

A MONETARY CONDITIONS INDEX FOR ALBANIA

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ABSTRACT: The goal of the construction of a Monetary Conditions Index (MCI) is to analyze both the interest rate channel and the exchange rate channel. The construction is based on standard open economy macroeconomic models. MCI is the weighted sum of the change in short-term interest rate and the exchange rate with the base period, with weights that are usually taken from empirical econometric models and that reflect the estimated impact of these variables to the product or to inflation. MCI change, gives in a single number the degree of narrowing or release (expansion) of monetary conditions. In this paper is proposed a MCI for Albania. Based in the calculations done by the author and after the comparison of this type of MCI with the type of MCI calculated from Bank of Albania, the author recommends to Bank of Albania the use of the MCI calculated in this paper. The reason of this recommendation is the more accurate description and explanation of monetary policy stance obtained from the use of MCI calculated in this paper.

Key words: monetary policy, interest rate, exchange rate, Monetary Conditions Index, real effective exchange rate

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