University of Michigan (MS), Consensus Forecasts (CF), Cleveland Fed (market-based expectations).

Key takeaways

- Distributions of household inflation expectations contain important information about future inflation and potential de-anchoring of longer-term expectations
  - Useful complement to market-implied inflation measures and expectations of professional forecasters
- Since the pandemic, near-term household expectations have shifted right in all four advanced economies studied, while changes in longer-term expectations vary
- Recent shifts in 5-year expectations in the US and the UK are a source for concern
- Advanced-economy central banks should keep a close eye on these shifts in expectations and take decisive action to rein in inflation