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Reflections on Operating Inflation Targeting

In a paper delivered today at the Graduate School of Business of the University of Chicago, Paul Tucker – Executive Director, Markets and a member of the Monetary Policy Committee (MPC) – sets out some reflections on the operation of an inflation targeting regime after four years on the MPC.

Two key threads about inflation targeting and the challenges facing policymakers run through his comments: the need to anchor medium-to-long term inflation expectations and the importance of straightforward communications about policy objectives and the conduct of policy.

On inflation expectations, Paul Tucker notes that "...maintaining real aggregate demand in line with supply is not a sufficient condition for achieving an inflation target". Whether or not medium-to-long term inflation expectations are well anchored on the inflation target is the 'best test' of whether the MPC has made any big mistakes. He says central banks need to convey that they are ready to do whatever is necessary to maintain well-anchored inflation expectations. Credibility "is not to be taken for granted".

On communications, he stresses that as policymakers "we should not kid ourselves that households and firms are studying our every utterance or examining in detail the economy in which they live and work. That points, I think, to keeping things as straightforward as possible, without glossing over uncertainties and risks".

Key Resources

Reflections on Operating Inflation Targeting - Full paper

<http://webarchive.nationalarchives.gov.uk/20100114080129/http://www.bankofengland.co.uk/publications/speeches/2006/speech274.pdf>