CENTRAL BANK'S COMMUNICATION –
A NEW REGIME INFLATION TARGETING CHALLANGE (THE CASE OF REPUBLIC OF MOLDOVA)

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Abstract:

In this article, we try to examine the definitive aspects of a transparent frame and credible capable to ensure anchoring inflation expectation, case that actually most central banks with inflation targeting regime have gambled. Making reference to Republic of Moldova, we can mention that from the moment of obtaining independence, Republic of Moldova has faced with the problem of high inflation, the cause that got milder once the national banking system reoriented of the inflation targeting strategy. The implementation of inflation targeted strategy has imposed a lot of challenges in the perimeter of National Bank of Moldova communication politics, because the success of this strategy is caused by the anchoring inflation expectations and therefore the credibility of institution. Starting with the other central bank's experience, we come with the remedies for improving the communication of National Bank of Moldova in order to achieve the inflation target.

Key words: inflation targeted system, communication, monetary policy, inflation expectations,

JEL classification codes: E31, E52, E58.

Introduction

Central bank's communication principles have evolved during a long period of time from one limit to another. If during the period of 1920-1944, Montagu, Norman - the Bank of England governor said (Holmes, 2013 p.68) "Never explain, never apologize" then later, Issing – the Bundesbank and European Central Bank's economist (1990-2006) emphasize the essential and indispensable role of the central bank's transparency, saying (2005, p.66): "Today, there is a general consensus among central bankers for the fact that transparency if not only an obligation for public entity. But also a real benefit of the institutions and its policies". The theoretic literature related to monetary policy outfitted the need of monetary policy communication (Blinder, 1998, Woodford, 2001, Bernanke, 2004, Blinder, Ehrmann, Fratzscher, Hann and Jansen, 2008). Blinder (1998, pp.70-72) support the idea that: "A more informative enhanced openness could enhance the effectiveness of monetary policy… [Because] the expectations related to the future behavior of a central bank's provides a vital link between long-term and short-term rates. A more opened central bank … provides market with the information about its views in the context of fundamental factors, which guides monetary policy … thus creating a viscos circle. By predictability of its behavior, central bank contributes to the creation of more predictable market reaction in the context of monetary policy. This in turn causes more enhanced economy management". And, Woodford (2001,p. 12) insist on the fact that successful monetary policy conditionality is not reflected in the management of overnight interest rates, but the management of inflation expectations, focusing of the primary role of central bank's transparency to achieve the objective of monetary policy. Guided by those judgments, central banks around the world over the last 20 years have increased the effort for communication to the general public, reiterating its importance for guiding public expectations.

To note that, central bank's communication depends on monetary policy regime that seeks to achieve the fundamental objectives of the bank. From figure 1 we can see that effective workability of the inflation targeted system implies also a more complex communication, diversified and broad overlapping with providing simple concise and authentic explanations, so as to give the central banks credibility and predictability, as well as repetition of the sent messages to obtain a better understanding among the general public.

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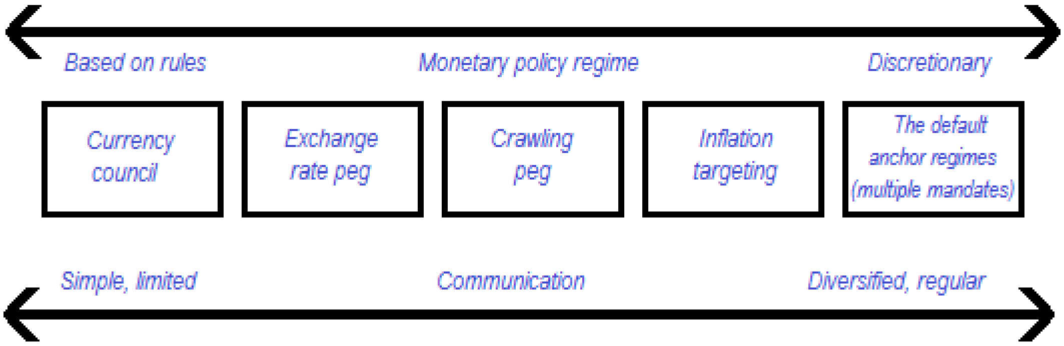
Figure 1 - Central Bank Communications in terms of monetary policy



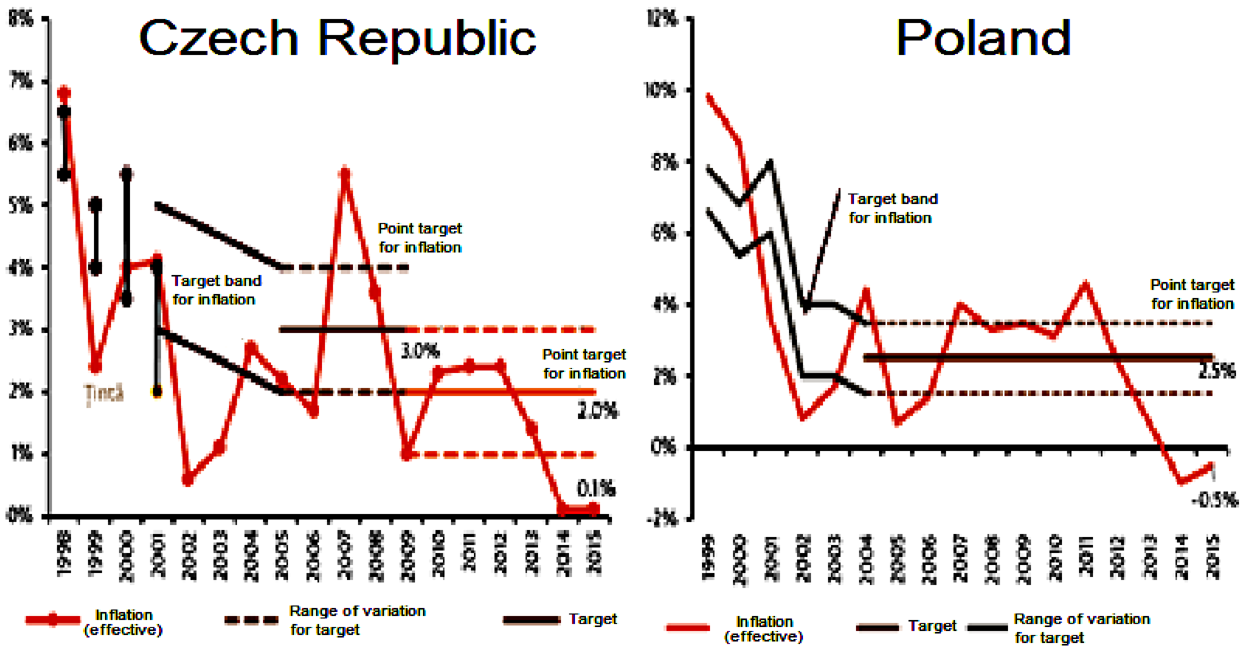
Source: made by the authod based on Blinder A., Goodhart C., Hildebrand P., Lipton D., Wyplosz C. (2001). „How do central banks talk?", International Central for Monetary and Banking Studies, Geneva Reports on the World Economy, 3, pp. 10-11

Compared to the strategy of targeting exchange rate and monetary aggregates, the inflation targeting strategy depending on internal circumstances permits monetary policy to react on internal shocks both external and internal, it enjoys of high independence, transparence and responsibility, those three pillars, gives the central bank's credibility and provides central bank with reputational gains while the channels and communicational tools used are exploited to its maximum.

Communication of Czech Republic and Poland's monetary policy towards the perspective of achieving inflation objectives.

In the 90's once with the rationale advantages of medium term price stability, central banks of Eastern and Central Europe have resorted to abandon various categories of exchange rate, monetary councils, intermediate targets for inflation targeting strategy, of which is the Czech Republic and Poland. In both cases, this strategy has marked flattering success form the very first years of implementation, fact confirmed by alleviation of inflationary and further positioning this close to the inflationary target (Figure 2).

Figure 2 - Czech Republic and Poland's Central Banks performance in achieving inflation objectives



Source: elaborated by the author based on central bank reports on inflation in Czech Republic and Poland.

Form the Figure 2, we can observe that the Central Bank of Czech since 1998 – the year the regime of inflation targeting strategy was implemented hasn't failed to effectively manage the inflation till 2015, and so annual inflation was positioned within the confidence interval of the inflationary target ten times. Polish Central Bank, with the implementation of the inflationary targeting strategy has managed to temper the inflationary process, thus the annual inflation rate has come to range around with a market horizon of only four times during 1999-2015.

However, in order to achieve its primary objective of maintaining price stability, the Central Bank of the Czech Republic and Poland have relied on the credibility and predictability, creating a transparent framework capable of providing an effective communication policy. In this order, in both cases Inflation Report - published quarterly, was the mainstay of communication with the public. The difference according to the country was marked by the fact that the Czech Central Bank has been publishing quantitative forecast of inflation from the first reports, and in case of Poland starting with 2004, until then the Central Bank included only consideration of the likelihood of meeting the inflation target.

To mention that, the NBP develops two reports (Monetary Policy Council obligation under art. 227 of the Constitution of the Republic of Poland), called Policy guidelines and report on the implementation of monetary policy. The first contains a characterization of internal and external factors that confronts monetary policy, short-term objectives of monetary policy and, respectively, the tools to be used to achieve these objectives. While the second contains a performance assessment in achieving the inflation target, a description of macroeconomic conditions and monetary policy tools used to ensure the fundamental objective. Those tools of communication contributes to a greater understanding of monetary decisions and reception by the general public of causal link between what was proposed and what was achieved by actions of the monetary authority to achieve its primary objective. And last but not least it contributes to increased central bank accountability for its actions, although BNP status is devoiced of any provisions related to sanctions to be applied or justification for the deviation from the target, such as the Bank of England. Central Bank of Poland and the Czech Republic are transparent in dealing with macroeconomic forecasts (Table 1).

Table 1

Forecasted macroeconomic indicators, subject to publication

Indicators	Czech	Poland
Inflation (quantitative)	+	from 2004
Gross domestic product (quantitative)	+	+
Exchange rate (nominal)	2009-2013	-
Interest rate (quantitative)	3M PRIBOR	WIBOR
Labour market indicators (quantitative)	-	+
Macroeconomic forecasting model	-	+

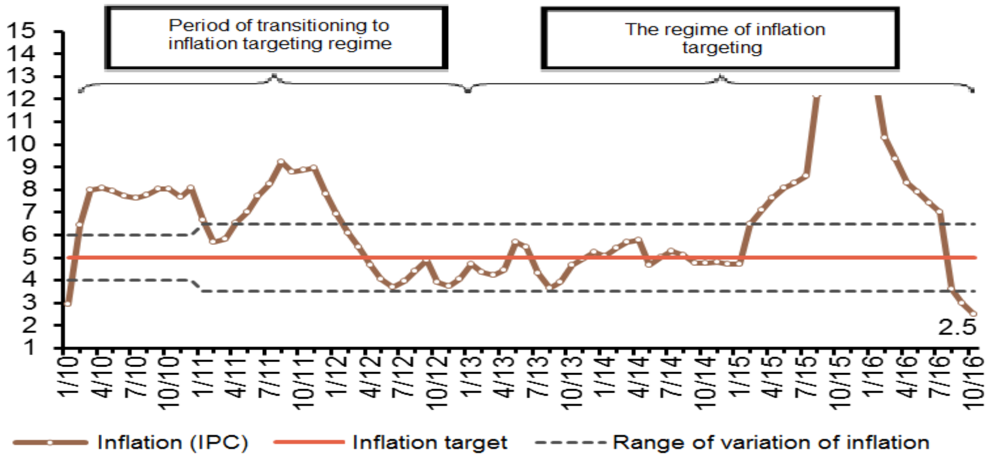
Source: elaborated by the author based on central bank reports on inflation in Czech Republic and Poland.

The monetary policy council meetings, personal choices of members, press releases and transcripts after every meetings, various educational projects, a number of publications, researches and case studies argued the understanding of the issues reflected in the monetary policy strategy of general public in both countries, thus contributing to improving the monetary policy transparency and anchoring inflation expectations respectively towards achieving the inflation target by analyzed central banks.

Inflation strategy management evaluation in Republic of Moldova under the monetary policy's transparency.

Referring to Republic of Moldova, we can find that the monetary policy authority's most important aim starting with 2006 is ensuring and maintaining price stability, at the same time, NBM is advocating for a healthy, stable financial system and economic policy support, without detriment to its fundamental objective. Transition to a inflation targeting strategy in 2016, have imposed a series of challenges in the action area of communication policy of the National Bank of Moldova, given the fact that before declaring the inflationary target system, NBM managed national inflation level by targeting monetary aggregates regime, that do not involve complex, systematic and diversified communication depending on the tools applied and targeted groups.

Figure 3 - National Bank of Moldova's performnce in achieving ionflation objective from the transition to inflation targeting regime.



Source: prepared by the author based on NBM monetary policy strategy and National Bureau of Statistics of Republic of Moldova statistical data.

During the transition to the inflation targeting system were created prerequisites for the implementation of the scheme itself, which also include placing the annual inflation rate in the corridor of variation target during 2012, continuing this trend until early 2015 as can be seen in figure 3, along with strengthening the independence of NBM, exchange rate flexibility, and last but not least – increase of NBM credibility from the public regarding the monetary policy transparency. In this context, under the realization process of tasks stipulated in the monetary policy strategy, as a result of reorientation to a inflation targeting regime, NBM has introduced new communicational tools, fact confirmed by the publication of Board meeting administration schedule (since august 2015 – Executive Committee) of NBM on monetary policy promotion, inflation report calendar publication (in 2010, Monetary Policy Report), alike the monetary policy operations balance. In order to ensure decision making process more transparent, NBM public after each meeting press releases about the monetary decisions. Develops press releases related to evolution of inflation level, with inflationary determinant factors. To mention that, the publication of reports on inflation are preceded by conferences with NBM governor and media representatives. We note that, National Bank of Moldova is reserved at the chapter of forecast indicators, only providing quantitative forecast on inflation and provide reflections related to the deviation of GDP. Table 2 reflects the defining characteristics of transparency in decision making process related to NBM monetary policy.

Table 2

Strenghts and weakneses of National Bank of Moldova in the context of monetary policy decisions

Arrangements for providing information related to monetary policy decisions	NBM
1. Decisions related to interest rate changes are anounced immeditely	Yes
2. Statements related to decisions that foresee any changes.	Yes (press release)
3. Minutes of committee meeting on monetary policy	Yes (after 6 months)
4. Official minutes to provide on formation about:	
- internal debate	Yes
- member's personal opinions	No
- personal choices of member's votes	No
5. Transcripts of the meets are available to the public after: (years)	No

Source: prepared by the author according to Blinder A., Goodhart C., Hildebrand P., Lipton D., Wyplosz C. (2001). „How do Central Banks talk?", International Central for Monetary and Banking Studies, Geneva Reports on the World Economy, 3, p. 48

Conclusions

Literature and international practice have demonstrated the indispensable role of central bank communication in order to achieve proposed objectives. Related to the case of Republic of Moldova, we consider that communication strategy within the NBM is one effective but incomplete in terms of tools and communication channels that need to be optimized in order to achieve the basic objective of ensuring and maintaining price stability. It is necessary to keep in mind that taking an international practice form the communication perspective, it is important to adjust this to the institutional and operational autochthonous specific in the context of inertial character of Moldovan economy, moderate financial education of the general public so as to avoid any excessive fluctuations on financial-currency market and speculative actions.

In this context we recommend organizing press conference after each monetary policy decisions explaining the fundamental decisions, thereby enhancing the understanding of the interplay between macroeconomic developments and NBM actions.

To increase the transparency and credibility of NBM, NBM is welcome to take responsibility in case of deviation from the basic objective through the immediate publication of the explanations along with a list of actions to be taken toward bringing inflation to its level. Supporting financial education by launching a project whose target audience is made up of students of economic faculties of major universities, teachers and doctoral students.

Only a flexible framework for communication with pro-active approach, extensive explanations of vision and bank strategy will build a predictable economy environment, and ultimately will help achieving the NBM objectives proposed

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