Asymmetric Behaviour of Inflation around the Target in Inflation-Targeting Countries

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Abstract: *We explore the asymmetric behaviour of inflation around the target level for inflation-targeting countries. The first rationale behind this asymmetry is the asymmetric policy response of the central bank around the target. Second rationale is the asymmetric inflation persistence. We suggest that recently developed Asymmetric Exponential Smooth Transition Autoregressive (AESTAR) model provides a convenient framework to capture the asymmetric behaviour of inflation driven by these two effects. We further conduct an out-of-sample forecasting exercise and show that the predictive power of AESTAR model for inflation is high for some countries in our sample, especially at long-horizons.*