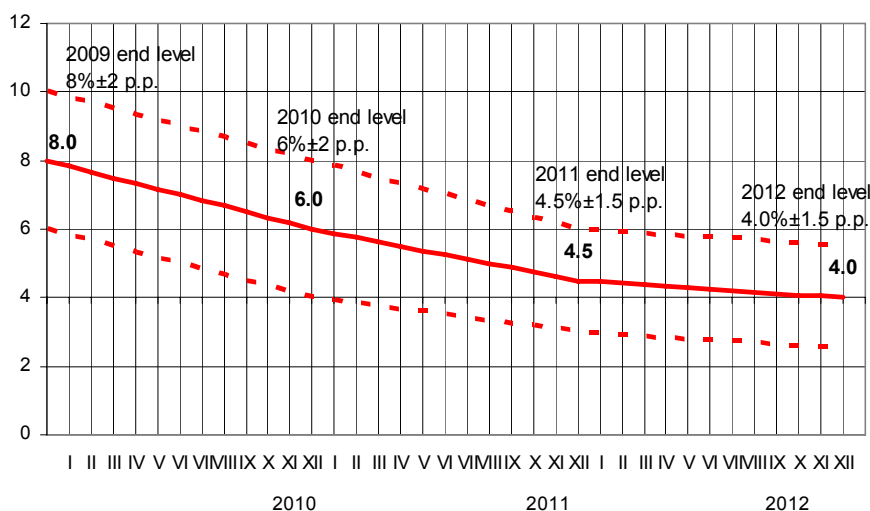


# Memorandum of the National Bank of Serbia on Setting Inflation Targets for the Period 2010–2012<sup>1</sup>

In line with the *Agreement between the National Bank of Serbia and the Government of the Republic of Serbia on Inflation Targeting*<sup>2</sup> and the *Memorandum of the National Bank of Serbia on Monetary Strategy*<sup>3</sup>, pursuant to which the National Bank of Serbia has committed to set inflation targets in cooperation with the Government, the Monetary Policy Committee of the National Bank of Serbia hereby sets the point **headline inflation targets (with a tolerance band)**, measured as annual percentage change in the consumer price index, for the period 2010–2012, with the inflation outturn at the end of the previous year as its starting point:

- December 2009: 8% with a tolerance band of  $\pm 2$  percentage points
- December 2010: 6% with a tolerance band of  $\pm 2$  percentage points
- December 2011: 4.5% with a tolerance band of  $\pm 1.5$  percentage points
- December 2012: 4% with a tolerance band of  $\pm 1.5$  percentage points

**Inflation target with a tolerance band for the period 2010-2012**



Inflation targets for 2010 and 2011<sup>4</sup> have not been changed from their previously determined levels. What has been changed is the way they are defined: they are no longer formulated as bands with a midpoint, but rather as points with a tolerance band. Thus formulated targets will enable a more efficient communication with the general public and stronger impact on inflation expectations, which are essential for the stabilisation of economic activity.

Inflation targets are set as point targets (with a tolerance band) for each month of the year, and the central bank will operate on the assumption of their continuous implementation

<sup>1</sup> The Memorandum was adopted in the NBS Monetary Policy Committee meeting of 14 December 2009.

<sup>2</sup> The Agreement was adopted in the meeting of the Government of the Republic of Serbia of 19 December 2008.

<sup>3</sup> The Memorandum was adopted in the NBS Monetary Policy Committee meeting of 22 December 2008.

<sup>4</sup> See the *Memorandum of the National Bank of Serbia on Setting Inflation Targets for the Period 2009–2011*.

December–December (see chart and table). The trajectory of inflation targets until 2012 is consistent with the need to achieve medium-term price stability which, in view of Serbia's medium-term ambition to converge to EU price and income levels, is defined as annual inflation of 2–4%.

Inflation targets for the period 2010–2012 have been set by the National Bank of Serbia in cooperation with the Government based on the analysis of current and expected macroeconomic developments and numerical guidelines for the increase in prices of products and services under the Government's direct or indirect regulation.<sup>5</sup>

Important features of inflation targets:

- **Target inflation rates are gradually declining.** The set inflation targets reflect intention to achieve price stability through gradual disinflation, without causing any disruptions to the macroeconomic processes. Gradual lowering of inflation targets is based on the assessment of long-term macroeconomic movements and the need to ease the pressures on the nominal exchange rate, and reduce the resulting risks from potentially negative impact on the competitiveness of the country's economy.

- **The inflation target is defined as a point with a tolerance band.** Such formulation of the target brings considerable advantages in terms of efficient communication with the general public. The target represents a clear and precise signal of the level of inflation that the central bank strives to achieve. Besides, the target is symmetrical, which provides a leeway to the central bank to communicate effectively if the target is missed in either direction. As it is not possible to keep inflation on target each and every month, the target set will provide a general idea of the monetary policy's medium-term focus.

The width of the tolerance band ( $\pm 2$  p.p. in 2010 and  $\pm 1.5$  p.p. in 2011 and 2012) reflects interest in the stabilisation of economic activity, as it provides scope for the flexibility of monetary policy in the period ahead without any detriment to its credibility. The tolerance band indicates a comfort zone providing for the fact that there may be many small transitory shocks causing short-term volatility of inflation, but not requiring a monetary policy response.

- **The target is continuous.** Point inflation target with a tolerance band is defined for each month of the year. This means that the achievement of inflation target is watched continuously, not only at a particular point in time (year-end). The continuity also helps anchor inflation expectations in situations when a large shock pushes inflation temporarily away from the targeted level.

- **The target is defined for several years ahead.** This reflects the MPC's focus on achieving medium-term price stability and helps anchor inflation expectations.

In cooperation with the Government, the National Bank of Serbia may change the set inflation targets. Such changes will be undertaken in exceptional circumstances only and subject to the provision of an adequate explanation by the National Bank of Serbia.

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<sup>5</sup> Following consultation with the National Bank of Serbia, the Government may revise the numerical guidelines subject to the provision of an adequate explanation for such revision (according to *the Agreement between the National Bank of Serbia and the Government of the Republic of Serbia on Inflation Targeting*).

**Inflation target with a tolerance band  
for the period 2010-2012**

Year	Inflation target In percent	Tolerance band In percentage points
<b>2010</b>		
I	7.8	±2
II	7.7	±2
III	7.5	±2
IV	7.3	±2
V	7.2	±2
VI	7.0	±2
VII	6.8	±2
VIII	6.7	±2
IX	6.5	±2
X	6.3	±2
XI	6.2	±2
XII	6.0	±2
<b>2011</b>		
I	5.9	±2,0
II	5.8	±1,9
III	5.6	±1,9
IV	5.5	±1,8
V	5.4	±1,8
VI	5.3	±1,8
VII	5.1	±1,7
VIII	5.0	±1,7
IX	4.9	±1,6
X	4.8	±1,6
XI	4.6	±1,5
XII	4.5	±1,5
<b>2012</b>		
I	4.5	±1,5
II	4.4	±1,5
III	4.4	±1,5
IV	4.3	±1,5
V	4.3	±1,5
VI	4.2	±1,5
VII	4.2	±1,5
VIII	4.2	±1,5
IX	4.1	±1,5
X	4.1	±1,5
XI	4.0	±1,5
XII	4.0	±1,5