Do the perceptions of exchange rates matter? The exchange rate impact on the import and consumer prices in Japan

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Abstract

We estimate the responses of the core consumer price index to external factor shocks and upper-stage price shocks in Japan between January 1985 and March 2025 using the local projection approach. The estimated results indicate that the pass-throughs from the exchange rate to import prices and from producer prices to consumer prices are substantial. The responses of import and consumer prices to exchange rate changes may vary depending on how firms and consumers perceive the current exchange rate. We propose estimating a threshold local projection model using the perceived exchange rate (PER) index as the threshold variable. Further, by breaking producer prices into intermediate stages, we found weak evidence that the perception of depreciation helps pass through more of an increase in producer prices to consumer prices.

Keywords: Cascade indirect effect, Distributional structure, Exchange rate pass-through.

JEL Classification codes: E31 (foreign exchange); F31 (price level); F41 (open economy macroeconomics)

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