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Central Bank Independence, Speed of Disinflation and the Sacrifice Ratio

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Abstract

Using a theoretical model in which the degree of central bank independence affects the degree of inflation persistence and therefore the speed of disinflation, this paper suggests that sacrifice ratios are lower when central bank independence is higher. Empirical tests, using estimates of sacrifice ratios based on disinflation episodes for 18 OECD countries during the 1960–90 period, show that this result also holds empirically. This finding seems to be consistent with the credibility hypothesis by pointing out that an independent central bank may produce a credibility bonus.

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