Abstract

The paper evaluates transition of the monetary policy in Georgia to inflation targeting and the record of the first years of experience with this policy. The inflation targeting was officially announced in 2009; nevertheless, the National bank of Georgia ("NBG") was investigating and planning the transition since 2006. The NBG implemented new instrument the monetary rate – as a precondition for switching to the inflation targeting. The NBG has also improved the independence and transparency following its introduction.

Then, we assess the success of the policy change by investigating the efficiency of the monetary transmission mechanism using vector auto-regression models with alternative identification schemes, in particular, the Cholesky decomposition and sign restrictions approach. Our findings suggest that the monetary transmission mechanism works primarily via the Tbilisi interbank rate while the effects of changes in the newly implemented monetary policy rate are bit weaker. The maximum price decrease is achieved after about 15-17 months and it somewhat coincides with the NBG's horizon (4-6 quarters). We have further established that the monetary policy supports the financial stability to a certain extent.

JEL Classification	E4, E52, P2
Keywords	Inflation targeting, Monetary Transmission Mechanism, Vector Auto-regression Models

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