

Why inflation targeting is the best thing since Ackee and Saltfish

MD

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Inflation Targeting: Getting the right temperature to shelter you from the storm...



Inflation is an all-encompassing variable. Managing inflation means by extension, managing almost everything else...

Fiscal policy

Trade policy

Exchange Rate

Money supply

Interest rates

Labour policies

and a long etcetera...

By measuring, monitoring and managing inflation, we affect many other variables, but most importantly, people's lives:

- Purchasing power
- Real wages / incomes
- Productivity
- Standard of living
- Poverty
- Inequality
- Brain drain / gain

"The Economic Determinants of Happiness" (2011):

1.0% increase in inflation



3.1% reduction in national happiness

*Source: "The Economic Determinants of Happiness",
Teng Guo, Lingyi Hu, Cornell University 2011.*

Therefore, managing inflation should yield better social outcomes...

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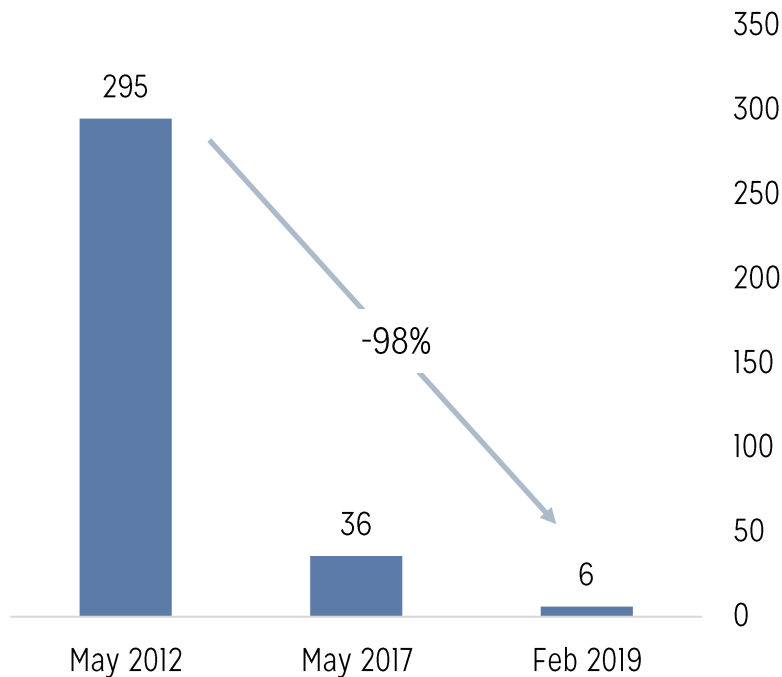
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What happens when inflation gets out of control?

We don't have too look far to see...

Venezuela: Monthly Minimum Wage

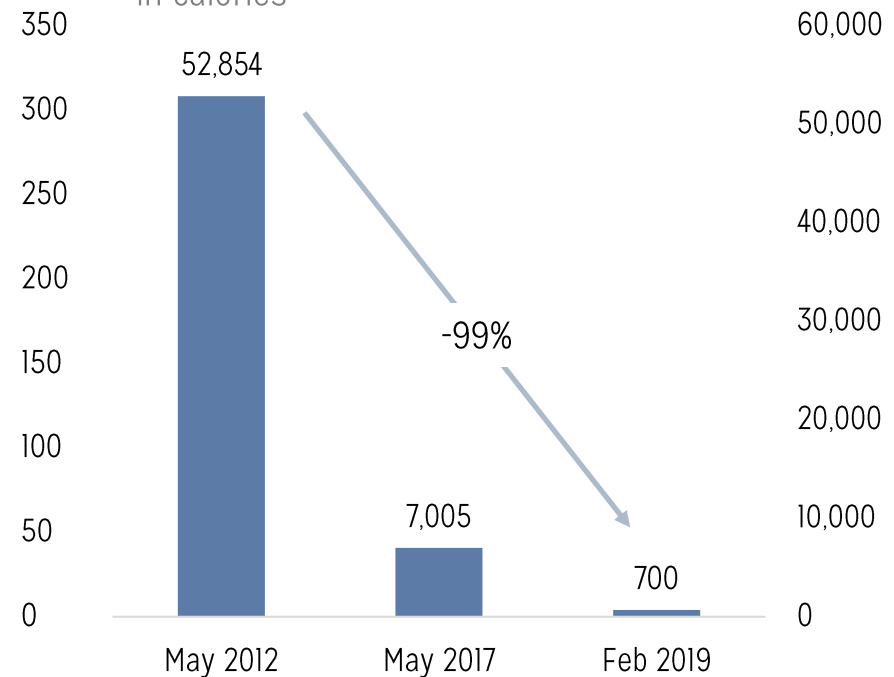
in USD



Source: Marla Dukharan, Economist Ricardo Hausmann, Harvard CID

Venezuela: Max Daily Calories Purchasable with Monthly Min Wage

in calories



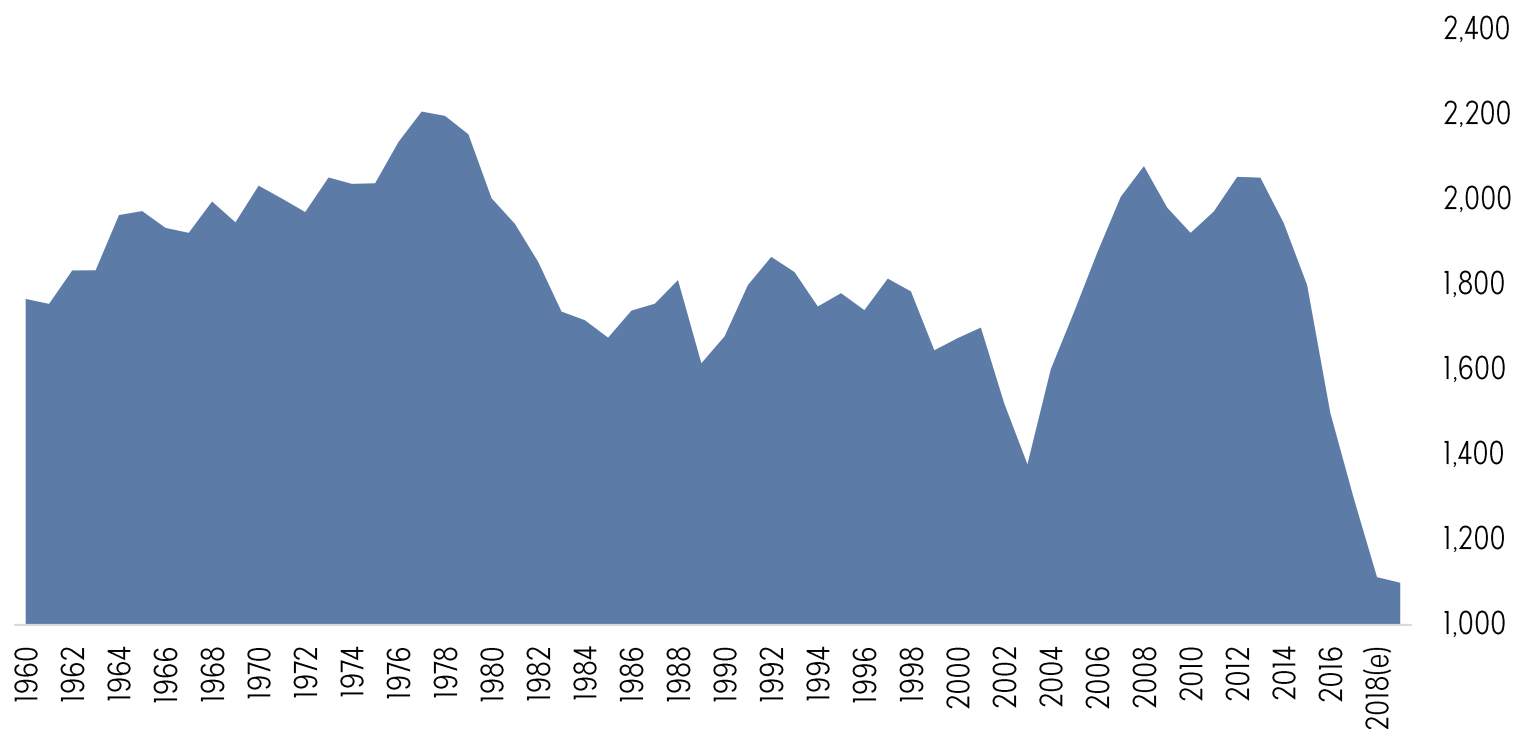
Source: Marla Dukharan, Economist Ricardo Hausmann, Harvard CID

2/3 of Venezuelans lost on average of 24 pounds in 2017
3/4 of Venezuelans lost an average of 19 pounds in 2016

While Venezuela's crisis is unique in many ways, it demonstrates clearly how irresponsible fiscal and other policies drive inflation, which undermines everything else...

Venezuela: GDP per capita last 60 years

Thousands of Bs at 1997 prices



Source: World Bank, International Monetary Fund, Marla Dukharan, José Manuel Puente

...causing people to flee in droves. Venezuela's is the worst migration/refugee crisis in the history of this Hemisphere



Source: UN Refugees (ANCUR)

Migration/Refugee Crisis

Over 3.4 million people have fled Vzla in the last 3 years, roughly 10% of the country's population.

This could reach 5.4 million in 2019 8.2 million in 2020, according to the OAS.

Compares to refugees from conflicts in Syria (5.6 million), Afghanistan (2.5 million) and South Sudan (2.3 million).

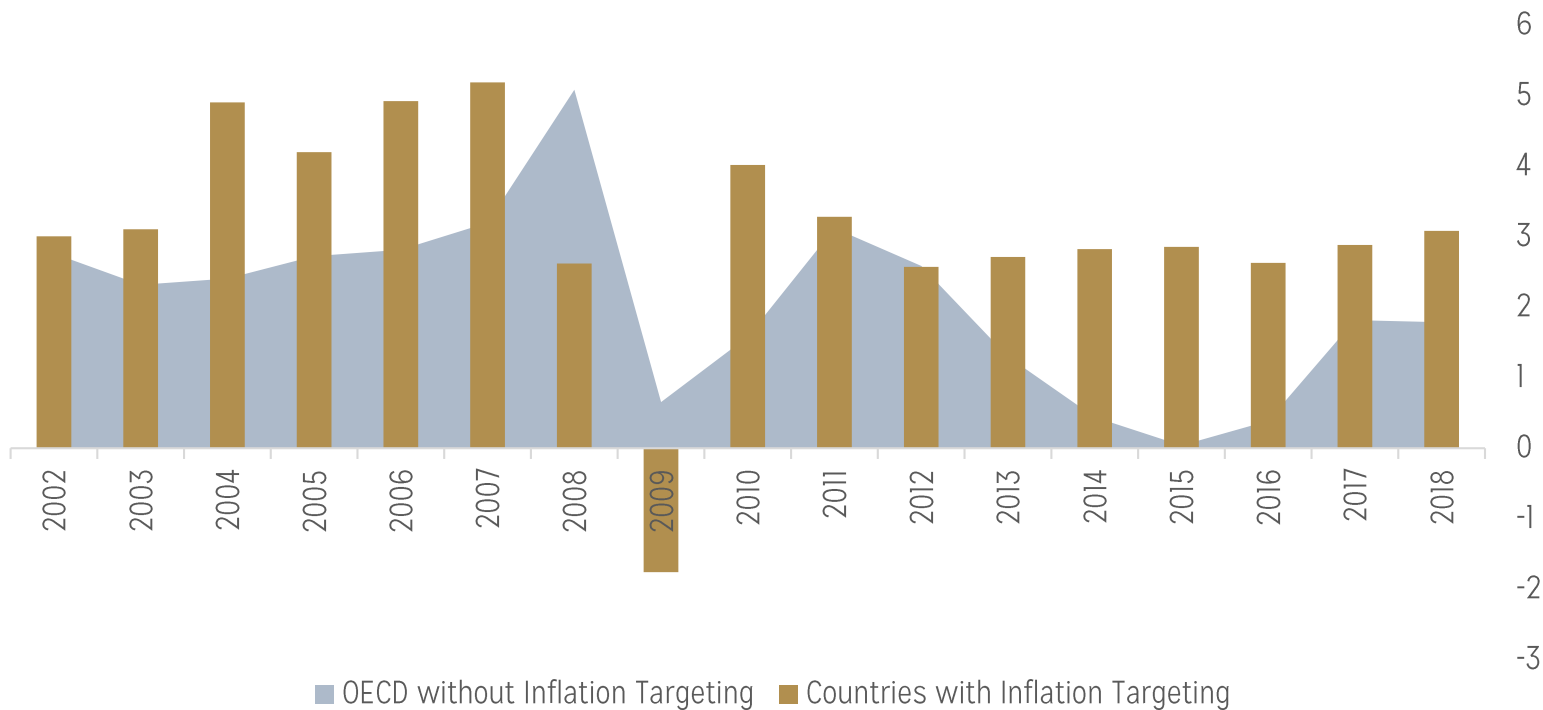
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What happens when we measure,
manage and control inflation?

How do countries under inflation targeting stack up, versus countries without inflation targeting?

GDP Growth

Average annual percent change (%)

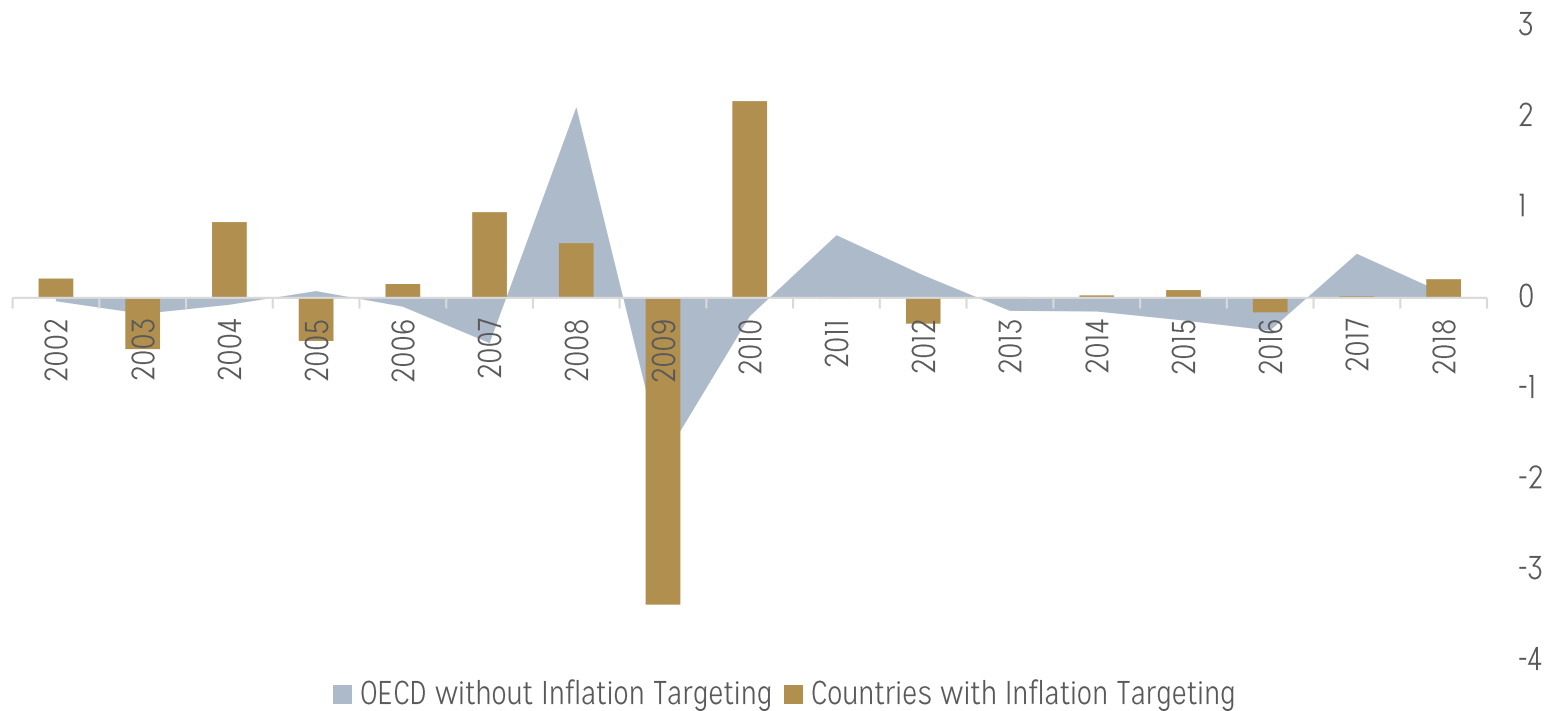


Source: IMF, Marla Dukharan

With inflation targeting, growth and broader economic conditions become more stable and predictable...

Volatility of GDP Growth

Percentage (%)

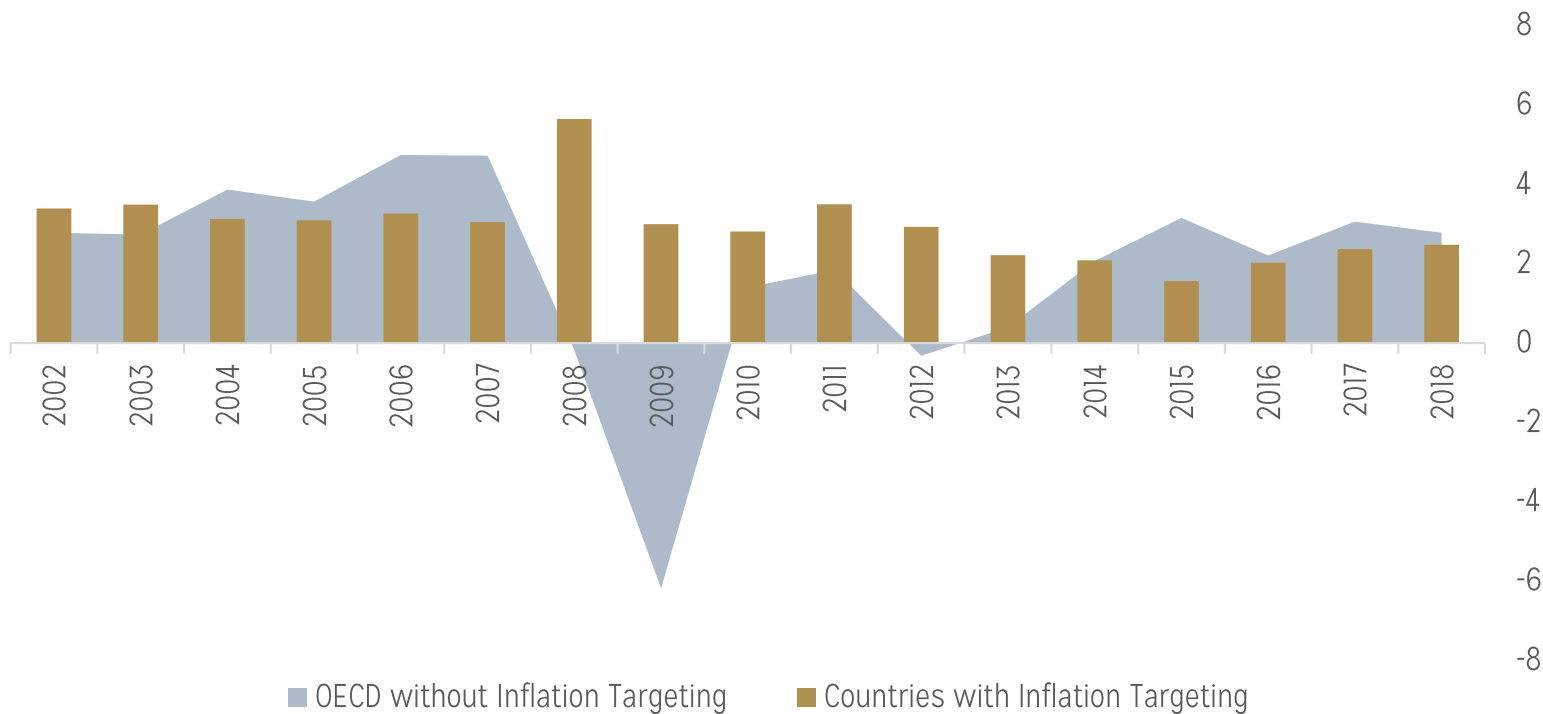


Source: IMF, Marla Dukharan

OECD countries with inflation targeting regimes, have lower inflation on average, than those without...

Inflation

Average annual percent change (%)

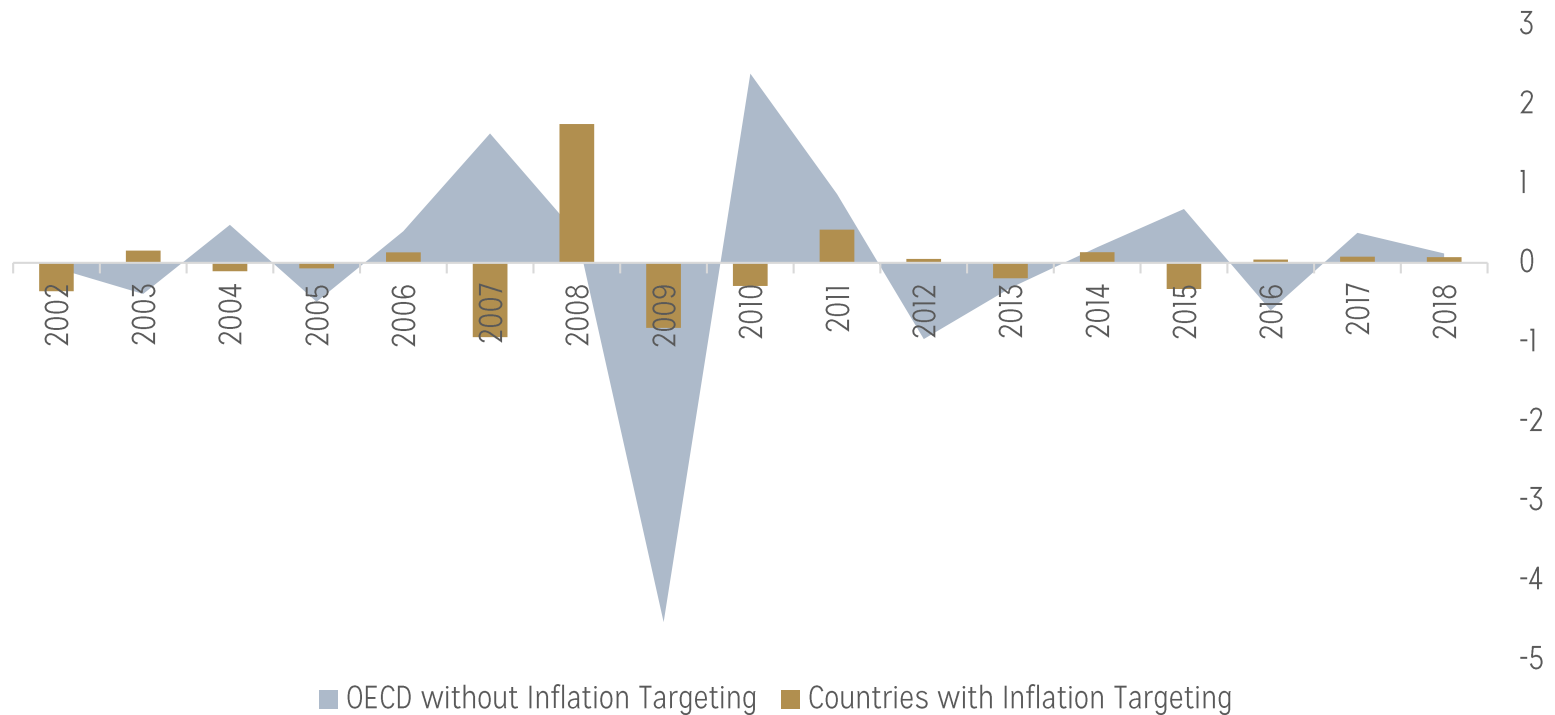


Source: IMF, Marla Dukharan

And there is less volatility in the inflation rate, for those with inflation targeting regimes...

Volatility of Inflation

Percent (%)

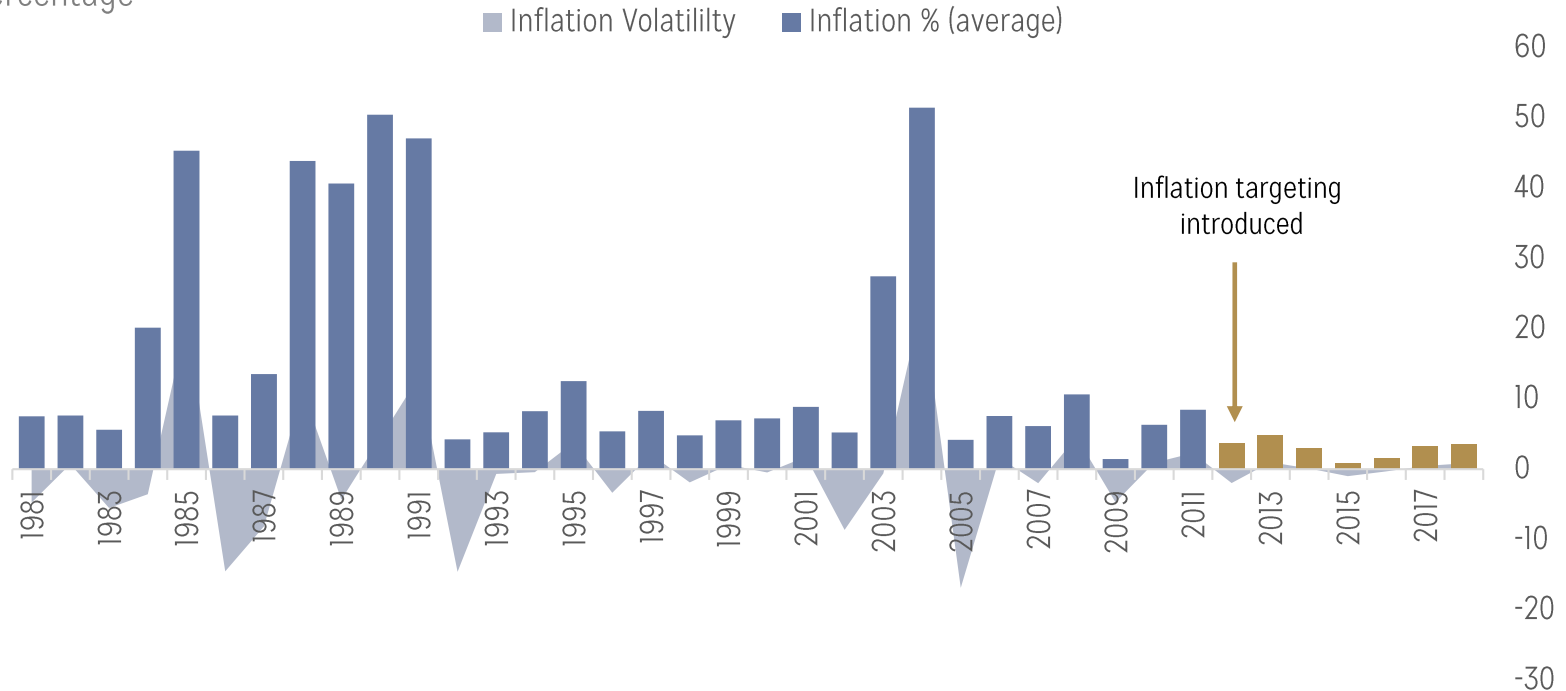


Source: IMF, Marla Dukharan

The Dominican Republic recorded inflation rates in excess of 20% NINE times between 1980 and the start of their inflation targeting regime in 2012

Inflation Rate and Volatility: Dominican Republic

Percentage

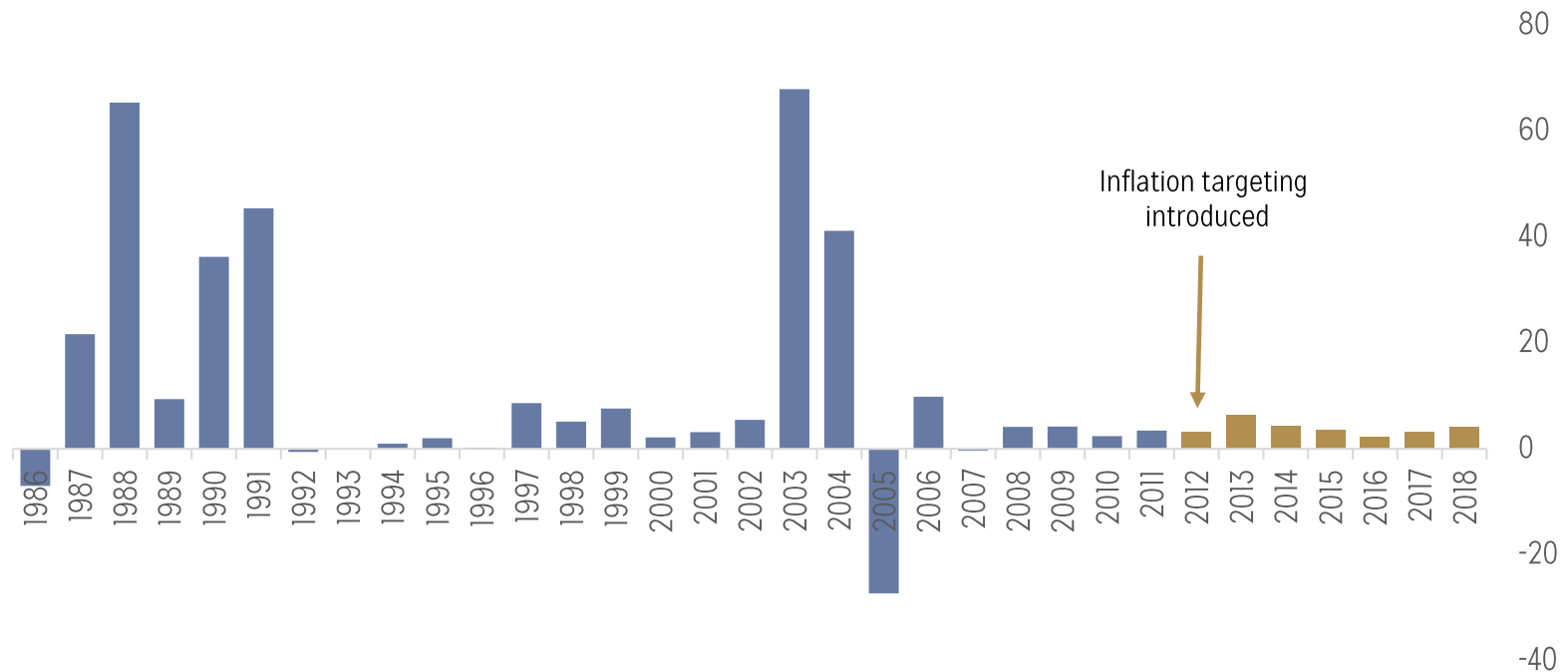


Source: IMF, Marla Dukharan

The Dominican Republic implemented their inflation targeting regime in 2012, further reducing exchange rate the volatility

Exchange Rate Variation: Dominican Republic

Nominal exchange rate variation percentage

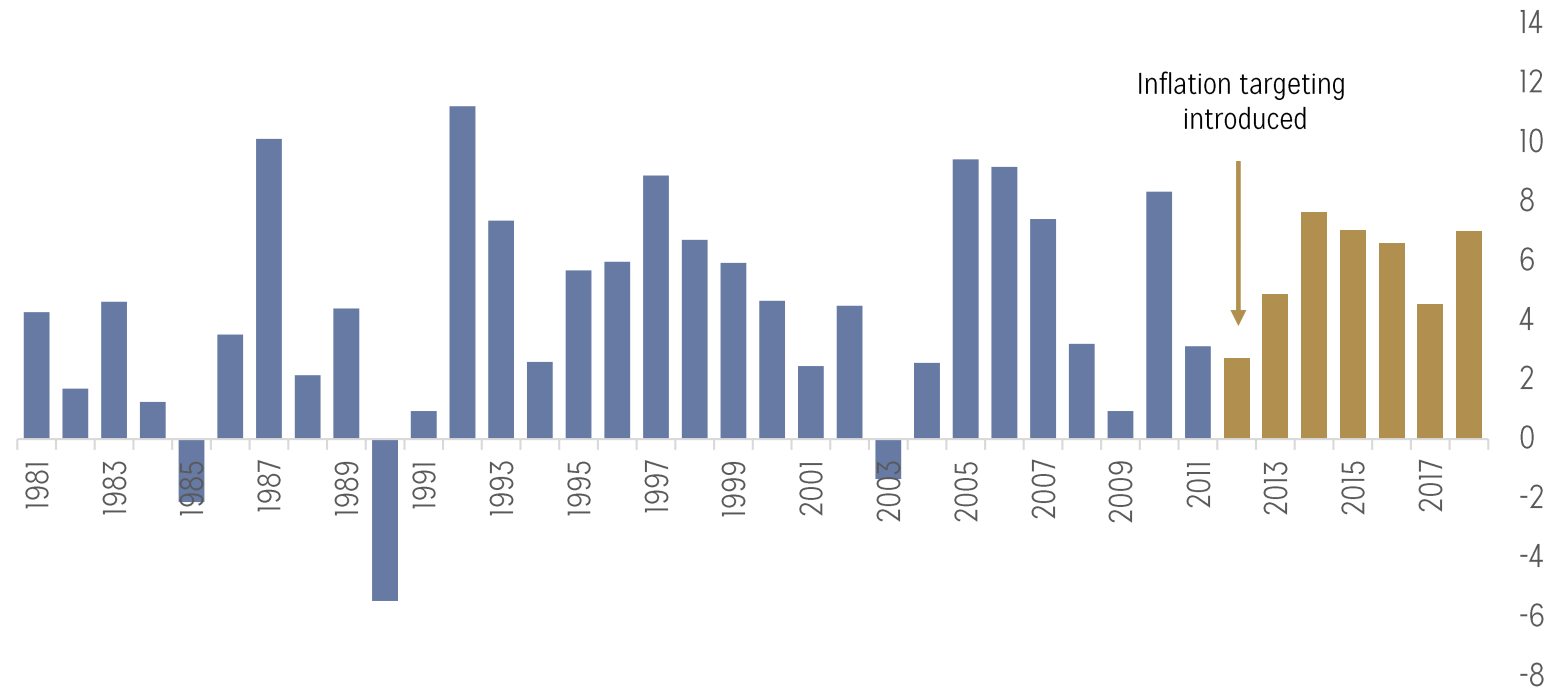


Source: IMF, Marla Dukharan

And while the economy was able to achieve strong growth in the years prior to the inflation targeting regime, the growth was more volatile...and social outcomes lagged

GDP Growth: Dominican Republic

Percentage Change y/y (%)

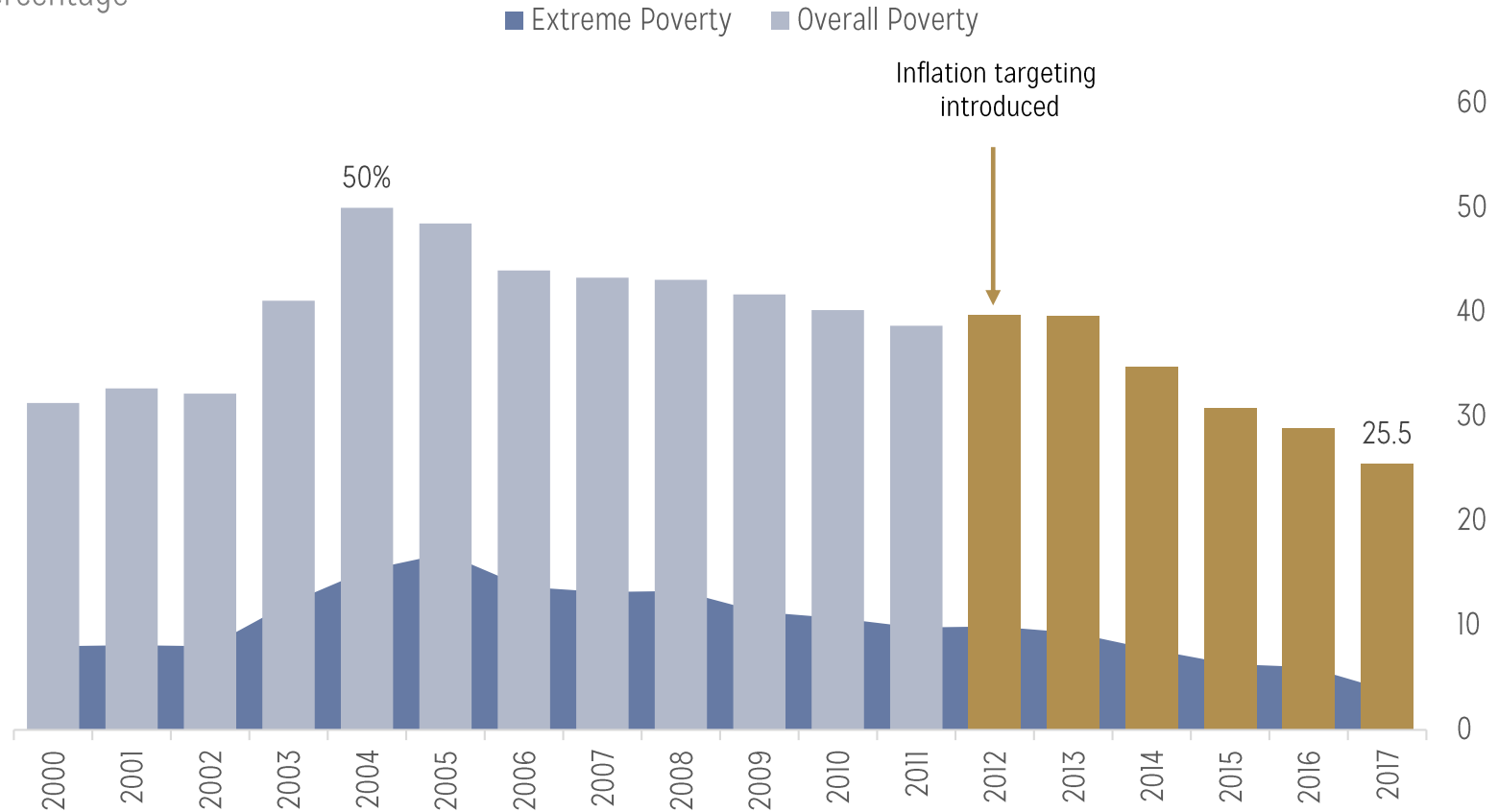


Source: IMF, Marla Dukharan

Poverty rates peaked at 50% in 2004, and in 2005, 17% of the population was living in extreme poverty. In 2017 extreme poverty affected less than 4% of the population

Poverty Rates: Dominican Republic

Percentage

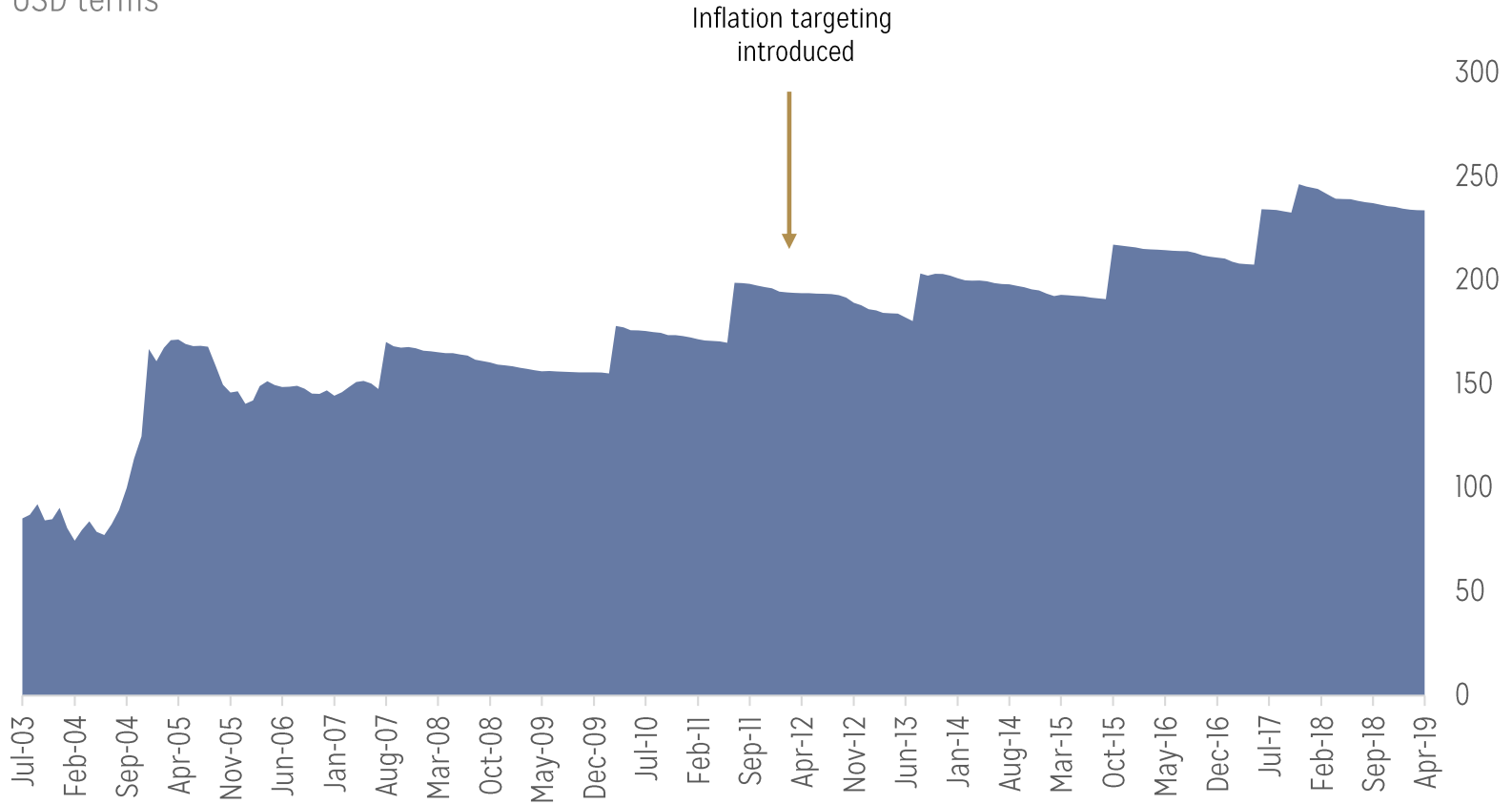


Source: Oficina Nacional de Estadísticas de la República Dominicana, Marla Dukharan

The minimum wage has risen 20% (in USD terms) since inflation targeting was introduced in 2012, maintaining / increasing purchasing power in 'real' terms

Minimum Wage: Dominican Republic

in USD terms

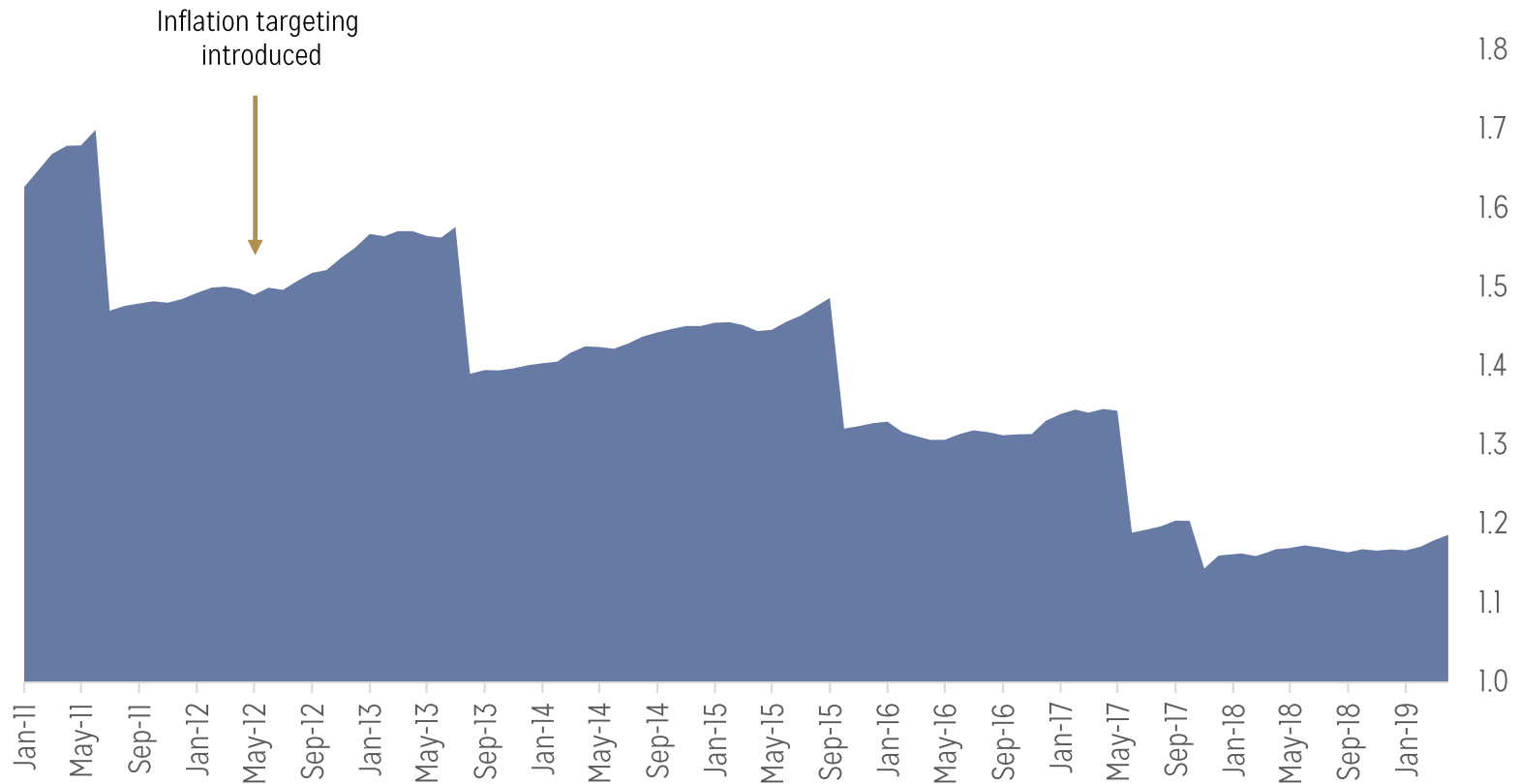


Source: Applicable Minimum Wage from Superintendencia de Pensiones, BCRD, Marla Dukharan

Since inflation targeting was introduced, the number of minimum wages needed to buy a basic basket of goods has declined to just under 1.2

Number of Minimum Wages to buy Basic Basket: Dominican Republic

in USD terms

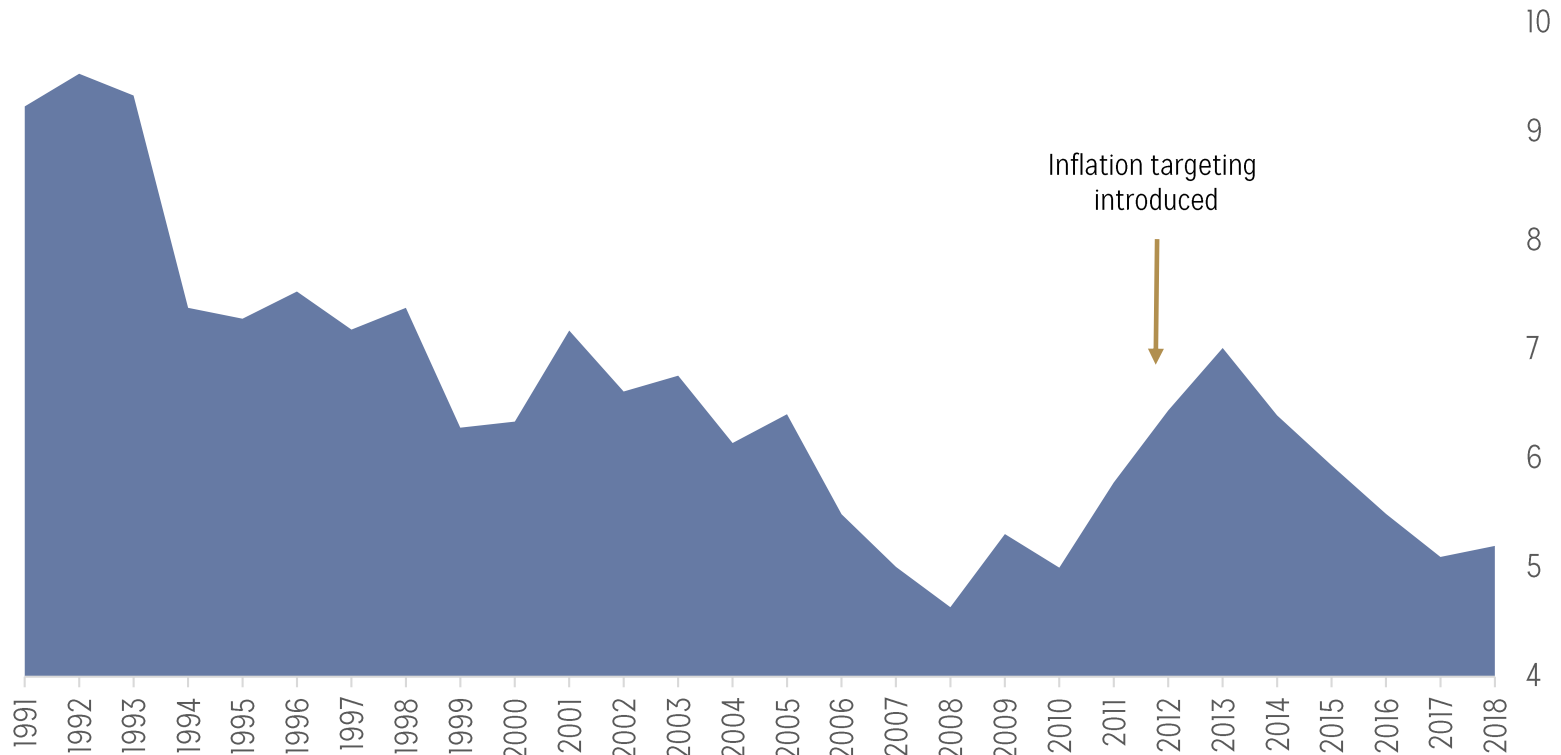


Source: Basic basket Quintile 1, Applicable Minimum Wage from Superintendencia de Pensiones, BCRD, Marla Dukharan

Unemployment began to rise in 2011, reaching 7% in 2013. It has now fallen to 5.8% - far below pre-inflation targeting average

Unemployment Rate: Dominican Republic

Percent

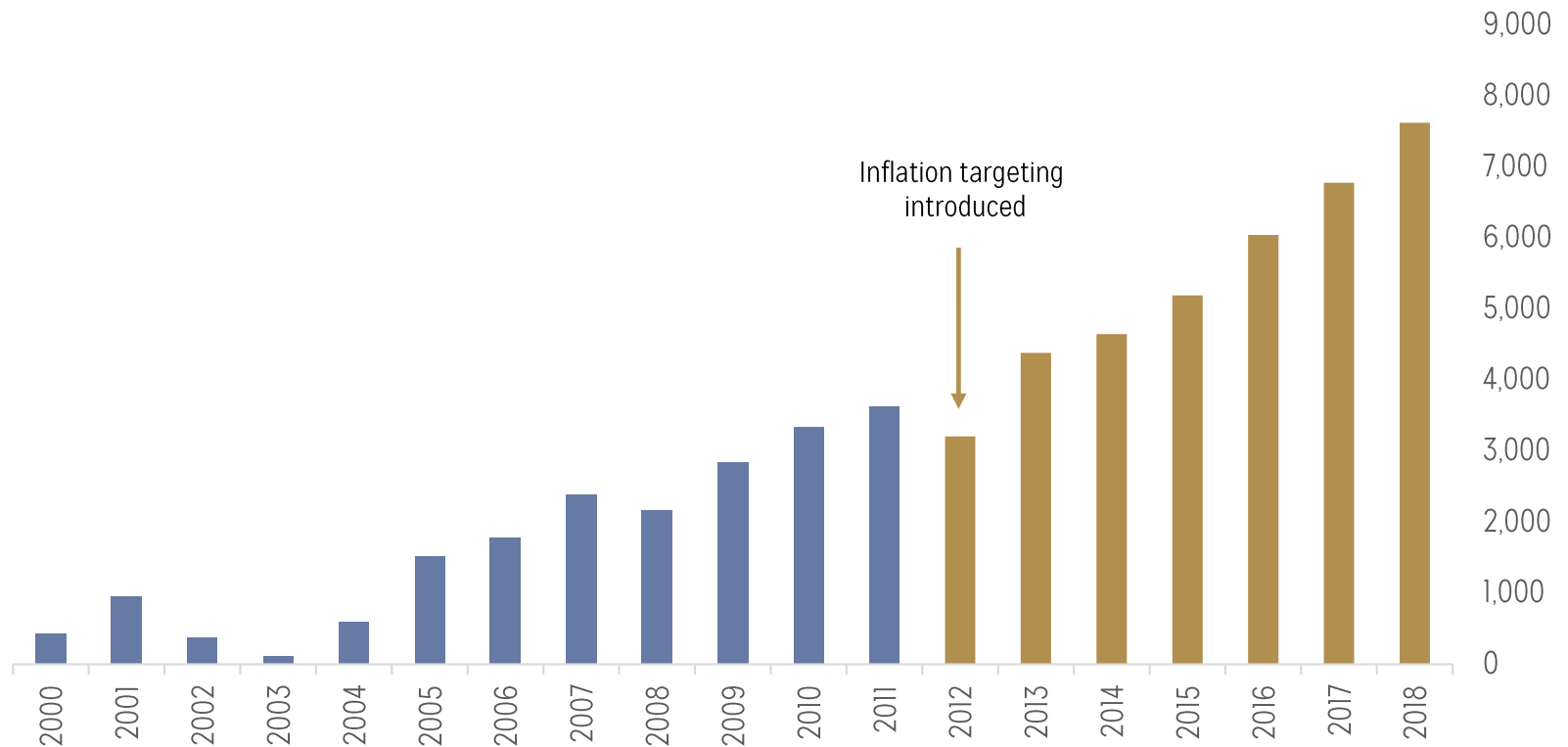


Source: IMF, Marla Dukharan

International Reserves have doubled since inflation targeting was introduced, from USD3.6 billion at the end of 2011 to USD7.6 billion at the end of 2018

International Reserves: Dominican Republic

in USD millions



Source: BCRD, Marla Dukharan

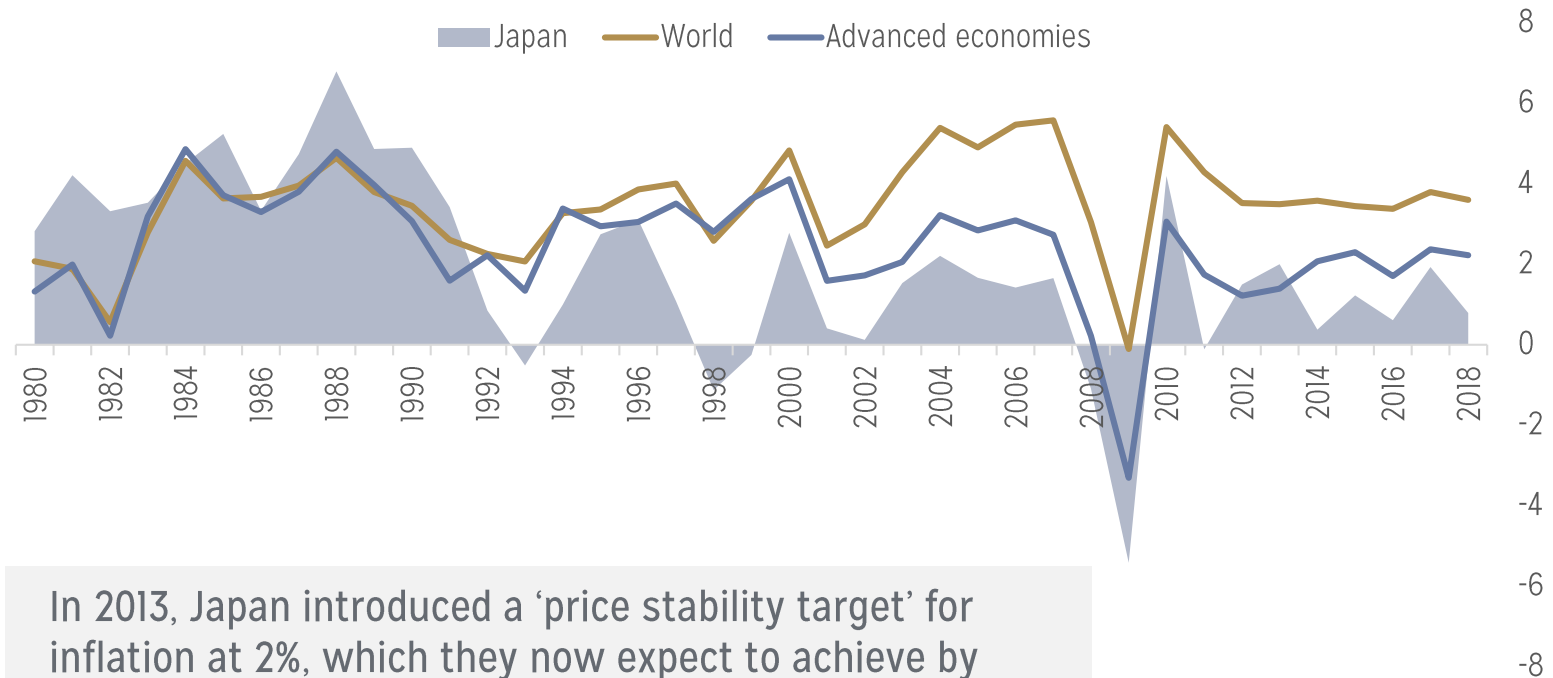
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What happens when
inflation goes too low?

Japan has been underperforming global growth for nearly 3 decades

GDP Growth: Japan

Percent Change (%)



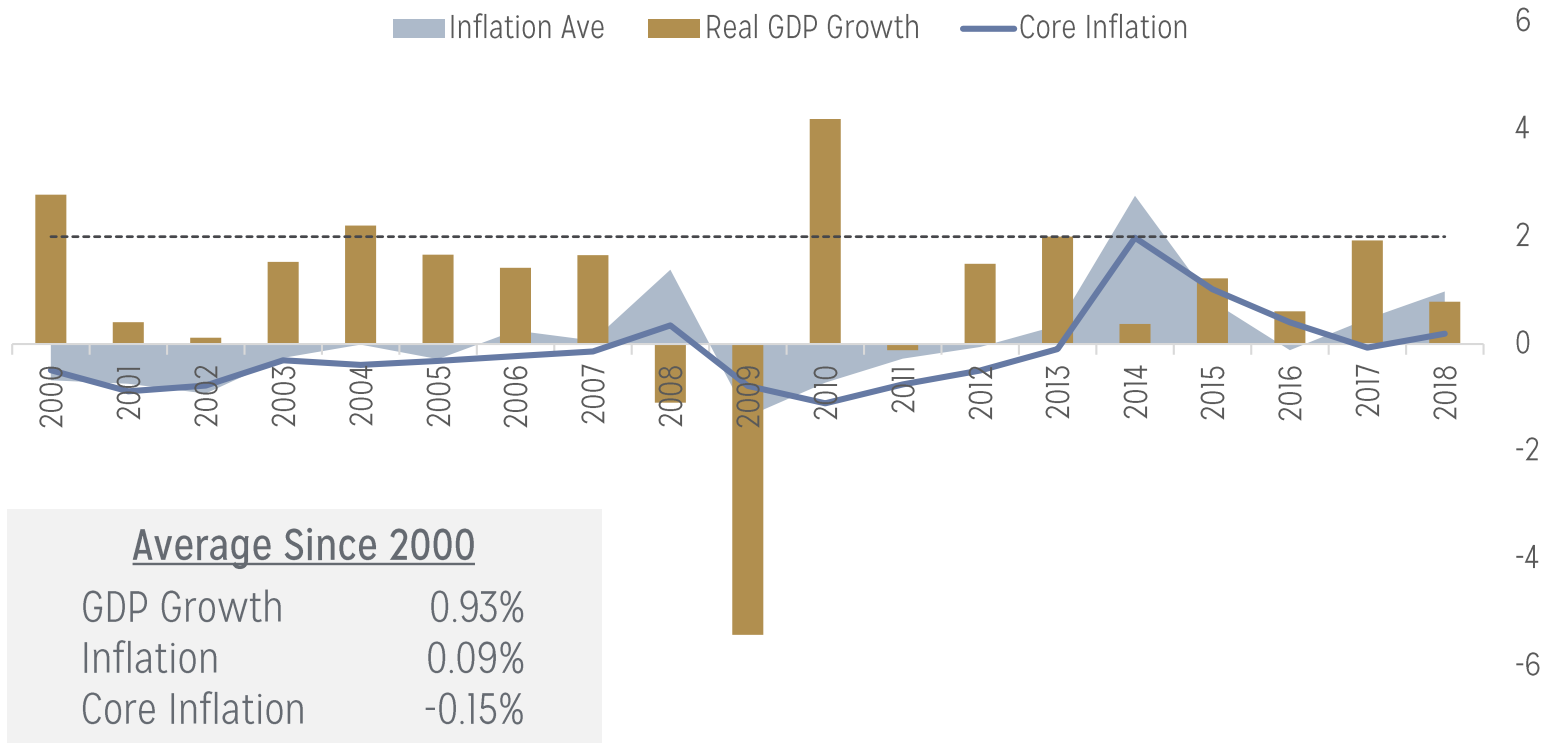
In 2013, Japan introduced a 'price stability target' for inflation at 2%, which they now expect to achieve by 2020.

Source: IMF, OECD, Marla Dukharan

Annual economic growth in Japan has only been above 2% THREE times this century... while the country experienced 11 years of negative inflation

GDP Growth and Inflation: Japan

Percent change (%)



Source: IMF, OECD, Marla Dukharan

But low inflation doesn't always mean low growth...

What matters is not so much the inflation rate itself, but **WHY** the inflation rate is above or below target.

External

- ✓ Global commodity prices
- ✓ USD strength / weakness
- ✓ Major trading partners' inflation
- ✓ Geopolitical events
- ✓ Climate related shocks

Domestic

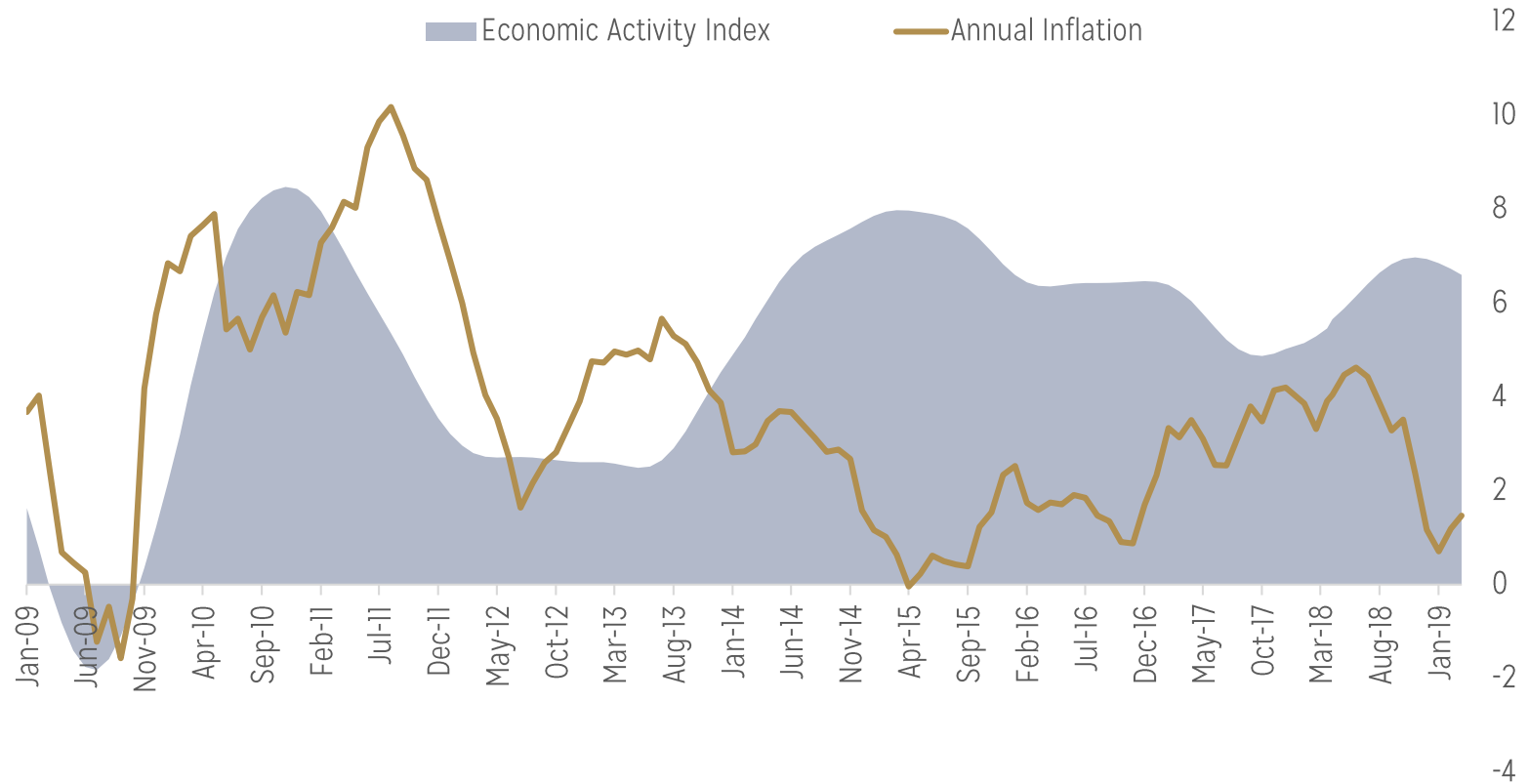
- ✓ Tax policy
- ✓ Fiscal stance
- ✓ Exchange rate
- ✓ Weather-related events
- ✓ Effects on agriculture (both positive and negative)

Some factors can be influenced by monetary policy, but others can't...

The Dominican Republic has had low inflation (below target) while economic activity continues to expand at a pace above 6%.

Inflation and Economic Growth: Dominican Republic

Percent (%)

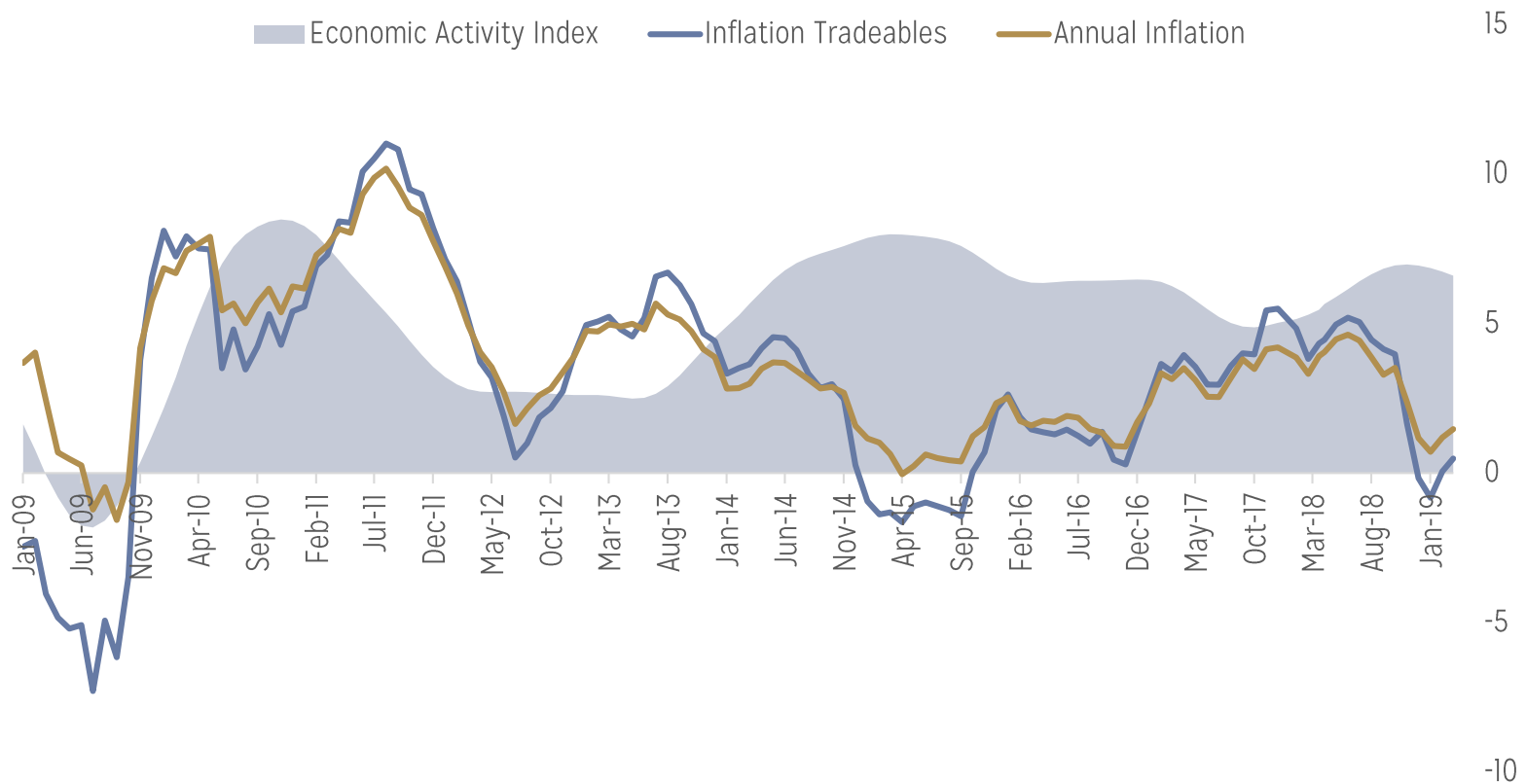


Source: BCRD, Marla Dukharan

In the Dominican Republic, the 'tradeables' sector is pulling the overall inflation rate lower

Tradeables Inflation and Economic Growth: Dominican Republic

Percent (%)

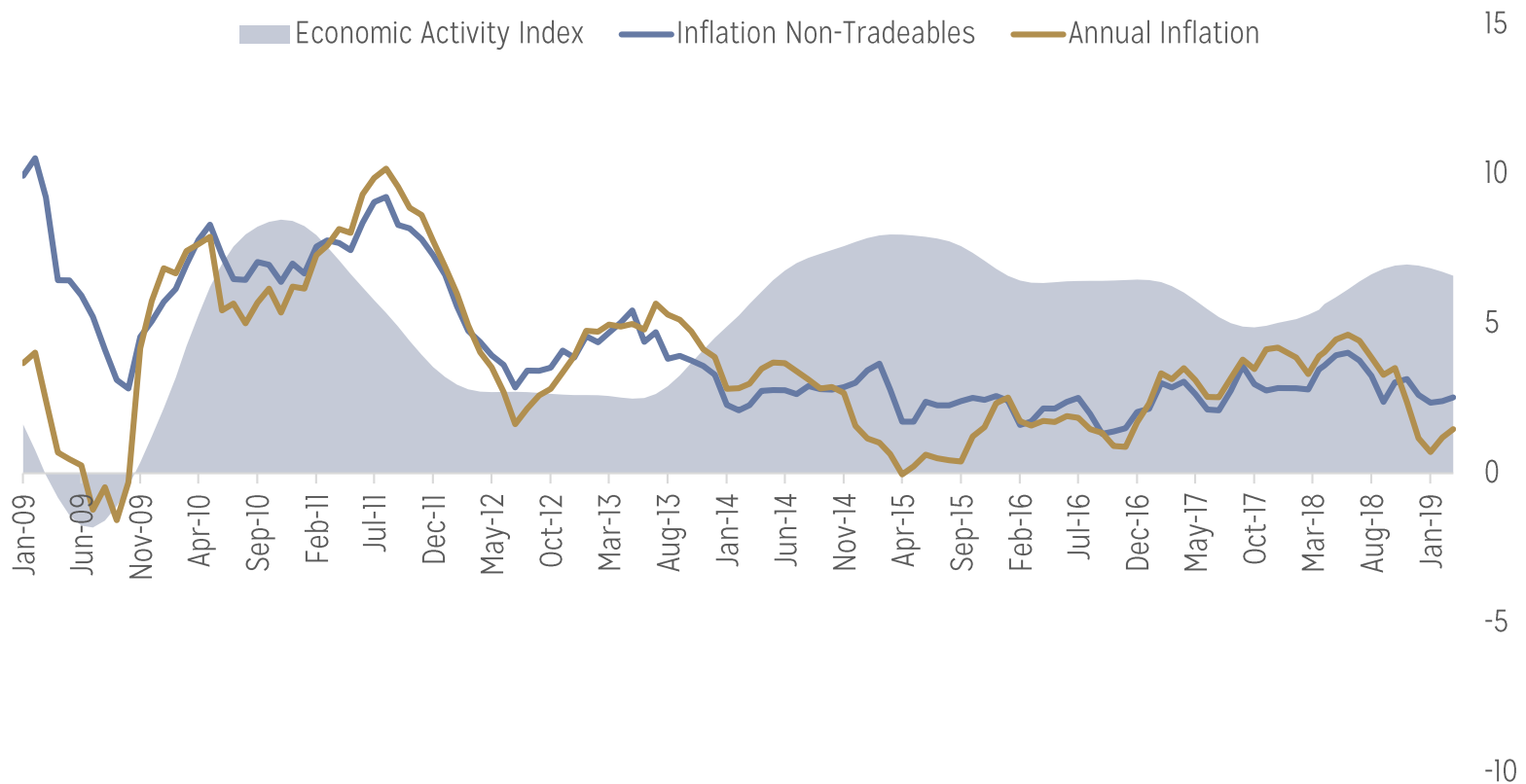


Source: BCRD, Marla Dukharan

Meanwhile, the inflation in the non-tradeables has been much closer aligned to the inflation target range of 4% ± 1%.

Non-Tradeables Inflation and Economic Growth: Dominican Republic

Percent (%)



Source: BCRD, Marla Dukharan

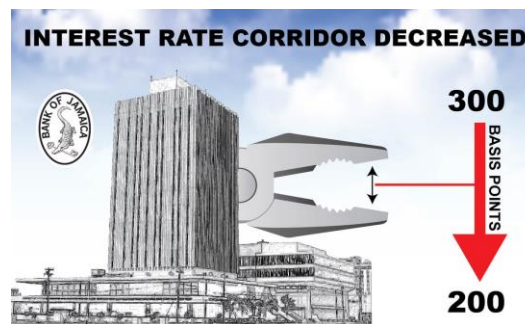
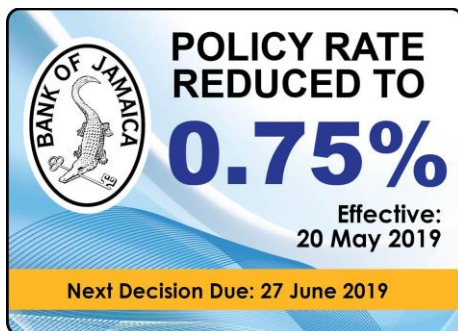
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What does it take to make
inflation targeting work?

“There is strong and systematic evidence that central bank independence contributes significantly and robustly to lower inflation.” – IDB.
Here are other important factors :

Policy Actions

- ✓ Lower interest rates
- ✓ Lower reserve ratio
- ✓ FX interventions



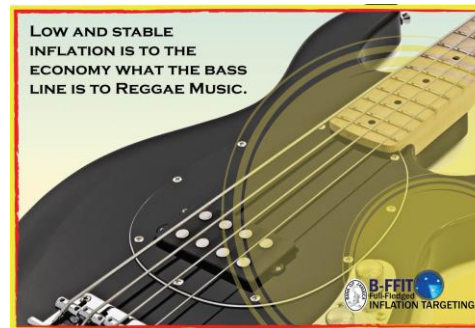
Bank of Jamaica intervened in the FX market today, 08 May 2019, with US\$30 million in a B-FXITT flash sale to authorized dealers and cambios.



The Bank of Jamaica should be expecting its Emmy and Academy award nominations soon...

Clear Communication

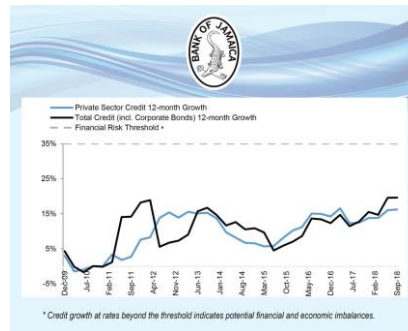
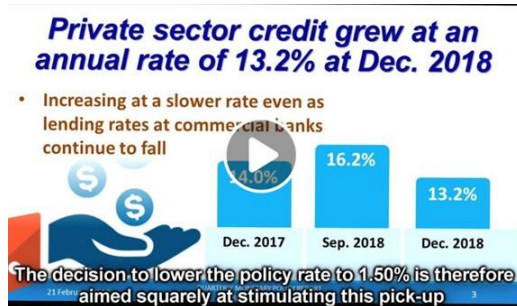
- ✓ Jodi-anne Murdock
- ✓ Tarrus Riley
- ✓ Donald Anderson
- ✓ Talia Soares
- ✓ Everyone is talking about #InflationTargeting



Consumer and investor confidence are high and rising...

Private Expectations

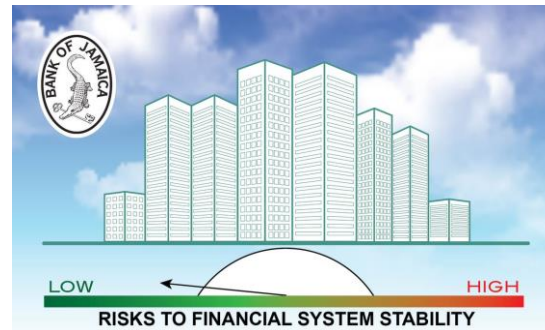
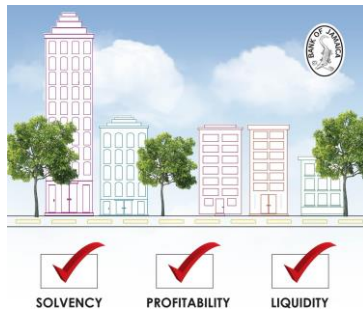
- ✓ Consumer and business confidence are high and rising



The Bank of Jamaica is the BEST Central Bank in the Caribbean!

Credibility of the Central Bank

- ✓ 1st CB to publish 2018 annual report in region
- ✓ Consistently reporting on time
- ✓ The only REAL financial stability report in the region



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Achieving better outcomes
for Jamaica

Other regional scenarios...

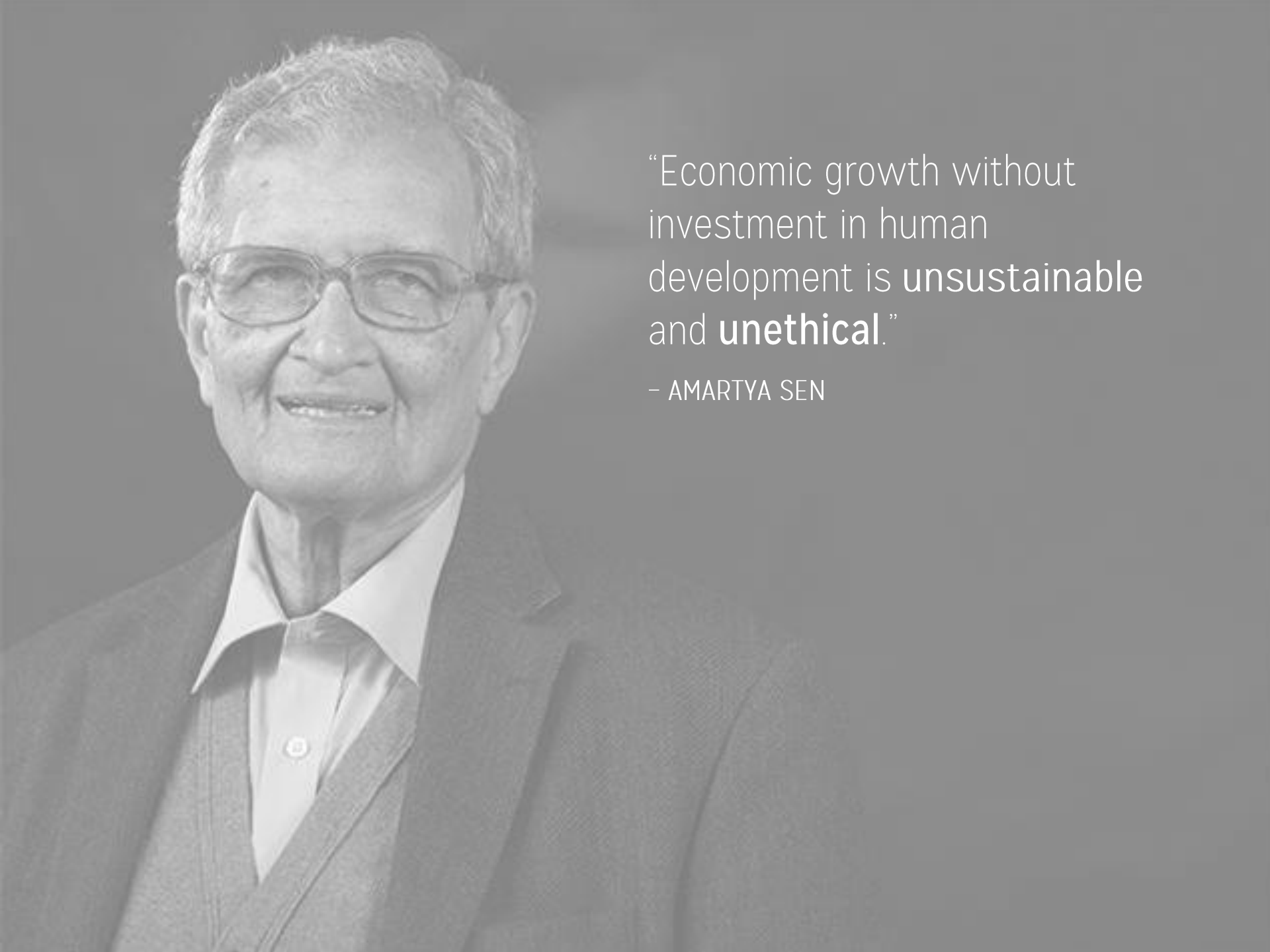
Unemployment
targeting

Growth targeting

Nothing targeting

Votes targeting

*Each of these has potential negative implications,
short and long term, for stability and broader social outcomes.*



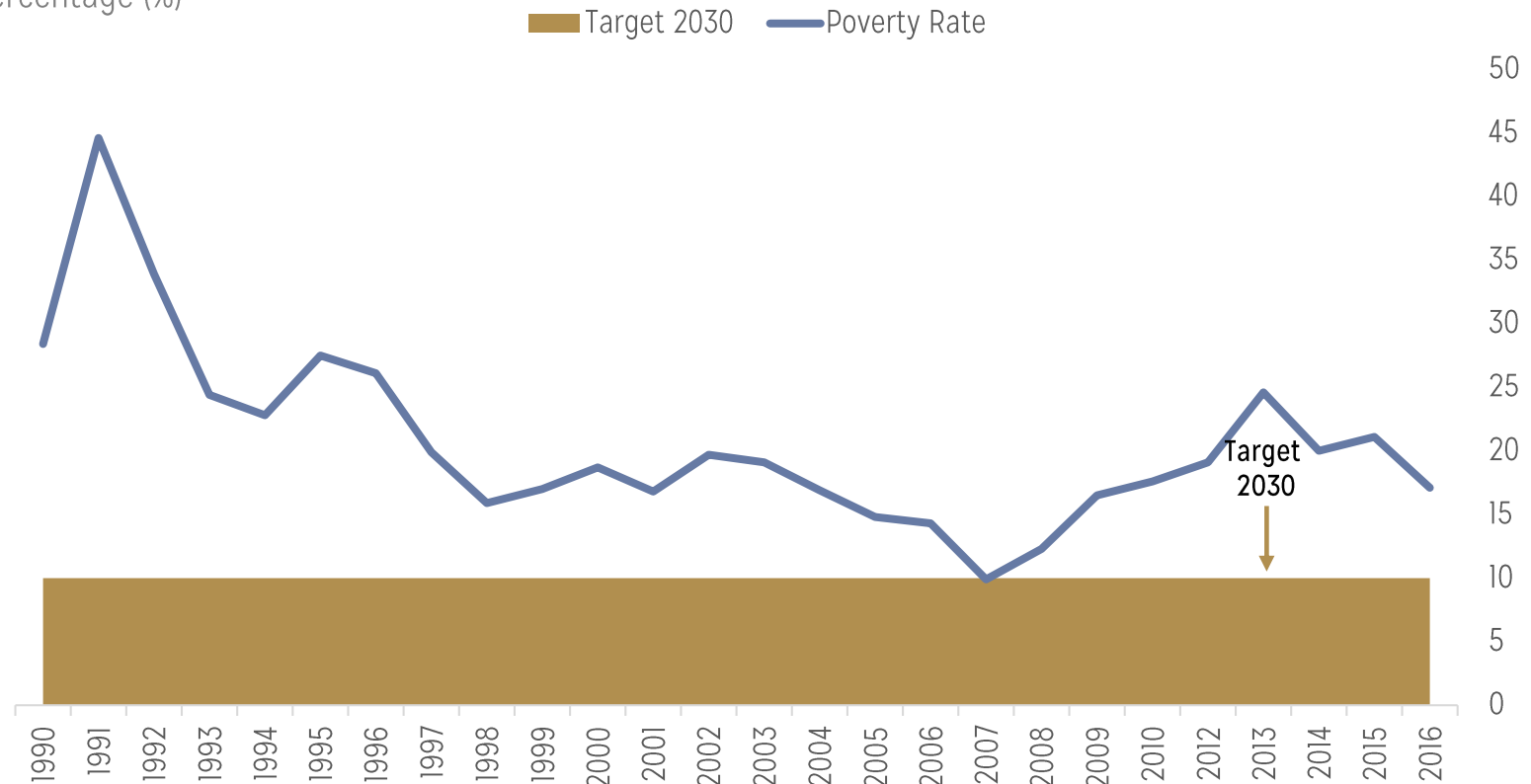
“Economic growth without investment in human development is **unsustainable** and **unethical**.”

– AMARTYA SEN

Jamaica's poverty rate is declining and has been on a downward trend since 2013, which is not the trend observed in the wider sovereign English-speaking Caribbean nations

Poverty Rate: Jamaica

Percentage (%)

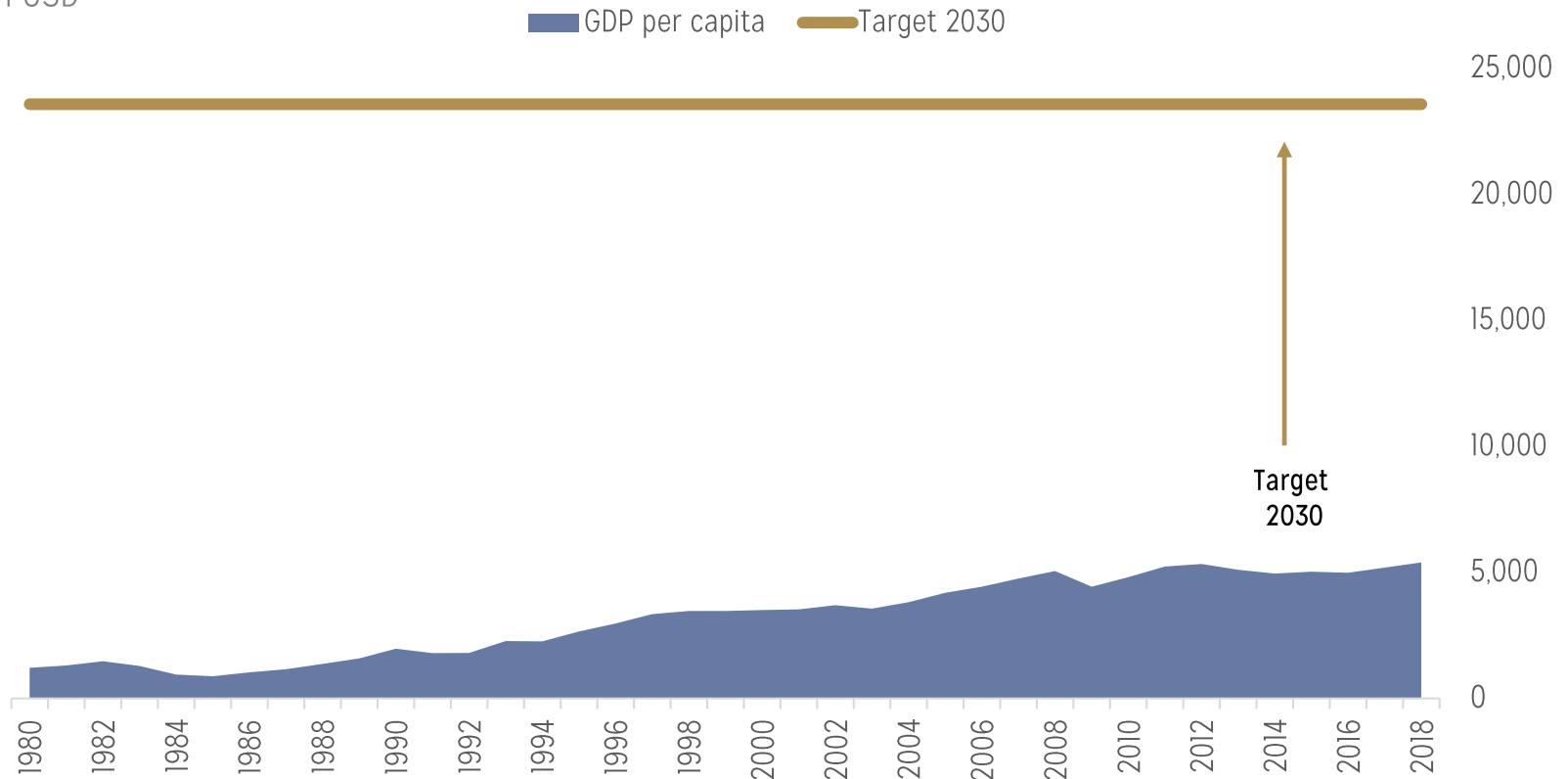


Source: National Policy on Poverty Reduction, Planning Institute of Jamaica, Marla Dukharan

Per-capita GDP is increasing – again, not the recent norm in the sovereign English-speaking Caribbean nations. T&T and Barbados have seen their GDP per capita decline in recent years

GDP per capita: Jamaica

in USD

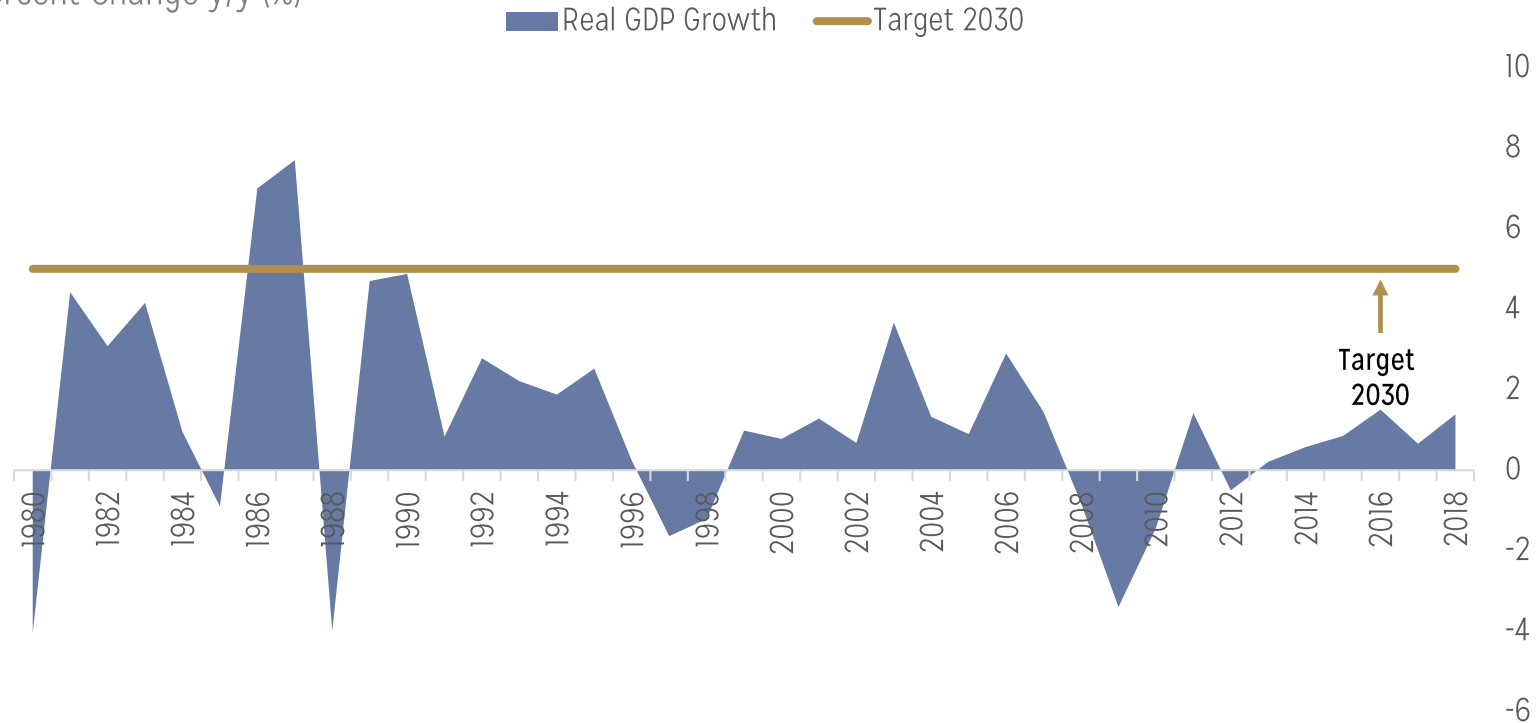


Source: Vision 2030, IMF, Marla Dukharan

Growth is positive, and consistently so, for the past 5-6 years – again, this is not the case in most of the sovereign English-speaking Caribbean nations

Real GDP Growth: Jamaica

Percent Change y/y (%)

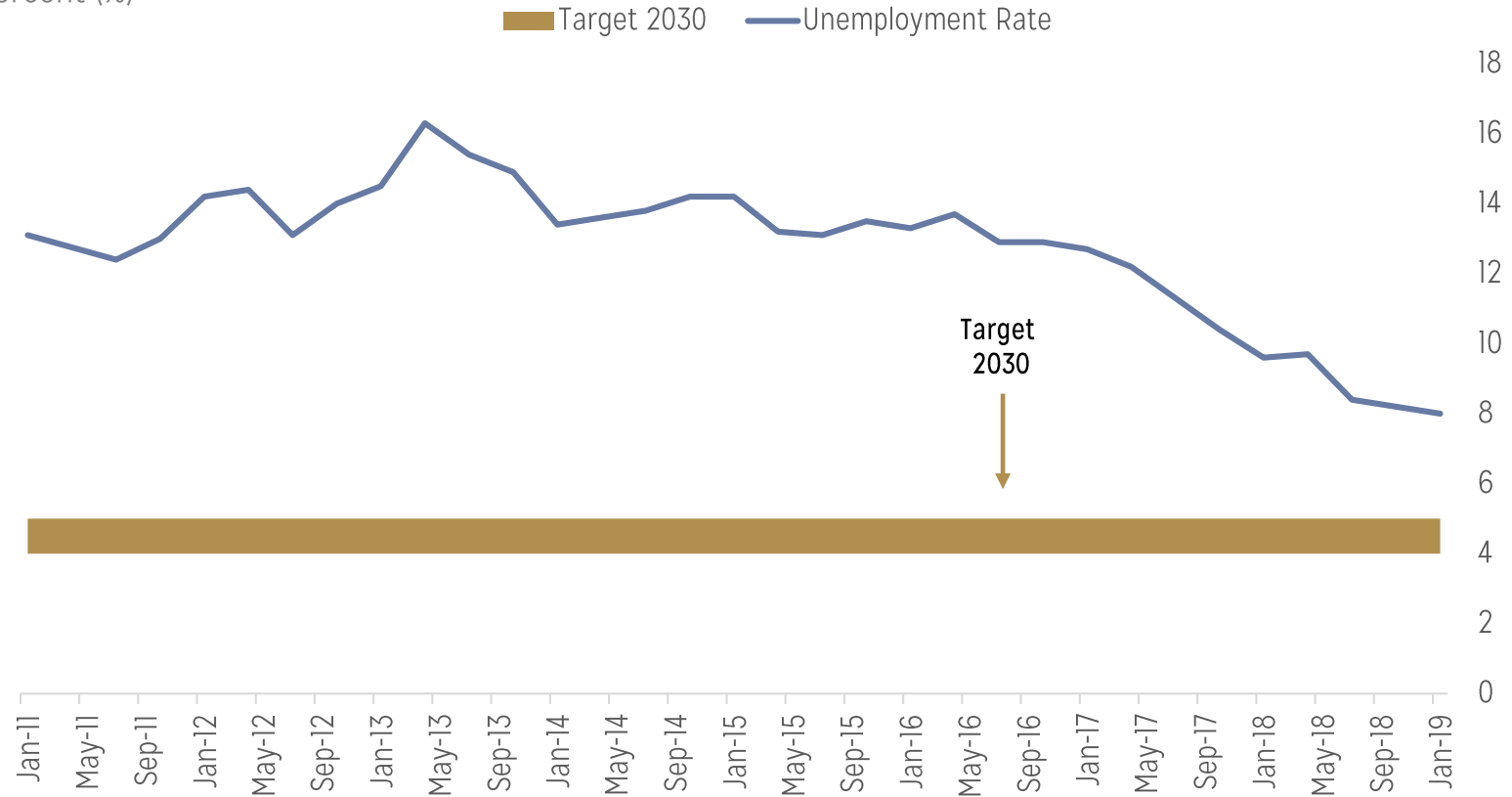


Source: Vision 2030, IMF, Marla Dukharan

How long has Jamaica waited for this kind of unemployment rate?
Only in the Cayman Islands do we see a trend like this, taking
unemployment to record lows

Unemployment Rate: Jamaica

Percent (%)

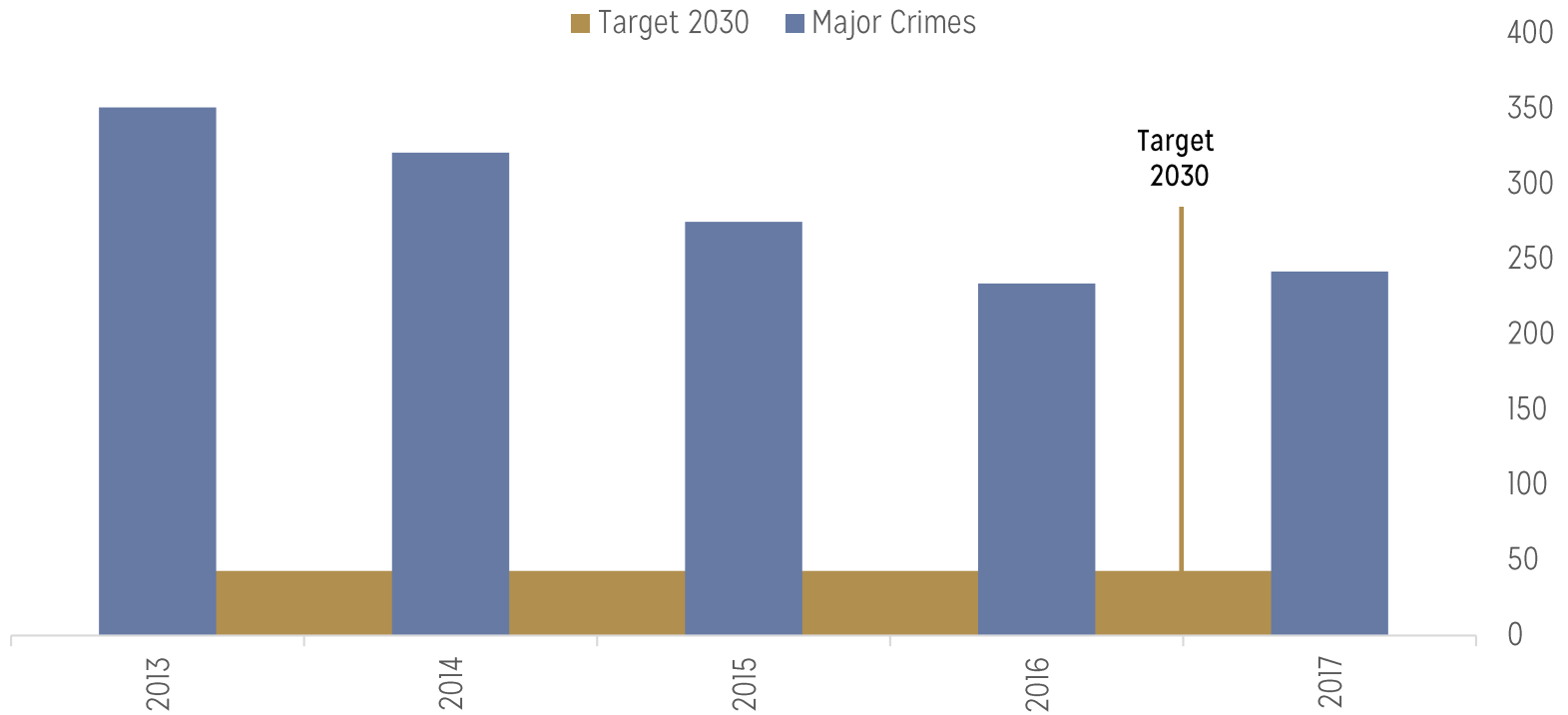


Source: Vision 2030, STATIN, Marla Dukharan

Crime and overall social conditions are the most important policy agenda. Without social stability and improvements in wellbeing, the positive macroeconomic outcomes are at risk of being undermined

Crime Rate: Jamaica

per 100,000 crimes (major crimes)

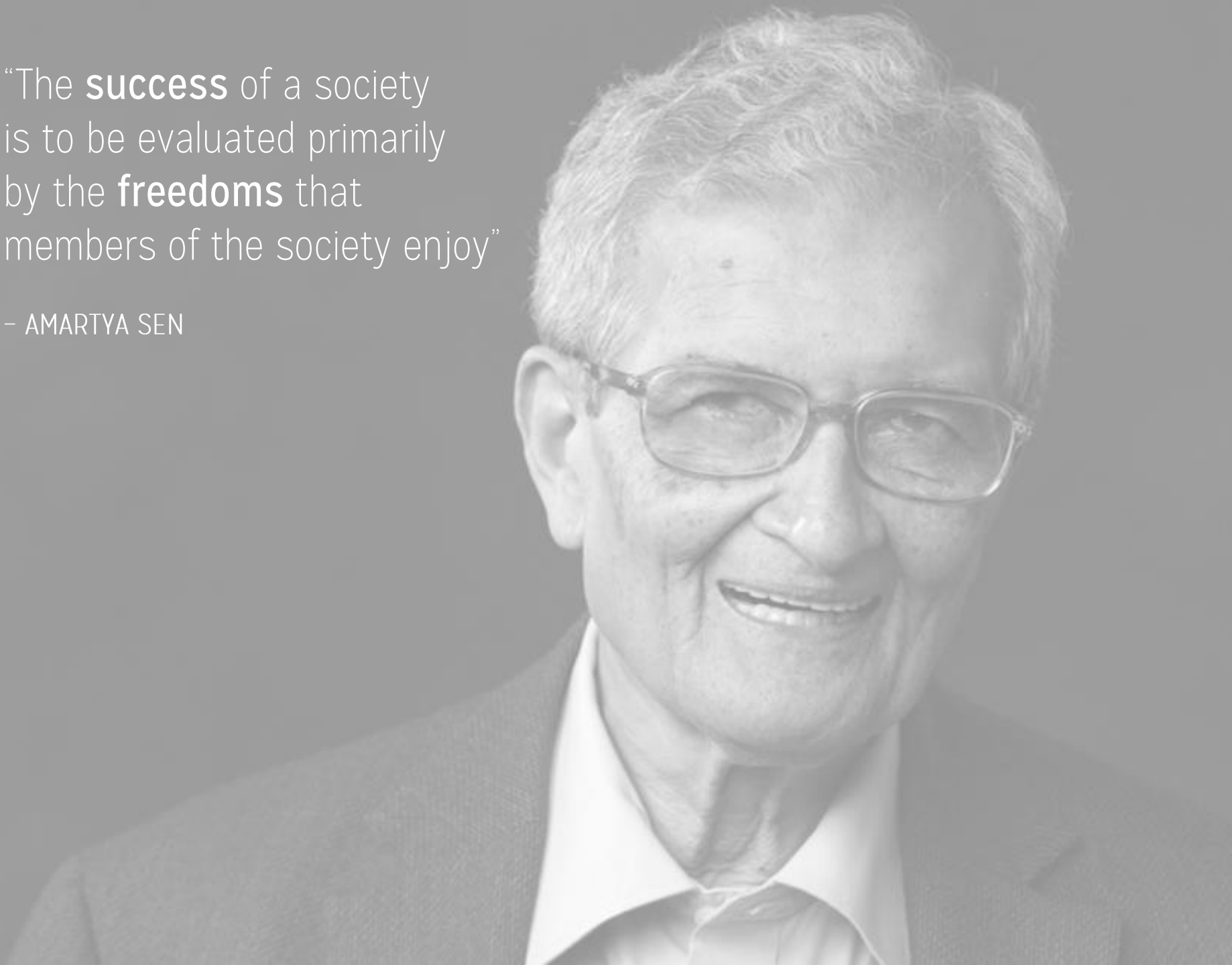


Source: Vision 2030, Planning Institute of Jamaica, Marla Dukharan

IDB estimates cost of crime at 3.99% of GDP for Jamaica

“The **success** of a society
is to be evaluated primarily
by the **freedoms** that
members of the society enjoy”

– AMARTYA SEN





“It’s a competitive world for low-budget people, spending the dime while **earning the nickel.**”

– BUJU BANTON

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We need the means of the right to achieve the ideals of the left.

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