

# BOK's FG in the context of CBA's FPAS Mark II \*

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## ▪ **Shift in Monetary Policy Perception**

- ✓ Transition from "expert forecasting" to "risk management."
- ✓ "Most likely future" as a baseline scenario.
- ✓ Macroeconomic narratives for case scenarios (Case A, B, X/Y) with market references.

## ▪ **Analytical Framework**

- ✓ Robust analytical framework and suite of models.

## ▪ **Human Capital**

- ✓ Investment in human capital.

## ▪ **Transparency and Accountability**

- ✓ Upholding the highest degree of transparency and accountability.

## ■ Definition of Forward Guidance

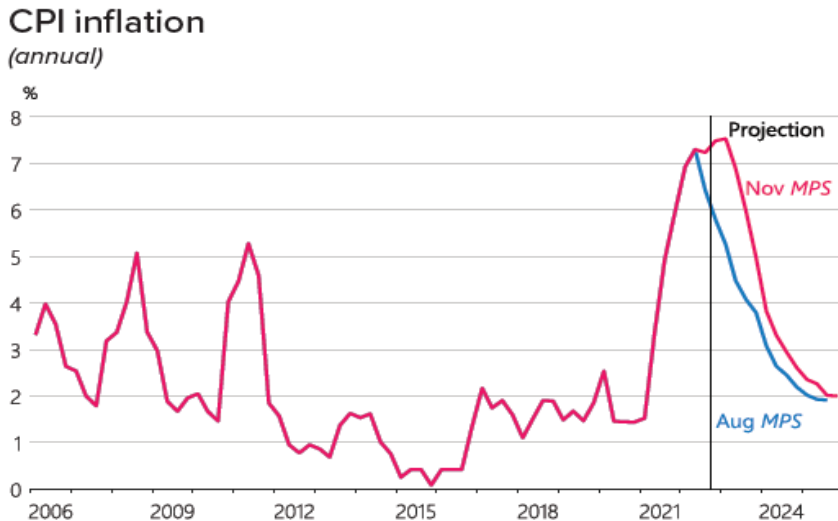
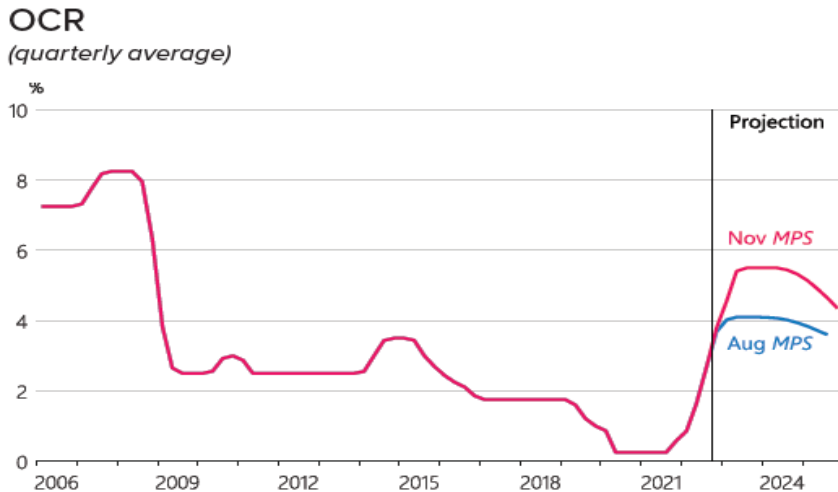
- ✓ Explicit statements by a central bank regarding the outlook of future policy (Woodford, 2012).
- ✓ Communication on how monetary policy makers anticipate economic and policy development (Bernanke, 2020).

## ■ Quantitative vs. Qualitative Forward Guidance

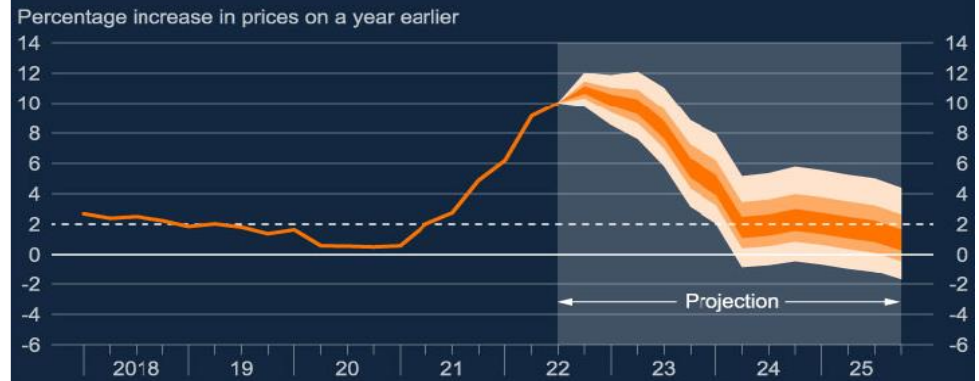
- ✓ **Definition of quantitative FG:** Publishing a numerical path for future policy rates aligned with macroeconomic forecasts (Blinder et al., JEL 2008).
- ✓ **Quantitative FG examples:** Reserve Bank of New Zealand, Norges Bank (Norway), Sveriges Riksbank (Sweden), Bank of Israel, Czech National Bank, Federal Reserve (US).
- ✓ **Qualitative FG examples:** Bank of England, European Central Bank.

# RBNZ (FPAS Mark I)

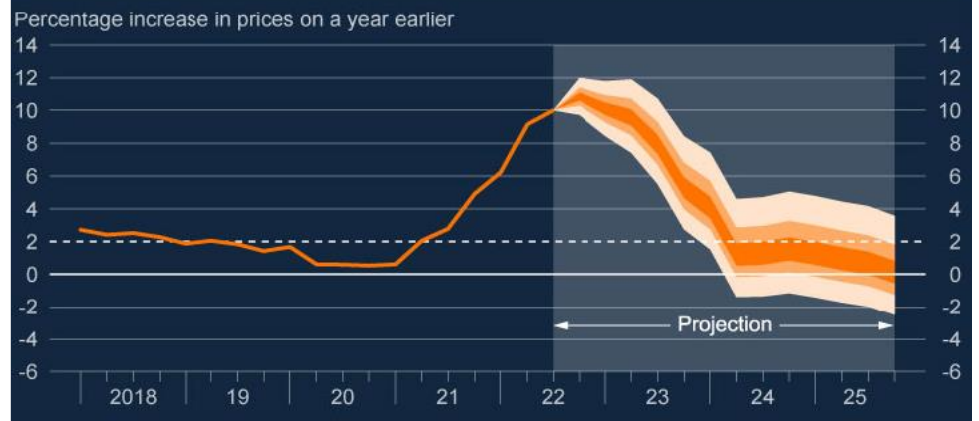
# BOE: No quantitative FG



**Chart 1.5: CPI inflation projection based on constant interest rates at 3%, other policy measures as announced**



**Chart 1.4: CPI inflation projection based on market interest rate expectations, other policy measures as announced**

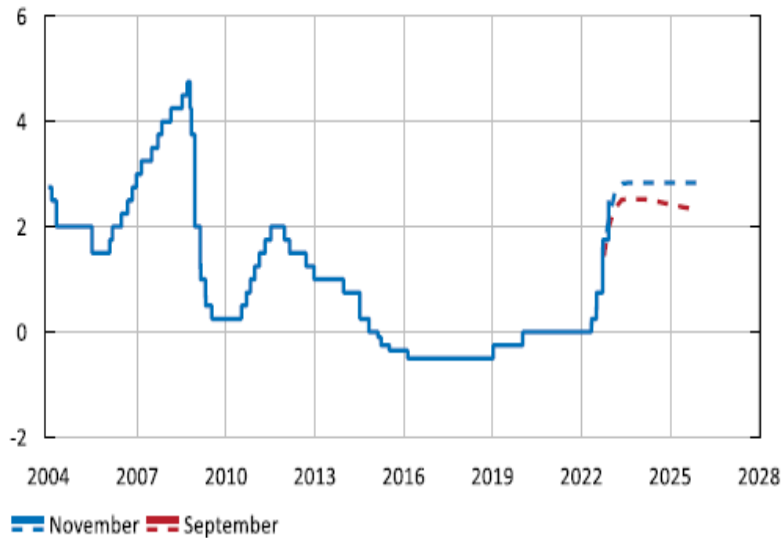


Source: Reserve Bank of New Zealand, Monetary Policy Statement, November 2022.  
Bank of England, Monetary Policy Report, November 2022.

# Riksbank (FPAS MARK I)

## Policy rates

Per cent



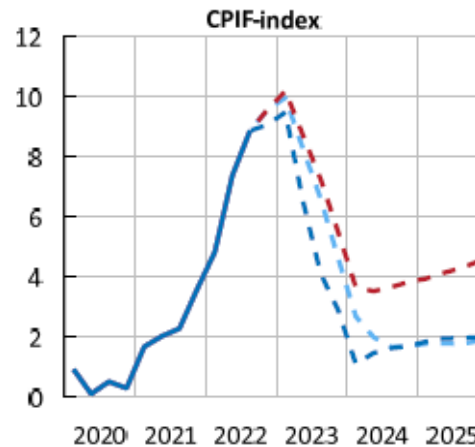
Note. Solid line refers to outcome, broken line represents the Riksbank's forecast. Outcomes are daily rates and the forecasts refer to quarterly averages.

Source: The Riksbank.

Source: Sveriges Riksbank, Monetary Policy Report, Nov. 2022

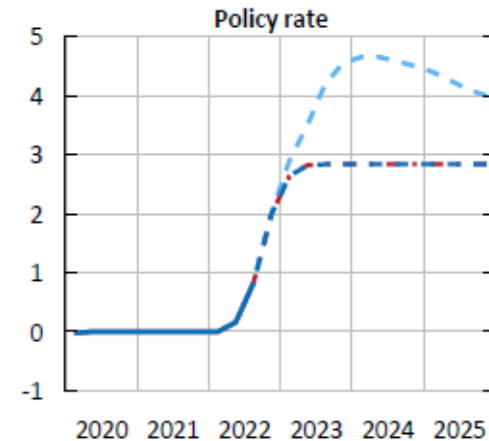
## Alternative scenario with persistently higher inflation

Annual percentage change and per cent



Legend: Main scenario (solid blue line), Alternative scenario: persistently higher inflation with policy rate from the main scenario (dashed blue line), inflation with policy rate from the main scenario (red dashed line)

Sources: Statistics Sweden and the Riksbank.

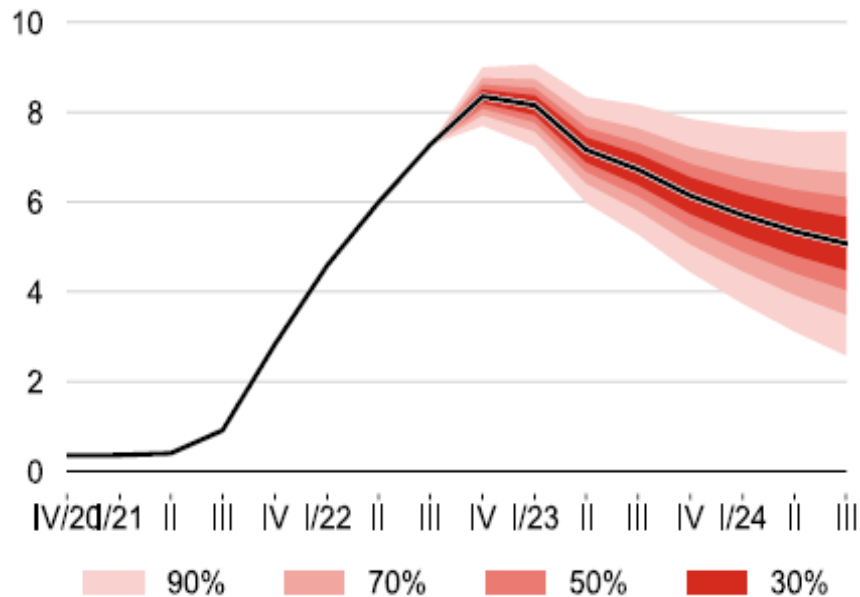


Legend: Alternative scenario: persistently higher inflation and higher repo rate (dashed blue line)

# CNB (FPAS MARK I)

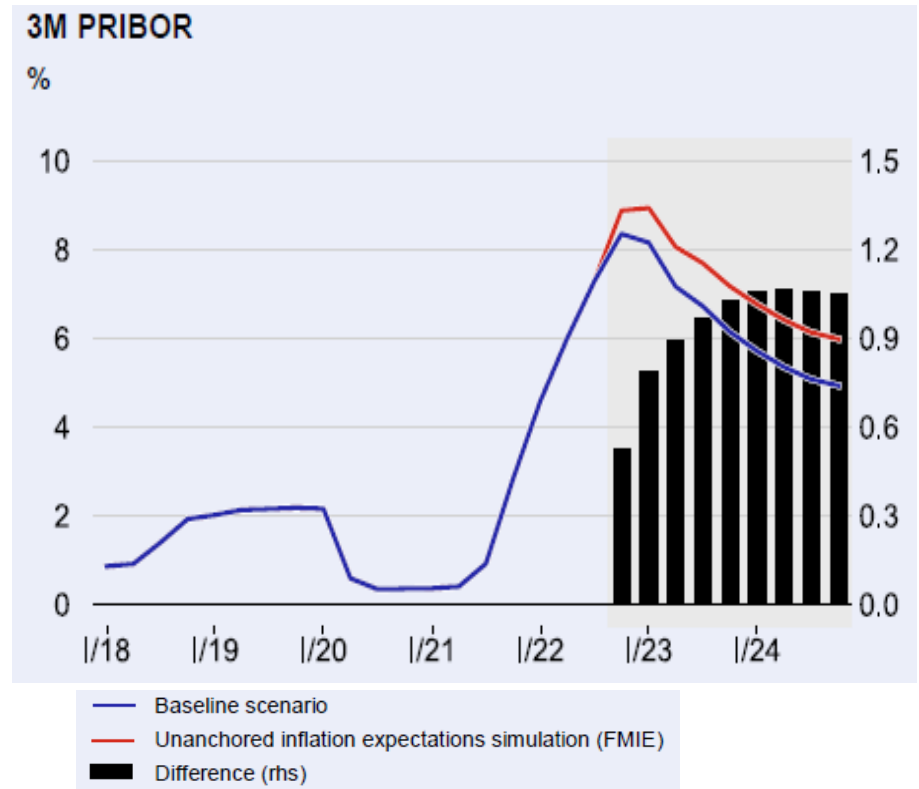
## Short-term Interest Rates\*

3M PRIBOR in %; confidence interval



\* 3M PRIBOR moves closely in tandem with policy rates (2W RP rates).

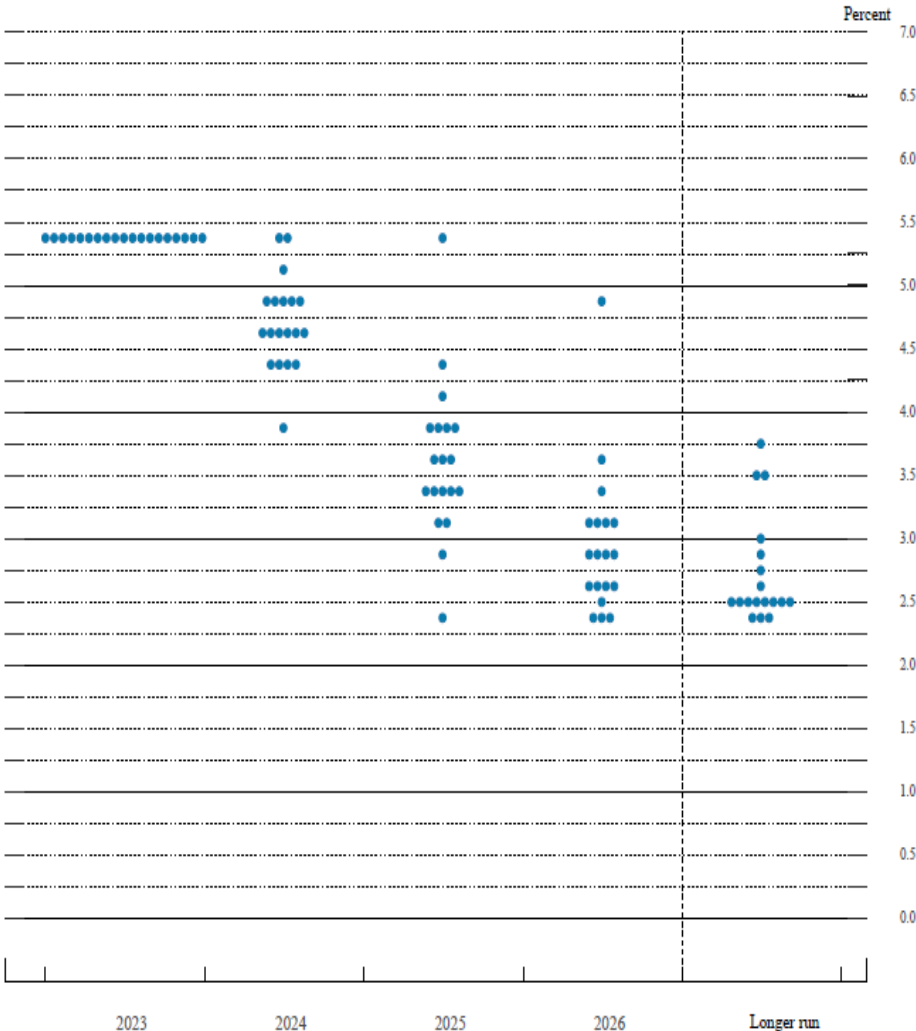
## Baseline vs. an alternative scenario



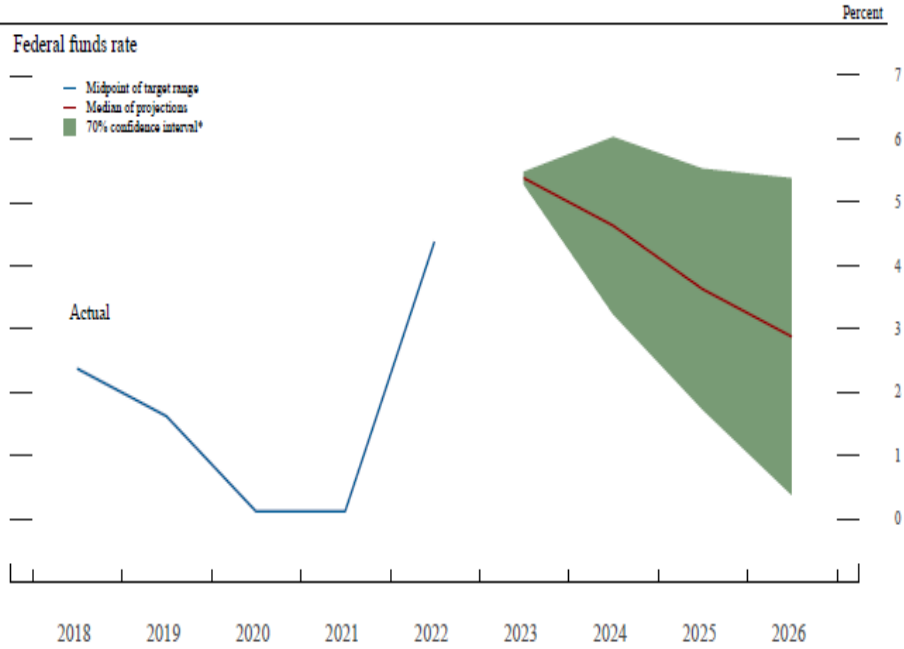
Source: Czech National Bank, Monetary Policy Report, Oct. 2022

# Fed's FG

## FOMC participants' assessment of appropriate FFRs



## Uncertainty and risks in dot plots



Note: The blue and red lines are on actual values and median projected values, respectively, of the Committee's target for the FFR at the end of the year indicated.

Source: Fed, SEP, Dec. 2023

- **Types of Forward Guidance** (Laxton and Rhee, 2022)
  - ✓ **Conventional:** Forecasts of macroeconomic variables with an endogenous policy rate path.
  - ✓ **Unconventional:** Qualitative, date-based, or threshold-based approaches.
  
- **Emerging Market Economies (EMEs) and Currency Convertibility**
  - ✓ Consensus against unconventional forward guidance for EMEs with non-convertible currencies.
  - ✓ High uncertainty and risk of currency depreciation are contributing factors.
  
- **Bank of Korea's (BOK) Policy Evolution**
  - Historically, BOK favored strategic ambiguity in policy directions.
  - Shifted importance towards managing inflation expectations with increased transparency and communication.



# Overview of BOK's Current Forward Guidance Strategy

Bank of Korea

- As of October 2022, the BOK has improved communication on future policy directions (Rhee and Park 2023).
- This is primarily through presenting **Monetary Policy Board members' forecasts on policy rates for the coming three months (conventional FG)**.
- There is an ongoing debate about the potential extension of FG to cover longer-term horizons.

## | Forecast for Policy Rate Levels within the Next 3 Months

	Oct. 22	Nov.	Jan. 23 <sup>1)</sup>	Feb. <sup>1)</sup>	Apr. <sup>1)</sup>	May, July, Aug <sup>1)</sup>	Oct.	Nov. <sup>1)</sup>
3.25	2	1	-	-	-	-	1 <sup>2)</sup>	
3.50 <sup>1)</sup>	4	3	3	1	1	0		2
3.75	-	2	3	5	5	6	5	4

Notes: 1) A view that it is necessary to leave open the possibility of raising the policy rate to 3.75%

2) A view that it is necessary to be flexible with the direction of the rate, which opens the possibility of both a rate hike or a rate cut

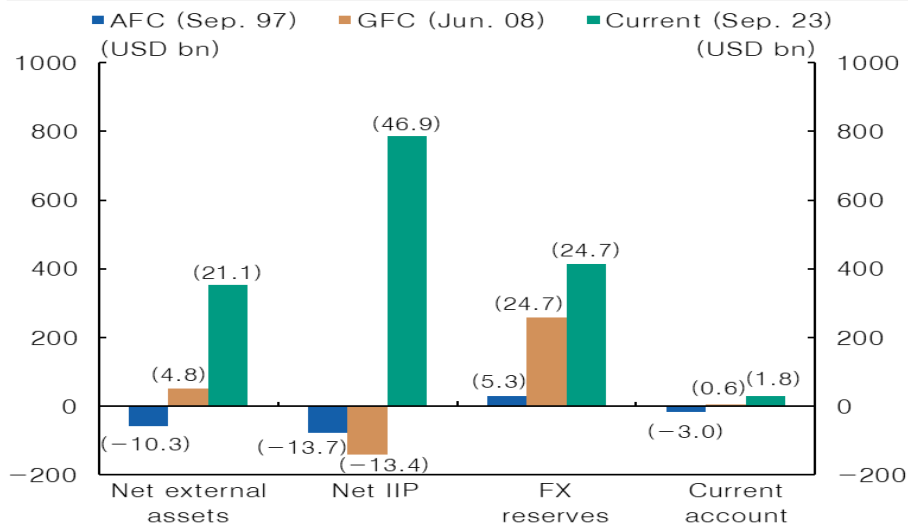
Source: Rhee and Park (2023)

# Lessons Learned During the Transition from Strategic Ambiguity to Forward Guidance

Bank of Korea

- A “Big Step” in Sep. 2022 after the FG of “baby steps” in Jul. and Aug. 2022.
  - ✓ This change was in response to rapid currency depreciation\*.
  - \* Despite a FX reserve over \$400 billion and a net external creditor status, there were concerns about the Asian Financial Crisis’ stigma effect, shallow market depth and the relatively short duration of FX derivatives.
- Intense criticism arose due to the confusion between a **firm commitment or promise** and a **conditional guidance** (Rhee, Speech at PIIE, Oct. 2022)

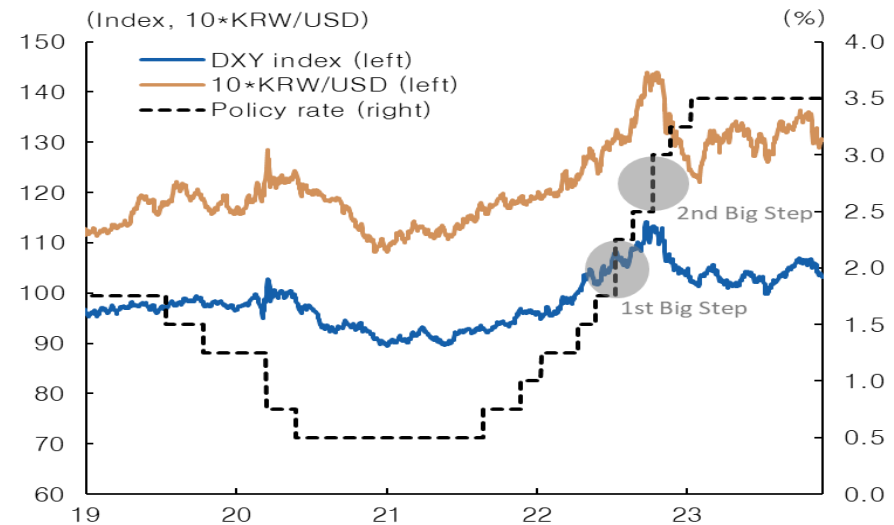
## External Soundness Indicators



Notes: AFC and GFC denote Asian Financial Crisis and Global Financial Crisis, respectively. Figures in parentheses are percentage of GDP.

Source: Bank of Korea

## Dollar Index, KRW/USD, Policy Rate



Sources: Bank of Korea, Bloomberg

## ■ Methodology for Projecting Policy Rates

- ✓ Comparison between Dot-plots and Policy Rate Paths.
- ✓ Contrast of Single Path without Confidence Interval and Fan Charts.
- ✓ Analysis of Scenarios using FPAS Mark I vs. FPAS Mark II Frameworks.

## ■ Time Horizon Considerations

- ✓ Discussion on 1-Year vs. 2-3 Year Projections.
- ✓ Calendar-Based Projections vs. Moving Window Approach.
- ✓ Examination of Quarterly vs. Annual Projection Frequencies.

## ■ Announcement Frequency

- ✓ Comparing Quarterly Announcements vs. Announcements at Each Monetary Policy Decision.

# Q & A

# Reference

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- Laxton, D., Galstyan, M. and V. Avagyan (2024), "Prudent Risk Management Approach to Monetary Policy: Theory and Practice of FPAS Mark II at the Central Bank of Armenia," Forthcoming.
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- Rhee, C. Y., and Y. H. Park (2023), "The Bank of Korea's Policy Response during the High Inflation after Covid-19 Pandemic", prepared for the CEPR volume "Central Banking During the Great Post-pandemic Inflation", forthcoming.
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