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Is Inflation Domestic or Global? Evidence from Emerging Markets

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I N T E R N A T I O N A L M O N E T A R Y F U N D

Is Inflation Domestic or Global? Evidence from Emerging Markets*

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Abstract

Following a period of disinflation during the 1990s and early 2000s, inflation in emerging markets has remained remarkably low. The volatility and persistence of inflation also fell considerably and remained low despite large swings in commodity prices, the global financial crisis, and periods of strong and sustained US dollar appreciation. A key question is whether this improved inflation performance is sustainable or rather reflects global disinflationary forces that could prove temporary. In this paper, we use a New-Keynesian Phillips curve framework and data for 19 large emerging market economies over 2004–18 to assess the contribution of domestic and global factors to domestic inflation dynamics. Our results suggest that longer-term inflation expectations, linked to domestic factors, were the main determinant of inflation. External factors played a considerably smaller role. The results underscore that although emerging markets are increasingly integrated into the global economy, policymakers remain largely in control of domestic inflation developments.

Keywords: Emerging markets, globalization, inflation, inflation expectations, Phillips Curve.

JEL Codes: E31, E58, F62.

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