

## **BOT's Inflation Targeting is Well Ahead of the Curve**

**Don Nakornthab**

**Team Executive**

**Monetary Policy Group**

WHILE NOT quite secret, the Bank of Thailand (BOT)'s regime for targeting inflation is certainly under the radar.

No, it's not that the BOT pays attention to economic growth along with inflation trends when making policy rate decisions. That is a common misunderstanding for people unfamiliar with modern monetary policy conduct and misled by the "inflation targeting" label. (Anyone following the BOT's conducting of monetary policy over the past 10 years would know that the bank puts a substantial weight on output stabilisation and is definitely not a single-minded "inflation nutter", in the words of Bank of England governor Mervyn King.)

The little known fact I am talking about is that since 2004, the BOT has monitored signs of financial imbalances in seven key areas: the property market, the stock market, the banking sector, the non-financial corporate sector, household debt situation, government finance and public debt, and the external sector. The goal of this surveillance is to have an early warning system for potential disruptions to financial stability, especially if the underlying imbalances are related to monetary policy actions.

In July 2004, the Monetary Policy Committee made "the monitoring of factors contributing to financial imbalances" a part of its policy formulation and an entire chapter on financial stability conditions and outlook was added to the bank's Inflation Report in July 2005. That few people are aware of this surveillance is therefore perplexing.

My guess here is that we may have inadvertently understated its importance when explaining policy to a wider audience. This could be because, prior to the Lehman Brothers crash, our take on financial stability was viewed by other inflation-targeting central banks as eccentric, not conforming to conventional practices where keeping price and economic stability in check is all that matters for monetary policy. While a number of these central banks publish widely read financial stability reports, these are not created by the monetary policy side of the banks.

With the current global financial crisis, this perception has clearly changed. The emerging post-crisis consensus is that monetary policy should pay more attention to financial stability, as it may cause or exacerbate financial imbalances and asset price misalignments.

The severity of the crisis has very much discredited the old consensus often associated with Alan Greenspan in which the role of monetary policy should be limited to ex-post reaction to the unwinding of asset price bubbles. In this respect, the BOT is well ahead of the curve in transitioning from traditional inflation targeting to the "inflation targeting plus (financial stability)" advocated by, among others, the Financial Times' associate editor Martin Wolf.

In an attempt to strengthen the surveillance process even further, the BOT last month formed a Subcommittee on Financial Institution System and Financial Market Stability with the deputy governor of monetary stability, and the deputy governor of financial institutions stability as its chair and vice-chair, respectively.

This new high-level subcommittee will bring together the surveillance capabilities from both sides of the bank, making the monitoring of financial imbalances more comprehensive and effective.

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**(The views expressed are the author's own.)**

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