

# Inflation Targeting: The Czech Case

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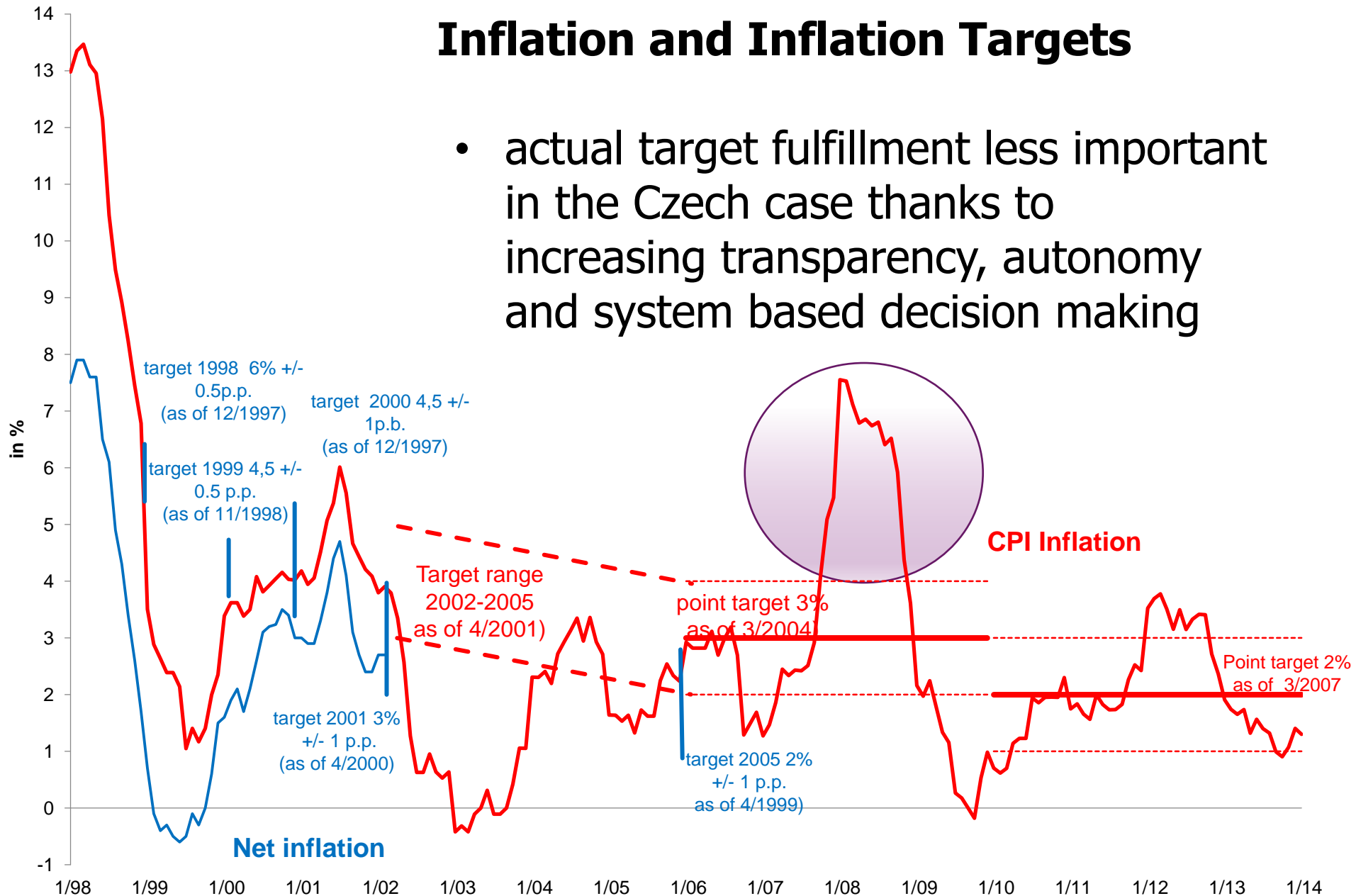


# Main issues

- **Inflation Targeting**
  - hitting or missing targets
  
- **Gradual development of the framework**
  - processes, decision making
  
- **Communication**
  - inherent part of inflation targeting

# Inflation and Inflation Targets

- actual target fulfillment less important in the Czech case thanks to increasing transparency, autonomy and system based decision making



# A sudden drop of inflation in 1998 ...

## Four options:

**1. Tůma joined the Czech National Bank**

**2. The Czech National Bank started to target inflation**

**3. Too tight monetary policy**

**4. Other**

# Monetary policy framework: milestones

- **definition of inflation: core/net vs headline**
- **setting up inflation target: declining path and price stability**
- **minutes of monetary policy meeting: desired picture vs mirror of discussion**
- **inflation report: gradual improvements/fine tuning**
- **model based decision making**
  - unconditional forecast (2002): support central bank's transparency/credibility
- **communication**

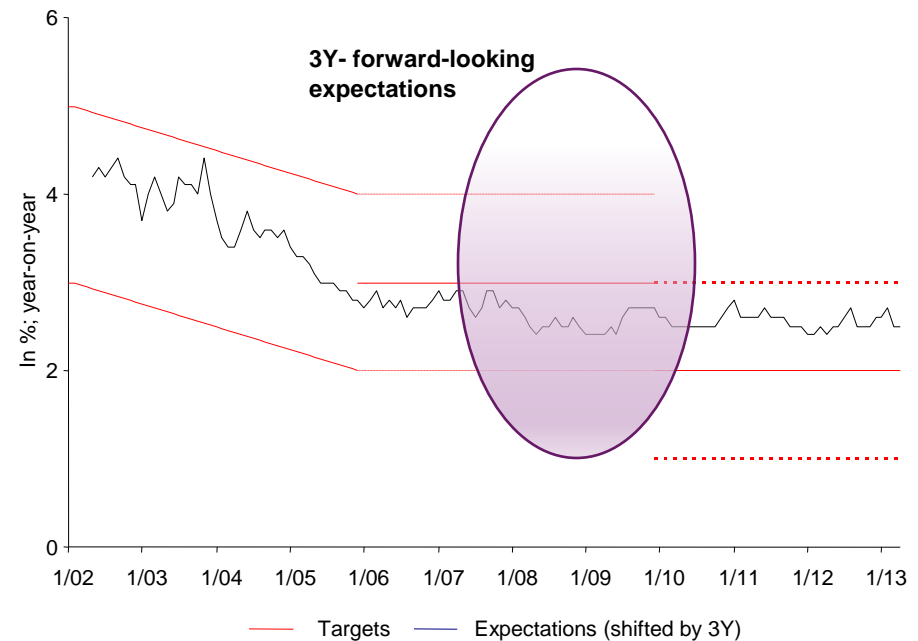
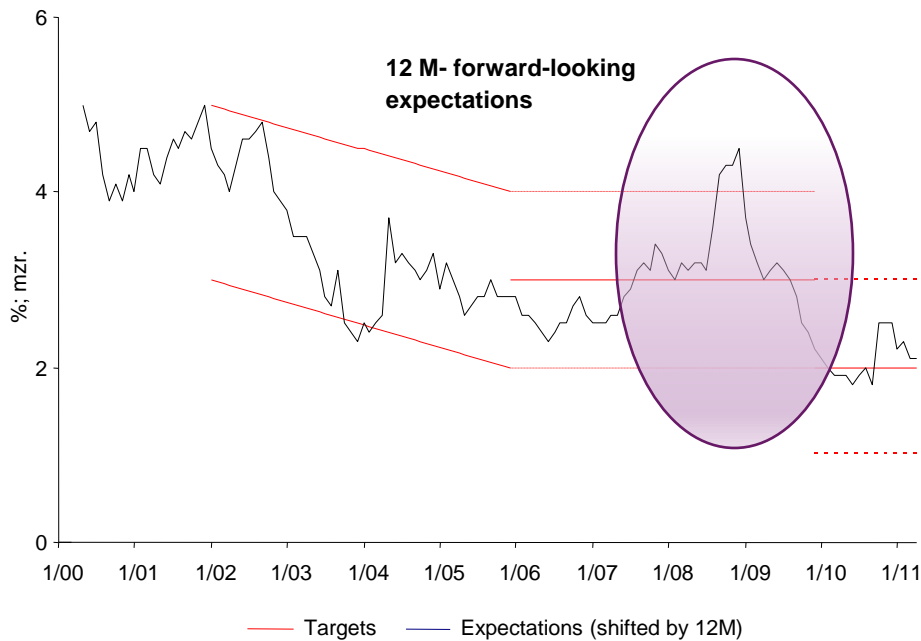
## **.communication**

- only verbal comments on interest and exchange rates paths (2002)
- publishing model based unconditional forecasts of interest rates (2008)
  - non-commitment emphasized
  - fan chartes to reflect uncertainty
- publishing model based unconditional forecasts of exchange rates (2009)
  - to provide a complete set of information for forecast users
  - staff projection – no policy intentions
- **winning arguments in favour**
  - full transparency for forecast users
  - improving policy transmission by affecting the yield curve
  - facilitating the Board' expression of a different opinion
- **individual votes published (2009 – till then, a vote tally only)**
  - pros and cons, number of questionmarks, see e.g. recent voting on forex interventions (November 2013)

# Reasons for high levels of dollarization

- **Historically unstable economic environment: high rates of inflations, sudden depreciations of the domestic money**
- **Monetary policy framework: heavy management over exchange rate developments**
- **Underdeveloped financial systems: low banking system penetration, no saving instruments**
- **Large interest rate spreads for loans in foreign and local currencies**
- **Large remittances inflows denominated in foreign currency**

# Achievements: Inflation expectations of analysts



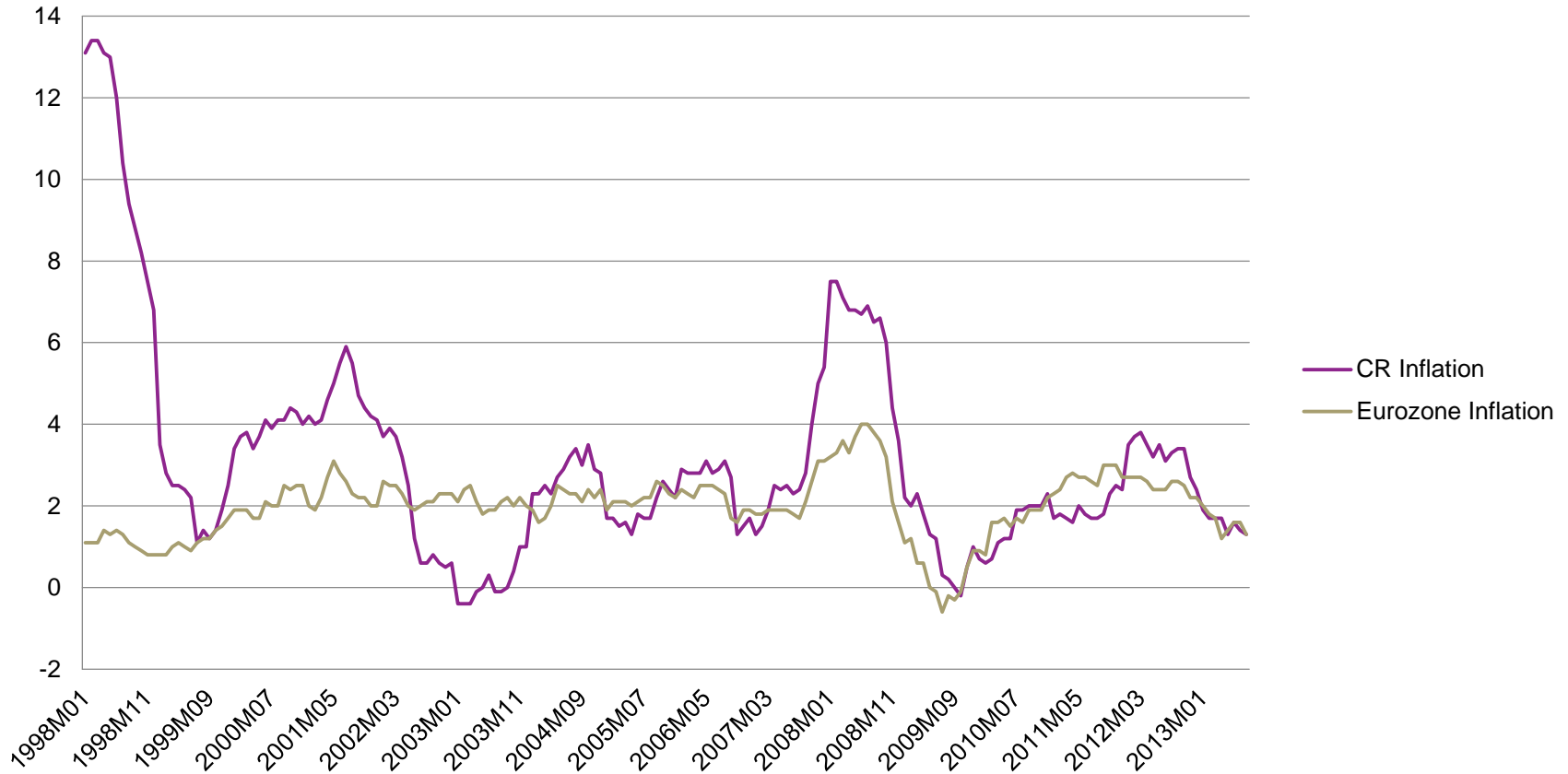
Source: CNB

- Long-term expectations were anchored regardless inflation volatility and target performance
- Adequate decision-making processes, improvement in the communication to the public and increase in transparency



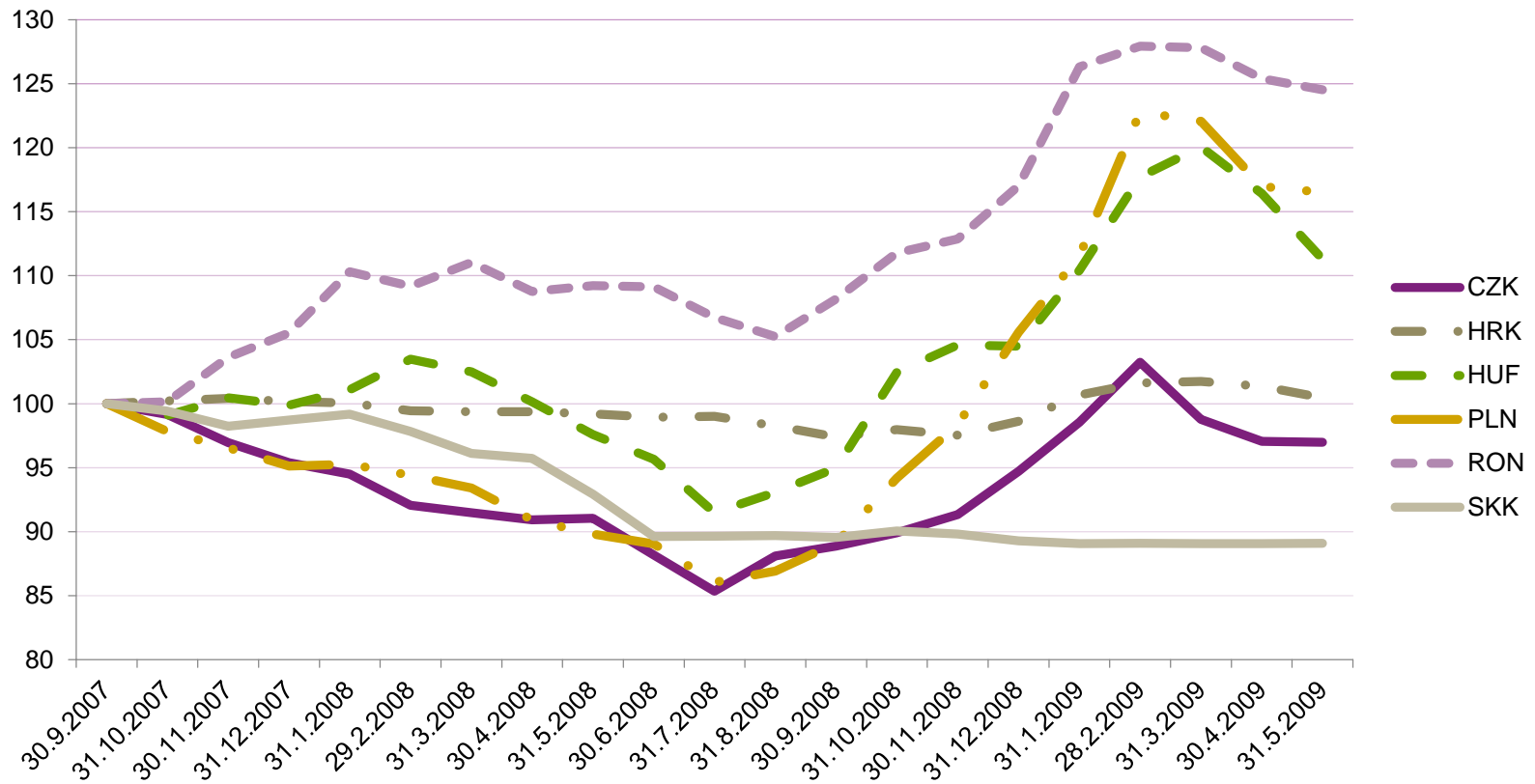
# Achievements: inflation convergence

## Inflation: CR and EZ



# Achievements: lower exchange rate volatility compared to peers

## Selected CESE Exchange Rates to EUR (normalized)



Source: Eurostat

# Lessons

- **Inflation Targeting is about missing targets inasmuch as about fulfilling them**
- **Missing the target gives opportunity to communicate the strategy and plans for bringing inflation back**
  - Fosters accountability and trust
- **Key is to keep inflation expectations on check**
- **Not to adjust targets in case of prolonged misperformance**
  - Inflation is at the end just a monetary phenomenon

**Thank you for your  
attention**





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