

**FOR
AGENDA**

EBS/14/24
Supplement 1

March 21, 2014

To: Members of the Executive Board

From: The Acting Secretary

Subject: **Conditionality in Evolving Monetary Policy Regimes—Draft Press Release**

Attached for consideration by the Executive Directors is the background section of the draft Press Release relating to the paper on conditionality in evolving monetary policy regimes (EBS/14/24, 3/5/14), which is tentatively scheduled for discussion on **Wednesday, March 26, 2014**.

The staff proposes the publication of the Press Release, together with the main paper, after the Board completes its discussion.

Questions may be referred to Mr. Lane (ext. 39852), Ms. Pattillo (ext. 37319), and Mr. Opoku-Afari (ext. 37183) in SPR.

This document will shortly be posted on the extranet, a secure website for Executive Directors and member country authorities.

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INTERNATIONAL MONETARY FUND



Press Release No. 14/xx
FOR IMMEDIATE RELEASE
March XX, 2014

International Monetary Fund
Washington, D.C. 20431 USA

IMF Executive Board Reviews Conditionality in Countries with Evolving Monetary Policy Regimes

On March 26, 2014, the Executive Board of the International Monetary Fund (IMF) discussed the monetary conditionality framework in Fund-supported programs in developing countries.

Background

Over the past decade there have been significant changes in monetary policy regimes in developing countries. Increasing numbers of both low-income and emerging market countries are shifting from exchange rate anchors and the use of monetary aggregates targets toward more flexible operational targets and more forward-looking policies, with increasing reliance on policy rates to signal the monetary policy stance. The financial landscape is also changing: significant financial deepening; lower inflation; and a weaker correlation between money growth and inflation. Empirical analysis of the performance of monetary conditionality in PRGT- and GRA-supported programs in countries with scope for independent monetary policy finds that while a high proportion of reserve money targets were not observed, program inflation objectives were generally not compromised provided that initial inflation was low.

The evolution of monetary policy frameworks has implications for monetary conditionality in Fund-supported programs. There are clear guidelines and established practices for monetary conditionality for money targeting and inflation targeting frameworks. However, neither of these existing conditionality frameworks is well-suited for countries with evolving monetary policy regimes.

The paper proposes an enhancement to the existing review-based conditionality framework by introducing a monetary policy consultation clause (MPCC), as an option for countries with evolving monetary policy regimes in place of a performance criterion on reserve money or net domestic assets. Programs would set a central path for a target variable (either a monetary aggregate or inflation) with a single tolerance band (with an option to have an inner

band where deemed necessary). Deviations from the band would require a formal consultation with the Executive Board, and would be informed by staff's assessment of whether deviations are explained by compensating factors and proposed remedial measures, where necessary, in order to complete a review. The review-based approach to monetary conditionality rests upon enhanced central bank capacity to analyze monetary conditions. The MPCC is expected to provide flexibility in the conduct of monetary policy and align conditionality to the changing monetary policy frameworks in countries with evolving monetary policy regimes.

Executive Board Assessment¹

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¹ An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.