

Inflation, Business Cycle, and Monetary Policy:

The Role of Inflationary Pressure

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Abstract

A novel empirical framework is proposed to analyze the causal relationships among future inflation, the business cycle, and monetary policy. It measures inflationary pressures as anticipated shocks to future inflation caused by changes in some predictors of inflation in the structural vector autoregressive model. Empirical results reveal that identified inflationary pressures represent demand-pull factors in inflation dynamics and act as driving forces for stochastic changes in trend inflation. Furthermore, the economic significance of inflationary pressures hinges on the systematic monetary policy responses to them. The results indicate that proactive policy reactions to inflation forecasts are crucial for achieving macroeconomic stability.

JEL Classification: C32; E31; E32; E52; E58.

Keywords: Inflationary pressure; Business cycle; Monetary policy; Vector autoregressive model; Anticipated shock.