Second evaluation of the quantitative inflation perceptions and expectations questions in the Consumer survey

Roberta Friz
Directorate General for Economic and Financial Affairs
European Commission

EU workshop on recent developments in business and consumers surveys
Brussels, 15 November 2010
Structure of the presentation

- Background
- Results of the second evaluation
- Conclusions and Way forward
Background

In 2003, two new optional quantitative questions were added in the consumer survey:

1) By how many percent do you think that consumer prices have gone up/down over the past 12 months?
   
   They have in-/decreased by ...% 

2) By how many percent do you think that consumer prices will go up/down over the next 12 months?
   
   They will in-/decrease by ...%
Background

- First evaluation of the results: in 2006, jointly with ECB
- Data showed quite high inflation perceptions and expectations
- Several doubts on the quality of the data and the formulation of the questions…

⇒ Creation of a task force
Main tasks of the task force:

- Probing respondents understanding of the survey questions
  - Interpretation of “stay about the same”
  - Basket of goods considered by respondents
  - Knowledge of official figures
- Testing alternative formulations of questions
  - Survey laboratory
  - Live
Background

Main conclusions of the task force:

- **Some difficulties in interpreting questions**
  - Consumers mainly think of frequently purchased items
  - Some misinterpret the answer category “stay about the same”

- Among consumers, there is an widespread lack of knowledge about inflation

- Rephrasing the questions did not alleviate the problem of inflation overestimation
Main conclusions of the task force:

- Quality is high
  - The means are not affected by outliers
  - Quantitative replies are consistent with qualitative
  - Quantitative and qualitative data are highly correlated
  - Provide a correct representation of consumers’ opinions

⇒ continue to collect quantitative inflation opinions
Quantitative estimates of inflation and the euro area HICP (annual % changes)

Source: DG ECFIN
Results

Difference between households' estimates of inflation and actual inflation (in average over the period May 2003 – June 2010)
Results

Euro area, Breakdown by category
Results

Euro area distribution of replies

![Graph showing perceived inflation rate and expected inflation rate distributions.](image-url)
Chart 9 – Trimmed mean measures of inflation sentiment in the euro area

(a) Inflation perceptions

(b) Inflation expectations

Note: annual averages. The 2010 values are averages over H1.

Source: European Commission.
The second evaluation of the experimental dataset confirmed that:

- Quality is high
- The means are not affected by outliers
- Quantitative replies are consistent with qualitative
- Provide a correct representation of consumers’ opinions
Conclusions

The second evaluation of the experimental dataset highlighted:

- Respondents significantly overestimate actual inflation (in particular perceptions)
- Size of the overestimation has narrowed considerably in more recent period
- We still find a high number of replies far beyond any “rational” assessment of past inflation developments.
- By contrast, less of such extreme responses are included in the replies for inflation expectations
Way forward

- We will continue to collect these data
- Results will not be reported in regular publication
- We aim to publish the papers written using the experimental dataset
- Further discussions on how to make available the data behind the papers
- More research is needed
Way forward

Possible further lines of research:

- Investigate further:
  - the underlying reasons for the national differences in the responses
  - for monetary policy purposes, inflation expectations in the medium term
  - wage expectations

- Learn more about
  - the formation of public inflation perception and expectations
  - Impact of inflation opinions on macroeconomic variables
Thanks for your attention