



Discussion of:  
Ditch the Ex!  
Measure Core Inflation  
with a Disaggregate Ensemble  
by Francesco Ravazzolo Shaun P. Vahey

Discussion By: Tara M. Sinclair  
The George Washington University

Challenges to Inflation in an Era  
of Relative Price Shocks Conference

Münster, Germany  
June 17, 2009



# How do we feel about the Ex?

- It may depend on what we use the Ex for...
  - Policy target?
  - Policy input?
  - This paper: **Forecasting**
    - The purpose of “core” here is to “predict measured inflation”.
    - A key aspect is it is not the point forecast, but the **complete forecast density**.



# Three Reasons to Leave the Ex

1. Zero-weighting food and energy in the construction of core discards important information.
  - The ex doesn't like your friends.
2. The core proposed by Ravazzolo and Vahey – 'Disaggregate Ensemble' is better for forecasting.
  - There are better fish in the sea.
3. The ex measure does particularly poorly for density forecasts.
  - The ex doesn't know the whole you.



# The New Squeeze (DE5-ANN)

- The Disaggregate Ensemble proposed by Ravazzolo and Vahey kind of looks like the Ex, but there are clear differences.
  - They model each disaggregate inflation series as a mixture innovation model then derive component weights to construct the ensemble forecast densities.
    - Ex core and food & energy
    - Durables, nondurables, and services
    - DE5-ANN combines both types of disaggregation and restricts the weights to be fixed for the four quarters of each calendar year.
  - Find a nonzero (but admitted small) weight on food and energy.
    - The new squeeze it lets you see your friends as much as you want, even if it's not much.
  - Approximately a 40 percent improvement over a benchmark AR(2).
    - It's better than being alone.
    - Note that with the Ex, it's statistically insignificantly better than being alone.



# Getting the Whole Picture

- Why Do We Care about the Complete Forecast Density?
  - Allows the researcher to be agnostic about the loss function of the monetary authority.
  - Provides insight on tail events:
    - Are we currently risking deflation?
    - Or skyrocketing inflation?
  - It's possible that food and energy shocks matter particularly for tail events.
    - It would be really nice to see some possible simulations to show how this would look.



# Lingering Questions

- Traditional core is used for policymaking as well as forecasting. How does the DE core do for policymaking?
  - Perhaps the focus should be more about forecasting, less about “core” if the DE measure doesn’t fit other aspects of the theoretical “core.”
- The construction of the DE core is much more complicated than the simple measure, is there some way to determine if it’s worth the effort, beyond simple statistical significance?
- Would it be worth it to disaggregate further than the broad categories used in this paper?
- For the role of the weights on the excluded components, could you try a simpler model (perhaps just for point forecasts?) to see if the role of food and energy change with a more complex model?