



A FRAMEWORK FOR INTEREST RATE POLICY IN BARBADOS

**XLIV Annual Caribbean Centre for Money and
Finance Monetary Conference**

NOVEMBER 7-9, 2012



Rationale For Study

- ▶ Ensure domestic rates are inline with comparable foreign interest rates with an appropriate spread
 - ▶ Through orderly intervention in the T-bill auction

- ▶ Providing guidance to the market on the interest rate structure
 - ▶ Estimation and publishing of notional yield curve



GENERAL POLICY FRAMEWORK

- ▶ **Policy informed by two key factors:**
 1. Trend in U.S. 3-month Treasury bill rate
 2. Liquidity in the banking system

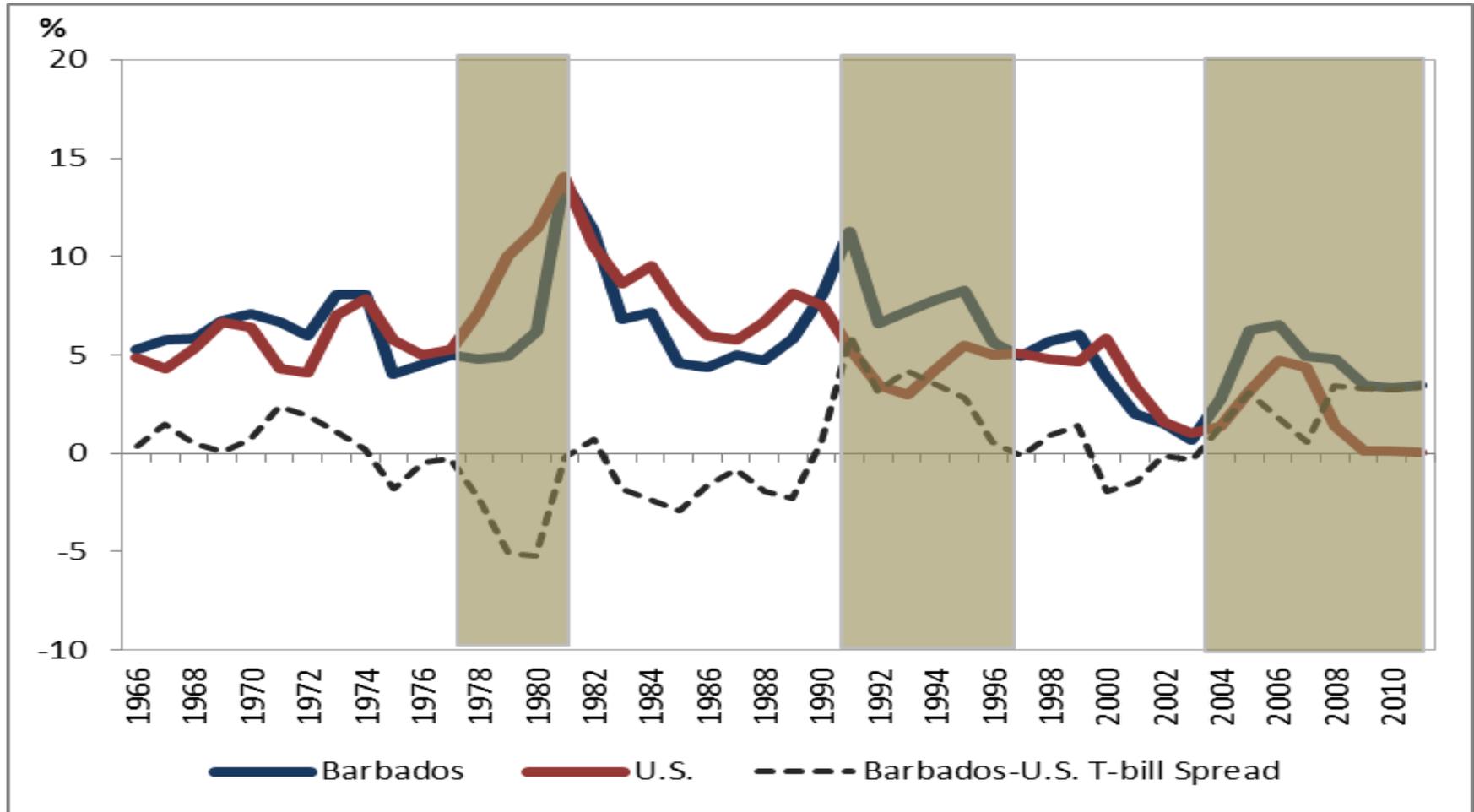
- ▶ **The domestic 3-month T-bill rate becomes the policy rate**

- ▶ **Minimum Deposit Rate (MDR)** will be no longer used as the policy rate. The Bank will revert to a Minimum Savings Deposit Rate, which will act as a floor on ordinary savings deposits of households.

- ▶ **Discount Rate** kept and will be linked to the policy rate

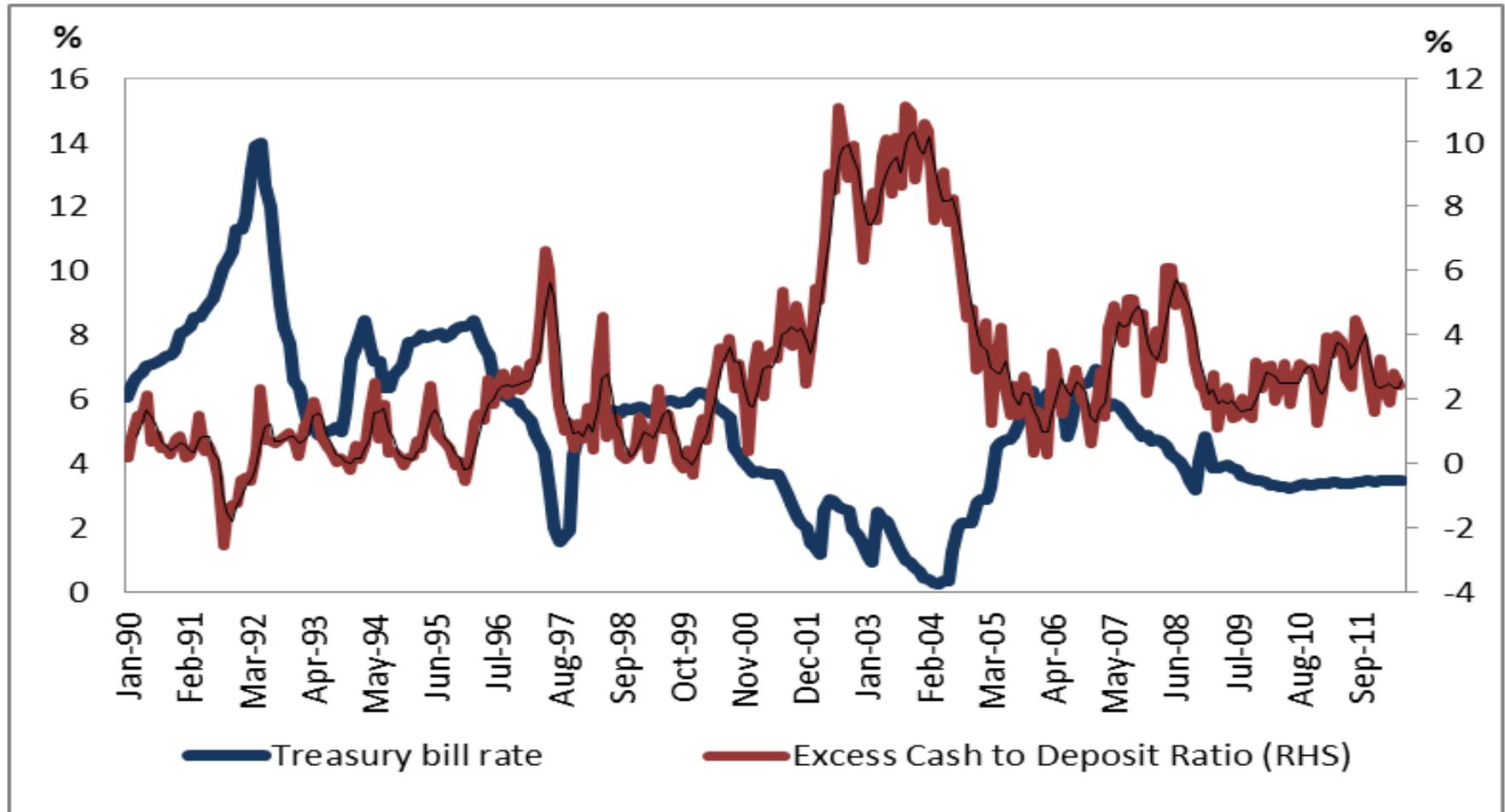


Barbados and U.S. 3-month T-bill rates



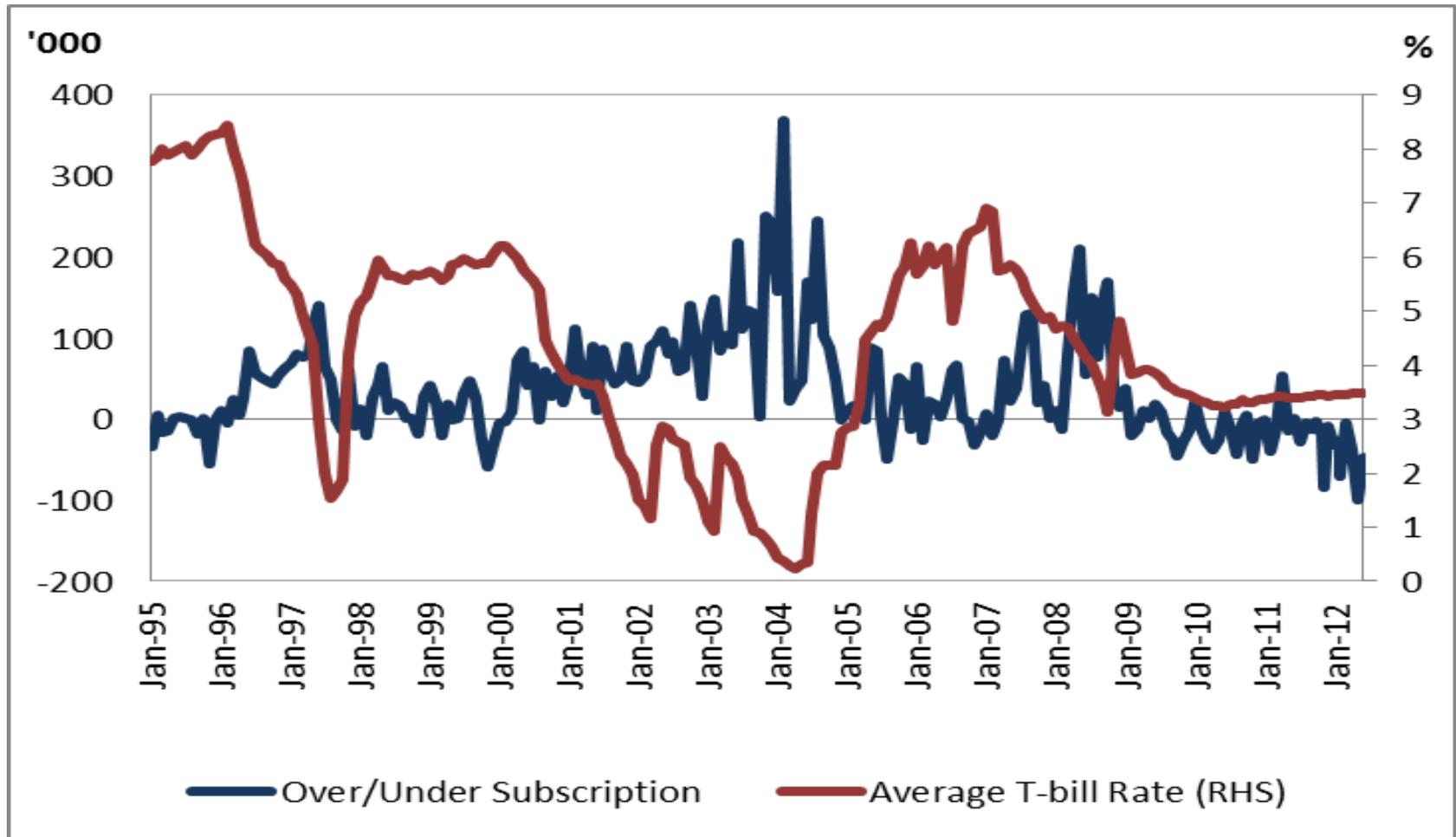


3-month T-bill rate and Excess Liquidity



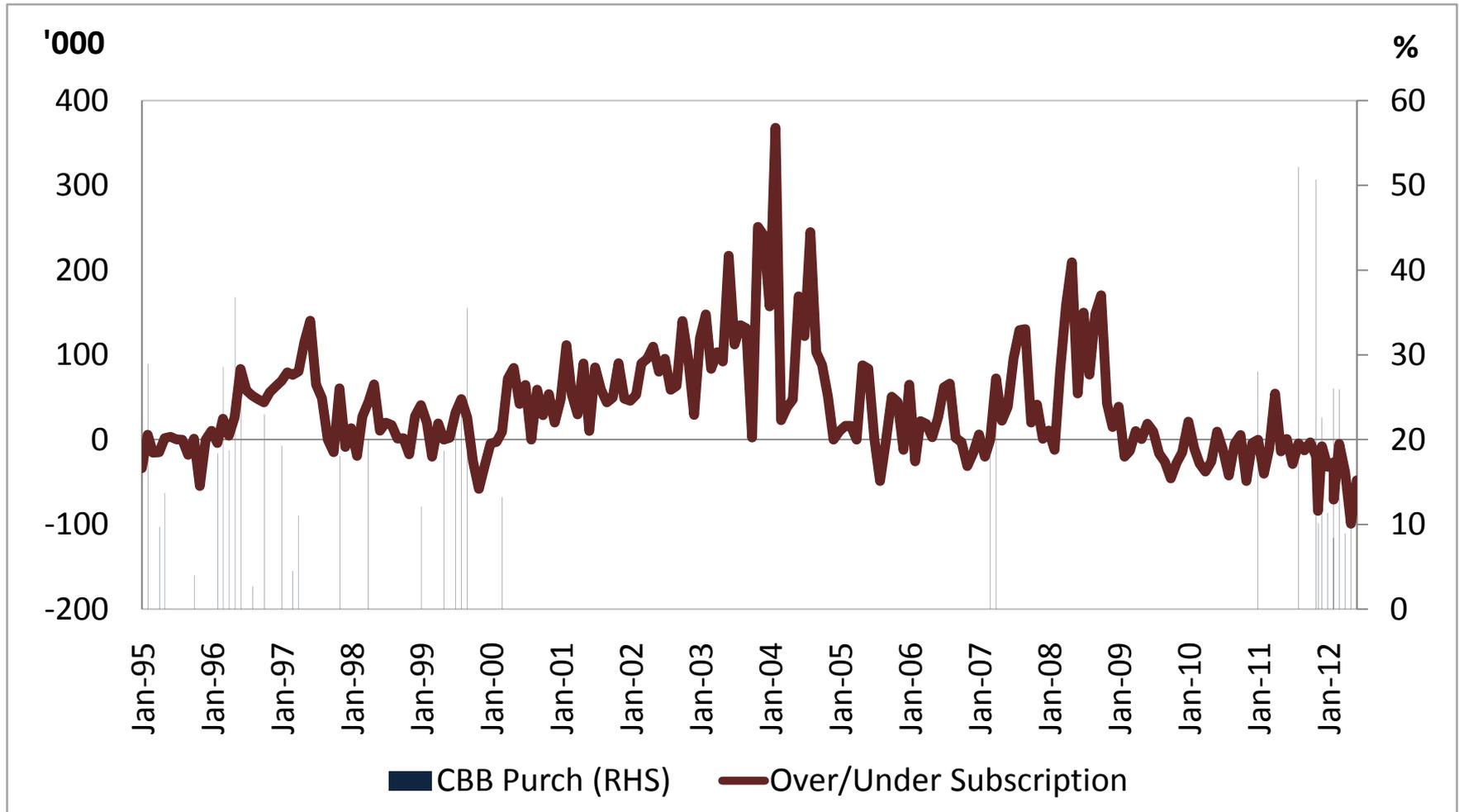


Over/Under Subscriptions and 3-month T-bill rates



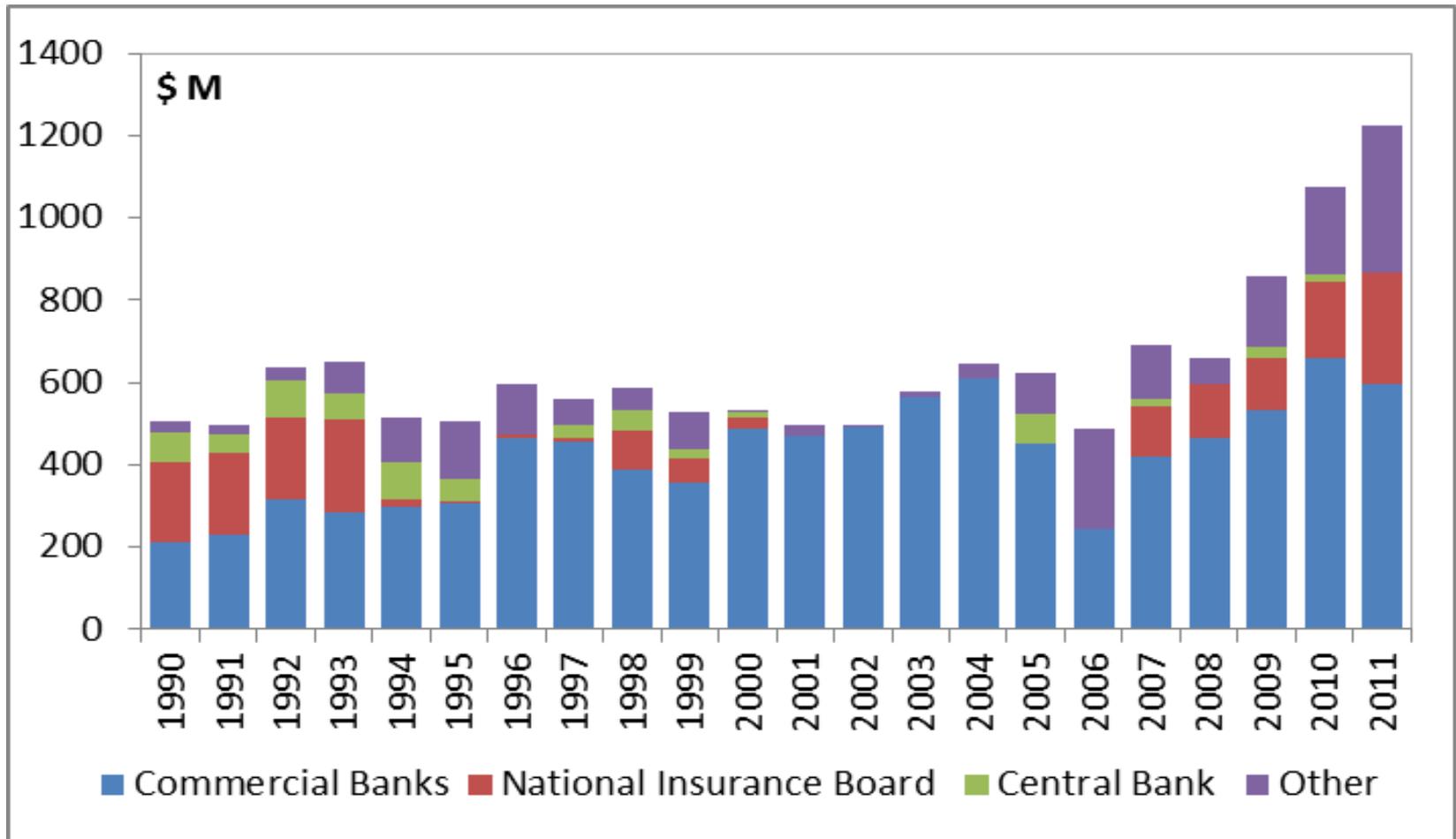


Over/Under Subscriptions and CBB Primary Purchases





Institutional Holders of 3-month T-Bills





MECHANICS OF POLICY FRAMEWORK

► Policy Framework

$$r_t^b = r_t^{eu} + \hat{\rho}_t$$

r_t^b is the average domestic 3-month T-bill rate

r_t^{eu} is the expected average US 3-month T-bill rate

$\hat{\rho}_t$ is the expected premium

► T-bill rate assessment

$$r_t^b = r_t^{*T} + /-50\text{bp}$$

r_t^{*T} is the Central Bank's target rate



LIQUIDITY FORECASTING FRAMEWORK

	09/26/ 2012	10/03/ 2012	10/17/ 2012
Amount offered for Tender	95.4	123.8	211.1
T-bills Maturing During Period	94.6	117.7	130.2
Excess Liquidity Position	3.2	3.4	3.1
Expected Allotment	84.3	123.8	161.1
Expected Shortfall	11.1	0	50
Central Bank Intervention	11	0	50
Target Rate	n.a.	n.a.	n.a.
Average T-bill Rate	3.52	3.53	3.54

Commercial Banks

Central Bank of Barbados

National Insurance Board

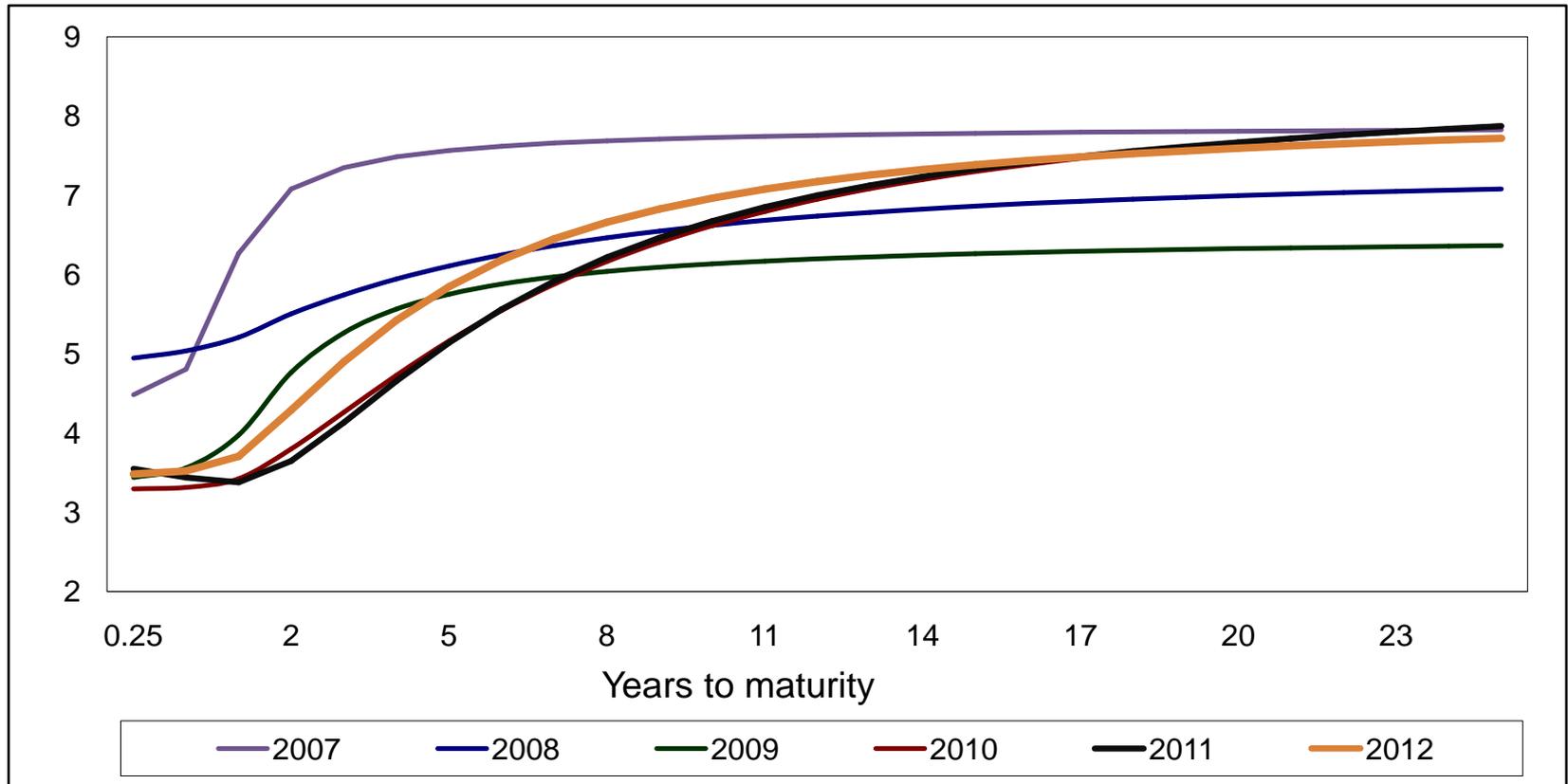
Trust Companies

Insurance Corporations

Others



NOTIONAL YIELD CURVES*



* Based on government bonds coupon rates



CONCLUSION

- ▶ Conventional approaches using interest rates as tools of monetary policy have not produced the intended policy outcomes.
- ▶ Proposed policy framework involves orderly intervention in the market for 3-month T-bills, when warranted, to ensure that interest rates are kept in line with comparable U.S. rates and to offer market guidance on the term structure of interest rates.
- ▶ Critical factors that will trigger policy intervention are the adverse movements in U.S. T-bill rates and the domestic liquidity conditions.
- ▶ Further work will seek to estimate premium to better inform notional target policy rate.



THANK YOU