Exploring the Relationship between the CPI and the PPI: The Colombian Case

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This article explores the nature of the existing relationship between the Producer Price Index (PPI) and theConsumer Price Index (CPI). In particular, it seeks to determine whether the PPI can be considered a leadingindicator of the CPI, using the methodology of coincident profiles proposed by Martinez (2010), which modifiesthe one presented by Banerji (1999). Previous studies for Colombia and other countries found links of all typesbetween these two price indexes. Yet, there is no evidence of previous studies that have eliminated themethodological differences between the two baskets, at least in the international literature reviewed for thisarticle. However, when these discrepancies are removed (homogenization of items and weights), desirableresults are found for the Colombian case; namely, the PPI leads the CPI and, depending on the analyzed group,this leadership might anticipate evolution of the CPI by one month or even more. These findings clearly areuseful as input to improve consumer inflation forecasting models and the monetary authority’s decision-makingprocess.