Time Inconsistency: Inflation versus Output in Thai Monetary Policy

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Abstract

The paper investigates the time inconsistency problem in Thai monetary policy. The problem arises when policy makers pursue the short-run goal, the output, instead of the long-run goal of price stability. Time inconsistency problem is more likely to incur during supply shock periods where output contracts but inflation increases. As Thailand has adopted the inflation targeting regime since May 2000, the monetary policy should respond more to the inflation. However, if the policy responds more to the output, then there is the time inconsistency problem in this paper's perspective. The paper detects some degree of time inconsistency problem in Thai monetary authority by using three methods including the observation on monetary policy committee (MPC)'s decision during supply shock periods, multinomial probit model to imitate the MPC's decision, and vector autoregressive model to measure the responsiveness of the policy rate on inflation and output. Nevertheless, any conclusion should be interpreted with cautions since there are limitations in each method.