Some aspects about the adoption of a scheme of explicit inflation targeting in Peru

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ABSTRACT

Since 1994, the monetary policy objective of Central Reserve Bank of Peru (CRBP) has been announced as a range for the rate of growth of Consumer Price Index. In order to achieve its objective, CRBP has implemented its monetary policy, using the average growth of monetary base as intermediate target, with no compromise with the exchange rate. Meanwhile, the operative target consists of a limit to deposits of commercial banks in CRBP, which is accomplished through open market operations. These operations are conducted using Certificates of Deposits of Central Reserve Bank of Peru (CDCRBP). Likewise, it is allowed that short term interbank interest rates are determined by market. The intermediate and operative targets are announced annually and monthly, respectively.

The use of an intermediate target of monetary base growth has been useful in the process of elimination of hyperinflation. Nevertheless, its ability to communicate the monetary policy position has been decreasing to the point of having little relevance in the process of formation of inflationary expectations in the private sector. For this reason, Central Bank has been evaluating the possibility to adopt a more transparent policy scheme, that enables the public understand its decisions and associate them with the objective of monetary stability. Specifically, it has been evaluating the scheme of explicit inflation targeting, by which the decision of the Board regarding the operative target is directly linked to the possibility of the accomplishment of an inflation targeting.

The objective of this work is to evaluate if Peru fulfill the conditions to implement an inflation targeting regime, as well as to identify what is needed to apply the monetary policy under this scheme. The work analyzes the characteristics of this monetary regime according the order in which it has been implemented in other countries, namely, the legal framework, the policy design, and finally, transparency and accountability.