

# Report on Master Thesis

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

**Student:** Ketevan Megrelishvili  
**Advisor:** PhDr. Jaromir Baxa, Ph.D.  
**Title of the thesis:** Inflation Targeting Turns Ten in Georgia: Assessment of the Experience

**OVERALL ASSESSMENT** (provided in English, Czech, or Slovak):

*Please provide your assessment of each of the following four categories, summary and suggested questions for the discussion. The minimum length of the report is 300 words.*

The master thesis of Ketevan Megrelishvili "Inflation Targeting Turns Ten in Georgia: Assessment of the Experience" is a work of several contradictions. On the one hand, it suggests and generally interesting and contributive macroeconomic topic of inflation targeting analysed from a non-standard point of view of the Georgian emerging economy. Interesting not only personally as I visited Georgia in 2010, a year after the inflation targeting adoption (and I still keep some Lari in my collection of foreign currencies) but also because it has a potential to contribute to the ongoing debate under what institutional circumstances and whether at all are developing economies ready for the inflation targeting regime. Moreover, this research potentially provides a comparison (not intended to be covered within this thesis) of experience with the generally successful case of the Czech Republic, which adopted inflation targeting in 1997, thus also in an emerging stage of a small economy.

On the other hand, the appealing research topic and a good intention in terms of application of a rather advanced methodology are considerably demeaned by some fundamental inadequacies in citing scientific sources, rather 'shallow' description of the methodology, and possibly also some disputable interpretations of empirical results. For instance, the credibility of otherwise very nicely and extensively elaborated chapter on the history of Georgian economy and of the development of the inflation targeting regime is to a large extent limited by almost a total absence of referencing regarding important historical or statistical data.

## Contribution

On top of what I suggest above, the intended contribution needs to be accentuated. The empirical research on Georgian monetary transmission is scarce and the work employs a very up-to-date dataset of variables comparable to the Bakradze and Billmeier (2008) paper that, nonetheless, only covers the pre-global financial crisis period. The results are different then in Bakradze and Billmeier (2008) and thus interesting.

Together with the main contributive results that the average transmission lag for price level is 15-17 months, that it takes almost a year for a price shock to die out, or that the output shock is smaller but more persistent, I also observe one potential inconsistency in author's interpretation of empirical results. The Granger causality test results (Table 6, pg. 65) are interpreted as a general rejection of the Granger causality ( $H_0$  nor rejected at 5% significance level) but the p-value for the price level is not even 6%. So for 6% (or 10%) significance level we would reject  $H_0$  of 'no Granger causality'... My opinion is that author's interpretation is rather strict, not supported by a strong statistical evidence, and partially arbitrary. Most interestingly, the results are opposite than those of Bakradze and Billmeier (2008).

## Methods

The description of the otherwise advanced and maybe challenging-to implement methodology is rather brief and to my mind partially incomplete. The structure of the VAR(p) model is only illustrated on the most trivial VAR (1), no theoretical derivation of its structure is provided. Formulas of information criteria seem to be copied from the lecture notes without deeper understanding what these really measure (the

# Report on Master Thesis

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

**Student:** Ketevan Megrelishvili  
**Advisor:** PhDr. Jaromir Baxa, Ph.D.  
**Title of the thesis:** Inflation Targeting Turns Ten in Georgia: Assessment of the Experience

author might want to disprove this during the defense). Some important concepts such as Cholesky factorization, lack of identification, or the MCMC algorithm are only mentioned without a proper explanation or reference. There is no proper explanation about the importance of the order of variables in the VAR structure. I also did not understand well the technique and details of sign restrictions which seems to be an important extension of the Bayesian VAR. The discussion about priors is rather short and based on one reference only.

There are also some incomprehensions w.r.t. elementary econometric concepts such as:  
"Brito and Bystedt (2010) regressed some models that..." (pg. 16, models are not being regressed, we can regress a variable on other variable(s) within a regression model)  
"All three are probability distributions and do not have any true parameters." (pg. 51, by definition, but maybe I only do not understand the meaning of this statement)

Does the monthly monetary rate on Fig 6 (bottom part, middle graph) really have a monthly frequency? Why only Schwartz Criterion is taken into account to determine number of lags: VAR(4) and BVAR(2)?

## Literature

Formally the weakest part of the thesis. The "vast literature on inflation targeting and monetary transmission mechanism" promised in the Introduction to motivate the analysed model shrinks to circa 8 papers

Some important and strong statements remain completely unsupported by any citation, several examples:

"However, there are sceptics who argue that developing countries... are not ready for the IT." (pg. 16)  
"Many economists claim that inflation targeting is the reason for the financial crisis." (pg. 16)  
"The opponents of inflation targeting claim that policy is too focused on the price level" (pg. 16)  
Jeffrey Frankel quoted there is not part of the Bibliography (pg. 16)  
"According to 2012's numbers, IT's share in the monetary policy regimes was 20%." (pg. 21, what numbers??)  
"Past analyses show that the exchange rate channel is the strongest in Georgia." (pg. 43)  
"Some authors find rather persistent increase in value of national currency, so called "delayed overshooting", whilst others report exchange rate depreciation, which also is referred as exchange rate puzzle." (pg. 47)

Mishkin (pg. 18) lacks year of publication to distinguish between 2 items from the Bibliography.

Macdonald, Egert and Halpern (2204) is in fact Egert et al. (2006) (pg. 19)

"In the last paper about inflation targeting in Georgia that was published in 2008,..." (pg. 47, authors missing)... etc.

Generally the sections 2.1, 2.2, otherwise extensively and very well elaborated, lack proper referencing regarding important historical or statistical data. I understand that a part of information can be considered common knowledge, but sources need to be clearly mentioned. The most problematic part from this point of view are then three sections (in italics, pg. 33, 36, 39) copied directly without proper referencing (generally years and internet addresses are missing, not in Bibliography, just in the footnote)..

Generally, the Bibliography section is inconsistent, I can see at least three styles of referring year of publication there.

# Report on Master Thesis

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

**Student:** Ketevan Megrelishvili  
**Advisor:** PhDr. Jaromir Baxa, Ph.D.  
**Title of the thesis:** Inflation Targeting Turns Ten in Georgia: Assessment of the Experience

## Manuscript form

First of all, the author refers to the work as to 'a paper'. It is incorrect at this is 'a thesis'. The thesis is generally poorly structured. The 'Literature review' should have already been labeled as Chapter 1 and divided into several subsections. Instead, it consists of 4.5 pages of rather unstructured text. Other chapters would also benefit from a division into more subsections. Subsection 4.1 should have been 4.2.

The flow of empirical results and their interpretation is disconnected by an additional section explaining what the nexus between monetary policy and financial stability.

The usage of 'bullet-points' to structure the text is not a nice text-formatting practice. Some typos or improper English such as "switch to IT was a necessary as...", "courtiers", etc. are then only minor shortcomings.

## Summary and suggested questions for the discussion during the defense

I am interested in the effect of the strong dollarisation in the country (not only at the moment of the inflation targeting adoption but generally over the whole analysed period, see Fig. 4 on pg. 41). Can you elaborate more on how specifically this dollarisation issue is likely to impede monetary policy in Georgia in general, the successful inflation targeting and monetary transmission? What channels it affects the most and what channels are least affected and why?

I was also interested in your argument that the inflation targeting "can be explained by the rational expectations hypothesis" (pg. 21). Can you explain this statement into detail.

Next, on pg. 37, you ask yourselves: "All of the above considered, is it sufficient to manage expectations?" but no answer is provided. You might want to provide the answer within the defense.

Lastly, I especially like one of your hypotheses:

"NBG manages to create correct expectations, which means that the prices and output response to policy interest rate shocks are consistent with economic theory".

But can you explain what the "correct" or, as you state further, the "right" expectations means? Do responses of macroeconomic variables that are consistent with economic theory really guarantee that expectations of economic agents are "correct"?

## SUMMARY OF POINTS AWARDED (for details, see below):

CATEGORY	POINTS
Contribution (max. 30 points)	26
Methods (max. 30 points)	22
Literature (max. 20 points)	6
Manuscript Form (max. 20 points)	9
<b>TOTAL POINTS (max. 100 points)</b>	<b>63</b>
<b>GRADE (A – B – C – D – E – F)</b>	<b>D</b>

**NAME OF THE REFEREE:** Jiří Kukačka

**DATE OF EVALUATION:** 25. 1. 2018

---

Referee Signature

# Report on Master Thesis

Institute of Economic Studies, Faculty of Social Sciences, Charles University in Prague

**Student:** Ketevan Megrelishvili  
**Advisor:** PhDr. Jaromir Baxa, Ph.D.  
**Title of the thesis:** Inflation Targeting Turns Ten in Georgia: Assessment of the Experience

## EXPLANATION OF CATEGORIES AND SCALE:

**CONTRIBUTION:** *The author presents original ideas on the topic demonstrating critical thinking and ability to draw conclusions based on the knowledge of relevant theory and empirics. There is a distinct value added of the thesis.*

<i>Strong</i>	<i>Average</i>	<i>Weak</i>
30	15	0

**METHODS:** *The tools used are relevant to the research question being investigated, and adequate to the author's level of studies. The thesis topic is comprehensively analyzed.*

<i>Strong</i>	<i>Average</i>	<i>Weak</i>
30	15	0

**LITERATURE REVIEW:** *The thesis demonstrates author's full understanding and command of recent literature. The author quotes relevant literature in a proper way.*

<i>Strong</i>	<i>Average</i>	<i>Weak</i>
20	10	0

**MANUSCRIPT FORM:** *The thesis is well structured. The student uses appropriate language and style, including academic format for graphs and tables. The text effectively refers to graphs and tables and disposes with a complete bibliography.*

<i>Strong</i>	<i>Average</i>	<i>Weak</i>
20	10	0

## Overall grading:

TOTAL	GRADE
91 – 100	<b>A</b>
81 - 90	<b>B</b>
71 - 80	<b>C</b>
61 – 70	<b>D</b>
51 – 60	<b>E</b>
0 – 50	<b>F</b>