

Time varying pass-through:  
Will the yen depreciation help Japan hit the inflation target?

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**Abstract**

This paper estimates time evolution of the exchange rate pass-through into Japanese domestic prices using the time-varying parameter-volatility VAR model. The Japanese yen has depreciated against the US dollar in recent months, from about 78 JPY/USD in early October 2012 to 91 JPY/USD in late January 2013. This rapid depreciation is expected to help the Bank of Japan hit the newly announced inflation target of 2%. On the other hand, it is believed that the rate of exchange rate pass-through to domestic prices has declined lately. It is important to know the extent of this decline. In this paper, based on the most updated estimates, I simulate the effects of the above 17% decline in the value of the Japanese currency on its domestic prices.

Key words: exchange rate pass-through; time-varying parameter-volatility VAR; simulation

JEL codes: C32, E31, F31

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