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Upward bias in inflation perceptions: Persistence, drivers, implications

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STUDY

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Monetary Dialogue Papers, February 2026



Upward Bias in Inflation Perceptions: Persistence, Drivers, Implications



EGOV
MONETARY POLICY

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Upward Bias in Inflation Perceptions: Persistence, Relevance, Implications

Abstract

This paper examines the persistent upward bias in euro area households' inflation perceptions and expectations, even when realized inflation is near the ECB's target. It discusses behavioural and informational drivers of this bias, its implications for consumption, wage setting, and monetary policy transmission, and the challenges it poses for ECB communication and credibility. The study concludes that improved monitoring and household-oriented communication are essential.

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LIST OF ABBREVIATIONS

CES	Consumer Expectations Survey
CPI	Consumer Price Index
ECB	European Central Bank
EC	European Commission
HICP	Harmonised Index of Consumer Prices
ILS	Inflation-Linked Swaps
VAT	Value-Added Tax

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EXECUTIVE SUMMARY

Background

The ECB's primary mandate is to maintain price stability in the euro area. Meeting this mandate hinges not only on controlling realised inflation, but also on shaping how inflation developments are perceived and expected by households. Hence, to meet its medium-term 2% inflation target, the ECB must anchor the medium-term inflation expectations of households, firms, and financial market participants close to that goal. Yet, the inflation perceptions and expectations of euro area households display an upward bias.

Key messages

1. The current upward bias in inflation expectations is largely a household-level phenomenon.
2. The upward bias in households' inflation expectation is a phenomenon that, though time-varying, is generally present in inflation expectation data.
3. Households' knowledge of inflation is highly incomplete.
4. Past experiences matter for future expectations. Therefore, the recent experience of an inflation surge likely still elevates inflation perceptions and expectations today.
5. Inflation expectations vary with household characteristics, such as gender, income, and education, which in part is driven by differences in consumption bundles.
6. The influence of recent inflation experiences will fade, but the upward bias is a general phenomenon that will likely persist.
7. Changes in households' inflation expectations affect their consumption-savings and wage bargaining decisions. However, identifying these effects empirically is challenging, and the existing evidence is mixed.
8. There is no evidence on whether the upward bias itself is important for economic behavior, above and beyond the evidence on changes in inflation expectation discussed under (7).
9. Survey-based measures of inflation expectations have been developed through a careful and systematic research program. In addition, a broader investigation into how people understand and respond to inflation is ongoing—and could prove fruitful.
10. The ECB treats inflation expectations as a key policy variable and has invested substantially in monitoring them—including through the Consumer Expectations Survey (CES). This is an important path that should be continued.
11. The upward bias in inflation beliefs shows that households' knowledge of inflation remains limited. This poses a credibility and communication challenge. However, improving "inflation literacy" is a joint effort and is unlikely to be achieved by the ECB alone.
12. Communication should be tailored so that households who might only have limited knowledge of the concept of inflation can follow and understand it.

1. INTRODUCTION

Box 1: KEY FINDINGS

Households in the euro area consistently perceive and expect inflation to be higher than actual inflation, creating a persistent upward bias that remains even when inflation is close to the ECB's 2% target. This bias reflects limited inflation knowledge, reliance on salient price changes, and the lasting influence of past inflation experiences. While the recent inflation surge may fade from memory, the underlying bias is likely to persist. Changes in inflation expectations can affect household spending, saving, and wage bargaining, though empirical evidence is mixed. The ECB's continued monitoring of expectations through surveys is crucial, and communication should better reflect households' limited inflation literacy and everyday perspectives.

The ECB's primary mandate is to maintain price stability in the euro area with a medium-term inflation target of 2%. Meeting this mandate hinges not only on controlling realized inflation, but also on shaping how inflation developments are perceived and expected by households. If households expect higher prices in the future, they might increase their purchases today, putting upward pressure on prices, but they may also negotiate higher wages to offset an expected loss in real purchasing power. Firms might already raise the prices they charge for their goods today in the presence of frictions that might limit future price adjustments.

Hence, to meet its medium-term 2% inflation target, the ECB must anchor the medium-term inflation expectations of households, firms, and financial market participants close to that goal. Yet the inflation perceptions and expectations of Euro area households display an *upward bias*. In December 2025, while actual inflation over the preceding twelve months was 1.9%, the median respondent¹ in the ECB's Consumer Expectations Survey (CES)² perceived it to be 3.2% (mean: 6.4%) and expected it to be 2.8% (mean: 4.7%) over the coming year.

The tendency of households to overestimate past inflation and to expect future inflation to be moderately—but meaningfully—above the ECB's target raises three main questions that we address in this paper:

1. Is the current upward bias in household inflation perceptions and expectations transitory or persistent?
2. Do measured inflation expectations and their upward bias matter for economic behavior and policy?
3. What do these patterns imply for the ECB's credibility and communication?

We consider these questions in turn, after providing further context.

¹ The CES currently covers 11 euro area countries.

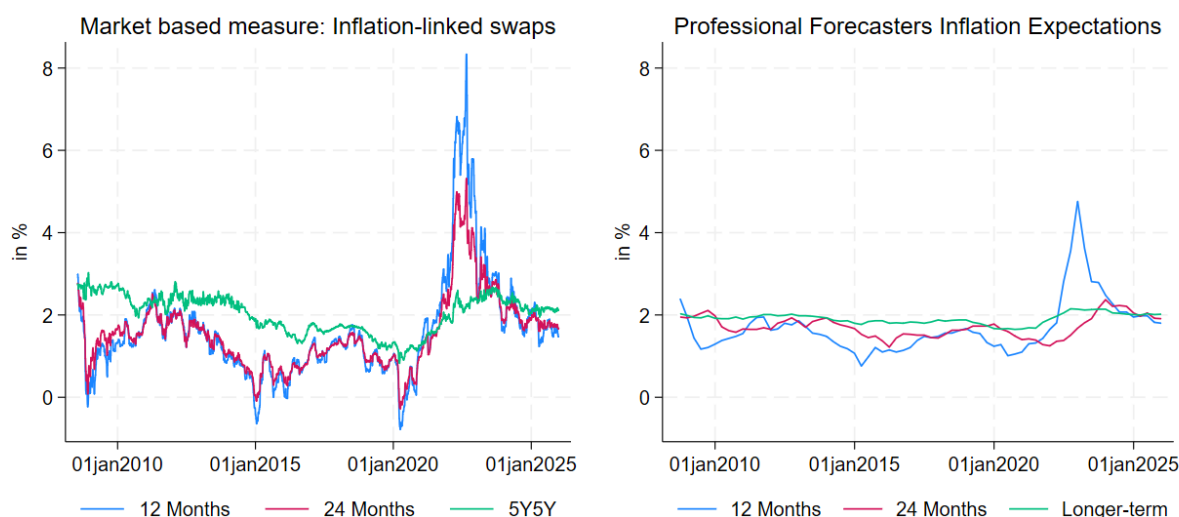
² See Box 2 in the appendix for details on how the CES is constructed, as well as potential limitations.

2. CONTEXT OF INFLATION EXPECTATIONS

1) *The current upward bias in inflation expectations is largely a household-level phenomenon.*

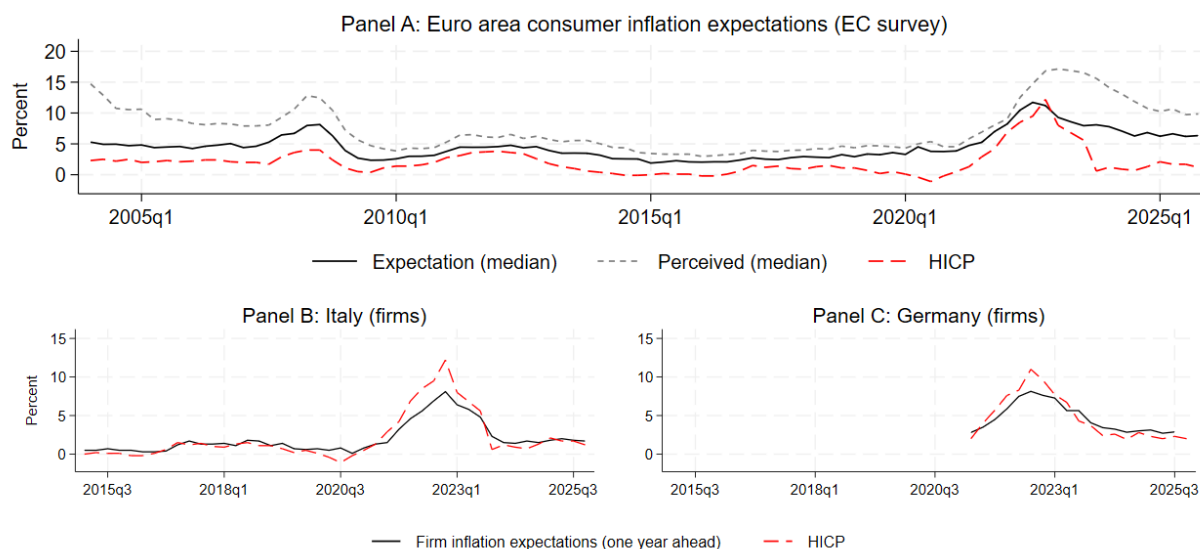
Traditionally, central banks focused their communication efforts on financial market participants. Their policy rate is only a short-term instrument, but what matters for the broader economy via mortgage rates, consumer loans, and business loans are longer term interest rates which depend critically on market expectations. And indeed, central banks overall have been very successful in managing the inflation expectations of professional forecasters and financial markets who are highly attentive and immediately adjust their outlook following both policy actions, rates, and announcements, even though the rate of success has varied over time and across countries. Figure 1 shows that market expectations derived from inflation-linked swaps and expectations of professional forecasts were close to 2% in recent months.

Figure 1: Professional Inflation Forecasts



Notes: Inflation-linked swaps are 7-day moving averages. 5Y5Y indicates inflation expectations of market participants for 5 years starting in 5 years and are calculated from the 5- and 10-year inflation swaps. The right-hand side depicts inflation expectations from professional forecasters surveyed at a quarterly frequency and shown at quarter-end. Longer term is 5 calendar years ahead in Q3 and Q4 rounds of the SPF and 4 years ahead in Q1 and Q2 rounds
Sources: ECB Survey of Professional Forecasters (SPF), LSEG, authors own calculations

Yet, professional forecasters and financial markets do not directly affect consumption, savings, debt choices, and investment but only indirectly through financial conditions. Therefore, central banks have recently focused their efforts on anchoring the expectations for households and firms, and here the evidence points to a different pattern. Figure 2 (Panel A) shows a longer time-series of perceived and expected inflation rates for households from the European Commission Consumer Survey as well as realized inflation measured by the Harmonised Index of Consumer Prices (HICP). The graph already indicates that households generally perceive and expect inflation rates to be higher than realized rates ex-post and a strong co-movement between both is present.

Figure 2: Consumers' and firms' inflation expectations and realized inflation

Notes: Panel A depicts consumer inflation expectations from the EC consumer survey (EA countries, changing composition) questions 51 (Price trends over last 12 months) and 61 (Price trends over next 12 months). HICP is EA countries, changing composition. Panel B depicts price inflation expectations by Italian industrial and service firms with 50 or more employees. Companies' responses are weighted by the number of firms. Panel C depicts the inflation expectations from a sample of German firms with a turnover greater than €22,000 or one employee subject to social security contributions. When calculating the mean inflation expectations of German firms, only responses between -12% and +12% have been taken into account. The value for Q2 2021 is the average of May and July 2021 values. Sources: Eurostat, European Commission – Business and consumer surveys, Banca D'Italia Survey on Inflation and Growth Expectations and Deutsche Bundesbank Survey on the Expectations of Firms in Germany

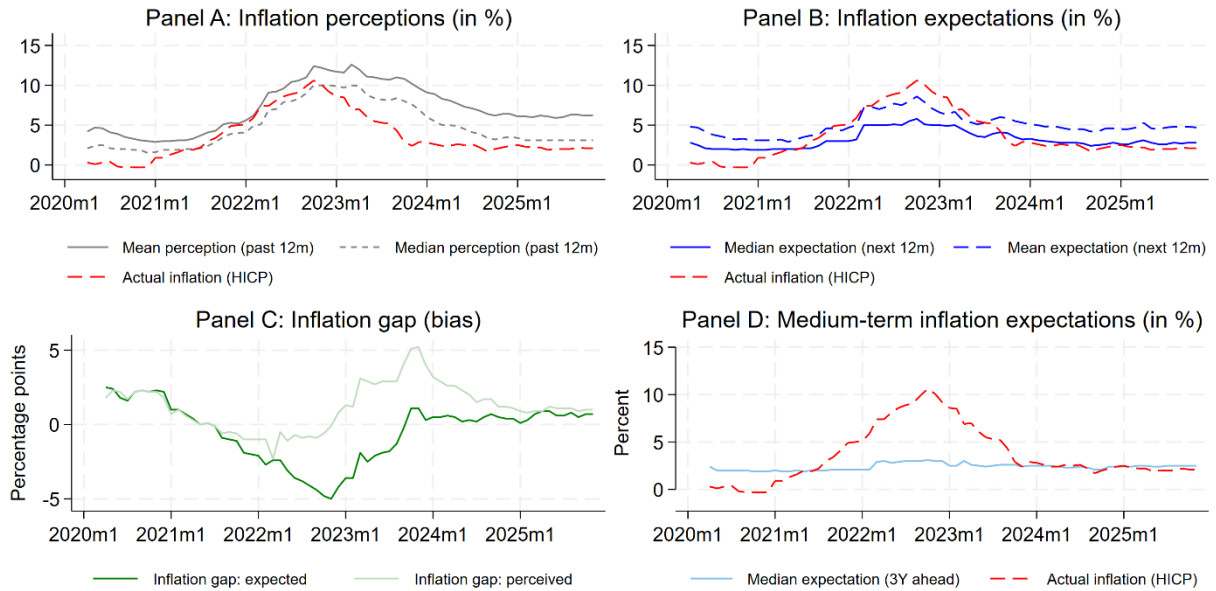
The evidence for firms is more limited in that no long running firm survey exists in the Euro Area. Figure 2 (Panel B and C) shows firms' average inflation expectation compared to the respective Harmonised Index of Consumer Prices (HICP) based on Banca D'Italia's Survey on Inflation and Growth Expectations and Deutsche Bundesbank Panel on Firms. The evidence suggests firms fall somewhat in between households and financial market participants, which is largely consistent with findings in the US (Weber et al., 2022).

2) The upward bias in households' inflation expectation is a phenomenon that, though time-varying, is generally present in inflation expectation data.

Elevated inflation perceptions and expectations are not a recent phenomenon. They have been a persistent feature of household responses, especially during periods of low and stable inflation, such as the years preceding the COVID-19 inflation surge (Weber et al., 2022)

For the Euro area, Figure 3 shows data from the CES conducted by the ECB. Median and mean inflation perceptions (Panel A) and median expectation (Panel B) consistently exceeded the actual inflation rate since the CES began. Panel C tracks the evolution of the upward bias—defined as perceived inflation minus actual current inflation—over time. For instance, the average bias in perceived inflation was 2.1 percentage points in 2020, compared to 1.0 percentage point in 2025. Inflation expectations over the next three years remained anchored slightly above 2% (Panel D).

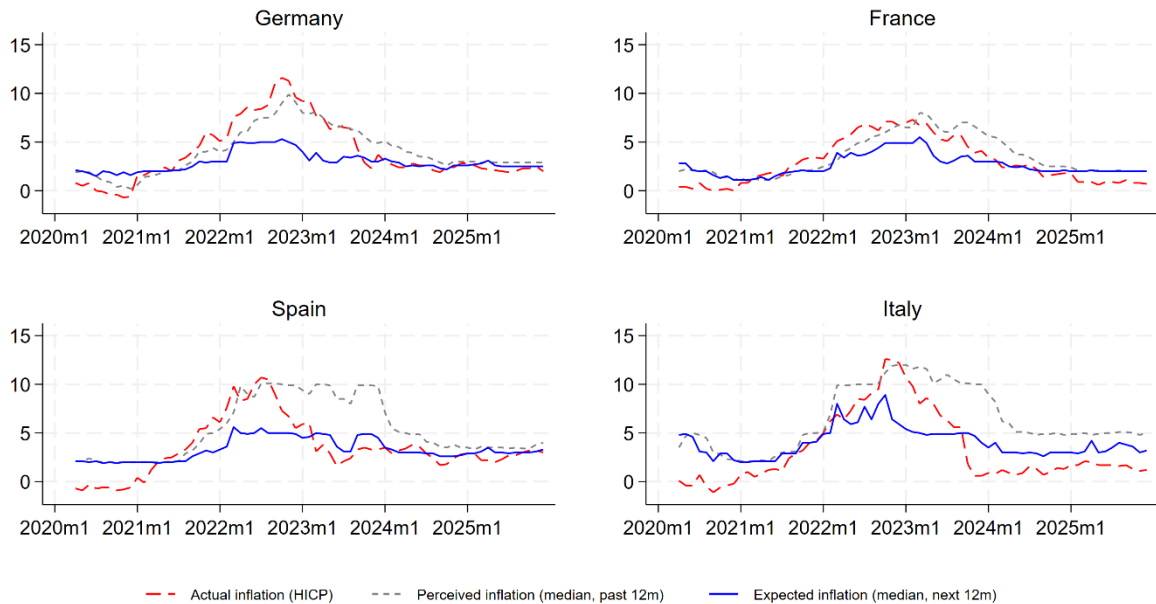
Figure 3: Inflation perceptions, expectations and biases



Notes: Panel A depicts the mean and median consumer perceived inflation over the past 12 months for the EA changing composition. Panel B depicts the mean and median consumer expected inflation over the next 12 months for the EA, changing composition. Panel C shows the inflation gap defined as the difference between median perceived/expected and realized inflation. Panel D depicts the median expected consumer inflation over the next three years for the EA, changing composition. Sources: Sources: ECB Consumer Expectations Survey (EA countries, changing composition), Eurostat (EA countries, changing composition), authors own calculations

A similar pattern holds across the largest euro area countries (see Figure 4 for selected examples). This bias is not unique to the Euro area. Comparable evidence can be found in the United States, based on both the Michigan Survey of Consumers and the New York Fed's Survey of Consumer Expectations (see Appendix).

Figure 4: Inflation: realized, perceived and expected (in %) in selected countries



Notes: All panels show median expected (perceived) inflation over the next (past) 12 months, as well as the realized inflation rate for each country. Sources: ECB Consumer Expectations Survey, Eurostat

Several behavioral and methodological factors may contribute to this persistent upward bias. Households tend to focus on goods they purchase frequently (D'Acunto et al., 2021a), overweigh large or salient price increases, selectively recall extreme changes, and focus on sources of information that are not representative for overall price developments rather than newspapers, official data releases or central bank communication (Coibion et al., 2022; D'Acunto et al., 2021a; D'Acunto and Weber, 2024; Weber et al., 2022). Households also focus more on price increases rather than equal size cuts (D'Acunto et al., 2021a). Measurement issues may reinforce these tendencies. Respondents report the likelihood that inflation will fall within specific intervals (e.g., 0–2%, 2–4%). This probabilistic format has

important advantages such as allowing for the measurement of inflation uncertainty (Armantier et al., 2013), but it also encourages respondents to assign positive probability mass across a range of positive inflation outcomes, leading to upwardly biased estimates (Hartzmark and Sussman, 2025). The bias is typically even larger when respondents are asked to state a point estimate of expected inflation directly (Weber et al., 2025).

Finally, Figure 2, Panel C also shows that the upward bias is not constant over time but time varying. Theories of rational inattention can provide one explanation for this temporal variation. Consumers have limited time and mental capacity. When inflation is low and stable, it is not worthwhile for them to focus their attention on the prevailing rate of inflation and its future determinants, as not being informed is not costly in terms of utility. Instead, when inflation increases and becomes more volatile, being uninformed can result in large mistakes on the part of consumers both in terms of consumption but also investment decisions. Consistent with this line of argument, Weber et al. (2025) show that for households and firms in the North and South America, in Europe and in New Zealand, that during times of low inflation, a large upward bias is present in their inflation perceptions and conditional on reaching them, both households and firms are very responsive in their inflation outlook. Yet, when inflation increases, the upward bias shrinks because inflation catches up with perceptions and households and firms actively acquire more information, but they also respond less to the provision of public information even if central banks reached them. This latter point means that simple communication of aggregate statistics by central banks is not sufficient to manage the inflation expectations of households during times of high inflation because this information is already in the information set of households. Instead, central banks need to focus on information that is new, relevant, and credible during times of high inflation when households actively seek to acquire new information.

3) Households' knowledge of inflation is highly incomplete.

A large body of research examines how households form their inflation expectations. A central finding is that households' (i) understanding of inflation, (ii) its causes and consequences, and (iii) their attention to inflation is often limited. We now discuss these different aspects of incomplete knowledge in turn.

This gap in knowledge starts with basic principles. For example, a sizable minority of households do not grasp that, with 2% inflation and a 1% interest rate, the real value of savings declines (Lusardi and Mitchell, 2014). Many also display "money illusion", evaluating income and returns in nominal rather than real, inflation-adjusted terms (Shafir et al., 1997). Both pieces of evidence suggest a general lack of inflation literacy but also a confusion of nominal and real quantities. Moreover, when thinking about inflation, many households focus on specific price changes of concrete goods (D'Acunto et al., 2023) rather than on the abstract concept and a broad based consumption bundle.

Households often rely on lay theories of inflation that diverge sharply from expert explanations (Andre et al., 2025, 2022). For instance, in the U.S., a significant share of households attributed the post-pandemic surge in inflation to government mismanagement or corporate greed—narratives largely absent from academic discussions (Andre et al., 2025). Similarly, households frequently struggle to assess how inflation affects their balance sheets, e.g., their stock market investments or the real value of their debt (Schnorpfeil et al., 2026, 2025), and often do not substitute intertemporally when expecting higher prices (D'Acunto et al., 2023)

Households also tend to pay little attention to inflation when it is low and stable, but their attention rises when inflation increases (Cavallo et al., 2017; Korenok et al., 2023; Link et al., 2025; Weber et al., 2025). Based on the most recent Consumer Expectations survey, 41% of households pay "much" or a "great deal" of attention to inflation, 42% pay "some" attention, and 18% pay "almost no" or "little" attention. Most EU households get their information about inflation from traditional media: around 50% cite television or radio, and nearly 40% cite newspapers (D'Acunto et al., 2024). The time variation in

attention is consistent with argument proposed in models of rational inattention but the evidence also points to an important role for cognitive constraints both in the conceptualization of inflation, the sources of information about inflation, and the linking of inflation to economic choices (D'Acunto et al., 2023).

High inflation is highly unpopular (Afrouzi et al., 2025; Hajdini et al., 2022; Stantcheva, 2024) and households have a high willingness to pay to bring inflation down to their preferred level which in fact would be slight deflation (Georgarakos et al., 2025). While this may seem obvious, it is less so from an economist's perspective, which also considers whether income growth keeps pace with inflation.

4) Past experiences matter for future expectations. Therefore, the recent experience of an inflation surge likely still elevates inflation perceptions and expectations today.

Perhaps because households' understanding of inflation is limited but also because some households might distrust the producers of official inflation statistics (D'Acunto and Weber, 2024), personal experience and direct exposure to price changes play a central role in shaping their perceptions and expectations. A growing literature shows that households tend to extrapolate from past inflation—especially recent experiences—when forming their expectations (Malmendier and Nagel, 2016). In line with this, perceived past inflation is one of the strongest predictors of expected future inflation (Weber et al., 2022). A direct implication of this evidence is that expectations will remain elevated even if realized inflation recedes given the persistent upward bias inflation perception. Remarkably, even distant historical episodes, such as the German hyperinflation of the 1920s, continue to shape inflation expectations today—likely through the intergenerational transmission of collective memory (Braggion et al., 2024).

This research suggests that, because recent inflation experiences heavily influence household expectations, paired with households' focus on price increases rather than equal-size price cuts, the post-pandemic inflation spike likely continues to shape households' inflation outlooks today. It is a plausible contributor to of the upward bias in inflation perceptions and expectations observed today.

5) Inflation expectations vary with household characteristics, such as gender, income, and education, which in part is driven by differences in consumption bundles.

Research has also examined which consumers expect higher inflation. Because these studies compare households observed at the same point in time—within the same inflation environment—the predictors of higher expected inflation align with those of the upward bias.

Women consistently report higher inflation expectations than men, in part because they are more likely to be the primary grocery shopper in the household (Bruine De Bruin et al., 2010; D'Acunto et al., 2021a). This gender gap in inflation expectations arises even within household and can be fully traced back to different information sources for forming inflation expectations: women are more likely to focus on the price changes of grocery times than men, but conditional on the information source, men and women form expectations equally (D'Acunto et al., 2021b). In contrast, consumers with higher income or greater educational attainment tend to report lower expected inflation (D'Acunto et al., 2024). Cognitive ability appears to matter as well: using IQ test scores from Finnish military records, D'Acunto et al. (2023) find that individuals with higher scores expect lower inflation. Similarly, CES data show that inflation forecast errors decline systematically with financial literacy (D'Acunto et al., 2024).

Because households with different age profiles or incomes often consume different bundles of goods and services or buy them at different locations or outlets, they face different price changes and have different exposures to inflation (D'Acunto et al., 2021a). Since past experiences matters for future expectations, these differences in experiences can explain part of the differences in expectations.

3. IS THE CURRENT UPWARD BIAS IN HOUSEHOLD INFLATION PERCEPTIONS AND EXPECTATIONS TRANSITORY OR PERSISTENT?

6) *The influence of recent inflation experiences will fade, but the upward bias is a general phenomenon and will likely persist.*

We discussed both the role of recent experiences and the general persistence of the upward bias in households' inflation perceptions and expectations above. In light of this, we expect that inflation perceptions and expectations could decline further — provided inflation remains stable near 2% and memories of the post-pandemic inflation surge continue to fade. The upward pressure arising from recent experience is a transitory phenomenon. However, the general upward bias in household inflation perceptions and expectations is likely to persist.

We cannot quantify the relative importance of these transitory and persistent components. But given that the current bias is not unusually high by historical standards, if anything, we would expect the persistent component to be the dominant force. Therefore, under current conditions, we do not expect a sizable decrease of the upward bias in the next years.

4. DO MEASURED INFLATION EXPECTATIONS AND THEIR UPWARD BIAS MATTER FOR ECONOMIC BEHAVIOR AND POLICY?

7) *Changes in households' inflation expectations affect their consumption-savings and wage bargaining decisions. However, identifying these effects empirically is challenging, and the existing evidence is mixed.*

In economic theory, inflation expectations play a central role in shaping household behavior. In particular, they shape their consumption-savings decisions. Box 1 briefly outlines the theoretical mechanisms and emphasizes that inflation need not affect all households in the same way.

Box 2: Inflation expectations and consumption in economic theory

Inflation can affect consumption and saving through two primary channels. First, inflation changes the relative price of consumption today versus in the future—this is the so-called *substitution effect*. Higher inflation makes future consumption more expensive, which can incentivize households to bring consumption forward, particularly for durable goods whose benefits accrue over time but whose costs are paid upfront. Second, inflation affects the real value of income and wealth—this is the *wealth or income effect*. The direction of this effect depends on a household's balance sheet. For indebted households, inflation erodes the real value of nominal liabilities, effectively increasing real net wealth, which may encourage higher current consumption. For households with nominal assets or fixed nominal incomes, inflation erodes real wealth or income, which may lead to reduced consumption. In standard New Keynesian models, the substitution effect typically dominates, but in heterogeneous-agent models that account for variation in wealth and debt, the income effect can play a prominent role, too. Finally, higher inflation typically coincides with higher inflation uncertainty which can result in a decrease in consumption due to *precautionary savings demands*.

The empirical evidence on the link between inflation expectations and consumption is mixed. Two caveats are worth mentioning. First, as noted in Box 1, even the theoretical effects point in different directions for different households, so average effects in the data may appear weak. Second, empirical identification of the causal effect of inflation expectations is challenging: it requires both an exogenous shift in expectations and reliable consumption data. Such conditions are rare.

The most credible evidence to date comes from (quasi-) experiments that manipulate inflation expectations and track behavioral responses in controlled settings. For example,

- D'Acunto et al. (2022) use Germany's pre-announced 2007 VAT hike as a natural experiment to isolate an exogenous increase in inflation expectations. Comparing German households to similar euro-area households, they show that higher expected inflation **raises durable spending**, consistent with intertemporal substitution.
- Coibion et al. (2022) experimentally manipulate U.S. households' inflation expectations and use scanner data to track consumption responses. They find that higher inflation expectations lead to **more spending**. However, the **effect on durable goods purchases appears to be negative**, a result replicated in Coibion et al. (2023). One explanation is that households with higher inflation expectations grow more pessimistic about their real income and overall economic outlook, leading to reduced spending (Coibion et al., 2023).

- Coibion et al. (2024a) offer another potential explanation: inflation uncertainty. In their experiment, higher inflation uncertainty reduces durable goods purchases. However, when holding inflation uncertainty constant, higher expectations **increase durable good spending**.

Additional evidence comes from surveys that ask households how they would respond to increases in inflation. In Jiang et al. (2024), most respondents report **no change** in their current spending. Many view inflation expectations as irrelevant or report sticking to fixed budgets. Among those who do adjust, most **reduce spending**—mainly due to wealth effects. As we wrote above, the empirical evidence on the link between inflation expectations and consumption is mixed.

Beyond consumption, inflation expectations also matter for wage setting. Evidence from the US shows workers are also more likely to search for a new job when inflation is high and they do not expect their current wages to keep up (Guerreiro et al., 2025; Pilossoph and Ryngaert, 2024). Inflation expectations could also be relevant for home ownership (Malmendier and Wellsjo, 2024), trading (Schnorpfel et al., 2025), and (re)financing decisions (Cenzon and Szabó, 2024).

We believe it would be a mistake to dismiss the importance of inflation expectations based on the mixed empirical findings. Instead, we interpret the evidence as reflecting the empirical challenges of isolating causal effects in this context—a subject of ongoing research. Given that several experimental studies do find effects, and that strong theoretical foundations support such mechanisms, we conclude with a cautious but affirmative statement: households' inflation expectations *can* influence their consumption-savings and wage bargaining decisions.

8) *There is no evidence on whether the upward bias itself is important for economic behavior, above and beyond the evidence on changes in inflation expectation discussed under (7)*

Empirical research can examine how changes in inflation expectations affect economic behavior. However, because the upward bias in expectations is a persistent feature—even during periods of low and stable inflation—empirical work cannot assess whether the presence of this bias in itself, alters behavior. Moreover, to the extent that the upward bias reflects a measurement artifact, it is unlikely to have real consequences for behavior. Researchers, and central banks are aware of this and therefore focus on changes in expectations over time rather than their absolute level.

In other words, when households state in surveys that they expect an inflation rate of 10% over the next 12 months, they do not behave and consume in a way consistent with such high rates. But when the same household increases their outlook from 10% to 12%, this difference is meaningfully related to economic behavior. This evidence can also explain why we see at the same time a persistent upward bias in inflation expectations and realized inflation close to central banks' targets over periods of time.

9) *Survey-based measures of inflation expectations have been developed through a careful and systematic research program. In addition, a broader investigation into how people understand and respond to inflation is ongoing—and could prove fruitful.*

The survey-based measures of inflation expectations that the CES uses have been developed in a careful and extensive research program (Armantier et al., 2013; Weber et al., 2022). Evidence that measured expectations correlate with consumers' shopping experiences and can be linked to behavior suggests that these surveys do capture meaningful variation in households' outlooks. Similar conclusions have been reached in other domains, such as return expectations or labor market expectations (Bachmann et al., 2023; Manski, 2018).

At the same time, the empirical relationship between expectations and behavior is often quantitatively weaker than standard theory would predict (Charles et al., 2024; Giglio et al., 2021; Yang, 2025) —a puzzle that motivates ongoing research.

Recently, work has also expanded beyond the narrow focus on expectation to explore how individuals reason about inflation more broadly. What subjective beliefs do people hold about the causes of inflation, its future drivers, and its implications for their own financial situation? How do they think

inflation is shaped by policy decisions? This broader perspective—examined in recent studies by Andre et al. (2022, 2022) and Schnorpfel et al. (Schnorpfel et al., 2026, 2025) —promises to deepen our understanding of how households form beliefs and make decisions in an inflationary environment.

5. WHAT DO THESE PATTERNS IMPLY FOR THE ECB'S CREDIBILITY AND COMMUNICATION?

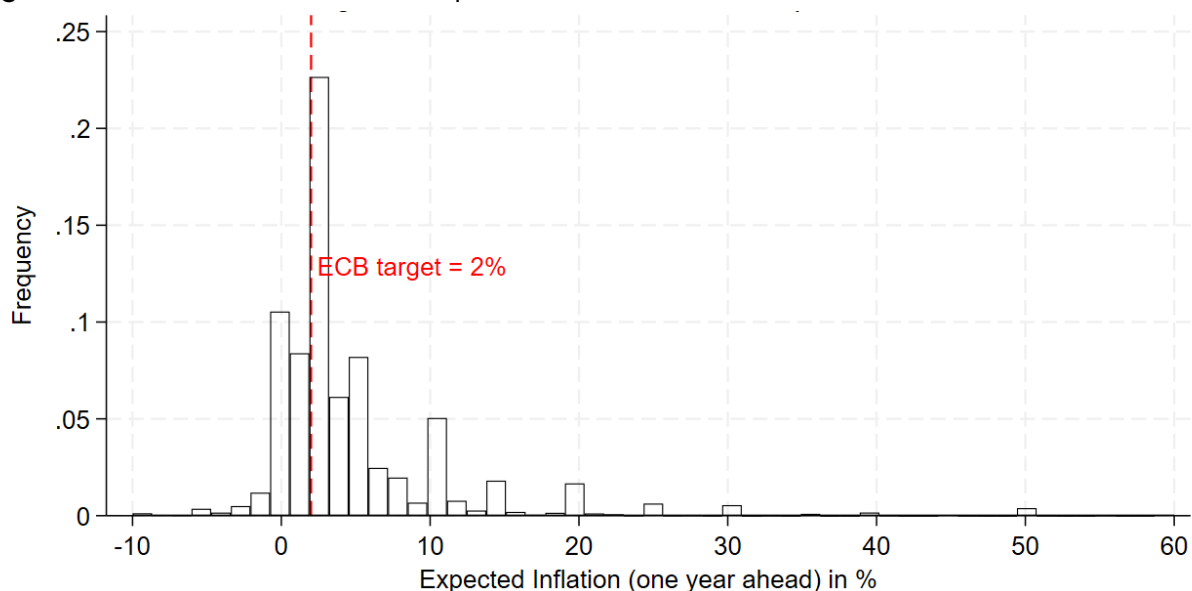
10) *The ECB treats inflation expectations as a key policy variable and has invested substantially in monitoring them—including through the CES. This is an important path that should be continued.*

The ECB, among other prominent central banks such as the U.S. Federal Reserve, has consistently emphasized that inflation expectations matter for the effective transmission of monetary policy and for achieving its medium-term inflation target. In line with this, the ECB tracks a wide set of expectation measures across different actors, including financial markets, professional forecasters, firms, and households. The CES represents a particularly valuable investment in this regard. Collecting high-frequency, cross-country household expectations data in a harmonized way is costly, but it provides policymakers with detailed and timely insights into how households perceive inflation and how they revise their beliefs over time and research documents that central finding. A further strength of the CES is its close integration with academic research. The survey has served not only as a policy tool but also as a platform for research that improves measurement, interpretation, and understanding of household belief formation (Coibion et al., 2024b).

Recommendation: *The ECB should continue to pursue this path, including the systematic tracking and research-based interpretation of household expectations.*

11) *The upward bias in inflation beliefs shows that households' knowledge of inflation remains limited. This poses a credibility and communication challenge. However, improving "inflation literacy" is a joint effort and is unlikely to be fully achievable by the ECB alone.*

Despite the ECB's increased outreach efforts, household inflation expectations and perceptions remain systematically above actual inflation and above the ECB's target. Notably, the median perception of 3.2% for past inflation and the median expectation of 2.8% for future inflation as of December 2025 mask a wide distribution of responses—including many households with implausibly high values (Figure 5). Over 10% of the respondents in the 2025 survey expected inflation to be higher than 10% over the next 12 months. These households are poorly informed about the actual inflation environment. This pattern reflects an incomplete "inflation literacy": many households do not have a clear understanding of inflation, what drives it, how monetary policy works, or what the ECB's objective implies for everyday economic outcomes.

Figure 5: Distribution of consumer's expected inflation

Notes: The figure depicts the unweighted cross-sectional distribution of consumers one-year ahead inflation expectations. The x-axis is truncated at -10 and 60 for visual clarity.
Sources: ECB Consumer Expectations Survey (EA-11), pooled 2025 data.

If households consistently perceive inflation as being far above target—even when inflation is close to 2%—this could undermine trust in the institution's ability to deliver price stability, or more broadly in its competence and legitimacy. Over time, credibility concerns could also become politically relevant: a central bank that appears misaligned with households lived inflation experience may face greater challenges in safeguarding its independence.

Recommendation: Higher "inflation literacy" would be desirable, both as an outcome in itself and as a way to reduce credibility risks.

A natural response to low inflation literacy is to intensify public communication and education efforts. However, it is unclear how much progress the ECB can achieve on its own. The ECB's direct outreach depends on broader media reporting and the political debate, where many other actors like politicians have greater visibility. Moreover, media incentives often favor "bad news", so it may also be easier to attract readership for bad inflation than for good inflation news. The ECB compared news coverage of inflation in general content newspapers from the four largest euro area countries and shows a strong correlation between inflation attention in the news and HICP inflation (Aarab et al., 2025). Nonetheless, since many EU households receive their information about inflation through traditional media, the ECB can benefit from effective communication through these channels—not only in "bad" times, when inflation is high, but also in "good" times, when it is low.

12) Communication should be tailored so that households who might only have limited knowledge of the concept of inflation can follow and understand it

Given these constraints, the realistic objective cannot be to "solve" households' inflation literacy in the short or medium run. Instead, ECB communication should take households' subjective perspectives on and understanding of inflation seriously as a starting point. Households interpret inflation through everyday experiences—frequent purchases, salient price changes, and subjective narratives. Communication is therefore likely to be more effective when it anticipates these interpretations and addresses them directly.

Recommendation: Because inflation literacy will not improve quickly, ECB communication should explicitly incorporate households' limited knowledge and lay perspectives when explaining inflation dynamics and policy decisions in the short run. In the medium run, an additional—but joint political—effort should be to further broaden the public's knowledge of the concept of inflation and how monetary policy operates.

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ANNEX

Box 2: Consumer Expectations Survey (CES) from the ECB

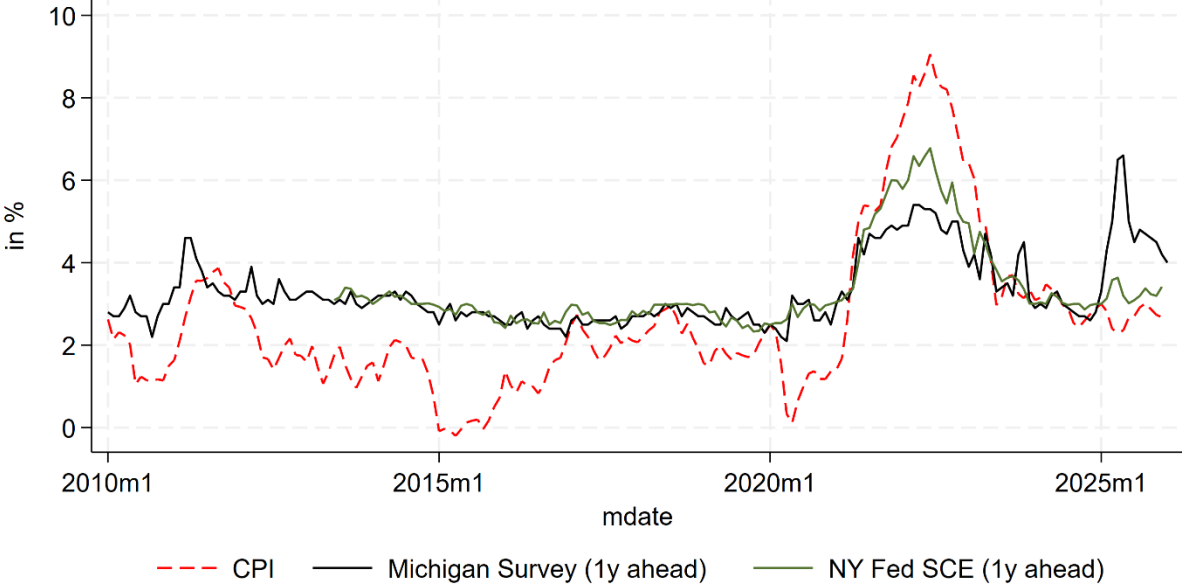
The ECB Consumer Expectations Survey (CES) is an online panel survey of adult consumers in the euro area designed to collect timely, high-frequency information on consumer perceptions, expectations and behaviour to be used for policy analysis and research. The survey includes a monthly core module on time sensitive information, as well as quarterly modules and annual topical modules. The CES was launched in 2020 covering the six largest euro area member states: Belgium, Germany, Spain, France, Italy and the Netherlands. It was expanded in 2022 to include five additional countries on a pilot basis: Ireland, Greece, Austria, Portugal and Finland, and, as of early 2024, these additional countries are officially included in both the reported aggregate results and the publicly available microdata. The CES now reflects data from 11 euro-area countries.

As part of the survey on inflation, Consumers are asked about their perceptions of inflation over the previous 12 months. This includes both qualitative and quantitative components. Respondents indicate direction of price changes (e.g., increases/decreases) and then provide a numeric estimate of how much prices in general are higher/lower now compared with 12 months ago. These responses are weighted and aggregated to generate indicators such as the median perceived inflation rate over the past 12 months.

Forward-looking inflation expectations are elicited at multiple horizons through a set of questions. These cover qualitative questions on whether respondents expect prices to increase, decrease, or remain the same as well as open-ended quantitative questions asking respondents to estimate the percentage change in the general price level at the specified horizon. Finally, the survey contains probabilistic questions in which respondents allocate probabilities across predefined inflation change intervals ("bins"), to capture not only point expectations but also individual uncertainty about future inflation.

While the CES is well designed and provides detailed and timely insights into household's perceptions and expectations, it is subject to typical limitations of online panel surveys, including coverage and selection biases, residual representativeness concerns, measurement error in inflation expectations. For example, the survey does not cover 10 smaller euro area countries and the elderly age group above 71 is small and underrepresented. Although the CES applies weighting procedures to improve population representativeness, not all potentially relevant household characteristics can be fully accounted for. Comparisons with external benchmark datasets suggest that certain socio-economic groups may remain over- or underrepresented, resulting in residual sample selection issues (Bańkowska et al. 2021).

Figure 6: Consumer expected inflation and CPI in the USA



Notes: Michigan and NY Fed SCE are median 1-year-ahead consumer expected inflation rates.
Sources: Michigan Survey of Consumers, New York Fed's Survey of Consumer Expectations, BLS

This paper examines the persistent upward bias in euro area households' inflation perceptions and expectations, even when realized inflation is near the ECB's target. It discusses behavioural and informational drivers of this bias, its implications for consumption, wage setting, and monetary policy transmission, and the challenges it poses for ECB credibility. The study concludes that improved monitoring and household-oriented communication are essential.

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