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Central banks' challenges

Dr T.K Jayaraman
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Reserve Bank of Fiji govenor Sada Reddy

AT no time were the challenges faced by central bankers greater than the ones faced today.

The challenges are due to extraordinary circumstances created by the global recession.

Under a fixed exchange rate regime adopted by Fiji, maintenance of international reserves at a desirable level of around four to five months of imports is critically important.

With foreign reserves reaching a record level at F$1.1billion, which are considered equivalent to 4 months of imports, the Reserve Bank of Fiji RBF) took two major decisions, after its Board of Directors meeting in late November.

One related to relaxation of foreign exchange controls.

For example, effective January 1, 2010, the limit for a traveller overseas can take with him has been revised upwards to F$10,000, as compared to F$5000 previously.

Exchange controls were imposed in April 2009 to meet an unprecedented decrease in foreign reserves. As these controls proved effective fully serving the purpose behind the controls, RBF relaxed them.

The goal of economic recovery has now become more focused.

Effective September 1, 2009, RBF removed credit ceilings, which were imposed in December 2006.

The credit ceilings were imposed following the overheating of the economy during 2006, when there was a credit boom leading to fast depletion of foreign reserves.

Interest spread

Another major decision taken in the November board meeting was on lending rates.

Effective January 1, 2010, the restrictive lending rate policies were also removed, keeping intact however the maintenance of spread of 4 percent between lending and deposit rates.

Earlier, following the rise in net foreign assets, there has been an increase in liquidity in the banking system as well.

The RBF felt it appropriate to raise the statutory deposit ratio effective December 7 to 7 per cent from 5 per cent of deposit liabilities.

The IMF Mission at the end of its visit to Fiji in late November noted the departure from the usual approach for mopping up liquidity by selling RBF notes.

If we look at the central banks in the advanced economies, there are striking differences between New Zealand and the US, which are still under recession, and Australia which is the only industrial country coming out of recession.

While Australia raised its indicator interest rate last month as a preemptive measure, to fight inflationary tendencies, Reserve Bank of New Zealand (RBNZ) and the Federal Reserve (the Fed) in the US decided to hold on to the current indicator rates of zero to 0.25%

The challenges

In the see-saw of bilateral exchange rates, the kiwi dollar was appreciating against the US dollar, hurting its dairy and other agricultural exports, besides tourism.

The leader of the opposition Labour Party wanted an end to the 20-year bi-partisan accord on monetary policy targeting inflation.

He urged RBNZ to give up its anti-inflationary bias and resort to a loose monetary policy. A cheap monetary policy would depreciate the exchange rate. He argued that RBNZ's policy targets did not help exports and growth.

In the US last week, the Fed came under severe criticism, when Chairman Ben Bernanke sought confirmation to a second term. His opponents in the US Congressional Committee were vocal that the Fed failed to manage the economy.

The critics blamed the Fed for creating the financial crisis by easy monetary policies and lax supervision of banks.

Bernanke's supporters were arguing that his crisis-response is restoring financial stability and the crisis was caused by errors committed by previous Chairman, Greenspan. Bernanke succeeded Greenspan in February, 2006. The critics however argued that like Greenspan, Bernanke did nothing to curb the rising real estate prices.

Defenders say that Bernanke moved very aggressively to exert government power and use all the tools at his disposal once the crisis began.

Curbing Fed's independence

The US Congress wants to introduce an audit system to control the Fed. The defenders are worried that it would destroy central bank independence. In his Senate testimony, Bernanke was against the idea of new audits on the Fed's monetary policy, saying the Fed is transparent about its overall balance sheet.

No doubt, a recovery may be in sight.

More importantly, when and where are the jobs going to come back?

Bernanke faces great anger for bailing out banks. Americans are under the crush of high unemployment, stagnant incomes and rising foreclosures.

Yet there is no alternative.

President Obama, a Democrat decided to give another term to Bernanke, a Republican.

Perhaps, he would have recalled President Theodore Roosevelt's memorable words:

"It is not the critic who counts; not the man who points out how the strong man stumbles or where the doer of deeds could have done them better. The credit belongs to the man who is actually in the arena, whose face is marred by dust and sweat and blood, who strives valiantly.