Volume Title: The Great Inflation: The Rebirth of Modern Central Banking

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Volume Publisher: University of Chicago Press

Volume ISBN: 0-226-006695-9, 978-0-226-06695-0 (cloth)

Volume URL: http://www.nber.org/books/bord08-1

Conference Date: September 25-27, 2008

Publication Date: June 2013

Chapter Title: Panel session I Discussion

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Chapter URL: http://www.nber.org/chapters/c12703

Chapter pages in book: (p. 57 - 58)

Panel Session I Discussion

Michael Bordo questioned Crow on the backlash that ensued due to the policy tightening during his tenure, given the political noise that followed. Crow pointed out that his predecessor was wildly unpopular through 1972 and 1987, and he took a different approach to policymaking by making speeches about the role of monetary policy, most notably his speech in Alberta that came to be known as the Edmonton Manifesto. The minister of finance was sympathetic to Crow, and the opposition was opposed to his policies without having any clear picture of what it wanted to do. While he could have stayed longer at the Bank of Canada, Crow decided to leave given the insistence that the government was placing on him to change the inflation target, as well as the bank's mandate. In the end, Crow fundamentally believed that price stability should be a central role, not the central role.

Lars Svensson inquired about Crow's opinion on the exact number for the inflation target, as well as his views on price-level targeting. Crow felt that an inflation target of zero was better than one, yet had no real grasp on the exact number it should be. When the inflation targets were put into effect, the Bank of Canada was targeting a level of two, and then would reexamine the situation once they reached that level. Admittedly, an inflation target of two now seems to have a lot of acceptance and an iconic status in Canada as a decent number, and it is pleasing to know that the bank is reexamining the target now. In terms of price-level targeting, Crow had very little opinion other than selling it the way it was sold in Japan, in the sense that you should give inflation when you need it. But in the end, Crow felt that Canada, as a medium-sized open economy with a floating exchange rate, has to be tough on inflation.

Edward Nelson began the questions to Donald Brash, wanting more detail on the influence of the New Zealand experience on Australia. Brash described how the governor of the Reserve Bank of Australia in the 1990s was negative about inflation targeting, yet his successor was quite keen on it. There was a bit of trading going on between the two countries; Australia adopted the inflation target, while New Zealand adopted the interest rate instrument of the cash rate. Australia's framework was similar, except that interest rate decisions were made by a board rather than by the government. Brash also commented that he benefitted a lot from interactions with Crow and the Bank of Canada. Crow interjected that the Reserve Bank of Australia jokingly got inflation down without even knowing it in the 1990s, mostly due to the influence of inflation-targeting practices.

Allan Meltzer asked about the bank's reaction to onetime price shocks, pointing out that Milton Friedman always stressed how inflation is always and everywhere a monetary phenomenon. But Friedman also understood that if you have excise tax increases, onetime devaluations, oil price shocks, and so forth, then it is not inflation, but relative price changes that matter.

Brash was quick to clarify that the policy agreements of the Reserve Bank of New Zealand stressed that price level shocks that are totally exogenous are not included in the definition of the central bank's target. He cited the example of the introduction of 10 percent value added tax, which tacked on approximately 8.9 percent to the Consumer Price Index. This is something that the bank did not try to offset. In terms of exchange rate movements, the bank was less clear. Thus, if the shock is totally exogenous, do not react. If there is some sort of pass-through into the economy, then the bank should look into it more. Meltzer worried that explaining this to the public was difficult. Brash agreed, and added that by and large the public understood. But he remembered that in the early 1990s, the minister of finance was proposing amending the mandate of the bank, but there was fear that it would be thrown out. The bank had instituted a forward track policy, with which they predicted a path for inflation and set a target band for inflation in the future. Alan Blinder wondered whether there were arguments against these forward tracks, and Brash stressed that if the bank was projecting an inflation rate far outside the target under the current policy, then this was not sensible policy and it would not be allowed to happen voluntarily. When inflation was being predicted, they needed to simultaneously predict what path of interest rates would deliver that path of inflation. Blinder clarified by specifying that the rationale for it was then to explain the inflation path and how to get it back on track.

Benjamin Friedman expressed wonderment about how the empirical literature that studies industrialized countries has not found a difference across countries in terms of macroeconomic performance when comparing inflation-targeting versus non-inflation-targeting monetary policy regimes. Brash did not seem surprised, and claimed that inflation targeting is not magic. It is an effort to be more explicit to the public about what the central bank is doing. Regardless of being an inflation-targeting central bank, if your objective is to keep inflation under control, then your reaction function might look similar to that of a central bank that explicitly has an inflation target. Friedman continued by asking whether it would matter if one said that the objective was to simultaneously keep inflation low and to achieve maximal sustainable employment. Brash concluded by referring to a former governor of the Reserve Bank of Australia, who emphasized that he interpreted his inflation target as achieving the maximal possible growth rate of Australia along with stable prices.