

# Internal rules on the preparation, rationale and presentation of monetary policy decisions

*The Central Bank Act No. 36/2001 states that the Board of Governors lays down internal rules on the preparation of, arguments for and presentation of its monetary policy decisions. In accordance with this provision, internal rules were ratified in January 2002.<sup>1</sup> They have now been revised and the new rules ratified in February 2006.*

In the commentary accompanying the draft bill on the Central Bank, the explanatory notes on the article providing for the Bank's internal rules stated that: "Decisions reached at meetings of the Board of Governors shall be recorded in suitable fashion and confirmed with the signatures of the Governors. In order to ensure the most professional approach towards formulating and implementing monetary policy at all times, given the provisions on the Bank's main objectives in Article 3, it is felt that legal provisions are warranted for separate internal rules covering preparations of, arguments for and presentation of the Board of Governors' monetary policy decisions. For example, this refers to the procedures by which decisions are prepared, the information on which they are based and the possible involvement of other Bank officials in this process, although ultimately the decision is formally made by the Governors. It is also important to give a clear account of the Governors' decisions, especially those involving the use of the Bank's monetary instruments. Decisions are to be made public with an outline of the assumptions on which they are based and what they entail. The provisions in this Article seek to ensure the most professional possible basis for the Governors' decisions, transparency of monetary policy and the accountability of the Governors towards the government and general public. The Article does not oblige the Board of Directors to publish accounts of discussions at meetings when monetary policy decisions are made, nor of the standpoints of individual Governors."

The first rules to this effect were set in January 2002. They have now been revised in light of experience and also the fact that as of 2006, the Board of Governors of the Central Bank of Iceland announces its interest rate decisions on fixed, preannounced days. The new rules were formally ratified on February 24, 2006. They are as follows:

## **Internal rules on the preparation, rationale and presentation of monetary policy decisions**

The following internal Rules are set with reference to the provisions of paragraph 3, Article 24 of Act No. 36/2001 on the Central Bank of Iceland. They are based on the following principles:

- Monetary policy decisions shall be consistent with the Bank's objectives.
- The highest degree of professionalism shall be exercised in monetary policy decisions, which shall be made on a sound basis.

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1. Published in *Monetary Bulletin* 2002/1.

- It shall be ensured that relevant information and employees' knowledge are used in monetary policy decision-making.
- The decision-making process shall enhance the transparency of monetary policy and facilitate its presentation.
- When a decision has been made, it shall be clear how it was reached and on what grounds.

According to paragraph 1, Article 23 of Act No. 36/2001, the Board of Governors has the authority to make monetary policy decisions.

Article 3 of Act No. 36/2001 states that the main objective of the Central Bank is to promote price stability. The joint declaration by the Government of Iceland and Central Bank of Iceland from March 27, 2001, sets a numerical target for inflation which is defined as a twelve-month rise in the CPI of as close to 2½% as possible on average.

### Work process for monetary policy decisions

1. The Central Bank of Iceland produces an inflation forecast which shall be published in its *Monetary Bulletin*. The inflation forecast is produced by the Bank's Economics Department and based on a macroeconomic forecast and other forecasting models that it uses and develops. The Board of Governors formally ratifies the inflation forecast for publication in *Monetary Bulletin*. The assumptions underlying each forecast shall be explained in detail.
2. Before the end of each calendar year, the Board of Governors shall decide and announce publicly no fewer than six interest rate decision days for the following year. Publication dates of *Monetary Bulletin* may coincide with the formal interest rate decision days.
3. Prior to its interest rate decision, the Board of Governors convenes monetary policy meetings as follows:
  - a. Roughly one week before the interest rate decision day, the Board of Governors calls a meeting where economic and monetary developments and prospects are discussed in detail. All available data which is relevant in analysis of unfolding economic developments, and the Bank's assessment of how closely the monetary policy stance is geared to the inflation target, shall be presented to this meeting. Material includes *Economic Indicators*, further indicators for the development of demand, foreign trade and the labour market, and information on transmission of monetary policy and the liquidity effect of Central Bank measures.

In cases where the interest rate decision day coincides with the publication date of *Monetary Bulletin*, draft versions of the macroeconomic and inflation forecast and the main sections of *Monetary Bulletin* shall be presented to the meeting for discussion. The Chief Economist and Department Directors present material produced by the departments.
  - b. Closer to the interest rate decision day, the Board of Governors convenes a meeting to present and discuss the assessment of the monetary policy stance in light of the analysis of the

position and outlook that was presented and discussed at the previous meeting as per item a. above. A draft introduction to *Monetary Bulletin* shall be presented for discussion, or a press release on the proposed decision by the Board of Governors when the interest rate decision day does not coincide with the publication of *Monetary Bulletin*.

Monetary policy meetings as per item a. shall be attended by the Board of Governors, Assistant Governor, Chief Economist and his deputy, the Directors of the International, Financial Stability, Monetary and Statistics Departments, and other experts as decided by the Board of Governor on a case-by-case basis.

Monetary policy meetings as per item b. shall be attended by the Board of Governors, Assistant Governor, Chief Economist and his deputy, and the Directors of the Financial Stability and Monetary Departments.

The Chairman of the Board of Governors chairs the monetary policy meetings. The main topic of the meeting, the documents presented to it and the conclusion shall be recorded in the minutes as appropriate.

4. At the Governors' interest rate decision meeting, the Chairman presents a proposal for the interest rate. After making its decision the Board of Governors consults attendees of policy meetings as per item b., and others as appropriate, on the final version of the text announcing the decision in the introduction to *Monetary Bulletin* or a Central Bank press release, cf. section 6.
5. The Board of Governors holds other meetings on monetary policy and economic and monetary developments as it considers appropriate and consults with others on a case-by-case basis. Decisions relating to monetary policy but not specifically to the policy interest rate are made by the Board of Governors after consultation with the appropriate parties in each instance.
6. Supporting arguments for interest rate decisions by the Board of Governors are published in *Monetary Bulletin* when their announcement coincides with its publication date. On other interest rate decision days, the Bank issues a press release announcing the Board of Governors' decision, together with the rationale behind it. Interest rate decisions by the Board of Governors are announced at a press conference, both on the publication dates of *Monetary Bulletin* and on other interest rate decision days.

#### **Entry into force**

These Rules were ratified by a meeting of the Supervisory Board of the Central Bank of Iceland on February 23, 2006 and enter into force immediately. They replace the Rules ratified by a meeting of the Supervisory Board on January 10, 2002 and formally set by the Board of Governors on January 14, 2002.

