Macroprudential policies and integrated inflation targeting

Luiz Awazu Pereira da Silva[1]

The Turkish presidency of the G20 during 2015 deserves great credit for sponsoring a number of fruitful meetings in order to deepen the analysis of macroprudential policies. The BIS was pleased on several occasions to collaborate with the CBRT in such endeavours. Economists from the BIS and the CBRT have worked closely and productively together on a number of topics.

This joint CBRT/BIS/IMF conference, instigated by then-Governor Başçı, gave much food for thought. Allow me to record a special word of thanks to him not only for encouraging such collaboration but also for his most thoughtful contributions over many years. He was always rigorous and imaginative constantly challenging conventional thinking. For this he earned wide respect. Thanks are also due to the staff of the IMF for their dedication to our joint project.

Central banks, especially in the post-global financial crisis world, have to grapple with two policy objectives – macroeconomic stability and financial stability. They have to analyse the many, and changing, links between the macroeconomy and financial markets. Tinbergen suggested that with two policy objectives, we need two instruments – in this case, the policy interest rate and a macroprudential tool. But we cannot assume that a one-for-one assignment of each instrument to a specific objective (eg the policy interest rate only to the macroeconomic objective) would necessarily work best. This is because each instrument is likely to affect more than one objective (eg low interest rates can encourage excessive leverage, and so undermine financial stability). Many of the papers in this volume address some of the complexities of this assignment problem.

During the conference, we debated about the likely effectiveness of potential macroprudential tools that have not been widely tried. Learning from experience abroad can help assess how an instrument that is new to one country – but has been tried in other countries – might work. Putting too much reliance only on those instruments we have used in the past can actually be counterproductive because there may be diminishing marginal returns to using any particular instrument.

Macroprudential tools have proved to be effective not only in moderating booms, but also in building up buffers which serve to limit the fall-out from busts. There are of course caveats to this positive assessment. If over-used, such policies create distortions. In addition, they can be circumvented: careful design and good international co-operation can reduce this risk. Monetary policy can be a key component, especially when experimenting with new macroprudential tools. There is, in short, a need for what I have termed elsewhere **integrated inflation targeting** (IIT).[2] Monetary and macroprudential policies need to be calibrated jointly to achieve macroeconomic and financial stability. Many of the papers in this volume seek to take

[1] Deputy General Manager, Bank for International Settlements.

[2] Agénor, P-R and L A Pereira da Silva (2013): *Inflation targeting and financial stability*, Inter-American Development Bank and CEMLA.

account of how macroprudential regimes can alter the monetary transmission mechanism, and better understanding such links is a big priority.

Further efforts will be needed to continue examining the issues posed by achieving both macroeconomic and financial stability in a world of globalised financial flows, interconnected economies and monetary policy spill-overs. This conference constitutes a step in building knowledge and sharing experiences towards that common goal.