

Toward a Macromodel for Kyrgyzstan by Altynai Aidarova: Comment

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Introduction

- ❖ I am not really acting as a discussant of Altynai Aidarova's paper – I feel more like a co-author
- ❖ Have been involved – jointly with Altynai – in developing macromodels for the Kyrgyz economy that may be used for forecasting inflation
- ❖ At first, estimates of simple approaches to determining Kyrgyz inflation, either in the form of OLS equations or VARs and VECRs
- ❖ Results encouraging: Kyrgyz inflation determined by foreign commodity prices, the exchange rate, the monetary base and (?) remittances from abroad

Limitations of simple approaches

- ❖ Models based on simple approaches may be used to generate unconditional forecasts
- ❖ However, they do not yield forecasts conditional on a given policy stance of the NBKR
- ❖ Therefore, they cannot be used for answering the question of how the NBKR should deploy its policy instruments in order to achieve its inflation objective
- ❖ To produce conditional forecasts, we need a macromodel that takes explicit account of the policy instruments used by the NBKR

Towards a macromodel:

- ❖ In the following, I mention three problems arising from Altynai's model requiring further discussion

Problem 1: Transmission of foreign inflation

- ❖ The exchange rate does not meaningfully respond to foreign prices unless domestic consumption responds to changes in remittances of Kyrgyz nationals working abroad (see solution for $\Delta \log(ER)$ on page 13 of Altynai's paper)
- ❖ This implausible and calls for a re-specification of the model

Problem 2: Real balance effect

- ❖ A real-balance effect on domestic consumption and imports plays a key role in transmitting monetary impulses to the real economy
- ❖ Evidence of real-balance effect – though plausible – is weak – Further work is needed

Problem 3: Monetary policy

- ❖ Modelling of monetary sector and monetary policy still to be done
- ❖ Various difficulties:
- ❖ Not clear how and why NBKR increased foreign exchange reserve, especially after 2008
- ❖ Link between balance of payments and monetary base still to be investigated – To what extent is NBKR able to sterilize inflows of foreign exchange – What instruments can it use to this end?
- ❖ Is there a fiscal-dominance problem in the Kyrgyz Republic?