

Policy Forum on
**Challenges for Monetary Policy
Amidst Changing Inflation Dynamics**

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Discussion by
Pongsak Luangaram
Chulalongkorn University

1. Rethinking the Drivers of Thai Inflation: Endogenous Policy Outcome?

- **BOT's key message:** Inflation in Thailand is largely supply-driven; demand factors play little role.
- **Alternative view:** Could this result be partly endogenous to policy?
 - Empirical evidence: Under inflation targeting, the BOT systematically responds to deviations from inflation target, (Nookhwun and Waiyawatjakorn, 2023).
 - The fact that core inflation has persistently undershot headline may reflect that systematic policy responses have effectively contained demand pressures — which could be viewed as a strength — but also makes it harder to disentangle the true role of demand in inflation dynamics.
- **Implication:** What appears as “supply dominance” may not just reflect structural features of the Thai economy, but also the outcome of the policy framework itself.
- **Discussion point:** This raises an important question — are we diagnosing the drivers of inflation, or the consequences of our own policy stance?
 - Bergholt et al. (2024) observed "disconnect" between inflation and economic activity is not due to a flattening of the Phillips curve but rather to the Federal Reserve's stronger commitment to its inflation target over time, which primarily affects the slope of the aggregate demand curve and alters the relative importance of demand versus supply shocks.

Another Alternative Explanation: The Cost Channel of Monetary Policy

- Beaudry et al. (2024): The stance of policy itself could strongly affect observed inflation dynamics.

$$\pi_t = \beta E_t \pi_{t+1} + \kappa mc_t + \mu_t,$$

$$mc_t = \gamma_y y_t + \gamma_r (i_t - E_t \pi_{t+1}),$$

$$y_t = \alpha_y E_t y_{t+1} - \alpha_r (i_t - E_t \pi_{t+1}) + d_t.$$

- Reduced-form PC estimation (with appropriate identification strategies):

$$\pi_t = \beta \pi_{t+1}^e + \gamma_y x_t + \gamma_r (i_t - \pi_{t+1}^e) + \mu_t,$$

- Albertazzi et al. (2025) for Euro zone; Nie et al. (2025) for China
- **Way forward:** This kind of specifications on Thai data could help us assess whether monetary policy has contributed to the observed inflation dynamics, including the persistent weakness of the demand-driven component.

2. Measuring Underlying Inflation: Improving Signal Extraction

- **Challenge:** Underlying inflation is unobservable + conventional indicators (core inflation) are subject to various measurement problems.
- **Two broad categories:**
 - Exclusion-based (Core, Trimmed mean, Sticky CPI).
 - Model-based (MUCSVO, Manopimoke and Limjaroenrat, 2017; Supercore; Structural models).
- **International practice:**
 - Fed (Almuzara and Sbordone, 2024): Trimmed Mean PCE, Median PCE, Supply vs Demand Decomposition.
 - ECB (Banbura and Bobeica, 2020) : PCCI (Persistent & Common Component), LIMI (Low Import Intensity).
- **Academic insights:**
 - Shapiro (2024): Demand vs Supply decomposition.
 - Rubbo (2023, 2024): Divine Coincidence Index (weighting sectoral sales shares and price adjustment frequencies) which does not depend on relative price changes.
- **Way forward:** Monitoring a range of indicators reduces the risk of relying on any single, biased measure and the increasing use of disaggregated data (Apaitan et al. 2020; Nookhwun and Manopimoke, 2023).

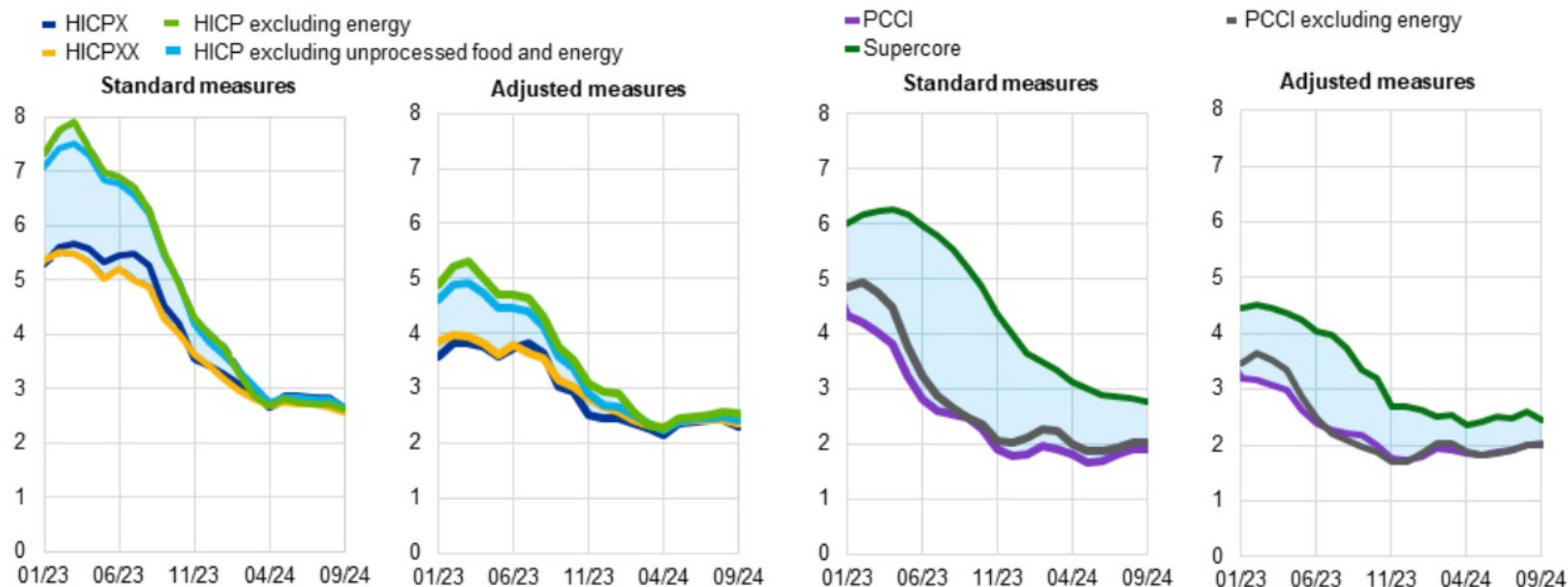
ECB example: The Importance of Monitoring Underlying Inflation

Euro area underlying inflation measures and their adjusted counterpart

(annual percentage changes)

Exclusion-based measures

Model-based measures

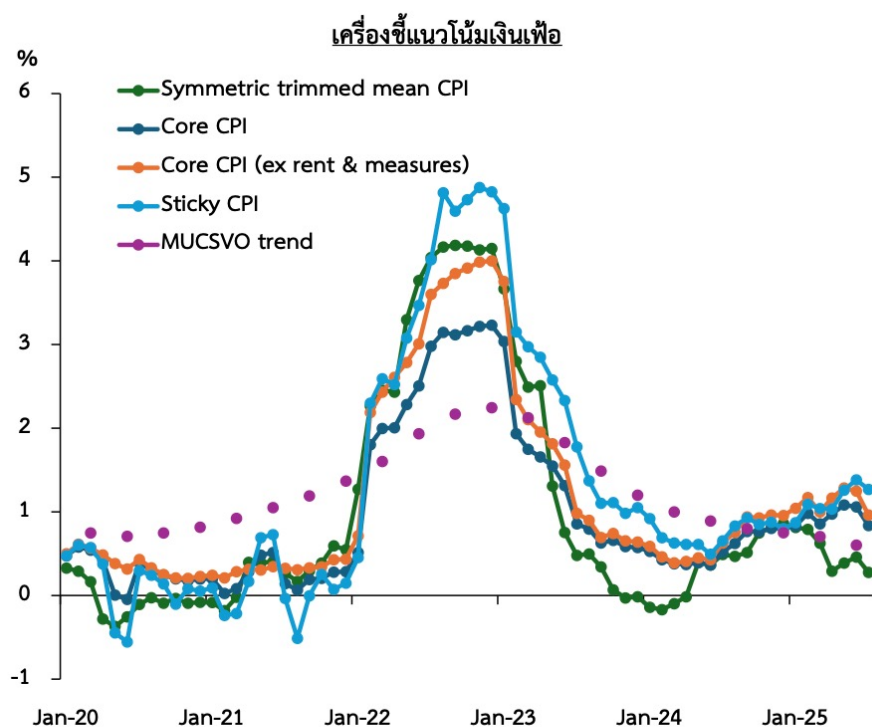


Source: Philip Lane (2024), Underlying inflation: An Update.

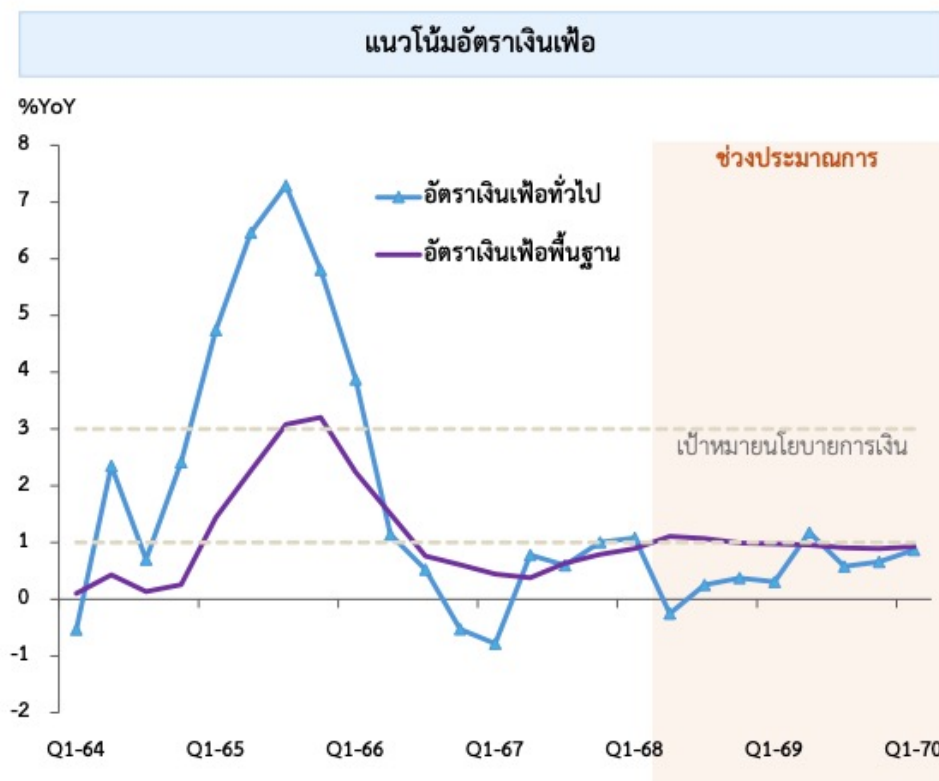
3. Monetary Policy Challenges: Operating within a Low-Inflation Regime

- **BOT's key message:** When 'relative price changes' dominate, policy should not respond.
- **Academic insights:**
 - BIS (2022) and Borio et al. (2023): Two regimes of inflation
 - Key challenge for central banks is to (1) ensure that relative price changes do not translate into entrenched inflation (2) avoid transitions from low- to high-inflation regimes in the first place → Targeting common component and identifying warning indicators
 - Rubbo (2023): Multi-sector economies with input-output linkages → consumer price targeting is suboptimal.
 - Monetary policy has considerably limited power to influence relative prices across multiple sectors → the model's policy implication is to prioritize stabilizing the output gap as closely as possible, even while tolerating some unavoidable relative price distortions.
- **Monetary Policy Strategy: ECB's Two-Step Approach** (Philip Lane, 2023)
 - “The assessment of underlying inflation should be viewed as a complementary cross-check”
 - Step 1: Forecast/scenario provide baseline narrative.
 - Step 2: Cross-check with underlying inflation (wages, expectations).
 - If aligned → confidence reinforced; if divergent → decisive policy action required.
- **Way forward:** An adaptive two-step approach: forecast → cross-check → adjust. Tolerate temporary shocks but pivot decisively if expectations risk de-anchoring.

Measures of Underlying Inflation VS Inflation Forecast in Thailand



หมายเหตุ: ค่าตัวเลข %YoY ของเครื่องชี้เป็นรายเดือน ยกเว้น MUCSVO ที่เป็นรายไตรมาส
 Symmetric trimmed mean คำนวณโดยตัดสินค้าและบริการที่ราคาเปลี่ยนแปลงมากที่สุด 10% และน้อยที่สุด 10% ของน้ำหนัก
 ในตะกร้า CPI / Sticky CPI คำนวณจากสินค้าและบริการที่มีความหนืดในการปรับราคามากกว่าค่าเฉลี่ยของตะกร้าที่ 4.8 เดือนต่อ
 ครั้ง อ้างอิงจาก Bryan and Meyer (2010) / MUCSVO trend คำนวณโดยอ้างอิงจาก Stock and Watson (2015)
 ที่มา: กระทรวงพาณิชย์ คำนวณโดย ธปท.



ที่มา: กระทรวงพาณิชย์ และประมาณการโดย ธปท.

Source: Bank of Thailand

4. Framework Credibility Problem: The Case for a Review

- **Challenge:** Persistent undershooting risks eroding credibility.
- **International practice:** Reviews have become an institutional norm; not reviewing risks frameworks drifting out of sync with structural changes.
 - Framework reviews are conducted at roughly five-year intervals for four central banks (BOC, ECB, RBNZ, and Riksbank)
 - Central bank reviews (Fry-McKibbin et al. 2025) serve dual purpose: (1) to foster institutional evaluation and (2) enhance public accountability of central bank actions.
- **Way forward:** Institutionalize *periodic* framework reviews (e.g. every 5 years) to:
 - Re-assess the appropriate level of inflation target.
 - Decide on a suite of underlying inflation indicators to formally guide policy.
 - Strengthen transparency via expert and public engagement.

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