Inflation Targeting With Special Review on Appliction in Serbia

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Summary: Inflation targeting represents monetary regime primarily applied in New Zealand in 1989. Since then, this regime has extended into over 30 countries and it is recommended by International Monetary Fund within its business arrangements in last couple of years. The last country that announced this regime was Serbia. It is regularly introduced when previous one had poor performances. Its nature is determined by targeted inflation rate, high level of transparency in monetary policies conducting, absence of secondary goals, as well as responsibility for realized targeted inflation rates. Within work, theoretical presumptions are analyzed regarding implementation of this regime, and the most important aspects of its functioning in chosen countries, and its application in Serbia is a subject of particular consideration.

Key words: Inflation targeting, Monetary policy, Serbia, Transparency.

JEL: E31, E42, E52

1. Basic Characteristics of Inflation Targeting

While most innovations in economic policy have spread from large to small countries, inflation targeting is an exception. The first time inflation targeting was applied in 1989 by New Zealand, and since then this concept has become increasingly popular, being accepted by over 30 countries so far. Many countries adopted it after experiencing exchange rate or inflationary crises. Although the European Central Bank has not officially accepted this concept, the monetary policy followed by the ECB is largely similar to inflation targeting. Even though there have been debates in the USA for many years about introducing inflation targeting, so far the FED has not yet decided to start with this concept.

Inflation targeting has usually been employed when some other monetary regime has yielded poor results. Many European countries accepted this concept after the unexpected ERM collapse in 1992. Great Britain adopted an inflation targeting regime in 1992 after abandoning the exchange rate mechanism. Shortly afterwards the concept was accepted by Sweden (1993), Finland (1993), and

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Spain (1994). Canada (1991) introduced inflation targeting after poor results from monetary targeting.

B. Bernanke (1999, p. 23) defined the inflation targeting concept as a monetary policy framework whose characteristics are a public announcement of the numeric target (or zone) for one or more time periods, and an explicit statement that a low, stable inflation rate represents the main monetary policy objective. Other important characteristics of inflation targeting are related to great efforts in communicating with the public about the plans and objectives of monetary policy.

Stone (2003, p. 128) believes that four prerequisites are necessary for inflation targeting to be implemented. The first one refers to reducing inflation as an objective of a central bank, simultaneously making it one of the responsibilities of a central bank. The second prerequisite relates to avoiding a situation where inflation downsizing is subordinate to some other objective, while the third one concerns a well-developed and stable financial system. The last prerequisite implies the utilization of monetary policy instruments aimed at reducing, i.e. sustaining the inflation rate.

At first glance there may be the dilemma whether this could even be a monetary regime, and how an intermediate objective could simultaneously be the ultimate objective. This is, however, a monetary regime since it implies a structural approach to achieving the objective. The main difference between this regime and one where there is complete monetary policy discretion lies in the procedure of selecting a monetary policy objective, the initiative for achieving the objective, as well as a high level of monetary policy transparency.

Four main principles serve as the grounds for targeting inflation:
- Pursuing price stability,
- A numerically represented inflation rate target,
- A high level of system transparency: publishing reports, econometric assessments, guest appearances in the media, and
- The responsibility for results achieved.

Box 1 - Sanctions in a Case of Inflation Target Breach – New Zealand Experience

The most drastic example of sanctioning a Governor for an inflation target breach is New Zealand. In such a case, a Governor may be relieved of their duties. The dismissal procedure is not immediate, and the decision on the dismissal may be passed by the Minister of Finance or the Government. Breaches of the agreed target are considered acceptable in cases of exceptional circumstances, such as:

- Sudden global prices rise,
- Changes in taxation,

- Government policy that affects price movements, and
- Natural disasters.

The nature of these unforeseen circumstances must be explained in detail, and the Minister of Finance has „the final word" in deciding whether the alleged reasons are justifiable. Targets were not achieved twice in the mid-1990`s, but the deviations were relatively small. Instead of dismissing the Governor, the Government decided to extend the target range.

In order for inflation targeting to be successful, a high level of central bank independence is a sine qua non. In most cases, countries that have accepted inflation targeting have the liberty to choose the instruments for achieving the targeted inflation rate, but not the choice of the target. The selection of a target in this regime is usually made by a government, a Parliament, or an appointed politician. This concept excludes the possibility of a central bank having any other goal except the targeted rate of inflation. This concept also implies a high level of central bank transparency and credibility because, as underlined by B. Friedman (2003, p. 120), targeting inflation is way of manipulating with expectations about future inflation.

The announcement of the inflation target itself is not considered the targeting inflation process, and as pointed by Carare (2003, p. 152), many years may pass from the announcement of inflation target until acceptance of inflation targeting regime.

The first dilemma that emerges when introducing the inflation target may be the setting of the time horizon for it. There have been various solutions to this issue in practice because the inflation target cannot be set once and for all since inflation is always under the influence of unpredicted shocks and time lags. If interest rates affect the inflation rate, then it is pointless to set a target for the following year. Only a small number of central banks that have accepted this concept have set as their objective to bring inflation to the targeted value in the short-term because such policies would „knock" the economy off balance. An optimum time horizon could be viewed as a time period required for economic policy to give some results in practise. For example, at the beginning of targeting inflation, Canada and New Zealand adopted a period of 18 months, Australia defined it as the business cycle period, while in Great Britain the Government may change the target every year or adjust it to the cycle phase.

Another dilemma may be which index to target. Most countries accepted the solution for this to be the consumer price index, using the core inflation concept at first in order to avoid the negative effects of potential shocks due to increases in food prices, energy products, indirect taxes, and the like.

Inflation target could be defined in various ways: as a unique value, as the fluctuation zone, or as the fluctuation zone around fixed central parity. Nevertheless, a relatively small number of banks define the target as a numerical value,

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and in most cases it is defined around the fluctuation zone. No central bank has defined inflation target as a zero inflation rate, and a very few of them that target the fluctuation zone define the zone from the zero rate upward. Most of the inflation targets range between 1% and 4%, and higher than that could only be found in developing countries. The proposal provided by Svensson (1997) is also interesting, suggesting that the inflation target should be the rate forecasted by a central bank. If any shock or monetary policy instrument lead to a divergence from the forecasted rate of inflation, then a central bank should undertake corrective measures in order to bring back the rate onto the forecasted track. The following graph shows the inflation target definition in different countries.

Graph 1. *Inflation target selection*
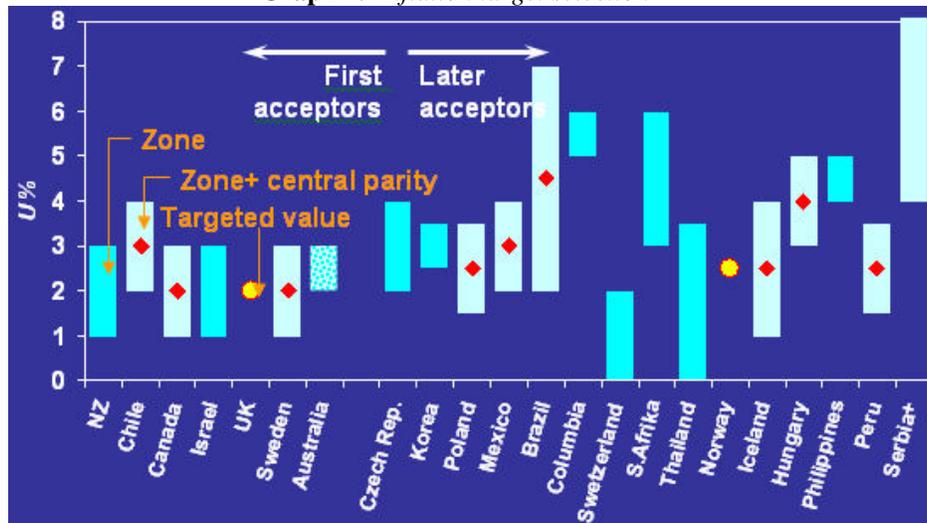
**Source:** Kutner, K. (2004.), „Monetary Policy – Framework and Rules" * - fulfilled by author

In this regime it is not possible to use the foreign exchange rate as the nominal anchor, but this does not rule out foreign exchange market interventions that could primarily be used for moderating the consequences of occasional shocks. Interesting examples may be Chile and Israel which used a managed float regime at the moment of introducing inflation targeting due to the great importance of the exchange rate for stability. Both countries intervened in the foreign exchange market in order to preserve the exchange rates within the zone. The zones expanded over time, thus not being an impediment to monetary policy following the inflation targeting policy, and Israel later abolished them.

A dilemma may also be about who is responsible for setting and announcing the inflation target. Three options have emerged in practise: a central bank, a government (usually the Ministry of Finance), or jointly a central bank and a government. In most cases it was done jointly by central bank and government

in order to show that there is no conflict between monetary and fiscal policy and that all policy makers are devoted to achieving the target.

Box 2 Targeting Inflation in Great Britain

One of the most famous examples of targeting inflation is Great Britain, which accepted this concept in 1992, right after Canada and New Zealand, after abandoning the EU exchange rate mechanism. Due to an earlier inadequate monetary policy, which started from the agreement between inflation and unemployment, the results were periodical inflation upsurges, a 25% peak being recorded in 1975.
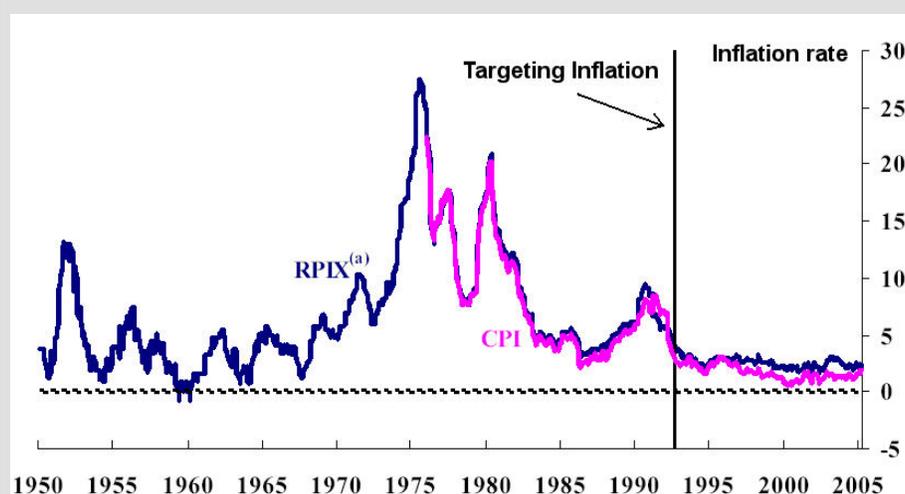

In England, the Government announces the targeted rate of inflation, and the Bank of England is the one which should strive to keep inflation within the planned band. The communication campaign is simultaneously led by both the Government and the Bank of England. If the inflation rate exceeds 1%, the Bank of England Governor writes an open letter to the Chancellor of the Exchequer informing him/her about the reasons for failing to achieve the target, as well as the corrective measures the Bank intends to undertake.

Unlike monetary targeting that basically focuses on a short- or a long-term timeframe, with a passive role of monetary policy, inflation targeting is aimed at the short-term, playing a much more active role. The fundamental nature of inflation targeting reflects in that if the estimated inflation rate is higher (lower) than the targeted, then it is necessary to increase (lower) the level of short-term interest rates.

A high level of system transparency is of great importance for successful inflation targeting. All central banks in this regime, as a rule, publish numerous

reports that support the targeted inflation rate. These reduce any uncertainties with regard to the inflation rate, aiming at increasing central bank credibility by representing it as a „fair player". Graph 2 show the types of reports and communication instruments used by central banks that have introduced this concept. However, there is no consensus about how far transparency should go. Some central banks, like the Bank of England, reveal publicly different points of view of the monetary board members, while others consider it a much better solution to announce only those things that have been agreed upon to a great extent.

Graph 2. *Central bank reports used for targeting inflation*
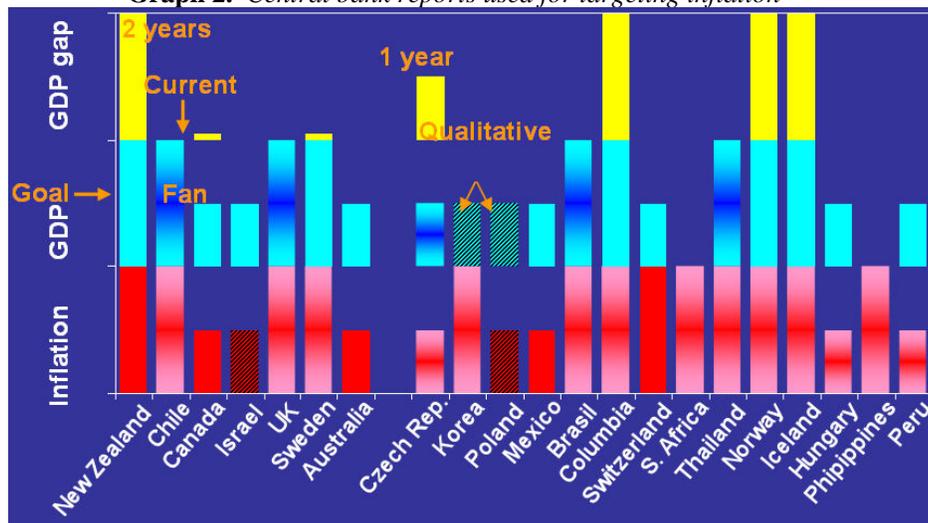
Source: Kutner, K. (2004.), „Monetary Policy – Framework and Rules

A common characteristic of all countries exercising inflation targeting is that they use the model for estimating the future inflation rate. Unlike in a monetary targeting regime wherein the estimate of inflation is based only on the monetary stocks, the inflation targeting regime uses all the information available to assess the rate of inflation. This could be a potential problem, because econometric model are still suffer from a lot of unresolved problems.[1]

This model has proved to be very successful in practice when it comes to lowering inflation. B. Friedman (2003), Svensson (2000), Bernanrke (1999), Jonsson (1999), and many others have come to the conclusion that countries exercising inflation targeting have achieved relatively low rates of inflation. However, most of them also concluded that the performance of these countries with regard to inflation did not differ from that of developed countries that have used

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[1] For more detail see: Central Banking in Theory and Practice, pp 160 - 165.

some other monetary regimes (Bernarke 1999, Jonsson 1999).[2] A recent IMF study (2005) showed that inflation targeting in developing countries has no negative effects on economic growth, whereas the rate of inflation is much lower than that in developing countries that exercise some other monetary regime. However, this conclusion would hardly be sustainable if observing only European countries in transition that have pegged their exchange rates to the euro. The ECB (2006, p.8) points out that the successful sustainability of this regime in economies in transition requires institutional central bank independence, a well-developed technical infrastructure, and the absence of too great a sensitivity to exchange rate developments. The implementation of this regime is hindered by underdeveloped capital markets, fiscal dominance, and insufficiently powerful monetary policy instruments. This regime implies a free exchange rate fluctuation and may lead to negative economic performance since in periods of large capital inflows it brings about the appreciation of a national currency and the weakening of an economy`s competitiveness.

Critics of this regime argue that even though it is based on rules, inflation targeting actually represent a pure discretion, and too great a discretion may lead to large inflation rate fluctuations. They also stress that regardless of insisting on transparency, this regime remains insufficiently transparent since its essence represents a model-estimated inflation rate serving as the basis for manipulating monetary policy variables. An estimated inflation rate is often conditional, associated with movements of interest rates, exchange rates, and the like. The public often do not understand how the model has been created and how it functions, so it can be considered as being a non-transparent approach. Its weakness is also in that this regime mainly rests on a forecasted inflation rate, and forecasting techniques are still insufficiently reliable. Also, the basis of this model is a free exchange rate fluctuation that could have negative effects on some economies in transition and developing countries that are less competitive, with poor credibility of economic policy creators, and insufficiently developed financial markets.

The objection to this model is that the public could come to the conclusion that a central bank focuses only on price stability, simultaneously neglecting other economic objectives. This conclusion is correct because the central bank task is to maintain the inflation rate within the set target. Since every economy is exposed to various shocks and occasional mistakes by the creators of economic policy, sporadic divergences from this target are present. In such conditions, central banks take corrective measures to bring back the inflation rate to the planned framework, and such measures could often have discouraging effects on economic growth.

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[2] It should be taken into account that low inflation rates were achieved in all developed countries in the late 1990`s. That is why this period is called the „Great stability". There are many reasons for such low rates: the understanding of what monetary policy *can and cannot do* improved, as well as the econometric models and data sources, the fear of inflation and accompanying costs also increased, as have the level of central bank independence and central bank credibility.

2. New monetary framework in Serbia[3]

On the meeting held on August, 30th 2006, National Bank of Serbia (NBS) Monetary Board agreed on new principles and rules for managing monetary policy. New monetary framework is applied from September and it's rather similar to inflation targeting regime. As targeted inflation rate, zone between 7% and 9% is determined for year of 2006, as well as from 4% to 8% for 2007. NBS will try to realize targeted inflation rate through corrections of interest rates applied on two-week repo operations. Other monetary policy instruments, like emission of long-term valuable papers or mandatory reserve, will have auxiliary role in realizing targeted inflation rate. Its goal is to contribute unobstructed transmission of the main referent interest rate. Also, foreign currency reserves within new framework, according to announcement, will be used rarely if there is depletion of possibilities to influence inflation through referent interest rate, but no targeted numerical values will be determined for foreign currency exchange rate. It is foreseen to transfer onto floating foreign currency rate regime, after period of transition.[4]

Reasons for transferring to this new regime are consequence of prospective structural alternations, higher degree of opening to the EU and high degree of eurisation, which contribute to remarkably fast transmission of inflation collapses. Estimate of National Bank of Serbia is that, in such conditions, foreign currency rate regime or targeting of monetary aggregates cannot provide stabile and low inflation rate.

Is it wrong to orientate onto short-term approach is the first dilemma which occurs, with respect of time gaps in case of monetary policy. Namely, time gaps in terms of monetary policy are long-term and unpredictable. It means that alterations in monetary policy which are implemented today will affect price level after several quarters or years, i.e. monetary policy can neutralize collapses by the time, but they cannot be neutralized momentarily due to long time delays. It is obvious that application of short-term interest rate cannot influence current year inflation rate, but there is presumption for this year in accordance with Swenson's proposition (1997) that creators of Serbian monetary policy targeted inflation rate which is estimated that will be realized.[5] Dilemma remains how much is possible to influence onto inflation rate in the next year. However, having in mind choice of favorable moment for application of this regime (significant capital inflow) and the fact that in less developed economies there are

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[3] Information on new monetary framework of Serbia are took from document entitled "Memo of National Bank of Serbia on principles of new monetary framework".
[4] After transition period, system of rare foreign currency interventions will be established in order to: 1) limit daily fluctuations, 2) limit risks for finance and price stability and 3) preserve adequate level of foreign currency reserves.
[5] Target establishing for 2006 and 2007 was made at the end of third quarter in 2006.

shorter time delays during management of monetary policy, there is an impression that right moment is chosen. Also, it should be perceived that, longer time period for which targeted inflation rate is, lesser credibility level it bares.

However, appropriate moment can be the source of potential future instability. Namely, as a result of comprehensive capital flow it is expected at the end of this year that appreciation of dinar in ratio to EUR will amount 3% to 4%, and simultaneously inflation rate will amount around 8%. It means that in this year gap between inflation trend and foreign currency rate will amount 11% to 12%. Whether "strong" economy does not supporting this gap, it may be potential source for faster growth of foreign currency exchange rate from the growth of inflation in the period after cessation of significant capital inflow. It may initiate growth of inflation expectations and threat to the targeted inflation rate.

In dilemma should inflation target be announced by NBS, Government or mutually agreed option, is that NBS should substantively announce inflation target, and later to access counseling with the Government. It means that NBS preserved both target and instrument independence. Announcement of targets in selected countries is shown in the following table.

Table 1. Inflation target announcement[6]

Institution announcing the target	Country
Government	Brazil, Iceland, Israel, Norway, United Kingdom
Central bank	Chile, Columbia, Finland, Mexico, Poland, Spain, Sweden, Thailand
Government and central bank	Australia, Canada, Czech Republic, Hungary, Korea, New Zealand, Philippines, South African Republic

Source: "Establishing Initial Condition in Supporting Inflation Targeting", 2003.

In economies in transition and developing countries, the public debt to GDP ratio had been declining before the introduction of inflation targeting, and vice versa in developed countries. In transitional and developing countries which did not have satisfactory credibility the first thing to do was to send a strong signal to the public with regard to the systems sustainability. On the other hand, developed countries used to introduce this regime as a consequence of certain difficulties (e.g. an increase in public debt) and a resulting growth in inflation. Serbia, similar to the most other economies in transitions, transferred to utilization of this regime within environment of improved macroeconomic performances – reduced share of public dept in GDP, budget surplus and single digit inflation rate.

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[6] Information on Finland and Spain refer to the pre-eurozone period.

As price index, which will be the subject of targeting, base inflation rate is chosen. From the calculation of base inflation rate excluded products are as follows: fresh vegetables, fruits, eggs, fish, bread, milk, cigarettes, electricity, coal, heating oil, drugs, oil derivates, commodities, TV subscription, social protection services, traffic and postal services. It factually means that excluded prices are only the prices controlled by the state, affected by seasonal factors or international stock exchange trend results. Such selection of indexes is correct, because it consequently excludes the prices of products on which monetary policy cannot influence and which reduces a risk of unfeasible inflation target. Also, most of the countries on the beginning of implementation of this regime have selected basic inflation rate.

However, potential weakness of this process is NBS announcement (2006, p. 2): "Monetary policy will strive to implement other targets as well, on condition that it does not endanger realization of targeted inflation rate, i.e. if it does not endanger institutional mandate of preserving financial stability, which is necessary to realize simultaneously with mandate of prices stability". Recently, there is a tendency of considering financial stability as a Central Bank target, however, as Icard (2003, p. 225) emphasizes no Central Bank explicitly specify financial stability as its basic target. Reasons are very precise, because Central Bank cannot cover all aspects of financial stability, nor the banks with the widest grade of supervisory rights are not controlling retirement funds, hedging of funds, and in only few cases control insurance companies. NBS, beside bank control, is authorized for control of insurance companies, yet cannot be responsible for other segments of financial market. Although price stability and financial stability mostly «go» along, the fact that should not be overlooked is that they can be conflict targets. For example, for preserving price stability contractionary monetary policy may be necessary and, through growth of interest rates, it may lead to violation of financial stability. However, this is a consequence of partially said NBS Law, which says that the main NBS target is maintenance of price stability, and then says that, beside basic target, NBS should realize financial stability, with no indication of clear prioritization of targets in case that these two targets become conflict.[7] Beside wide interest for financial stability, it is unlikely that it will become explicit target of the central banks. The reasons are multiple, because financial stability do not conform basic conditions for becoming the target of the Central Bank: precisely defined, publicly comprehendible and that is under the control of the Central Bank.

In order to strengthen the role of referent interest rate two-week repo auctions is announced on which price will be determined in advance, as well as two-month repo auctions. Also, issuing of long-term financial records is foreseen. However, the remaining dilemma is whether reference interest rate is sufficiently «strong» to affect reduction of inflation expectance, in conditions of widely

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[7] Law on National Bank of Serbia, Official Gazette RS 72/2003.

spread out informal eurisation (reducing effectiveness of monetary policy), insufficiently developed market of money and capital. Factually, inflation expectations in Serbia until recently were connected to level of foreign currency exchange rate, and if with continual appreciation of dinar in the last four, five months prices did not decrease, there's still dilemma about variable which dominantly influence on inflation expectations. The most likely it is public estimate that «strengthen» of dinar exchange rate is only temporary,[8] so inflation expectations are directed toward long-term expected dinar exchange rate.

Critical success factor of inflation targeting represents high level of monetary policy transparency and «offensive» public performance. Time when central banks used to be traditionally closed institutions and when they provided publicity with poor and selected information is long gone. Inflation targeting significantly influenced onto increasing of transparency of Central Banks, which led to regular communication between publicity and Central Bank. «Offensive» media campaign is important to persuade publicity in realization feasibility of targeted inflation rate and accordingly to influence on reduction of inflation expectance. Also, insufficient level of transparency rise doubt whether Central Bank's conducts policy of public good. In some countries there are laws on freedom of information, which disable secrecy of Central Banks operations and hiding of documents. For recent NBS monetary policy it could not be said that it conformed the highest transparency standards, although it was not performed in secrecy. There is an impression that, until now, NBS did not provide sufficient information on particular decisions rationales, associated risks, future forecasts, as well as announcing information from Monetary Council and Monetary Board meetings. Thus, very positive announcement of NBS is that it will soon initiate new publication entitled „Inflation report", as well as regular press conferences after Monetary Board meetings in which decisions will be made. Also, according to announcement of NBS, publicity will regularly be informed on inflation targets realization with reasons rationale representing base to such actions, as well as monetary policy measures conducted for the purpose of realizing targeted inflation rate in the future. This announcement represents positive step toward the increasing of credibility of monetary policy creator and reducing of inflation expectations.

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[8] There are numerous reasons for expecting temporarily strengthens of dinar exchange rate. First, it is mainly based on large capital inflow through banking system, privatization and foreign investments. Expectation is that these factors will not be able to have long-term affects strengthens of dinar currency, given it is not supported by «strengthens» of economy. Likewise, in conditions of long-term high deficit in checking accounts in balance of payments, it is inevitably, sooner or later, leading to depreciation of dinar exchange rate.

Table 2. Communication instruments in countries exercising inflation targeting

Country	Announce-ment of monetary policy measure in the media	Inflation/monetary policy reports			Other means of communication		
		Fre-quency	Inflation overview and monetary policy actions	Inflation forecast	Announce-ment of inflation forecasting model	Media and public presenta-tions	An-nounce-ment of reports from MPC meetings
Economies in transition and developing countries							
Brazil	Yes	Quarterly	Yes	Two-year forecast	Yes	Yes	Yes
Chile	Yes	Quarterly	Yes	Two-year forecast	Not all	Yes	No
Columbia	Yes	Monthly	Yes	Two-year forecast	Yes	Yes	No
Czech Rep.	Yes	Quarterly	Yes	Annual forecast	No	Yes	Yes
Hungary	Yes	Quarterly	Yes	Two-year forecast	Not all	Yes	No
Israel	Yes	Monthly	Yes	Two-year forecast	Not all	Yes	No
Mexico	Yes	Quarterly	Yes	Forecast quality discussion	No	Yes	No
Poland	Yes	Quarterly	Yes	Two-year forecast	No	Yes	Yes
Philippines	Yes	Quarterly	Yes	Two-year forecast	No	Yes	Yes
Serbia*	Yes	Quarterly	Yes	Five quar-ter fore-cast	No	Yes	No
Thailand	Yes	Quarterly	Yes	Two-year forecast	Yes	Yes	No
Developed countries							
Australia	Yes	Quarterly	Yes	Two-year forecast	Yes	Yes	No
Canada	Yes	Semi-annually	Yes	Annual forecast	Yes	Yes	No
Iceland	Yes	Quarterly	Yes	Two-year forecast	No	Yes	No
Korea	Yes	Quarterly	Yes	Annual forecast	No	Yes	No
Now Zea-land	Yes	Quarterly	Yes	Two-year forecast	Yes	Yes	No
Norway	Yes	Every four months	Yes	Two-year forecast	Yes	Yes	No
Sweden	Yes	Quarterly	Yes	Two-year forecast	Yes	Yes	Yes
Great Britain	Yes	Quarterly	Yes	Two-year forecast	Yes	Yes	Yes

Source: "Establishing Initial Condition in Supporting Inflation Targeting", 2003. * - Column for Serbia was filled out by author of paper

Precondition for application of inflation targeting represents high level of Central Bank independence. There is an impression that it is the highest risk factor for inflation targeting in Serbia. Although, observed through law regulation NBS has satisfactory level of independence, actual independence level can be estimated as unsatisfactory. The best way to see this is through number of governors which used to officiate on this position from October 2000. Until November 2000, Treasurer position was held by Vlatković, afterwards superseded by Dinkić, then Udovički in July 2003, and the last one was Jelašić, appointed in February 2004. After establishment of new Parliament, most likely to be held in February 2007, releasing of Jelašić is expected followed by appointment of the new governor. Within period of more than six years, which represents common governor's mandate, Serbia faced alternation of five governors due to political reasons. It produces a risk which bares a question will new governor be really independent and to manage only basic NBS mandate, i.e. on preserving price stability.

Likewise, application of inflation targeting regime implies responsibility in the event of target realization failure. This presumption is present in theory, but responsibility is not foreseen in all countries which use this regime. In Serbia, also, is not predicted responsibility in the case of failure of inflation target.

Potential problem may represent a fact that Serbia is within the process of accession to the EU. Condition for membership in European Monetary Union is two year participation in Exchange rate mechanism II, within which fixed exchanged rate must be maintained in acceptable fluctuation zone. It is clear that in the regime of inflation targeting is not possible to conduct two target policies – targeted inflation rates and targeted foreign currency exchange rate. However, European Monetary Union is distant future and this regime is practiced by some new EU members, like Czech, Poland, Hungary etc.

Given a fact that in theory sole announcement of inflation target is not considered as sufficient for conducting policy of inflation targeting, NBS decision to transfer to the inflation targeting regime when conditions are conformed is a good action, because this way potential failure risks will be minimized. NBS announced expectation to accept targeted inflation process in the close future, after expiration of transition period, which is not timely defined. Thus present regime may be evaluated as a lite inflation targeting.

The term of inflation targeting lite is introduced by M. Stone (2003.) This concept is related to those countries which use price stability as a target, but which are not in position to maintain inflation target successfully. The characteristics of this group of countries are that they do not have great monetary policy credibility, but have multiple objectives and undeveloped financial systems with frequent interventions in the exchange rate market[9]. Additionally, there is no

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[9] The reasons for frequent interventions in the foreign exchange markets are due to the fact that these are small countries with „narrow" foreign exchange markets which are often under the influence of exchange rate fluctuations.

transparency either in monetary policy objectives or monetary policy. The pegging of exchange rates is equally unsuitable for these countries because they would be vulnerable to external shocks, as is monetary aggregates targeting due to volatile money demand. At the same time, a „weak" fiscal position (a high level of public debt) and undeveloped capital markets prevent them from moving to the traditional concept of inflation targeting.

Stone has identified 19 countries that belong to this category. These are developing countries, such as: Algeria, Croatia, the Dominican Republic, Guatemala, Honduras, Indonesia, Jamaica, Kazakhstan, Mauritius, Peru, Philippines, Romania, and the like. The most realistic option for this group of countries is either a pegged exchange rate policy or moving to traditional inflation targeting.

Poland is a typical example of a country that moved from the lite variant towards traditional inflation targeting. During the 1990`s, Poland experienced hyperinflation, widespread dollarisation, many structural problems, a high current account deficit, and the like. However, with the implementation of structural reforms, a high inflow of foreign direct investments, continuous disinflation, growth in the Bank of Poland independence, and the like, the prerequisites were created for the introduction of inflation targeting. Therefore, in 1998, the Bank of Poland announced long-term (a six-year) and short-term (annual) targeted rates of inflation.

3. Conclusion

Inflation targeting regime undoubtedly has increasing popularity and the number of countries which use this regime is continually increasing, and it is real to expect this trend to proceed in the future. Econometric studies have shown that in countries which accepted inflation targeting policy the inflation rate fell, as well as inflationary expectations, and the spread between the nominal and real interest rates, and macroeconomic indicators stayed the same or improved.[10] Inflation targeting critics argue that the same has been achieved in the US although it had not introduced an inflation targeting policy.

Announcement of transferring to this regime in Serbia imposes numerous dilemmas, and before all, whether it is a good choice of monetary policy regime and is this regime prematurely introduced in Serbian monetary policy. There are numerous problems which will complicate implementation of this regime in Serbia in the future, as follow:

- Too short initially determined inflation targeting period,
- Poor effect of monetary policy instruments in conditions of widely prevalent informal eurisation,

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[10] For more details see: Gramlich, E., (2005), „The Politics of Inflation Targeting", Euromoney Inflation Conference, Paris

- ▪ Insufficiently developed currency and capital market, which additionally reduce efficiency of monetary policy instruments,
- ▪ Dilemmas whether two-week referent interest rate is sufficiently strong instrument to influence onto inflation expectations,
- ▪ Could appreciation of foreign exchange rate in conditions of 8% inflation represent a source of future depreciation of foreign exchange rate, after capital inflow cessation, and respectively generator of inflation expectations,
- ▪ Insufficient level of NBS independence and
- ▪ Insufficient level of monetary policy transparency (there are indications that this problem could be solved in the close future) etc.

Therefore, decision of National Bank of Serbia to formally not accept inflation targeting regime is reasonable, yet to transfer to this regime after certain (timely indefinite) period of transition. It is regime known in literature as inflation targeting lite. Apart from not being formally accepted in Serbia, inflation targeting encompasses numerous features of this regime. It can be concluded that sequence of actions is performed in accordance with recommendations present in theory literature based on the best practice.

Momentarily, this regime cannot be entirely evaluated, because its implementation is on the very beginning, but in the close future it will be clear whether the action of NBS was good or premature.

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Inflaciono targetiranje sa posebnim osvrtom na primenu u Srbiji

Rezime: Targetiranje inflacije predstavlja monetarni režim koji je prvi put primenio Novi Zeland 1989. godine. Od tada se ovaj režim proširio na preko četrdeset zemalja sveta, a poslednjih godina ovaj režim počinje i da preporučuje Međunarodni monetarni fond u okviru svojih aranžmana. Ovaj režim je po pravilu uvođen onda kada je prethodni režim dao loše rezultate. Njegovu suštinu predstavlja ciljna stopa inflacije, visok stepen transparentnosti u vođenju monetarne politike, odsustvo sekundarnih ciljeva, ali i odgovornost za ostvarenje ciljne stope inflacije. Samo objavljivanje inflacionog targeta se ne smatra procesom targetiranja inflacije i od objavljivanja inflacionog targeta do prihvatanja koncepcije targetiranja inflacije mogu proći godine.

Na prvi pogled može se javiti dilema da li ovo uopšte može biti monetarni režim i kako intermedijarni cilj može biti nešto što je i krajnji cilj. Ipak u pitanju je monetarni režim, jer on podrazumeva strukturni pristup da bi se ostvario cilj. Osnovna razlika između ovog režima i režima u kojem postoji potpuna diskrecija monetarne politike ogleda se u proceduri izbora cilja monetarne politike, inicijativi za ostvarenje cilja, kao i visokom stepenu transparentnosti monetarne politike.

U praksi ovaj model se pokazao dosta uspešnim kada je u pitanju obaranje stope inflacije. Međutim, većina kritičara je došla do zaključka da se performanse po pitanju stope inflacije, nisu značajnije razlikovale od performansi razvijenih zemalja, koje su koristile neki drugi monetarni režim.

Režim inflacionog targetiranja nesumnjivo ima rastuću popularnost i broj zemalja koji koristi ovaj režim je u stalnom porastu i realno je očekivati nastavak tog trenda i u budućnosti. Poslednja zemlja koja je prešla na ovaj režim je Srbija, ali u pitanju je blaža varijanta inflacionog targetiranja. Stoga je posebna pažnja u radu posvećena primeni ovog režima u Srbiji. Može se konstatovati da je redosled koraka prilikom uvođenja ovog režima urađen u skladu sa preporukama prisutnim u teorijskoj literaturi baziranoj na najboljoj praksi.

Najava prelaska na ovaj režim u Srbiji otvara brojne dileme, a pre svega da li je u pitanju dobar izbor režima monetarne politike i da li je možda ovaj režim preuranjeno uveden u monetarnu politiku Srbije. Postoje brojni problemi koji će u budućnosti otežati primenu ovog režima u Srbiji poput:

- Isuviše kratkog inicijalno određenog perioda targetiranja inflacije,
- Malog uticaja instrumenata monetarne politike u uslovima široko rasprostranjene neformalne eurizacije,
- Nedovoljno razvijenog tržišta novca i kapitala, koje dodatno smanjuje efikasnost instrumenata monetarne politike,

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- Dileme da li je dvonedeljna referentna kamatna stopa dovoljno snažan instrument da utiče na inflaciona očekivanja,
- Apresijacija deviznog kursa u uslovima inflacije od oko 8%, može biti izvor buduće depresijacije deviznog kursa, nakon prestanka priliva kapitala, i time generator inflacionih očekivanja,
- Nedovoljnog nivoa nezavisnosti Narodne banke Srbije,
- Nedovoljnog nivoa transparentnosti monetarne politike (postoje najave da bi u bliskoj budućnosti ovaj problem bio otklonjen) i dr.

U radu se zaključuje da se u ovom trenutku se ne može dati potpuna ocena ovog režima, pošto je njegova primena tek na početku, ali već u bliskoj budućnosti će se pokazati da li je bio u pitanju dobar ili preuranjen potez NBS.

Key words: Inflaciono targetiranje, Monetarna politika, Srbija, Transparentnost.

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