



Introduction to Monetary Policy

Introductory Workshop to
Financial Programming and Policies
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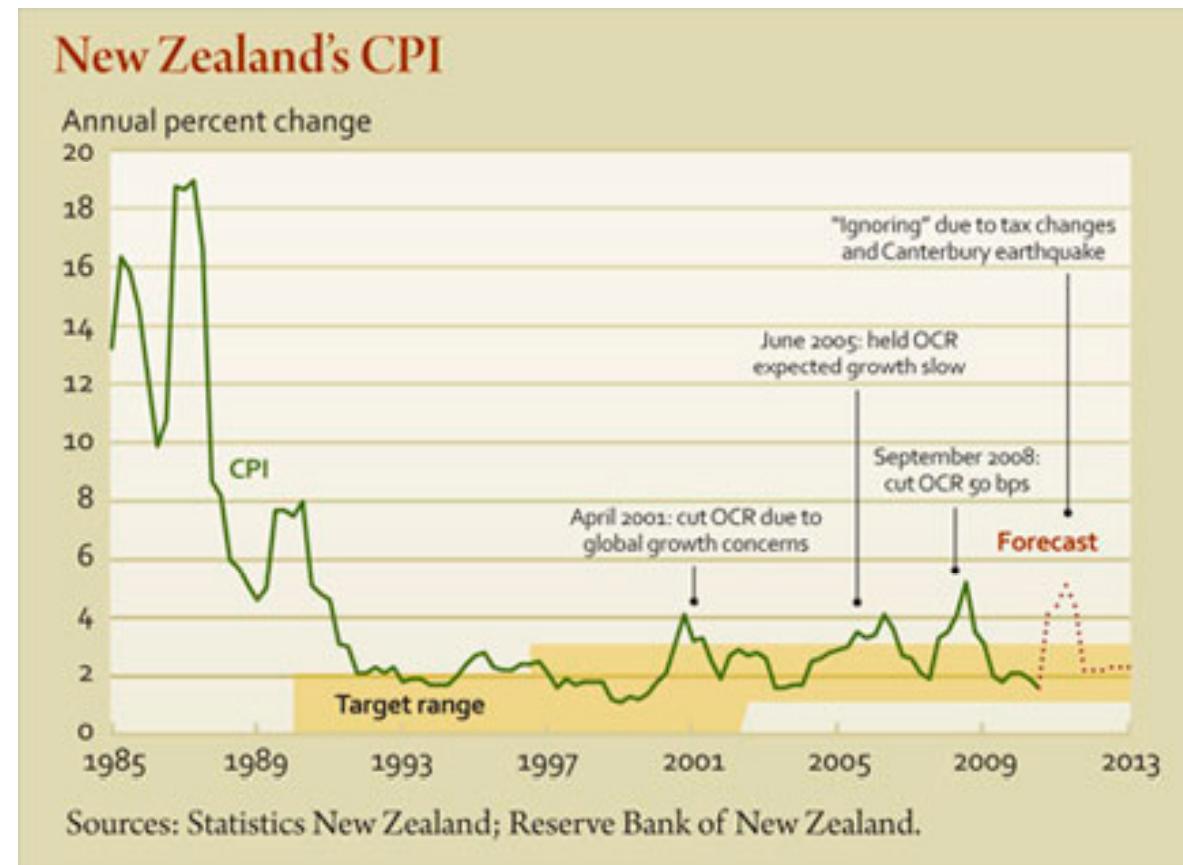
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Outline

I. Central Bank Objectives

II. Monetary Policy Frameworks

Central Bank Objectives: Inflation



“...it was clearly understood that my task was to get inflation above zero and below 2%.”

Don Brash, former RBNZ Governor

Central Bank Objectives: Foreign Exchange Stability

Avoiding large, sudden foreign exchange outflows!

- Shortage of foreign exchange can lead to loss of confidence in domestic currency
- Exchange rate needs to be competitive



Central Bank Objectives: Financial System Stability

Keeping the banking system solvent!

Well-functioning credit and payment system



Central Bank Objectives & Functions

Monetary Stability

- Monetary policy
- Exchange rate policy

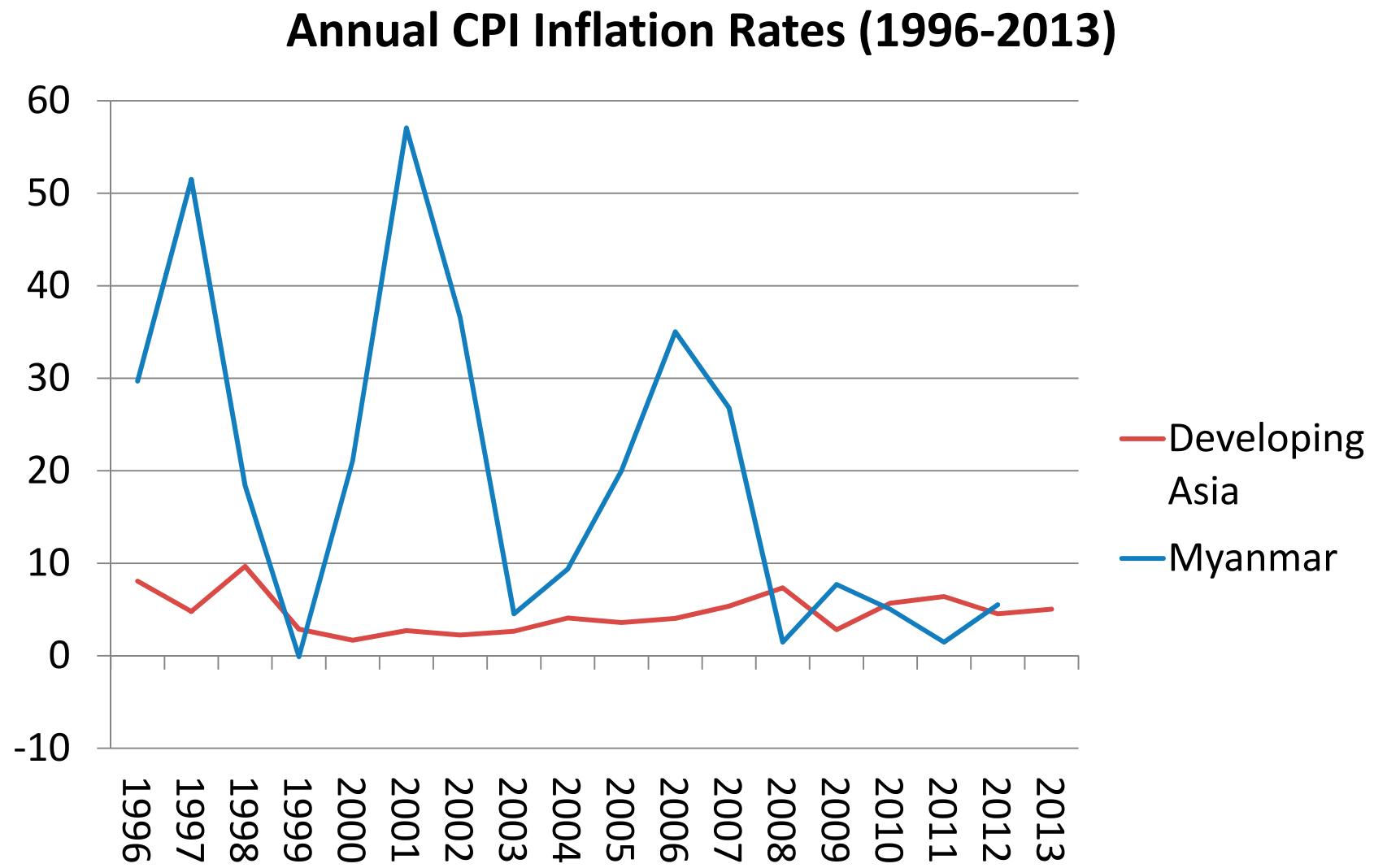
Financial stability

- Prudential policy
- Supervision, oversight

Policy Operation Functions

- FX intervention
- FX reserve management
- Liquidity management
- Lender of last resort

Central Bank Objectives: Historical Experience in Myanmar



Central Bank Objectives: CBM Law

Objectives specified in CBM law

CBM Law, Chapter II:

- The aim of the Central Bank shall be to maintain and preserve domestic price stability
- The Central Bank shall, in accordance with its aim, also endeavor to attain the following objectives:
 - ✓ To promote monetary stability
 - ✓ To enhance financial system stability
 - ✓ To develop efficient payments and settlement system
 - ✓ To support the general economic policy of the Government conducive to sustained economic development

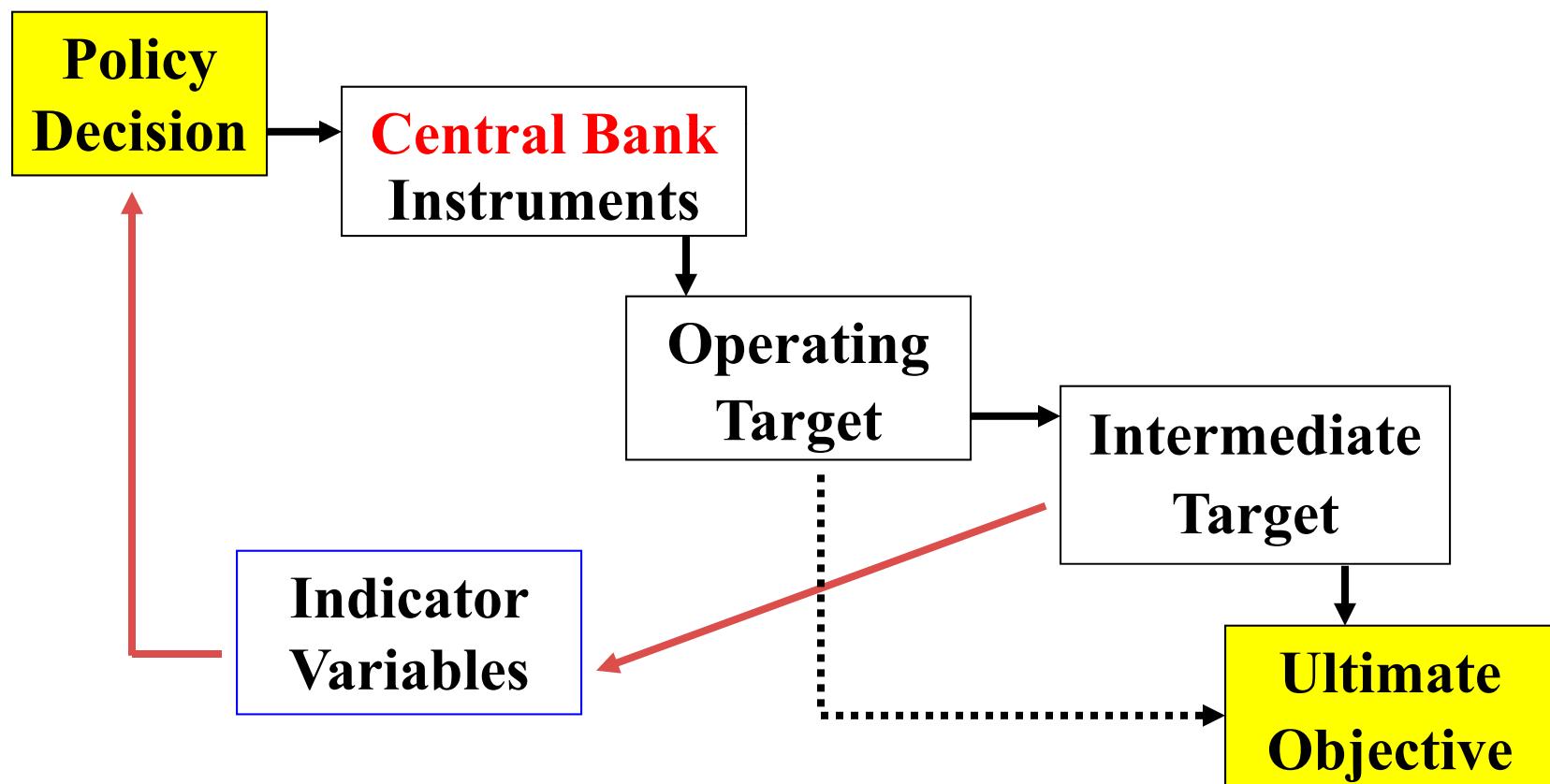
Outline

I. Central Bank Objectives

II. Monetary Policy Frameworks

Monetary Policy Frameworks

Central challenge for monetary policy frameworks:
Long gaps between policy decision and ultimate objective!



Role of Targets

As a result of the **long transmission lag** between central bank instrument and ultimate objective, **operating and intermediate targets are needed**

Target: proximate goals, not objectives in and of themselves; work directly toward achieving the long-term objectives of policy



Operating Targets

Operating target:
tactical goals that
the central bank can
influence in the short
run

- Reserve money/ monetary base: The central bank can control the size of its own balance sheet
- Short-term interest rates (e.g., interbank rate (“federal funds”) in the U.S.)



Intermediate Targets

Providing a Link to the Ultimate Objective

- Criteria for intermediate targets
 - Consistent with ultimate goals
 - Can be accurately measured
 - Timely
 - Can be influenced by the central bank

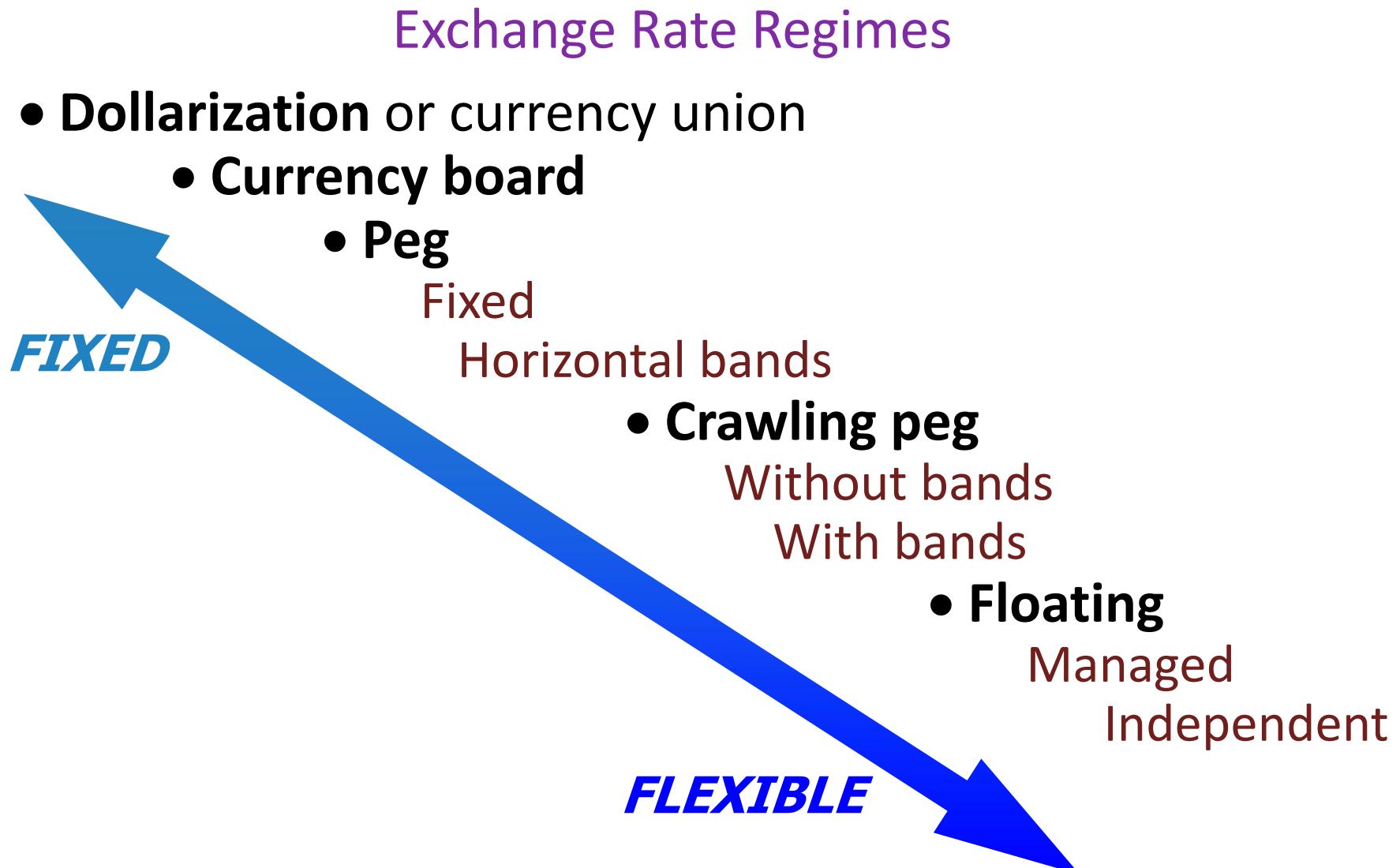


Intermediate Targets as Nominal Anchor

- A ‘nominal anchor’ is an intermediate target that helps to pin down inflationary expectations
- The choice of an intermediate target defines the monetary policy framework
 - Exchange rate anchor
 - Monetary aggregate target
 - Inflation targeting

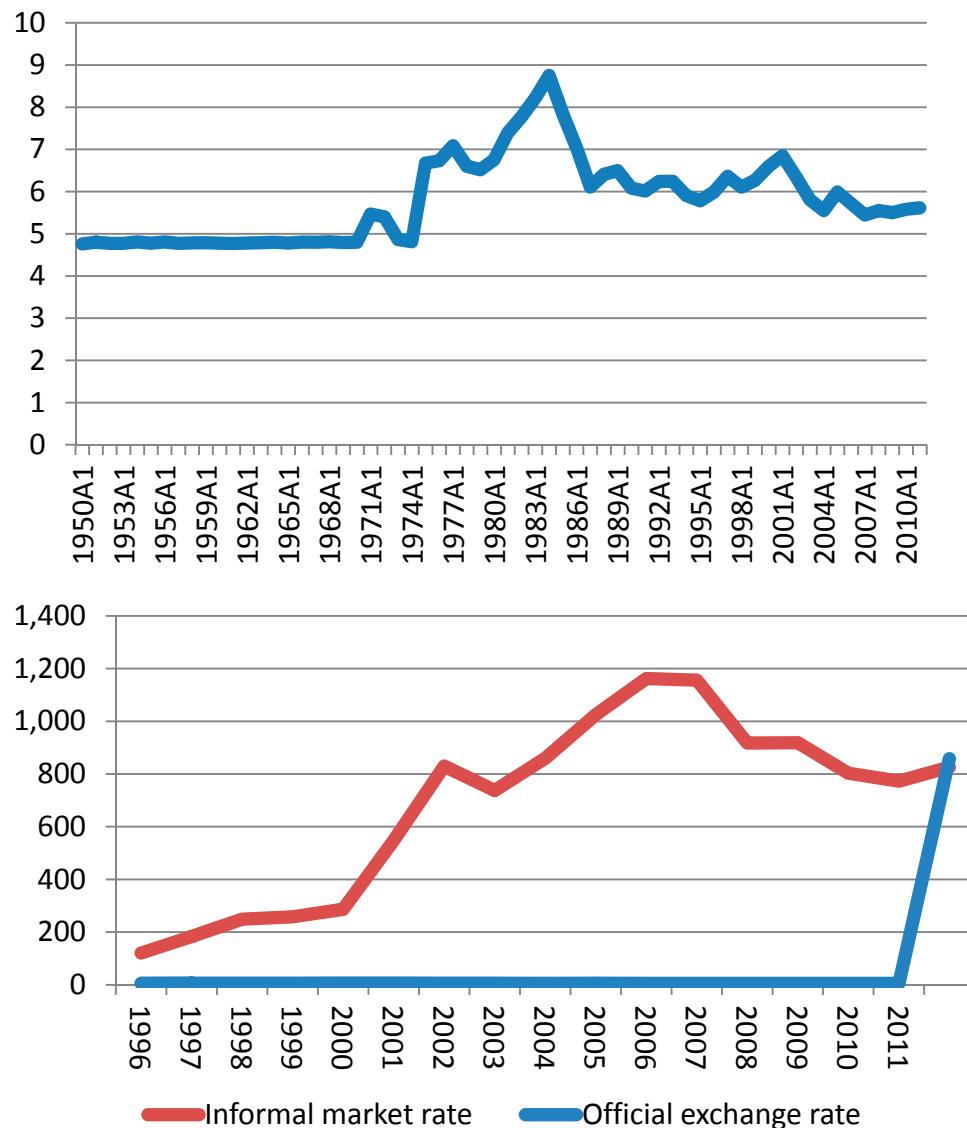


Classification of Monetary Frameworks



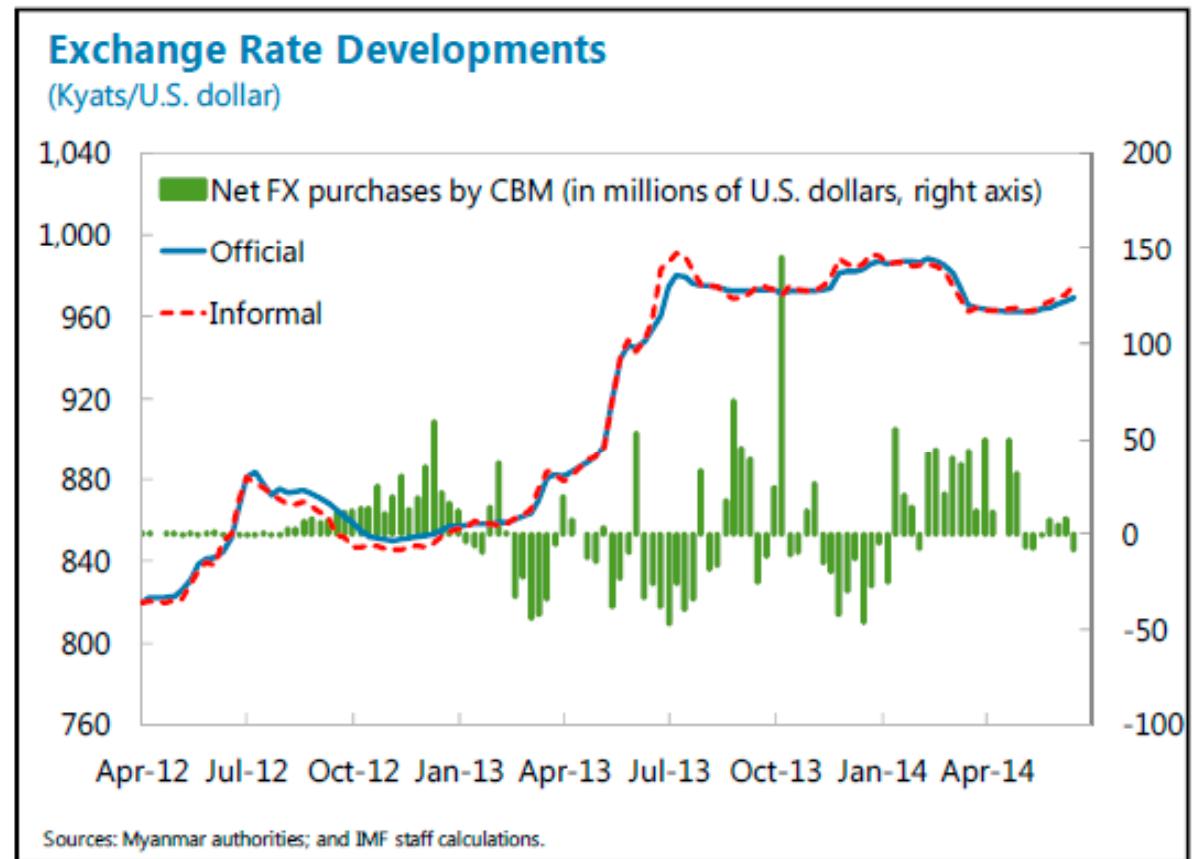
Exchange Rate Regime in Myanmar: Historical Perspective

- Official rate was very stable between 1950 and 2011—but it was set by government with no relationship to economic developments
- In 2012, official rate was allowed to float and brought in line with market rate

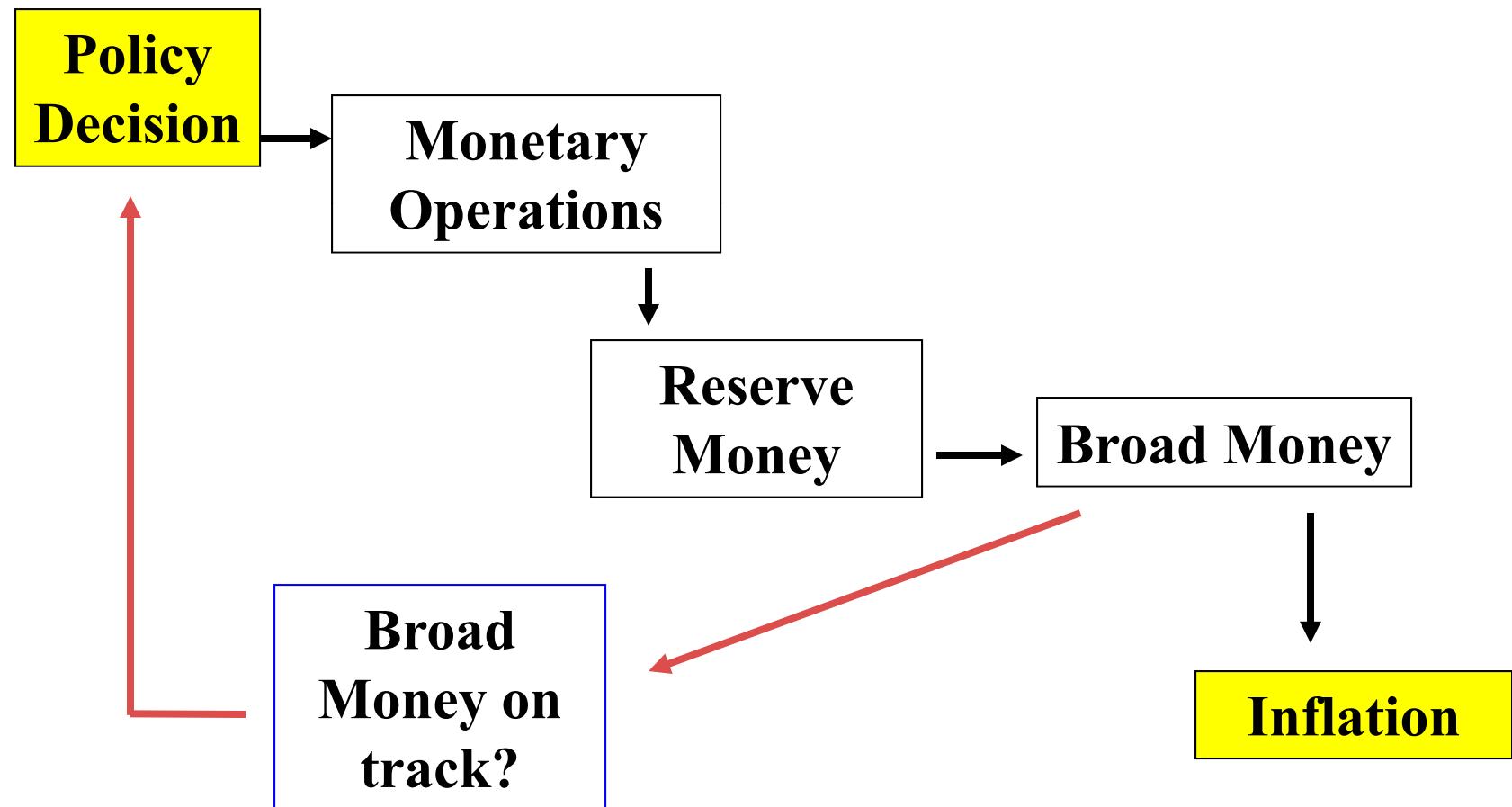


Exchange Rate Regime Myanmar: 2013

- April 2012: CBM started daily foreign currency auctions to determine exchange rate
- **De jure:** effective April 2, 2012, the de jure exchange rate arrangement was reclassified to a **managed float** from a conventional peg
- **De facto:** due to multiple exchange rates, de facto regime is classified as **other managed arrangement**

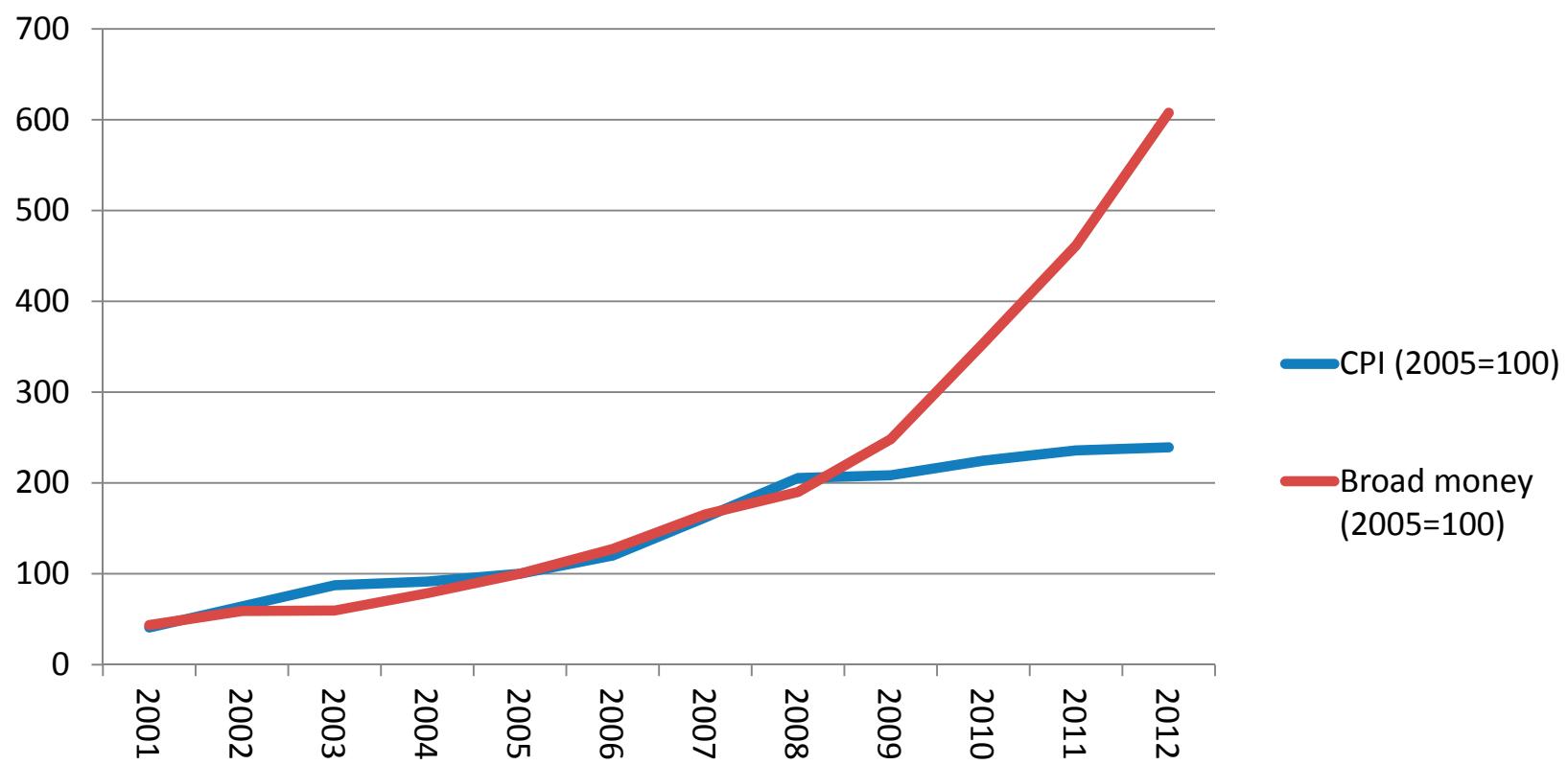


Monetary Targeting Regime



Monetary Framework in Myanmar

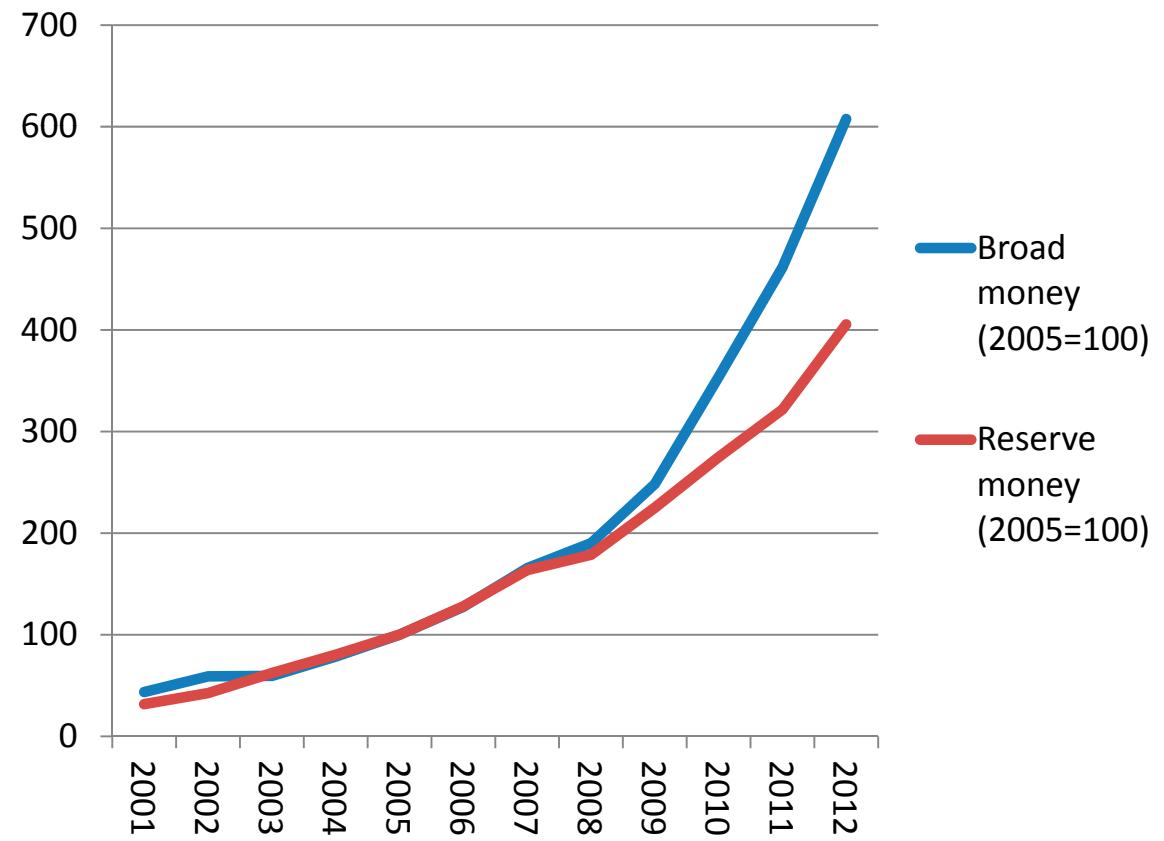
Historically close link between broad money and prices:



Monetary Framework in Myanmar

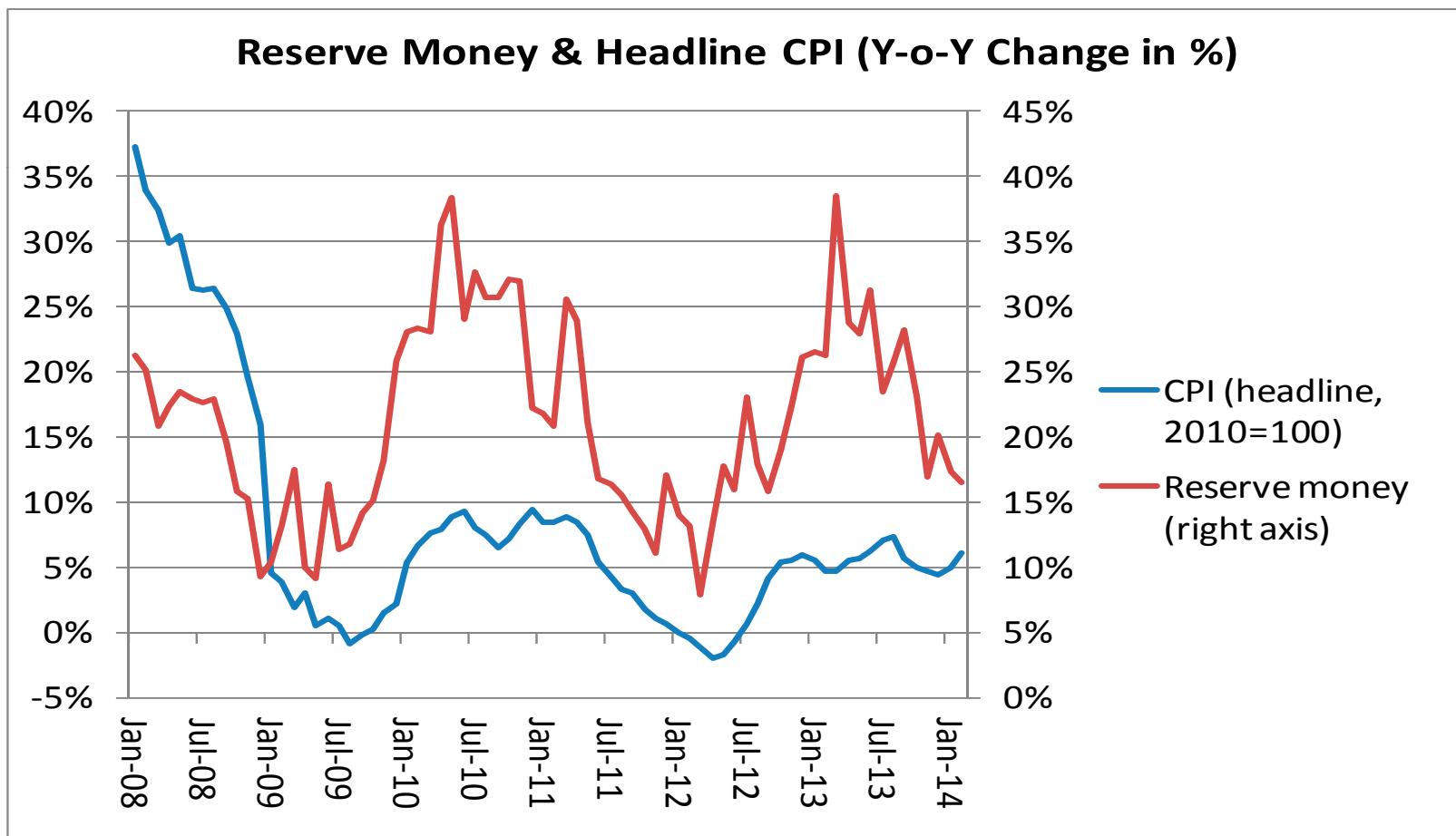
Historically, reserve money and broad money are also closely linked:

This opens possibility for central bank to influence prices via its control over reserve money and the broad money-price linkage



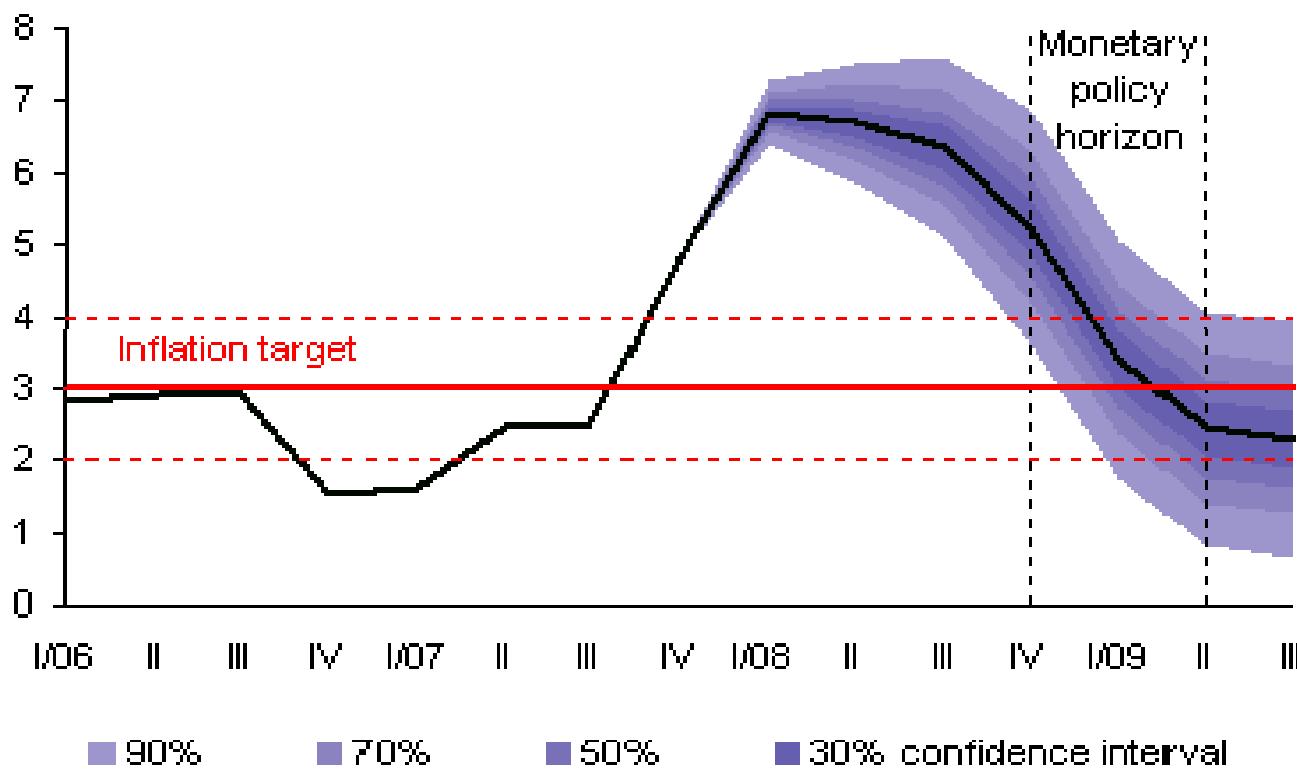
Monetary Framework in Myanmar

More recently, there is still a close link between reserve money growth and inflation:



Inflation Targeting Regime

Make a convincing case that inflation *forecast* is on track



Thank You!

In the next lecture, you are going to hear more about reserve money and the CBM balance sheet.