

Does Inflation Targeting Decrease Exchange Rate Pass-through in Emerging Countries?

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In this paper, we empirically examine the effect of inflation targeting on the exchange rate pass-through to prices in emerging countries. We use a panel VAR that allows us to use the larger data set on twenty-seven emerging countries (fifteen inflation targeters and twelve inflation nontargeters). Our evidence suggests that inflation targeting in emerging countries has helped to reduce the pass-through to various price indexes (import prices, producer prices and consumer prices) from a higher level to a new level that is significantly different from zero. The variance decomposition shows that the contribution of exchange rate shocks to prices fluctuations is more important in emerging targeters compared to nontargeters, and the contribution of exchange rate shocks to price fluctuations in emerging targeters declines after adopting inflation targeting.