



MONETARY POLICY DEPARTMENT

Methodology note on inflation expectations

The purpose of the assessment of inflation expectations

Inflation expectations are an important indicator for central bank as they affect the economic agents' decisions on consumption and investments. The growth or the decline of consumption and investments are reflected in a change of aggregate demand, which in turn shapes inflation pressures. Inflation expectations are of particular interest for central banks that have adopted the inflation targeting framework, which in itself is a forward looking regime. They serve also as an indicator of public confidence in central banks to achieve inflation target and maintain price stability in the medium term horizon. If economic agents believe that the central bank will react in order for inflation to converge to the target, their inflation expectations would be anchored around this target. Against this backdrop, setting the prices and wages would tend to be in line with the inflation target, resulting therefore in a process that is little dictated by short-term volatilities of the current inflation rates. Conversely, when inflation expectations are not in line with the inflation target, achieving price stability becomes a more difficult task. Hence, the scope for assessing inflation expectations should be expanded not only in terms of bolstering trust and confidence, but also in terms of including it in modelling processes and medium-term inflation forecasting.

Inflation expectations cannot be computed directly. Unlike the actual inflation, inflation expectations are part of those variables that cannot be measured or captured directly from official statistics. As such, expectations are assessed using indirect methods. The most widely used method is the collection of data through surveys with economic and financial agents.



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Assessment of inflation expectations in the case of Albania

In the case of Albania, inflation expectations are assessed by the Bank of Albania, on account of data collected through the business and consumer surveys in the context of Confidence Surveys¹ and through Financial Agents survey². We obtain both qualitative and quantitative assessments from the Confidence Surveys and only quantitative assessments in the case of Financial Agents Survey. Inflation expectations are assessed for various time horizons, extending beyond the moment the survey takes place, and at various frequencies.

Businesses and consumers are asked for their respective inflation expectations one year ahead. In other words, through Confidence Surveys we collect information on inflation expectations for a short-term horizon. In the case of Financial Agents Survey, one of the sections of the surveys requires that respondents give their expected inflation 1, 2 and 3 years ahead, hence covering a timeframe from short-term to medium-term horizon. This survey is conducted monthly.

The information collected through the surveys is processed and aggregated to produce an average level of inflation expectations from each of the surveyed groups. Inflation expectations' graphic layout and analyses are presented in monetary policy reports and research work at the Bank of Albania.

Quantitative inflation expectations of consumers have started to be collected in 2005, those of businesses in 2009, and those of financial agents in 2008. Over the years, the methodologies for the assessment of inflation expectations through surveys have been subject to improvement and will continue to be aligned with the best international practices. For any eventual change in the surveys, an explanation note will be posted. The relevant questions to assess the inflation expectations from three groups: business, consumers, and financial agents, are found in the respective time series data posted under "Inflation Expectations".

¹ For more information on Confidence Surveys, read the Businesses and Consumer Confidence Survey https://www.bankofalbania.org/Monetary_Policy/Surveys_11282/Business_and_consumers_survey/

² The survey is conducted with banks and non-bank financial institutions.