ABSTRACT

The central bank's policy mix integrates monetary and macroprudential policies into one coordinated policy framework to achieve the central bank's dual objectives of price stability and financial stability. In practice, the interaction of monetary and macroprudential policies can have an impact on each of the policy objectives. In the short term, monetary policy instruments through central bank's policy rates can have an impact on credit which affects financial system stability given that monetary and macroprudential policies work on the same transmission path. Moreover, under certain conditions, the use of both policies can also be challenging. Kim and Mehrotra (2017) mentioned that under conditions of low inflation and high credit growth, the simultaneous use of both instruments may lead to trade-offs or the objectives of both policies are counterproductive. On the other hand, if the central bank uses one or two policy instruments for the same purpose, the policy can only stabilize one of the objectives.

This study aims to analyze the impact of monetary and macroprudential policies on price stability and financial system stability and analyze the contribution between policies in influencing price stability and financial system stability under conditions of Low Inflation and High Credit Growth. This study uses the Structural VAR (SVAR) model approach with the help of Impulse Response Function and Forecast Error Variance Decomposition to analyze the impact of monetary and macroprudential policies on price stability and financial system stability. This study also uses Historical Decomposition to analyze the potential trade-offs that occur in conditions of Low Inflation and High Credit Growth in Indonesia. The results show that macroprudential policies such PLM, RIM, and LTV have a negative impact on the inflation rate. Meanwhile, policy rate negatively affects the level of Credit-to-GDP Gap significantly. This study also found trade-off periods where macroprudential policy contributed to lowering the inflation rate away from the target and monetary policy contributed to increasing the level of Credit-to-GDP Gap. Furthermore, this study also finds periods where both policies are complementary.

Keywords: *Policy Mix*, *Monetary Policy*, *Macroprudential Policy*, *Trade-off*, *Structural VAR*