

Central Bank Independence: Principles and Challenges

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20 Aniversario de la Autonomia

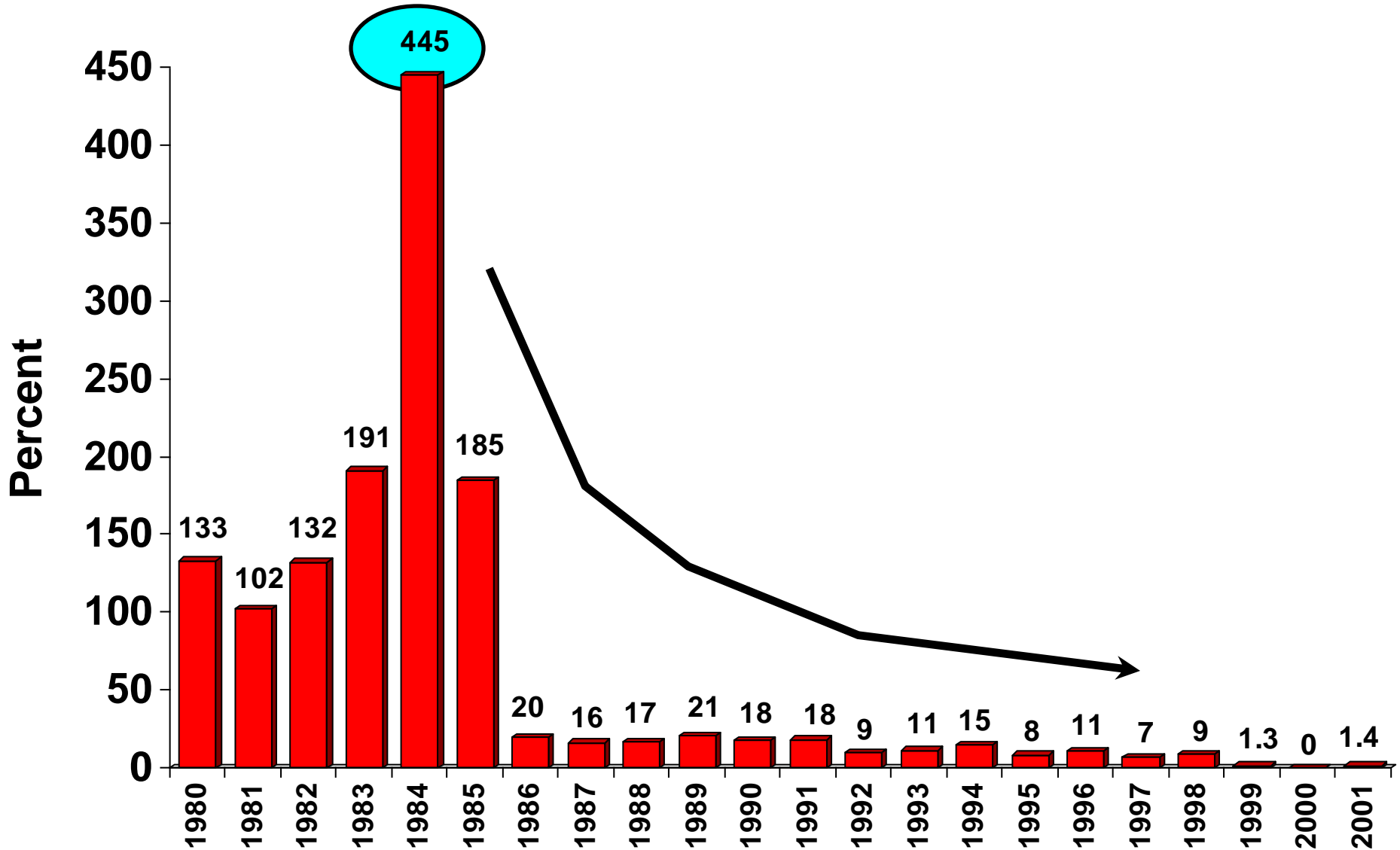
Del Banco de Mexico

Mexico City, October 14-15, 2013

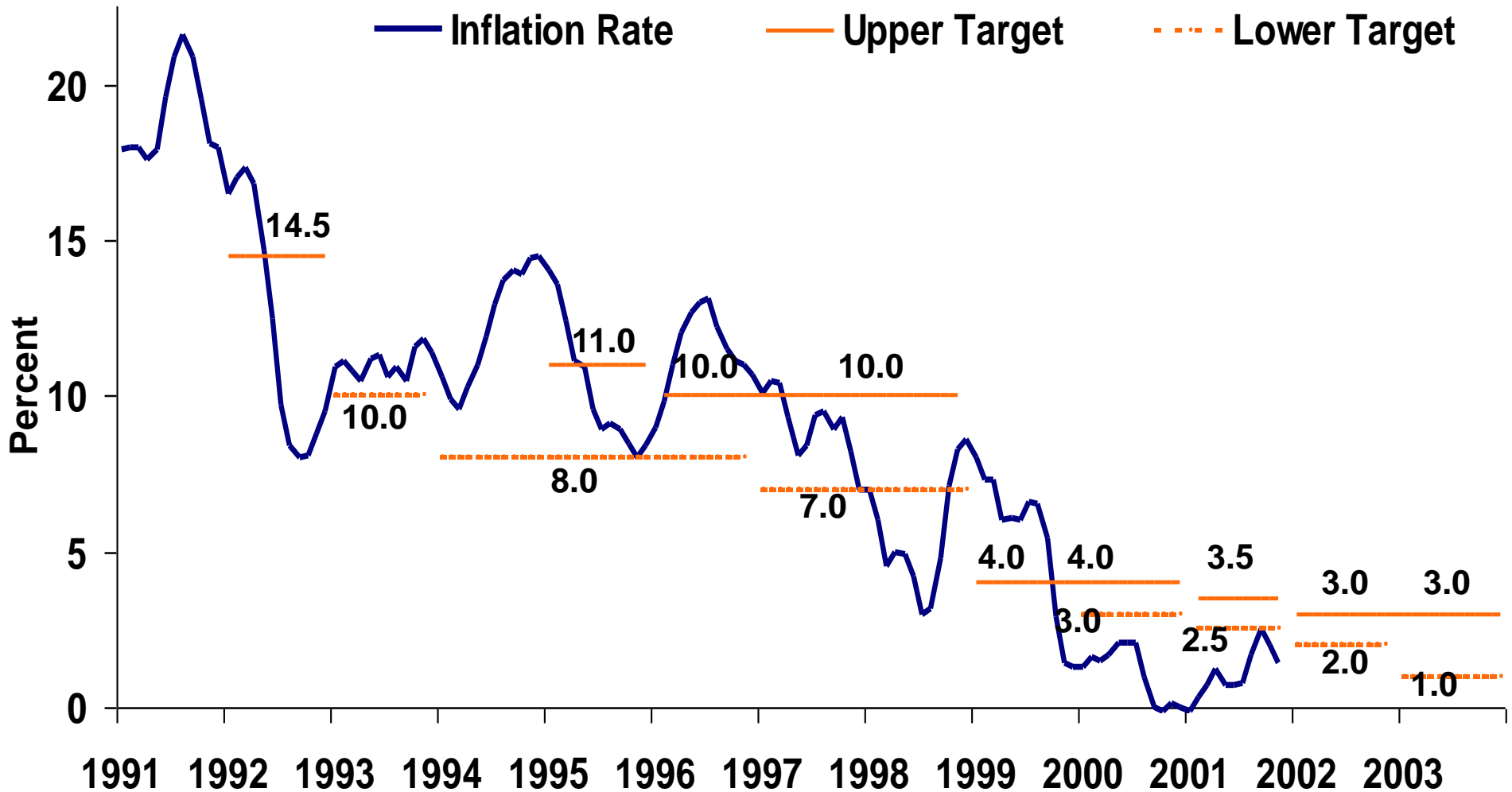
The Israeli Experience

- Inflation and Inflation Targets
- Interest Rates
- Expectations
- Useful “Background Music”

The Rate of Inflation



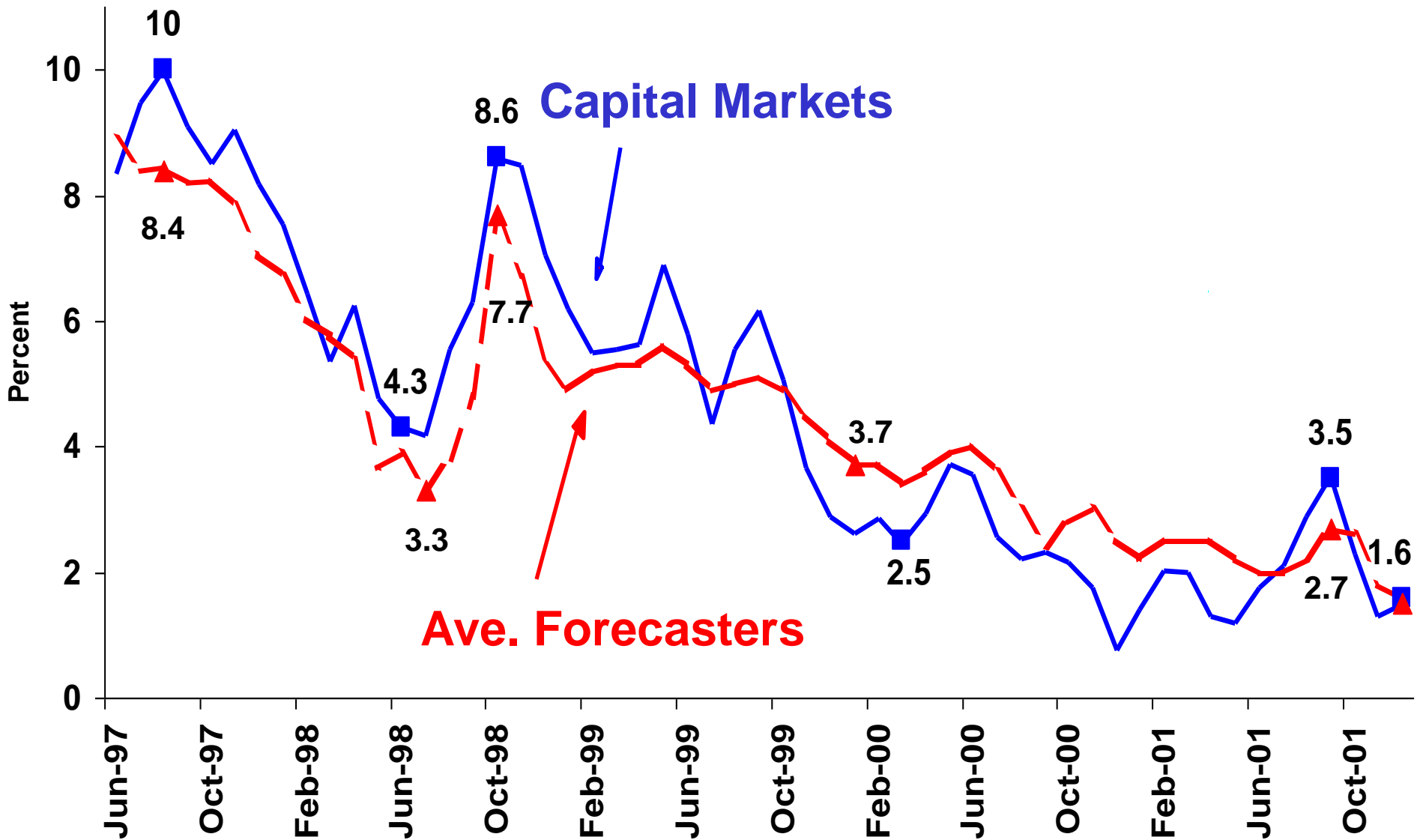
Inflation Rate* and the Inflation Target



* Previous 12 months

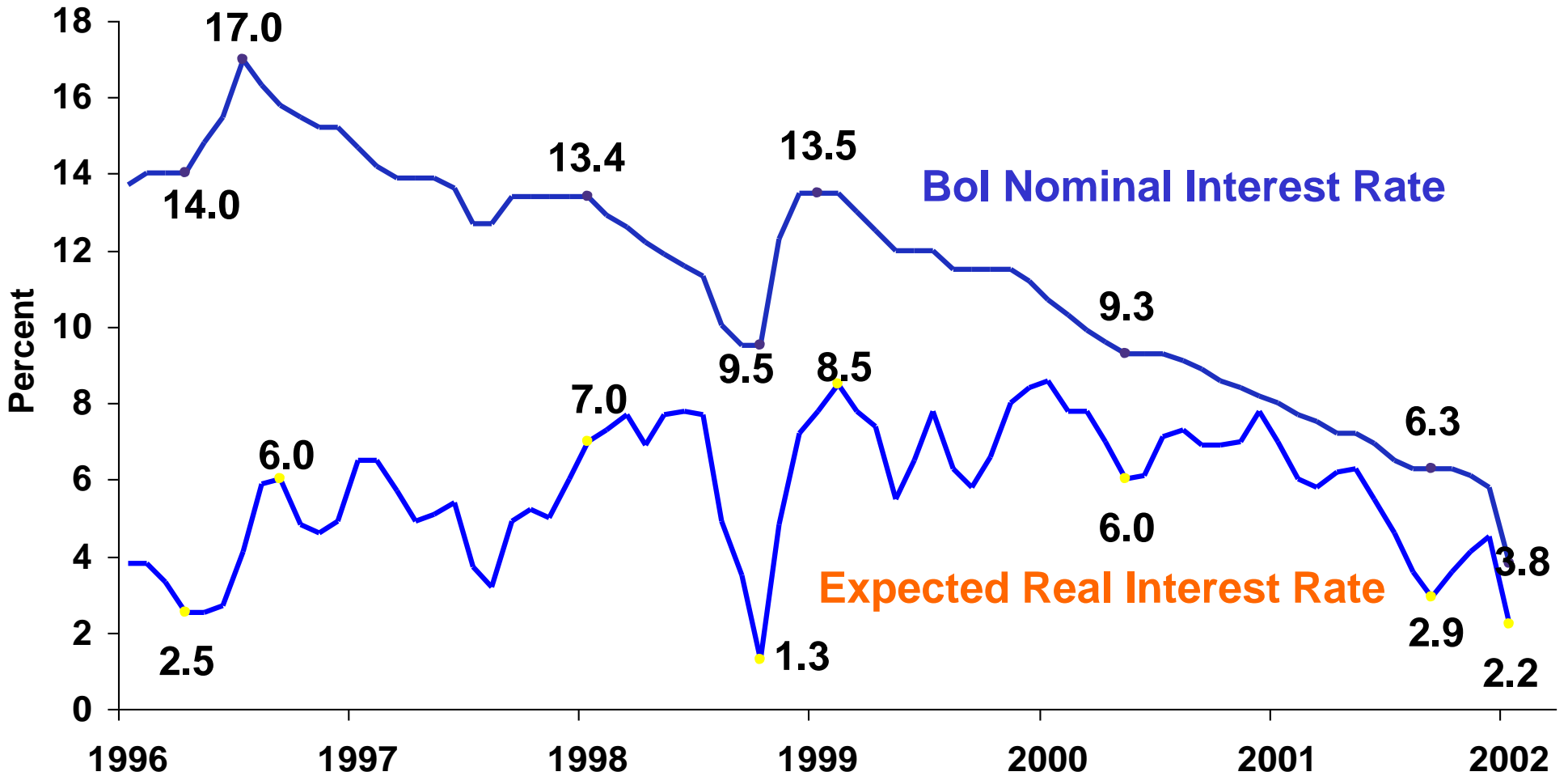
Date: December 2001

Inflation Expectations Indicators:



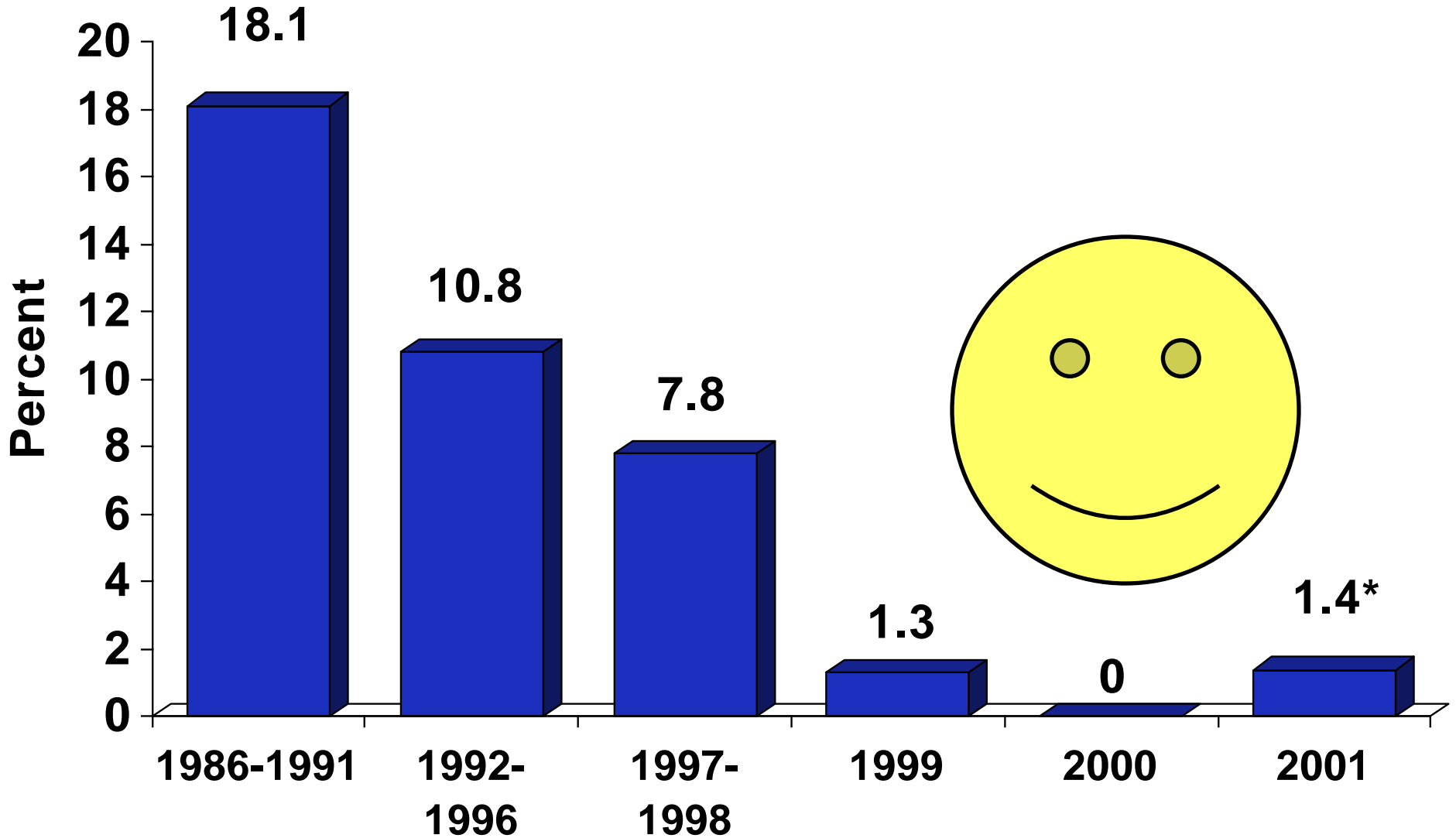
Bank of Israel Interest Rate

In Nominal and Expected Real Terms



Expected real interest rate = Effective Bank of Israel interest rate adjusted for inflation expectations

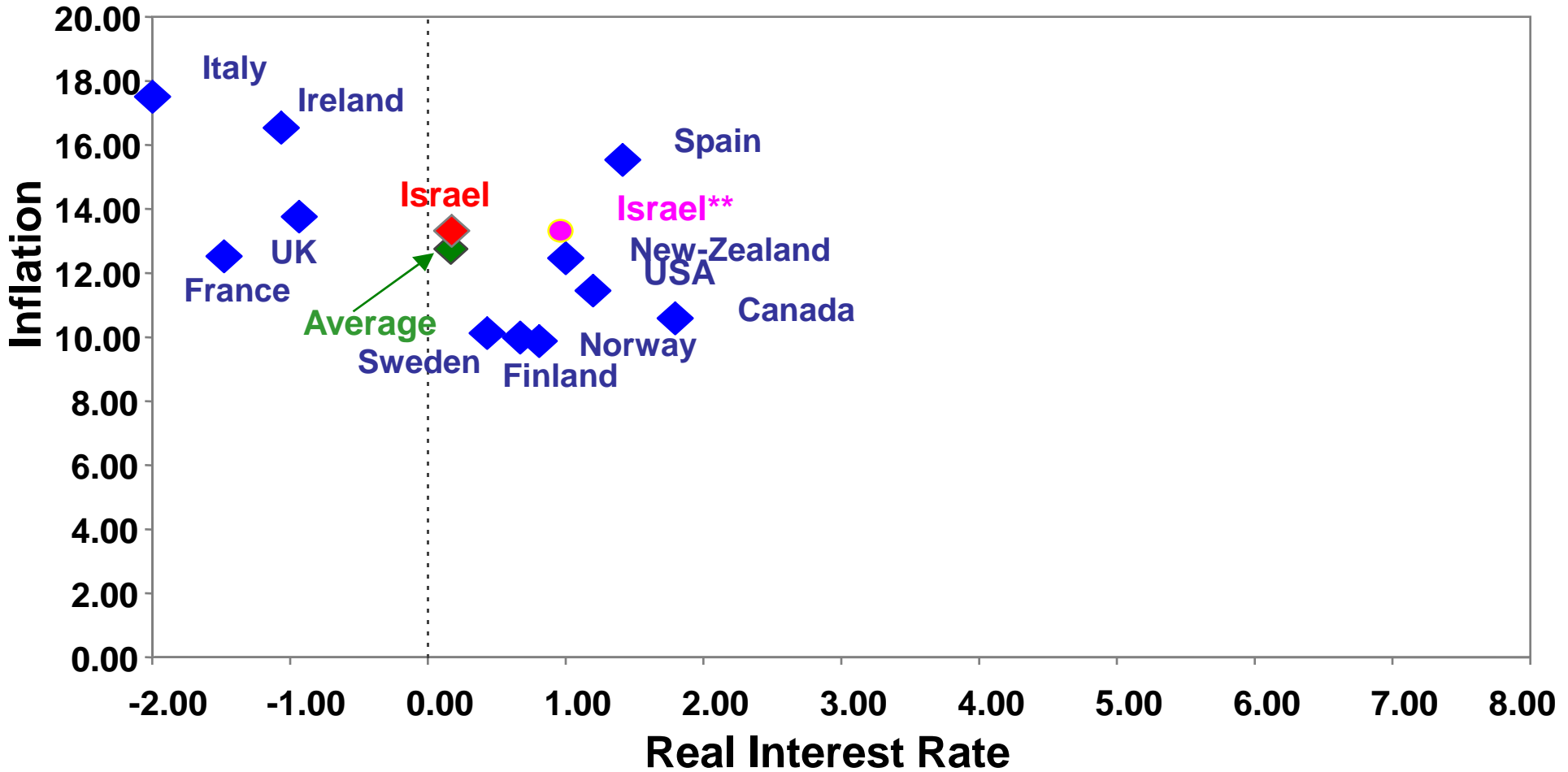
Change in the Annual CPI



* Note: data for 2001 refers to November 2001

Date: January 2002

Period of High Inflation

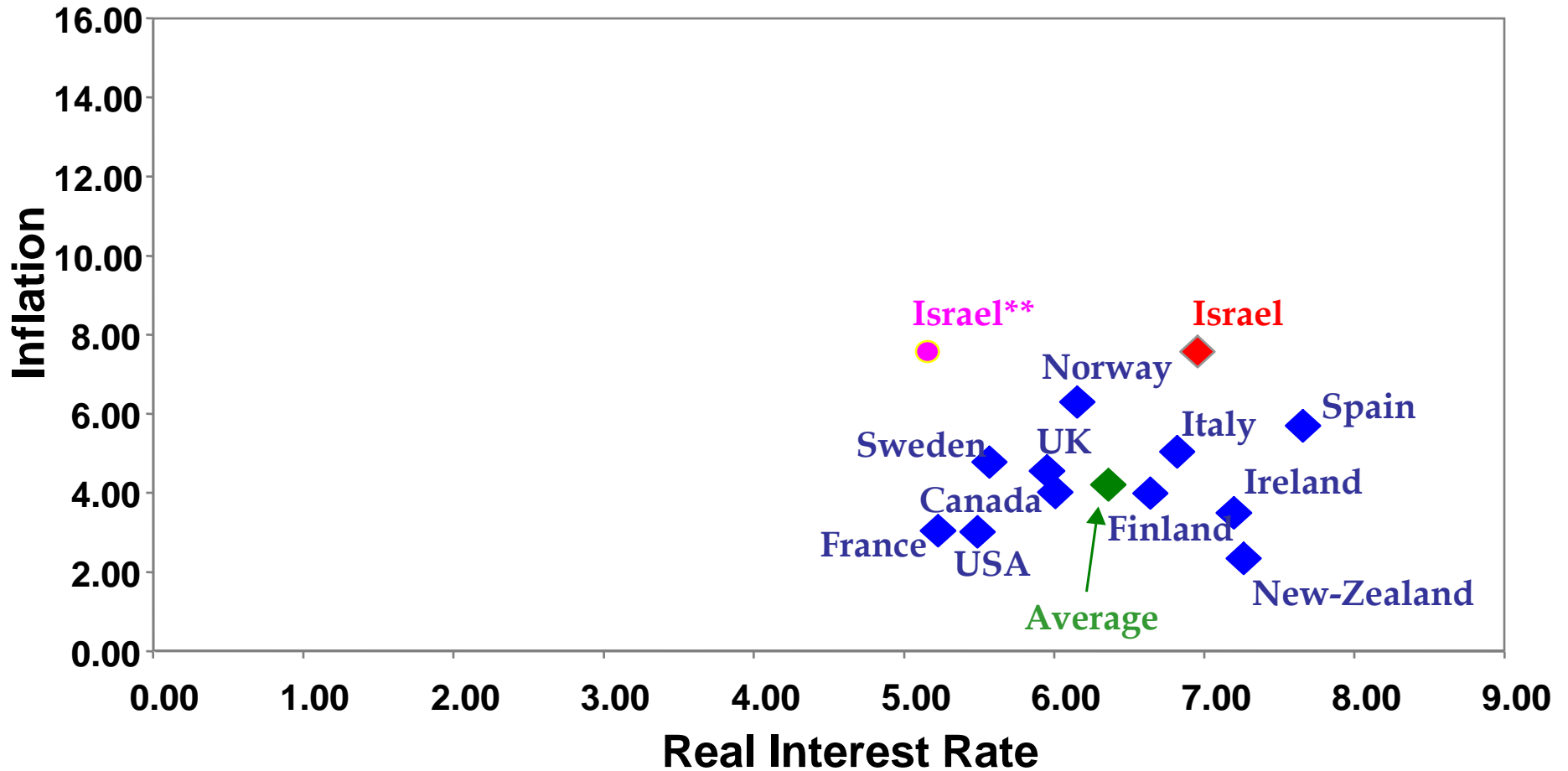


* Israel: January 1991 - November 1994

** based on expectations

Date: July 2000

Period of Disinflation*

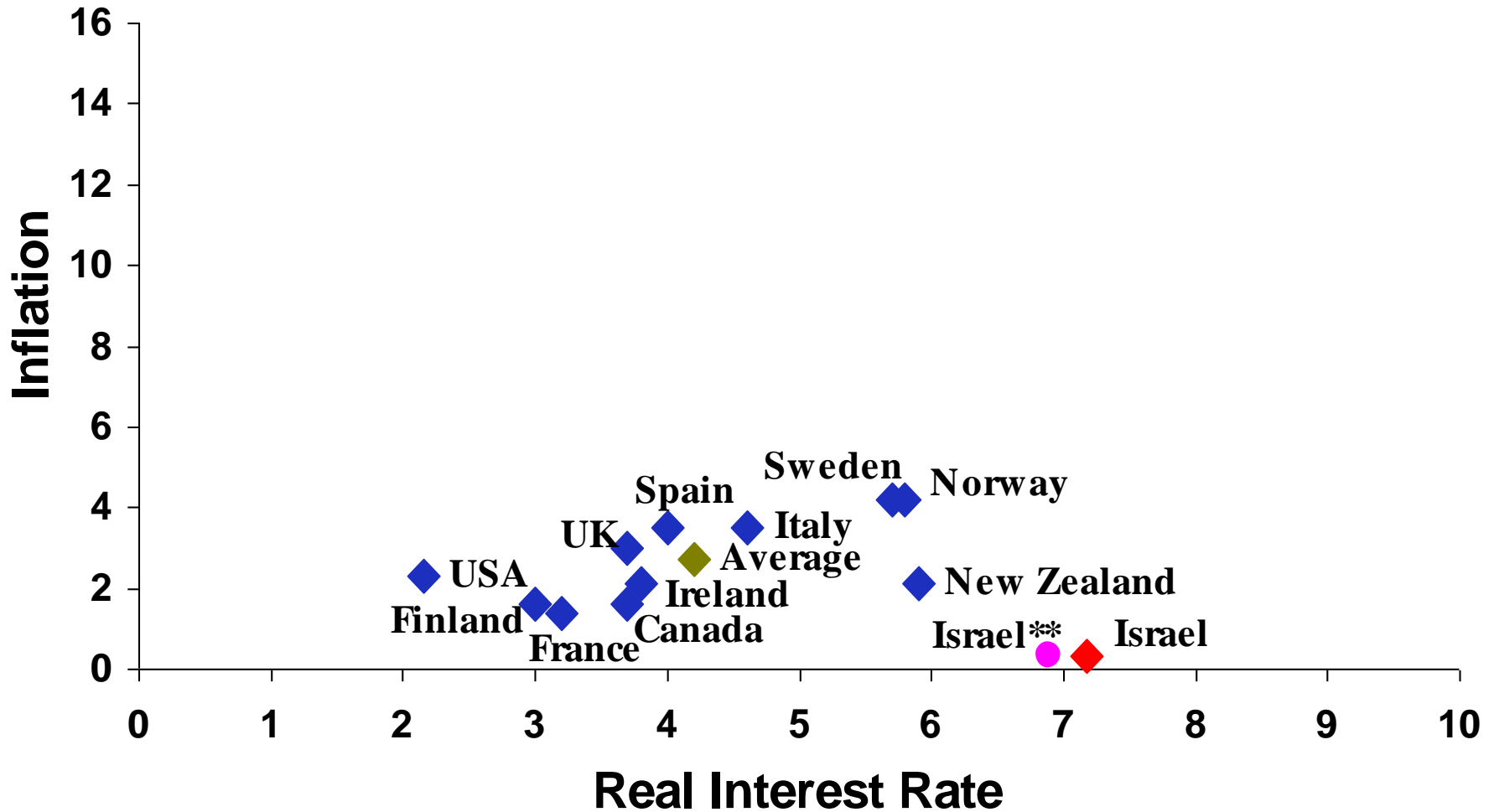


* Average disinflation period is about 4 years; In Israel 12/94-6/99

** based on expectations

Date: July 2000

Period of Low Inflation



* Israel July 99 - June 2000

** Based on expectations

Date: April 2001

Useful “Background Music”

- 1. A Solid Fiscal System**
- 2. A Functioning Foreign-Exchange Market**
- 3. A Flexible Exchange-Rate Regime**
- 4. Available Instruments of Monetary Policy**
- 5. Central-Bank Independence (Legal & Factual)**
- 6. A strong Banking System**
- 7. A Functioning Capital Market**
- 8. A Flexible Economic System (Goods, Services and Labor Markets)**

Global Central Banks Challenges

Interest Rates

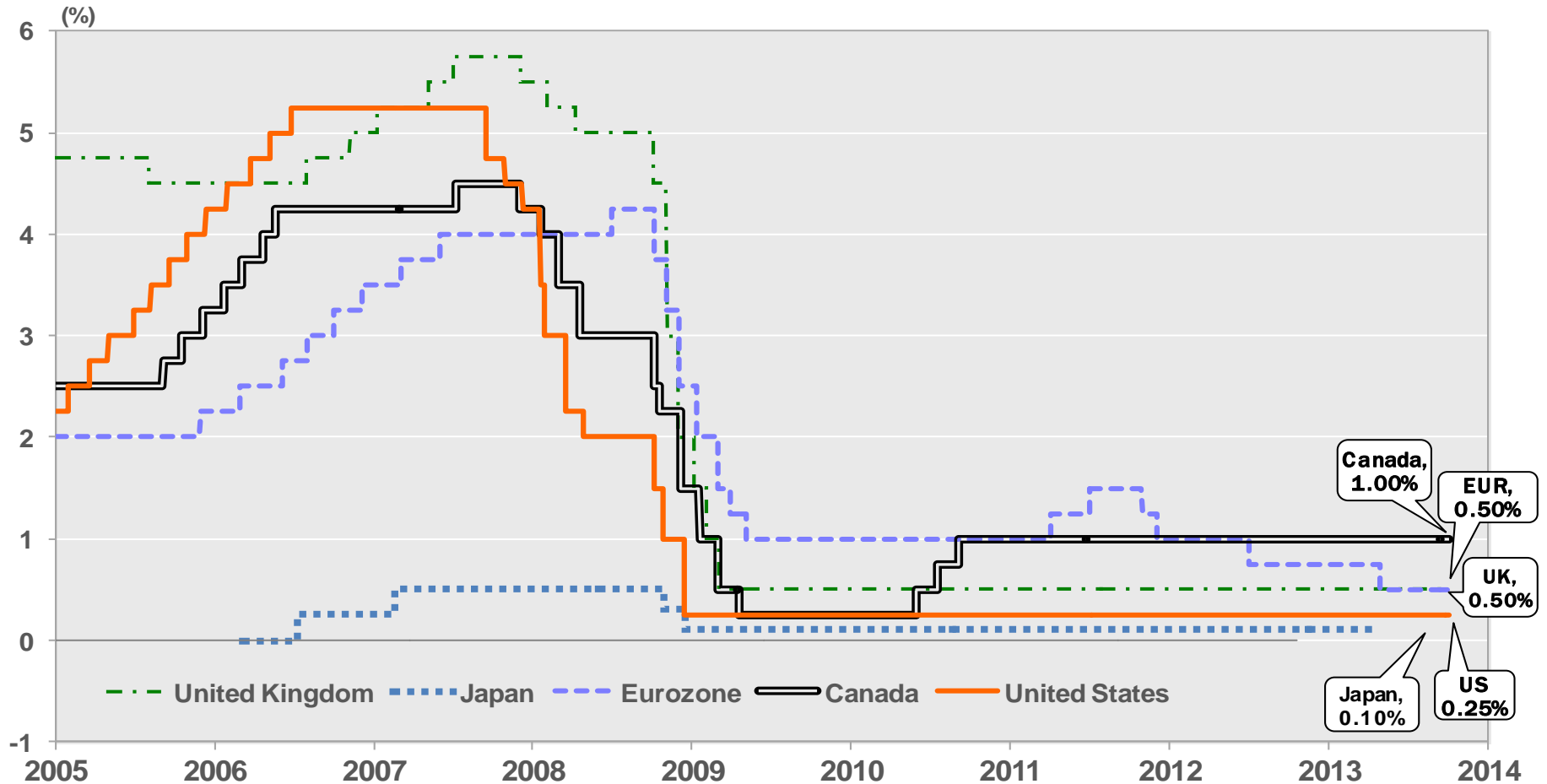
Central Bank Balance Sheets:

i. Size

ii. Composition

Guidance

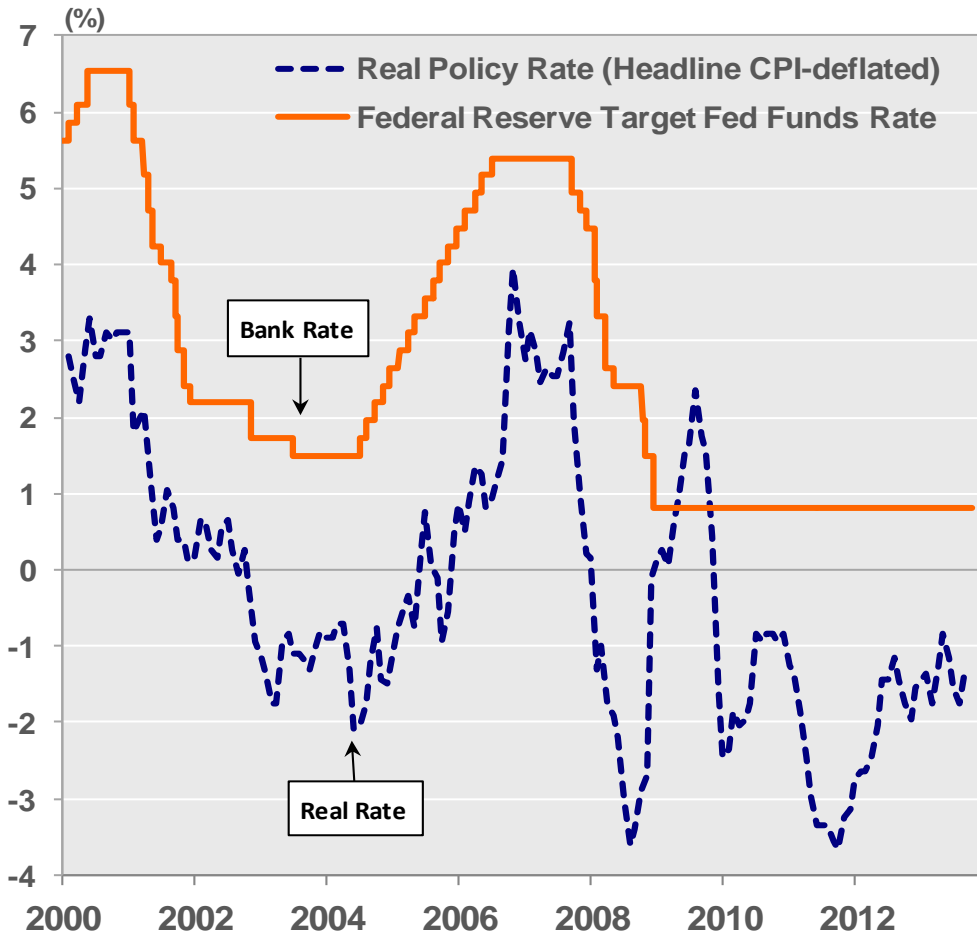
Central Bank Policy Interest Rate



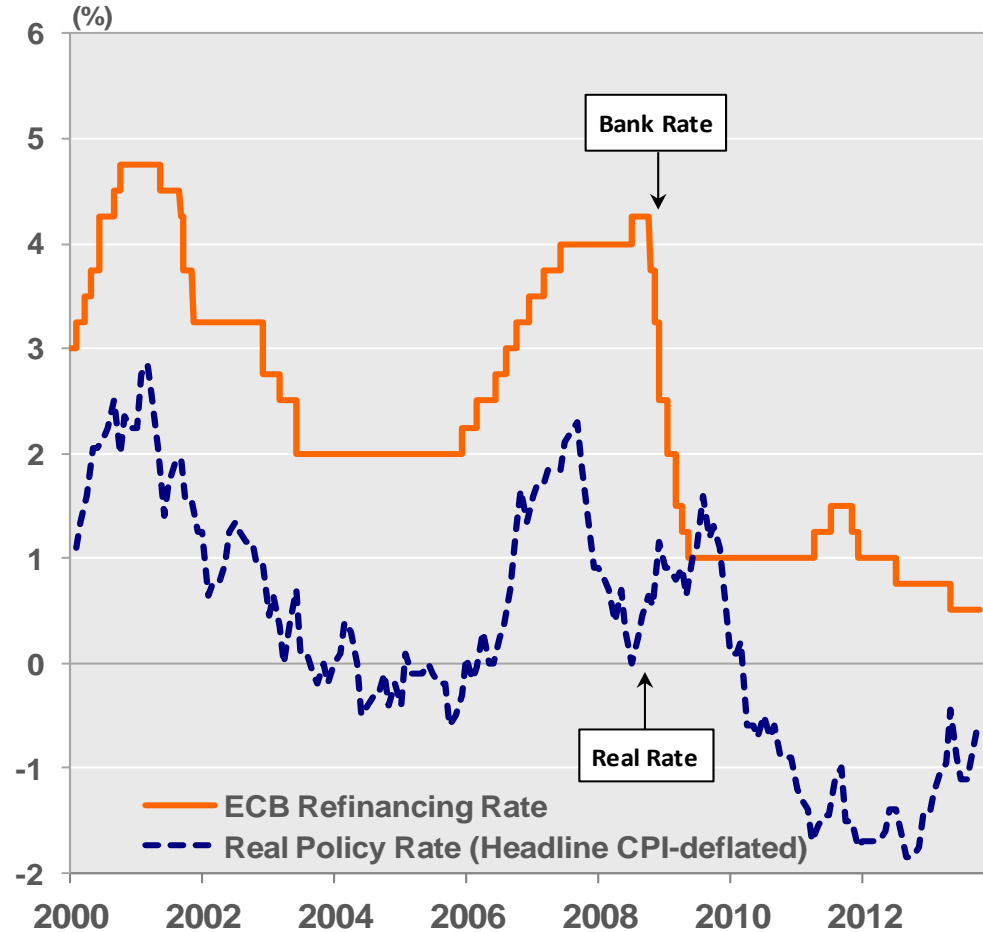
Source: Bloomberg Market Data, Last observation: 7 Oct, 2013

Global Policy Rates: Main Rate & Real Rates

Federal Reserve

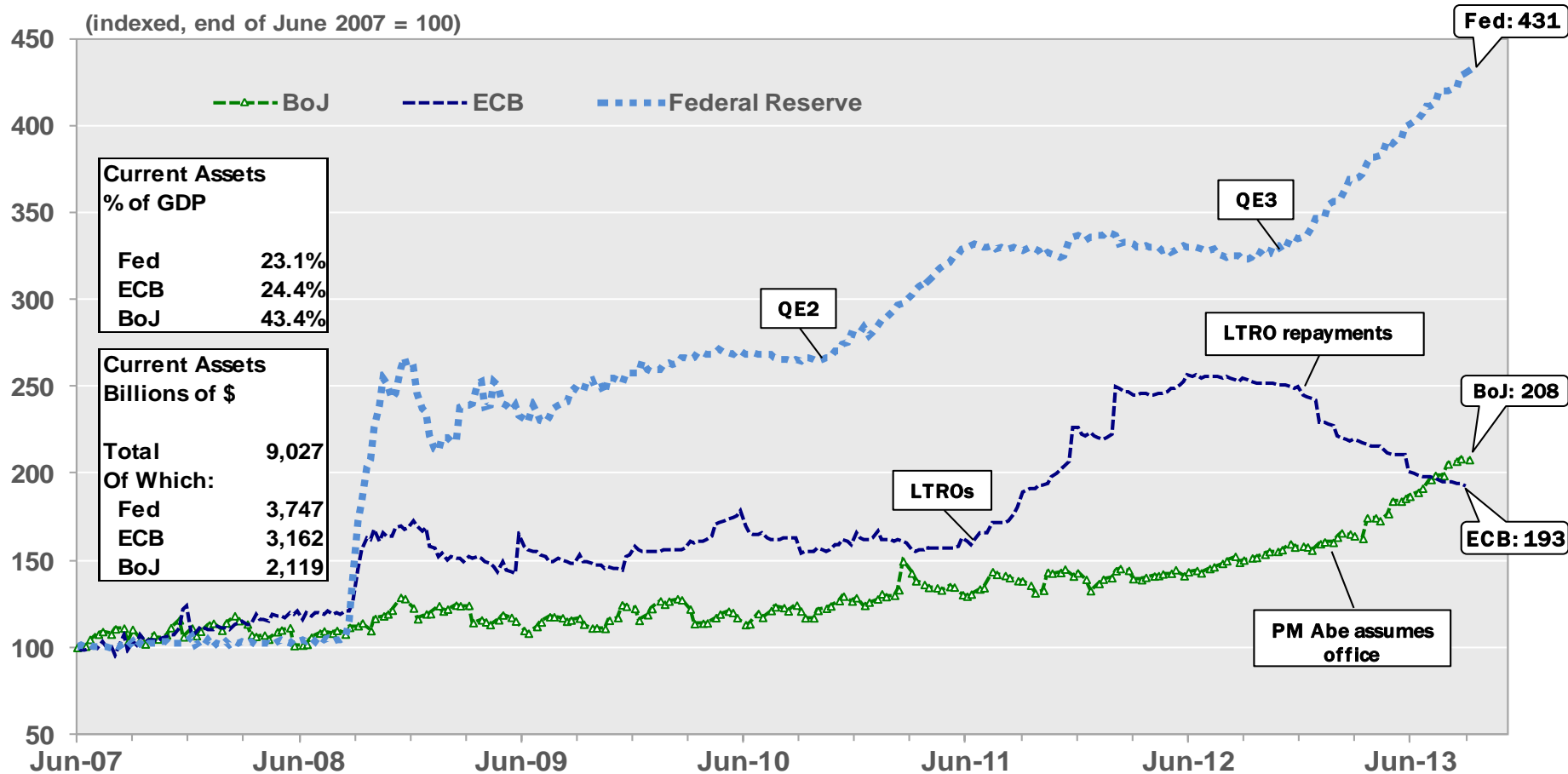


ECB



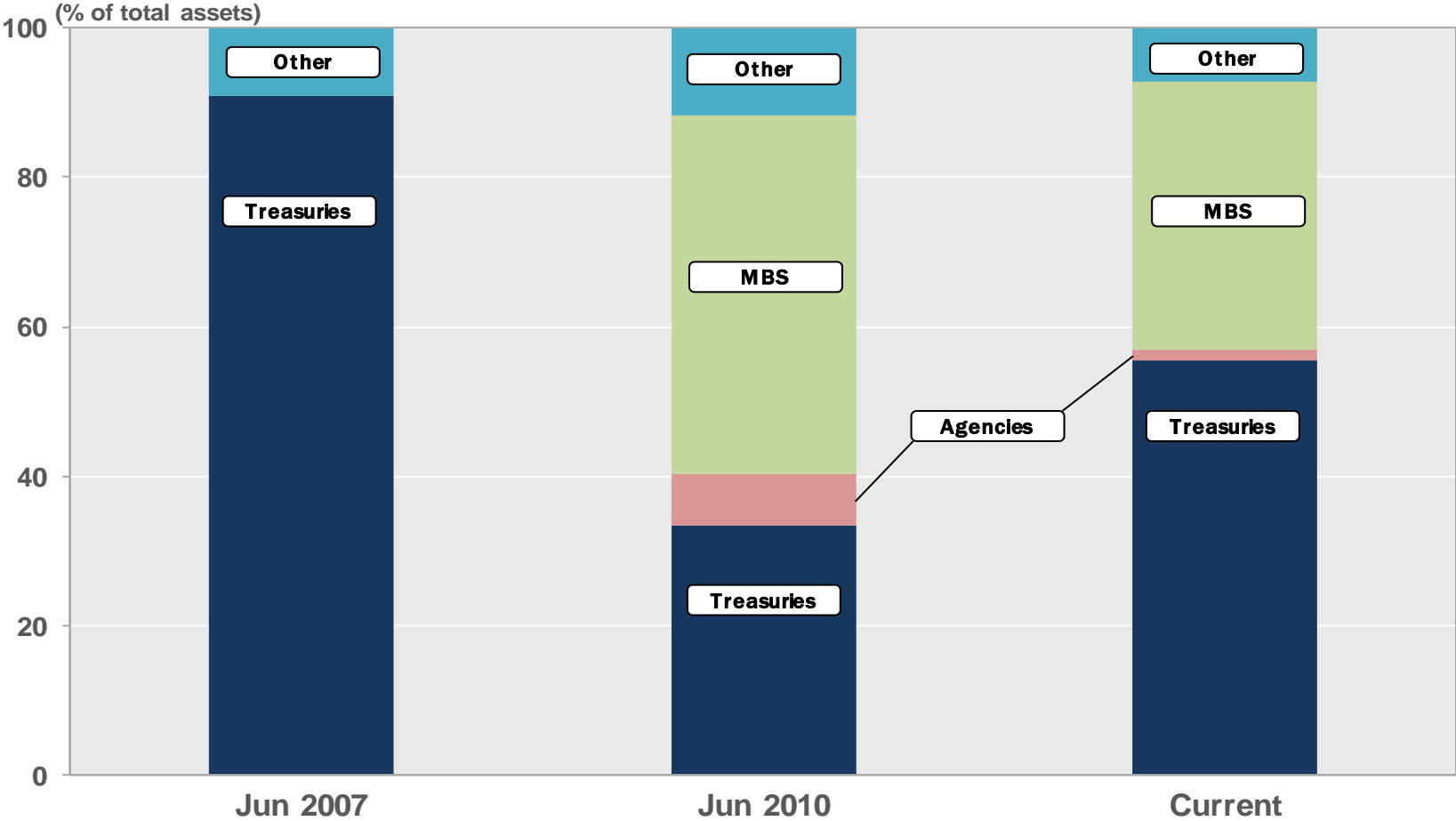
Source: ECB, Fed; Last Observation: Main Policy Rate - 7 Oct, 2013; Real Rate - Aug 2013 (Fed), Aug 2013

Total Assets of Key Central Banks (indexed levels)



Source: Bloomberg; Last Observation: Fed: Oct 2, 2013; ECB: Sep 27, 2013; BoJ: Sep 30, 2013.

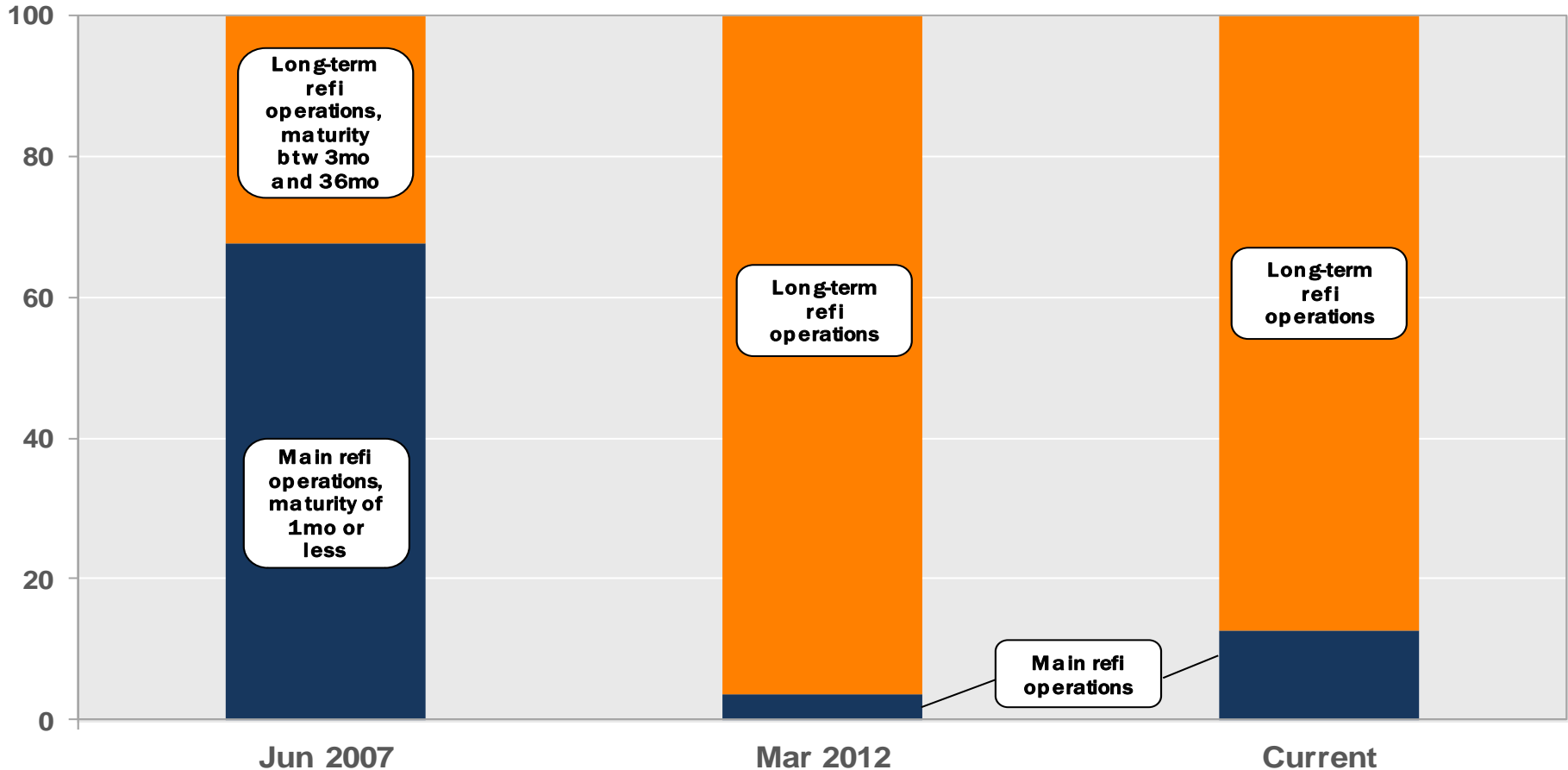
Composition of Federal Reserve Assets



Source: Federal Reserve, Bloomberg, Last Observation: October 2, 2013.

Composition of ECB Liquidity Facilities

(% of total liquidity measures)



Note: March 2012 follows two rounds of 36-month LTRO auctions that occurred December 21, 2011 and February 29, 2012.

Source: ECB, Last Observation: September 27, 2013

Current Central Bank Forward Guidance

Federal Reserve

“the Committee today reaffirmed its view that a highly accommodative stance of monetary policy will remain appropriate for a considerable time after the asset purchase program ends and the economic recovery strengthens.”

-Monetary Policy Release, September 18, 2013

ECB

“The Governing Council confirms that it expects the key ECB interest rates to remain at present or lower levels for an extended period of time. This expectation continues to be based on an unchanged overall subdued outlook for inflation extending into the medium term, given the broad-based weakness in the economy and subdued monetary dynamics.”

-ECB President Mario Draghi, Introductory statement to the press conference, October 2, 2013

BoE

“the MPC intends not to raise Bank Rate from its current level of 0.5% at least until the Labour Force Survey headline measure of the unemployment rate has fallen to a threshold of 7%, subject to the conditions below.”

-Inflation Report, August 7, 2013

BoJ

“The Bank will continue with quantitative and qualitative monetary easing, aiming to achieve the price stability target of 2 percent, as long as it is necessary for maintaining that target in a stable manner.”

-Statement of Monetary Policy, October 4, 2013

Evolution of Fed Forward Guidance

August 12, 2003

“the Committee believes that policy accommodation can be maintained for a considerable period.”

December 16, 2008

“the Committee anticipates that weak economic conditions are likely to warrant exceptionally low levels of the federal funds rate for some time.”

March 18, 2009

“The Committee will maintain the target range for the federal funds rate and anticipates that economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period.”

August 9, 2011

“The Committee currently anticipates that economic conditions--including low rates of resource utilization and a subdued outlook for inflation over the medium run--are likely to warrant exceptionally low levels for the federal funds rate at least through mid-2013.”

December 12, 2012

“the Committee...currently anticipates that this exceptionally low range for the federal funds rate will be appropriate at least as long as the unemployment rate remains above 6-1/2 percent, inflation between one and two years ahead is projected to be no more than a half percentage point above the Committee’s 2 percent longer-run goal, and longer-term inflation expectations continue to be well anchored.”

September 18, 2013

“the Committee today reaffirmed its view that a highly accommodative stance of monetary policy will remain appropriate for a considerable time after the asset purchase program ends and the economic recovery strengthens.”