In cooperation with

National Bank of Ukraine

German Economic Team

10|2022

POLICY BRIEFING UZBEKISTAN

Communication of Monetary Policy Decisions: Process And Substance

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Inflation targeting is the management of expectations ...

"Say what you are doing and do what you are saying"

Streamlining the Central Bank's decision-making system on the basis of the macroeconomic forecast

Announcing the target, conducting transparent and clear policy aimed at achieving it

Achieving a target, anchoring expectations

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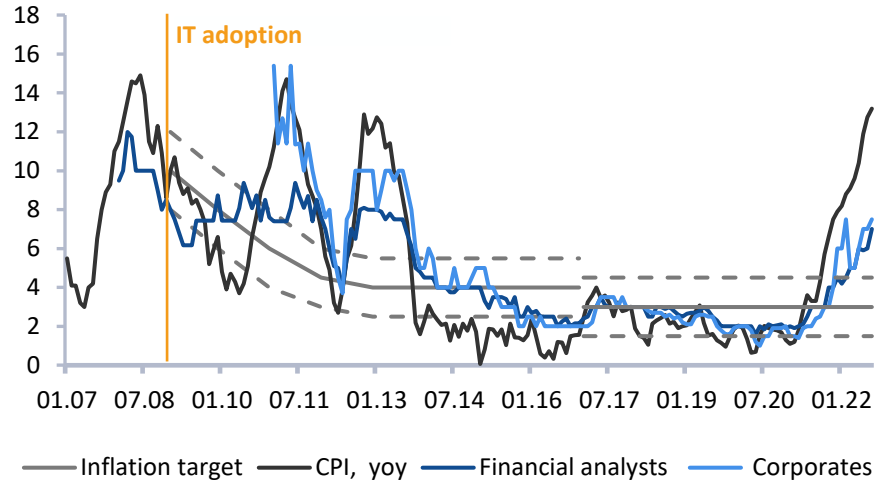
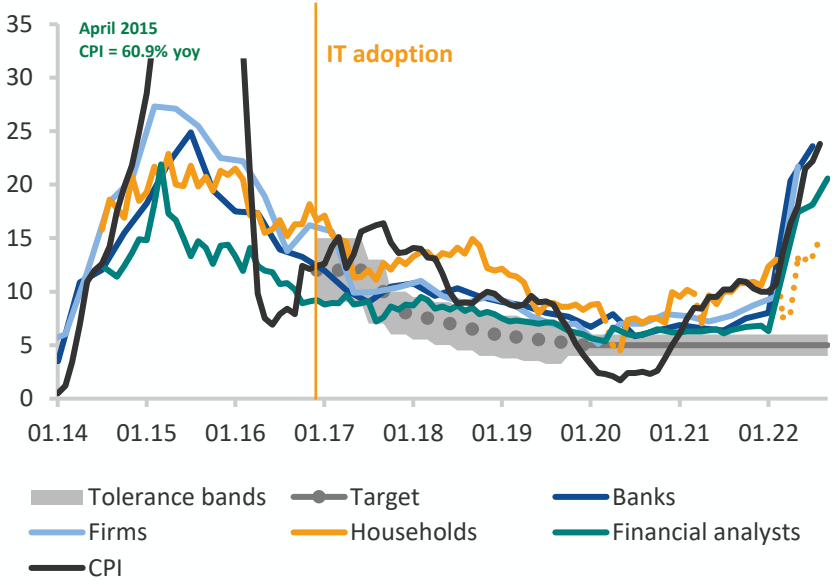
… and as a result – actual inflation

Serbia: CPI, inflation target, inflation expectations



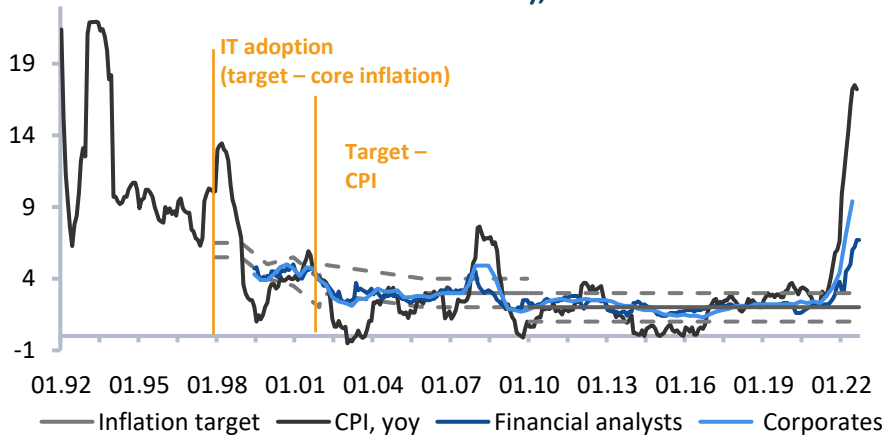
Source: National Bank of Serbia

Ukraine: CPI, inflation target, inflation expectations



** The dotted line indicates a change in the method of survey to a telephone interview.*
Source: NBU, GfK Ukraine, Info Sapiens.

Czech Republic: CPI, inflation target, inflation expectations (12-month-ahead), %



Source: Czech National Bank

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Why does central bank communicate?

Transparency is the cornerstone of the **inflation targeting regime, because…**

- Transparency enhances MP predictability and reduces economic and financial uncertainty
- Transparency is a tool to anchor inflation expectations
- Transparency is an element of accountability (given CB independence)

MONETARY POLICY EFFECTIVENESS

Principles of central banks` communication policy

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Principles of central banks` communication policy

- Communications regarding monetary policy should be aimed at increasing understanding and confidence in it and forming a predictable economic environment for all economic agents
- Central bank must disclose information regarding aims, principles, measures and results of monetary policy, assessment of economic stance and prospects of its development as quickly, fully and accessible as possible

PRINCIPLES OF NBU'S COMMUNICATIONS	
Effective transparency, proactivity, regularity and equal access	– results and reasoning of the decisions made are announced via press releases publishing and at press briefings (hold on the day of decision-making), as well as via publishing the Summary of Key Policy Rate Discussion by NBU Monetary Policy Committee (on the 11th day after the monetary decision) – meetings of the NBU Board on monetary policy issues are held according to a schedule announced in advance
Targeting and comprehension	Multi-level approach to different target audiences with different level of economic awareness is implemented to communicate monetary decisions
Forward-looking	Every press release on monetary decision includes a forward guidance regarding monetary policy prospects. The key policy rate projection (not a commitment of the CB) is announced quarterly as a part of macroeconomic forecast
Responsibility	– the first press release of the every calendar year informs about current level of inflation and its compliance with the inflation target, causes of its deviation (if exists) and the impact of monetary policy decisions made on price dynamics – NBU Inflation Update is published monthly. It informs about current level of inflation, its compliance with the forecasted level, causes of deviation (if exists) from the forecast

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The NBU's 'routine' monetary policy decision-making cycle

Stage 1 — Conducting of working meetings

The NBU staff prepares analytical materials regarding the current economic state, baseline and alternative forecast scenarios (quarterly) and staff proposal on key policy rate → basis for monetary policy decision-making

↓

Stage 2 — 7-day silence period on monetary policy

The silence period is intended to prevent public speculations around an upcoming MP decision of the NBU

↓

Stage 3 — Meetings of the Monetary Policy Committee

MPC serves as a forum for discussions, opinions exchange and reaching consensus

↓

Stage 4 — Meetings of the Board of the National Bank on monetary policy issues

Monetary policy decision

↓

Stage 5 — Announcement and communication of monetary policy decisions

Explanation of the decision made by the NBU Board

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Process of MP communications is strictly linked to MP decision-making cycle

Thursday, 14.00

NBU Leaves Its Key Policy Rate Unchanged at 25%

Press release and press briefing on the monetary decision:

- ✓ brief analysis of the current situation
- ✓ decision motivation
- ✓ expected future policy

quarterly

Thursday, on the 7th day

Inflation Report

The NBU's vision of the current and future state of Ukraine's economy **with an emphasis on inflationary development**

Monday, on the 11th day

Summary of Key Policy Rate Discussion by NBU Monetary Policy Committee

The impersonalized view of the MPC members regarding a monetary policy decision, and **the corresponding argumentation** not only of the majority of the MPC members, but also alternative opinions

quarterly

Tuesday, on the 12th day

Meeting with experts

Discussion of the forecast and the Inflation Report

"... central bank should be 'boring' "

King (2000)

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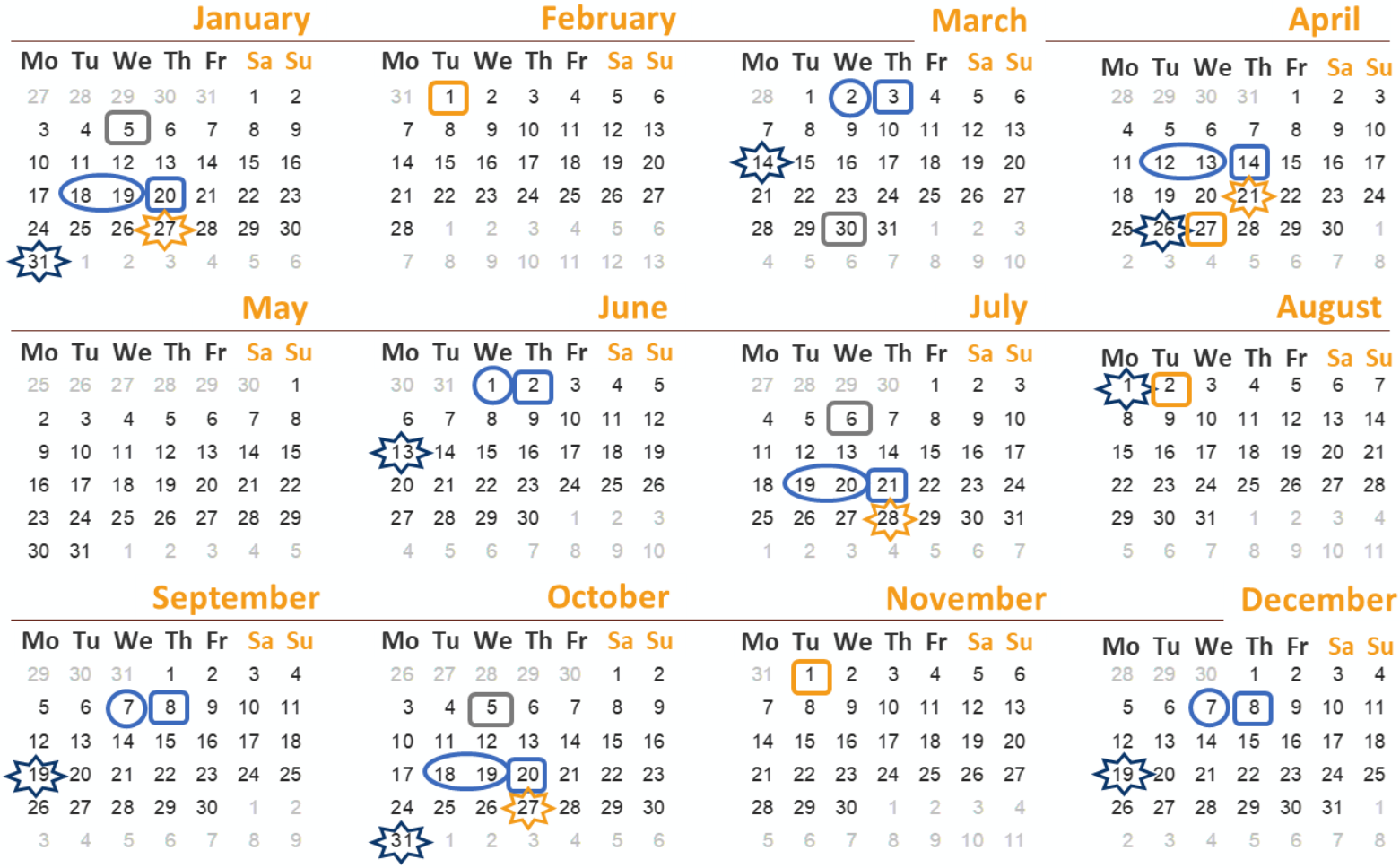
Meeting of the NBU Board on Monetary Policy Issues are held according to a pre-announced schedule

2022



- Preliminary forecast presentation
- Inflation Report
- MPC meeting
- Inflation Report and forecast discussion with experts
- Meeting of the NBU Board on MP issues
- Summaries of the discussion on the key policy rate at the MPC

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Roles and timing of MP communications preparations are assigned in advance

Week before MPC meeting

Wed (till 4 PM)
MPEAD + CD
Discussing and preparing key messages of **press release**

Fri (till 3 PM)
MPEAD + CD
Preparing key messages and additional information for **press release**

Wed (till 6 PM)
CD
Information field analysis in order to prepare questions for **Q&A list**

Thu (till 3 PM)
CD
Preparing **Q&A list** and sending it to DMPEA

Fri (till 6 PM)
MPEAD + CD
Preparing answers for **Q&A** within the competence of Departments

MPC meeting week

Mon (till 2 PM)
MPEAD
Preparing the draft **press release**
Sending to CD answers for **Q&A**

Mon (till 4 PM)
CD
Elaboration of draft **press release**

Mon (till 4 PM)
MPEAD + CD
Approval of draft **press release**

Mon (till 6 PM)
CD
Consolidation and finalization of Q&A

Tue (till 6 PM)
CD
Updating **Q&A** if needed

Wed (4-6 PM)
MPEAD + CD
Final approval of draft **press release**, preparing its alternative versions

Wed (till 7 PM)
CD
Sending draft **press release** and **Q&A** to the Board and for preliminary translation

Thu (till 8 AM)
CD
Sending alternative press **release versions** if exist to the Board and for preliminary translation

Thu (till 11:30 AM)
MPEAD + CD
Finalization of **press release** according to the Board`s opinion and sending it for translation

Thu (till 12:30 PM)
OEIIP
Translation of **press release**

Thu (till 12:45 PM)
MPEAD + OEIIP
Approval of English version of **press release**

Thu (till 1 PM)
CD
Preparing **press release** (Ukr and Eng) for embargo procedure with journalists, press briefing and publication on the website

***MPEAD** - Monetary Policy and Economic Analysis Department*

***CD** - Communications Department*

***OEIIP** - Office for European Integration and International Programs*

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Monetary cycle communications

(MPC meetings, at which new macroeconomic forecast is approved, shown in orange)

A week before the briefing

- Start of the "silence period" (14:00 Thu)
- Preparation of Q&A
- Preparation of the press release outlining the NBU Board's monetary policy decision
- Preparation of the Governor's speech

During the briefing week

- Monetary Policy Committee meeting (Tue / Tue-Wed)
- Sending invitations to journalists (Tue)

On the briefing day (Thu)

- 10:00–12:00 Meeting of the NBU Board on monetary Issues
- 12:00 Publication of the briefing announcement
- 13:00-14:00 Carrying out an embargo with information agencies
- 14:00 Start of the press briefing on monetary policy
- 14:00 Publication of the monetary policy decision
- 14:10 Publication of the Governor's speech
- 17:00-20:00 Publication of the Q&A session results

After the briefing

- Preparation of the MPC members discussion results and the Inflation Report release
- On the 6th day (Wed) after the briefing – sending the invitations to the experts for a meeting
- A week after (Thurs) the briefing – publication of the Inflation Report and the accompanying release
- On the 7th-8th day (Thu-Fri) after the briefing – sending the results of the quantitative evaluation of the effectiveness of monetary decision communication
- On the 11th day (Mon) after the briefing – publication of the Summary of Key Policy Rate Discussion by NBU MPC
- On the day 12 (Tue) after the briefing – a meeting with Ukrainian (10:00-11:30) and international experts (18:00-19:00)

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The structure of press release remains constant

The key policy rate level	The Board of the National Bank of Ukraine has decided to keep its key policy rate at 25% per annum from July 21, 2022
Brief analysis of the current situation	The war caused a disruption of supply chains, a decrease in supply of some goods, higher business expenses, physical destruction of production facilities and infrastructure, and temporary occupation of some territories. Persistently high energy prices and record-high inflation in partner countries also fueled price pressures in Ukraine… …As a result, inflation has been growing rapidly over the last months, reaching 21.5% yoy in June. The price growth was unevenly spread geographically: inflation peaked in territories that were temporarily occupied or close to combat areas
Quarterly → Forecast	» Inflation pressures will persist: inflation will exceed 30% yoy as of the end of 2022 » The economy of Ukraine will shrink by a third in 2022 but will return to growth in 2023–2024 if the Black Sea ports are unblocked » Despite showing a temporary surplus thanks to international aid, in future, the current account will return to deficit on the back of the economy's high need for imports, including imports for recovery
Risks	**The key risk** to the forecast is that the war of liberation against the russian invaders will last longer. **Other inflationary risks** have decreased in the short term since the NBU Board made its key policy rate decision in July. However, they remain significant in the long-term.
Decision motivation	In view of the **protracted period of significant pressures on prices and the prevalence of inflationary risks on the forecast horizon, coupled with the need to ensure the attractiveness of hryvnia assets and maintain exchange rate stability**, the NBU Board decided to keep the key policy rate unchanged, at 25%
Key policy rate forecast (forward guidance)	The baseline scenario of the macroeconomic forecast envisages that the key policy rate will be maintained at 25% at least until Q2 2024. At the same time, the balance of risks to the key policy rate forecast is assessed as having shifted upwards. If these risks materialize, **the NBU could raise its key policy rate and interest rates on its monetary operations beyond their current levels in order to safeguard monetary stability and to ensure inflationary processes remain under control**

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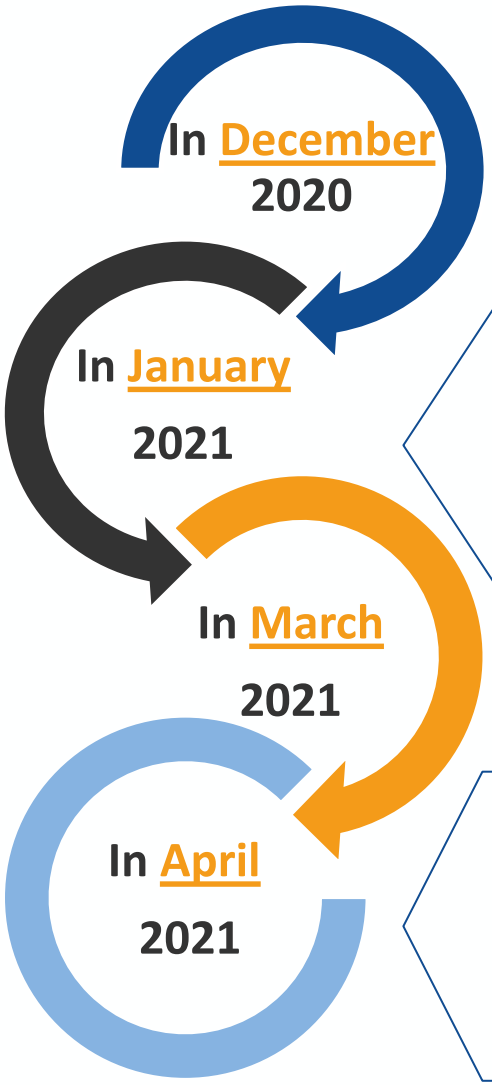
The forward guidance in the press releases explains the factors that may drive the next decision

Since July 2019, the NBU commenced quarterly publication of forecasts of its key policy rate



Looking ahead, the NBU's monetary policy will mainly depend on how the pandemic develops and how high inflation risks are. If the epidemiological situation stabilizes quickly, the economy will continue to revive, accompanied by a moderate increase in inflation. The main stimuli will be provided by fiscal policy, including by an expected rise in the minimum wage. That said, the NBU, while conducting a loose monetary policy, stands ready **to raise its key policy rate** in response to accelerating inflation on the back of a revival of the global and Ukrainian economies

The NBU stands ready to raise its key policy rate in future to bring inflation back to its target. The NBU takes into account the worsening of inflation expectations that occurred in late 2020, as well as stronger underlying pressures on prices arising from consumer demand. If the impact of these factors continues to increase and is not offset by other factors, such as a large capital inflow, the NBU will **raise its key policy rate**. This will enable the central bank to curb the rise in inflation in 2021 and bring inflation back to its target in 2022

The NBU stands ready **to raise its key policy rate more resolutely** in order to curb fundamental inflationary pressures, stabilize expectations, and bring inflation back to its target

The NBU's baseline forecast envisages that the key policy rate will remain unchanged, at 7.5%, until the end of 2021. Given current inflationary movements, this should suffice to bring inflation back to its 5% target in H1 2022. However, if underlying inflationary pressures rise more noticeably than currently expected, and if inflation expectations worsen, **there could be the need for further tighter monetary policy tightening.** The NBU stands ready to continue raising its key policy rate to a level that will bring inflation back to its 5% target in H1 2022

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Preparations of regular, occasional communications and interviews

Communications Department initiates interview or accepts the proposal from media

Communications Department shapes the request and asks **Monetary Policy and Economic Analysis Department** for materials

Monetary Policy and Economic Analysis Department prepares content

Communications Department edits the content and accompanies the speaker or sends content to website

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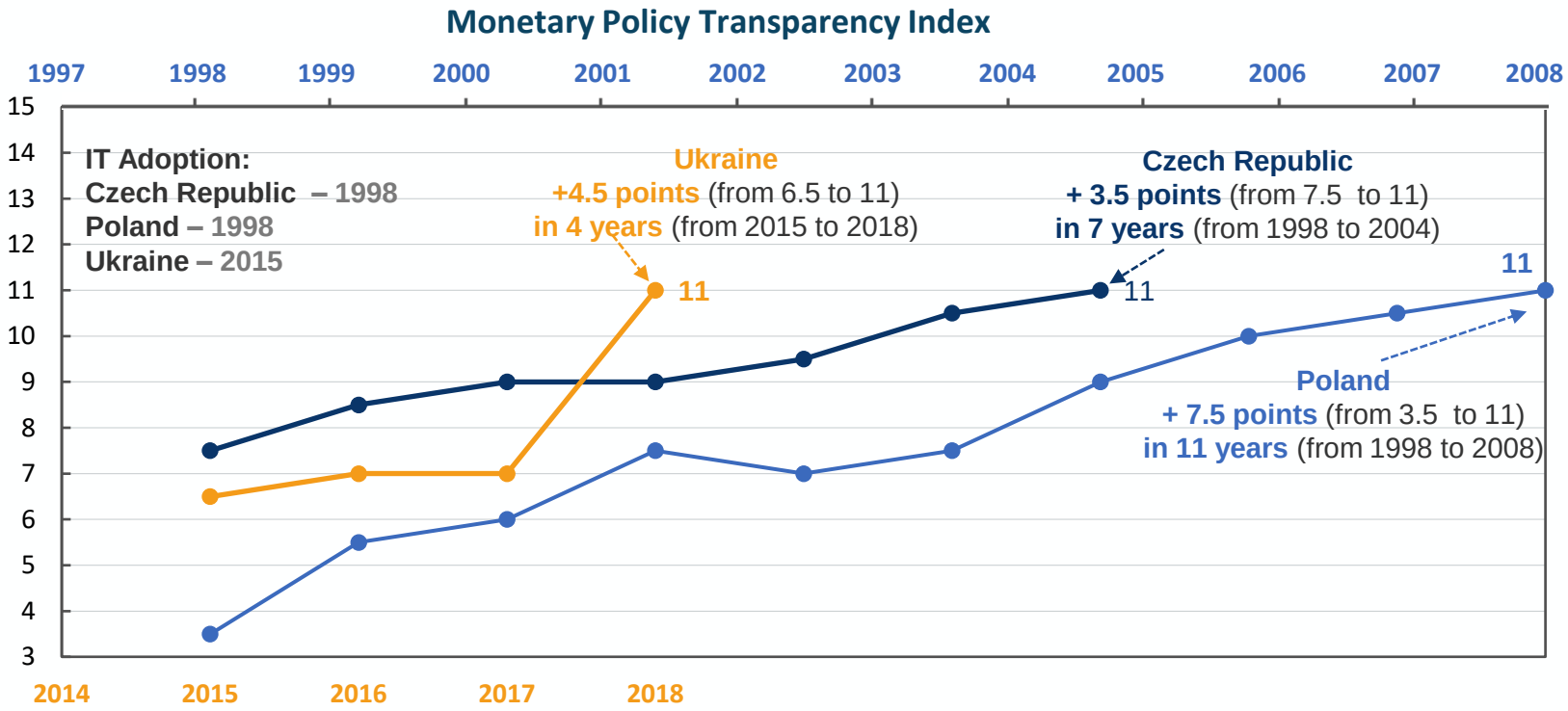
Central banks in emerging economies may benefit from tapping existing experience in central bank communication and transparency



Source: Dincer/Eichengreen/Geraats Central Bank Transparency Data for 1998-2019.

The NBU, following the examples of leading central banks on targeting inflation, has an opportunity to minimize the time lag between IT adoption and achieving a high level of monetary policy transparency

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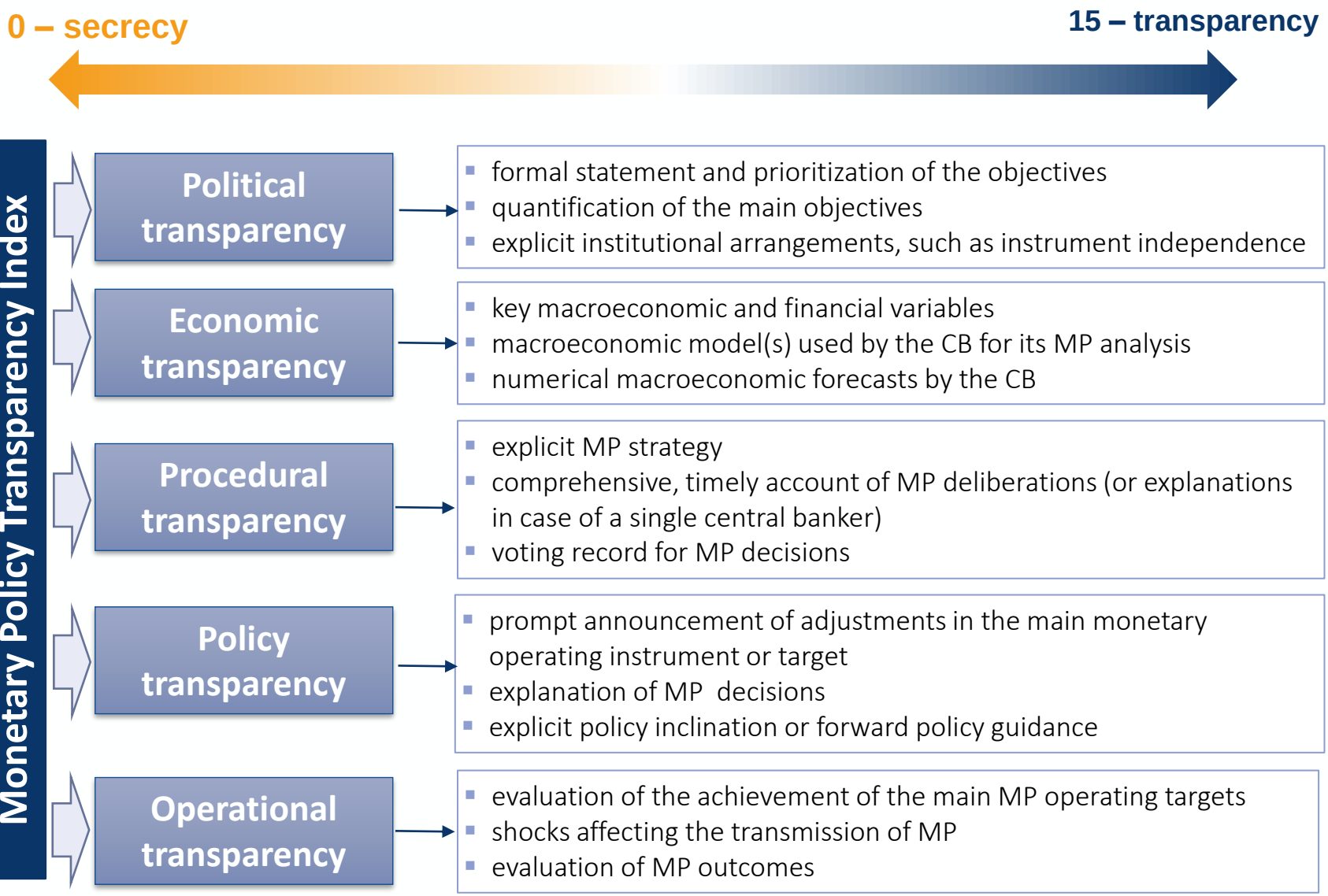
Quantitative assessment of CB's transparency (Dincer, Eichengreen, Geraats)



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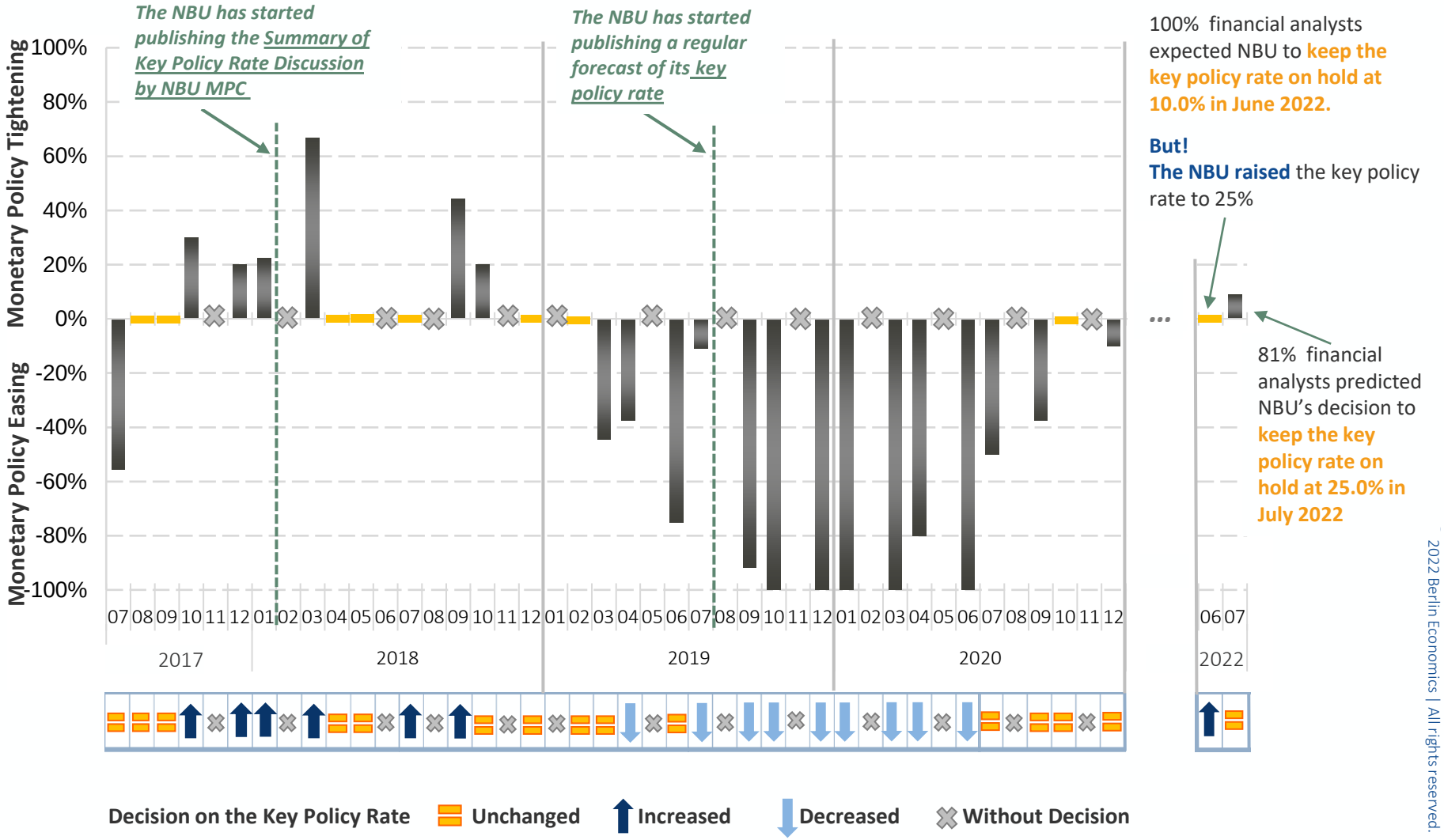
The more transparent MP, the better understanding of forward guidance and reasons behind decisions

Survey of financial analysts: "What changes in monetary policy do you expect?"



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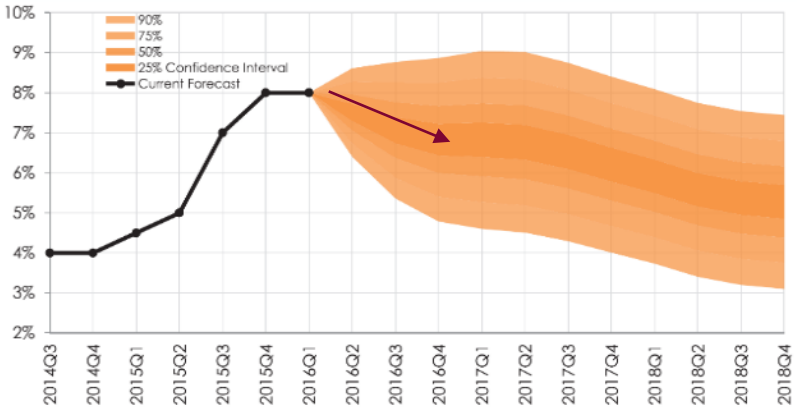
Publication of the key rate forecast affects the yield curve

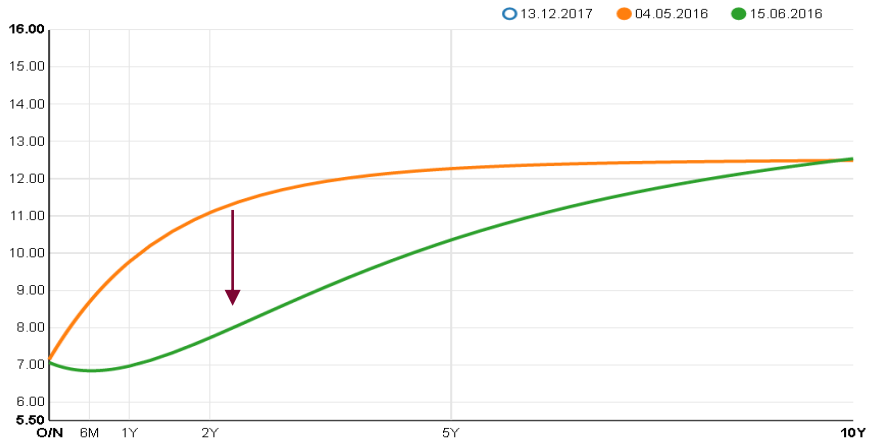
Case of Georgia

Forecast of the NBG key policy rate (IR, May 2016), %



Source: The National Bank of Georgia

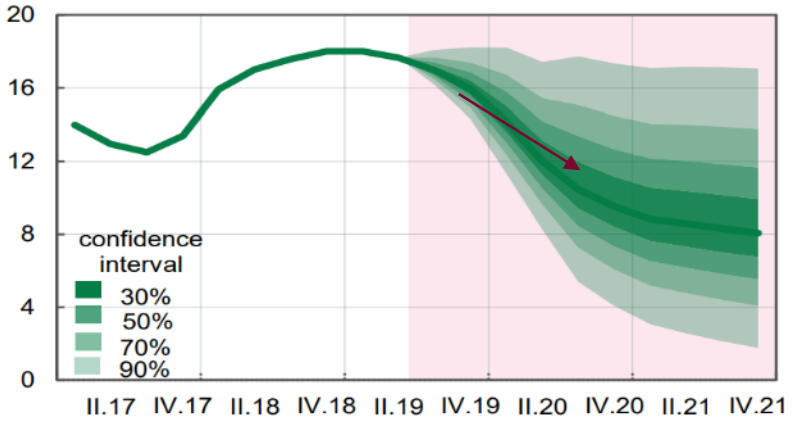
Yield curve



Source: The National Bank of Georgia

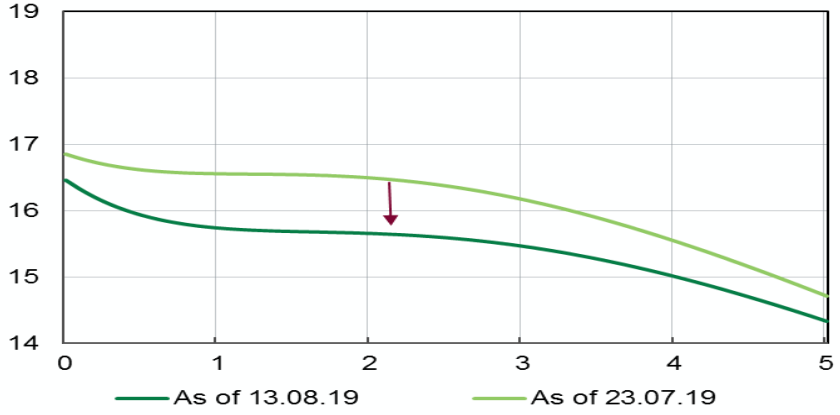
Case of Ukraine

Forecast of the NBU key policy rate (IR, July 2019), %



Source: The National Bank of Ukraine

Yield curve



Source: The National Bank of Ukraine

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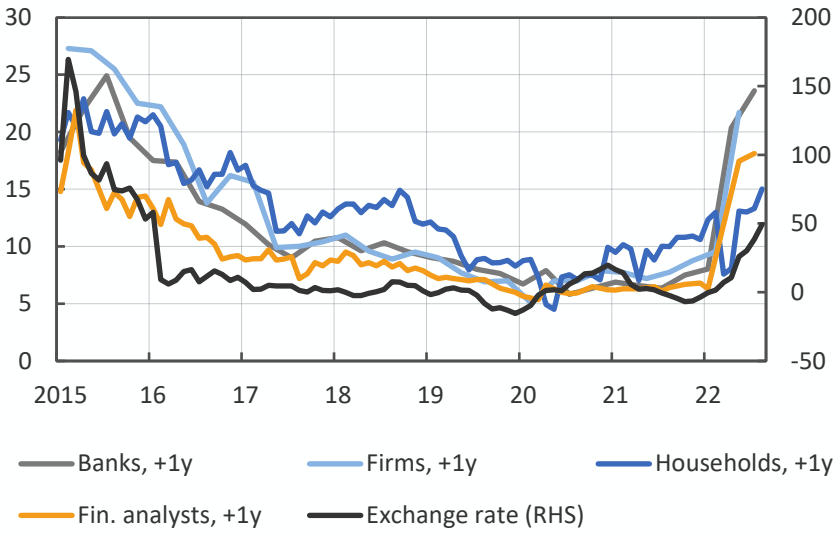
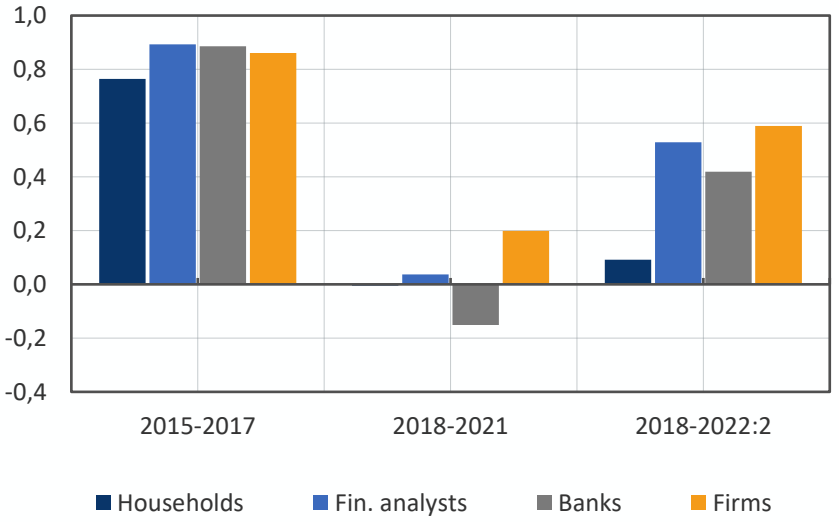
The ER in a small open economy matters a lot
Smoothing the ER volatility – minimizing shocks to expectations – more anchoring – more mature and stable FX market

Short-term inflation expectations and cash UAH/USD exchange rate, % yoy



Source: NBU, NBU staff calculations

Correlation between cash ER and short-term inflation expectations



Source: NBU, NBU staff calculations

» Coibion, Gorodnichenko (2015): One potential advantage of this signaling role of exchange rates for Ukrainian policy makers is that, unlike gasoline prices, the exchange rate is at least somewhat under their influence, so attempts to stabilize the exchange rate could have an unusually large positive externality through stable inflation expectations

Source: NBU, NBU staff calculations

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How to re-anchor expectations from Exchange rate to Inflation

- Clear commitment to inflation target and communication campaign on the topic
- Regular explanation of inflation dynamics
- Publications with massages that inflation is really important for welfare (instead of ER)
- Avoid any commitments regarding ER, solely commitment to inflation target
- Avoid forecasts and comment regarding ER dynamics, solely regarding the general situation on FX market

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Mechanisms that ensure effective and comprehensive coordination of monetary and other economic policies

1. **Financial Stability Board**
   (co-chaired by the Governor of the NBU and the Minister of Finance)

   Meetings → Take place regularly (at least once a quarter), on these meetings significant for financial stability issues are discussed

   Topics for discussions → Public finance risks, as well as coordination of the monetary and fiscal policy measures in the interests of macro-financial stability

2. **Regular high-level working meetings** between representatives of the NBU and the government, ministries, agencies; participation of the NBU's representatives in the Government working groups and commissions

3. During each forecast cycle, **NBU staff holds working meetings** with ministries' staff (Ministry of Economy, Ministry of Finance). **Purposes of such working meetings are:** to strengthen horizontal communications, exchange opinions, discuss any specific topics which depends on the possible behavior of the government and to detect weak spots of the CB's forecast

4. Preparation of proposals for projects of **strategic, program and planning policy documents** of the Government, as well as the Government draft laws

5. Preparation of recommendations regarding the **projects of the Budget Declaration and the State Budget of Ukraine**

6. Participation of the NBU in **fiscal risks assessment**

7. Regular communication between staff of the NBU and the Ministry of Finance regarding **operations on the money market and the capital market**, etc.

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Accountability of the NBU to the President of Ukraine and the Verkhovna Rada of Ukraine

The NBU is accountable to:

The Verkhovna Rada of Ukraine, once a year	➡	Report of the NBU Governor on **the NBU's activities** (every year, no later than May 1)
The President of Ukraine and the Verkhovna Rada, once a year	➡	» **Annual report on the conduct of monetary policy for the previous year** » **By March 1** the NBU provides approximate information on the calculation of the part of the projected profit before distribution, which will be transferred to the state budget, for the next three years; **by March 15** – forecast monetary indicators and indicators of exchange rate policy, for the next three years; **by April 15** – detailed information on the projected profit for distribution, for the next three years
The President of Ukraine and the Committee of the Verkhovna Rada, once a quarter	➡	**Information on non-cash issuance** (namely information on conducting bank refinancing operations, on carrying out interventions on the interbank foreign exchange market and on carrying out operations on the stock market)
The Government (the Cabinet of Ministers of Ukraine), on demand	➡	**Information on non-cash emissions and on monetary developments and money market**

According to Article 53 of the NBU Law, **any interference of the public authorities**, other public institutions or their officials, **any legal entities or individuals in the exercise of functions and powers** of the NBU, NBU Council, NBU Board, or NBU employees **shall be prohibited**, except for within the limits stipulated by the Constitution of Ukraine and the NBU Law.

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