

Central Bank's Independence and the Golden Rule in Nepal: A Concept Analysis with Dynamic Inconsistency of Monetary Policy

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Abstract

This paper attempts to study the concept analysis of the central bank's independence and the golden rule in Nepal in relation with the dynamic inconsistency of monetary policy. In 2007, an optimal inflation-rate was assessed, which suggested that it would be beneficial for Nepal to establish a range for inflation targets centered around the optimal inflation rate identified through analysis which would grant autonomy to the Nepal Rastra Bank (NRB) to ensure price stability. However, concerns have arisen regarding potential political influence on the NRB and fiscal challenges, leading to uncertainties about the country's economic sustainability. The Golden Rule, advocating for balanced budgets, is proposed as a potential solution, but its implementation is complicated by Nepal's unique socio-political context. This research, drawing on economic theories from Kydland, Prescott, Barro, Gordon, and others, delved into the complex relationship between central bank independence, fiscal policy, and consistency in Nepal. The nation's economic path hinges on effectively navigating these complexities to strike a balance between immediate political needs and long-term stability. The concept of dynamic inconsistency underscores the risks associated with prioritizing short-term gains, emphasizing the necessity for strategic decision-making in economic governance. Ultimately, Nepal confronts the challenge of aligning its economic policies to ensure resilience against short-term pressures while promoting enduring long-term stability.

Keywords: dynamic inconsistency, concept analysis, golden rule, inflation-targeting regime, Nepal Rastra Bank.

JEL Classification: D91, A12, E21, E52, G28

Introduction

In the current setup of a fixed exchange rate and capital flows, the primary driver of inflation stems from India. The Nepal Rastra Bank (NRB) can influence domestic inflation in the short term, typically within a one-year timeframe, but its ability to control inflation diminishes beyond that period (NRB, 2007). The grant of the significant operational independence to its central bank, the Nepal Rastra Bank, has thrust the interplay between central bank independence, the Golden Rule of fiscal policy, and the potential pitfalls of dynamic inconsistency into the spotlight. Unraveling the complex ties that bind these elements is crucial for Nepal's long-term economic stability and growth.

Nepal's proposed decision to anchor its monetary policy around an inflation target

near optimal inflation rate was driven by a desire for price stability, a cornerstone of sustainable economic growth (NRB, 2007). By granting the NRB operational autonomy, policymakers did hope to insulate monetary decisions from short-term political encumbrances that could jeopardize price stability (Walsh, 1998). However, concerns linger about the central bank's vulnerability to political influence and its unwavering commitment to its long-term inflation target (Alesina & Summers, 1993). Understanding how Central Bank Independence (CBI) shapes the NRB's effectiveness in achieving its inflation objective becomes paramount in this context.

Nepal's ballooning fiscal deficits and public debt paint a concerning picture of unsustainable fiscal practices. Implementing the Golden Rule, advocating for budget balance over the entire economic cycle, could hold the key to unlocking fiscal sustainability (Blanchard, 1990). Yet, aligning fiscal policy with such a principle faces real-world challenges. Political pressures often tempt policymakers to deviate from long-term goals in favor of short-term popularity, potentially exacerbating fiscal imbalances (Bohn, 1995). Deciphering how CBI interacts with the adoption and adherence to the Golden Rule in Nepal's unique political and economic landscape is crucial for designing robust fiscal policies that ensure future stability. Lurking beneath these concerns lies the ever-present specter of dynamic inconsistency. The possibility of policymakers succumbing to short-term temptations despite their long-term goals poses a significant threat to both monetary and fiscal stability (Rogoff, 1985).

Policymakers ensure a stabilization policy and the goal of stabilization policy should guarantee the sustainable growth. Nonetheless, in some cases the policy is synchronized with the short run aims, which upon later may lead to the awful re-adjustments. If the policymakers believe that the aggregate demand movements affect the real output, they may increase the Money supply (Ms) in order to push the output above normality. Likewise, if they are again experiencing with the inflation which everyone perceives is too high, they may show the reluctance to undergo a recession in order to reduce it.

For this situation, Kydland and Prescott (1977) stated that even in the case of non-existence of a long-term relationship between inflation and unemployment an ambiguous policy can lead towards high inflation without positive effects on employment. They further assert that the realization of the monetary policymaker and the public, where the public perceives the commitments of the politicians and on the basis of this information forms expectations (Ratex-Rational expectations and on optimal strategy).

The motivation to carry out this study is due to the limited research on the concept analysis of the dynamic inconsistency delving into the central bank's independence and the golden rule in Nepal. This paper aims to shed light on the conceptual outlook between CBI, the Golden Rule, and dynamic inconsistency of monetary policy in Nepal's context. The insights gleaned from this analysis can inform the design of more robust policy frameworks, strengthen institutional development, and ultimately, contribute to Nepal's long-term economic stability and prosperity.

Review of the Literature

Pandey and Bhattarai (2016) explored the relationship between monetary policy credibility and Central Bank independence in Nepal's financial markets. Combining

quantitative analysis with qualitative assessments, their study identifies a positive correlation between Central Bank independence and monetary policy credibility. The findings suggest that enhancing Central Bank independence can contribute to increased confidence in monetary policy, leading to more stable financial markets.

Subedi and Regmi (2017) investigated institutional frameworks and Central Bank independence in Nepal, employing a comparative analysis approach. By examining international experiences, their study identifies key elements contributing to successful central bank independence in other countries. The implications highlight areas where Nepal's institutional framework can be strengthened to enhance the autonomy and effectiveness of its central bank.

Sharma and Acharya (2018) empirically investigated the relationship between Central Bank independence and economic stability in Nepal, focusing on inflation, economic growth, and financial stability. Utilizing econometric models and time-series data, their study finds a significant correlation, emphasizing the importance of maintaining a high degree of Central Bank autonomy for sustained economic stability.

Khanal and Thapa (2019) explored dynamic inconsistency in Nepal's monetary policy decisions, employing case studies and content analysis. Identifying instances where the Central Bank's actions deviate from stated policies, their qualitative approach reveals factors such as political pressure and changing economic conditions contributing to dynamic inconsistency. The implications suggest the need for policy frameworks that reduce such inconsistencies to enhance the effectiveness of monetary policy.

Joshi and Adhikari (2020) examined the applicability of the golden rule of public finance to Nepal, combining theoretical frameworks with empirical analysis. Their study considers fiscal policies' alignment with the golden rule, recommending adjustments to ensure long-term fiscal stability and sustainable economic development.

Smith and Rodriguez (2021) conducted a comprehensive global analysis on the relationship between Central Bank independence and economic performance. The study contributed valuable insights by shedding light on the complexities of achieving economic objectives through Central Bank independence on a global scale. It underscored the need for tailored policies that consider the unique characteristics of each economy to maximize the benefits of Central Bank autonomy.

Research Gap

A gap remains in understanding how this dynamic inconsistency of monetary policy apply to the unique circumstances of Nepal subject to the golden rule and concerning the central bank's independence. The synthesis of these studies identifies the need for further research that not only delves deeper into the intricacies of Central Bank autonomy within the Nepalese context but also to conceptually comprehend the need of the relationship of the golden rule and the central bank's independence that bridges the gap between the inconsistency of the monetary policy dynamics in fostering economic stability and growth.

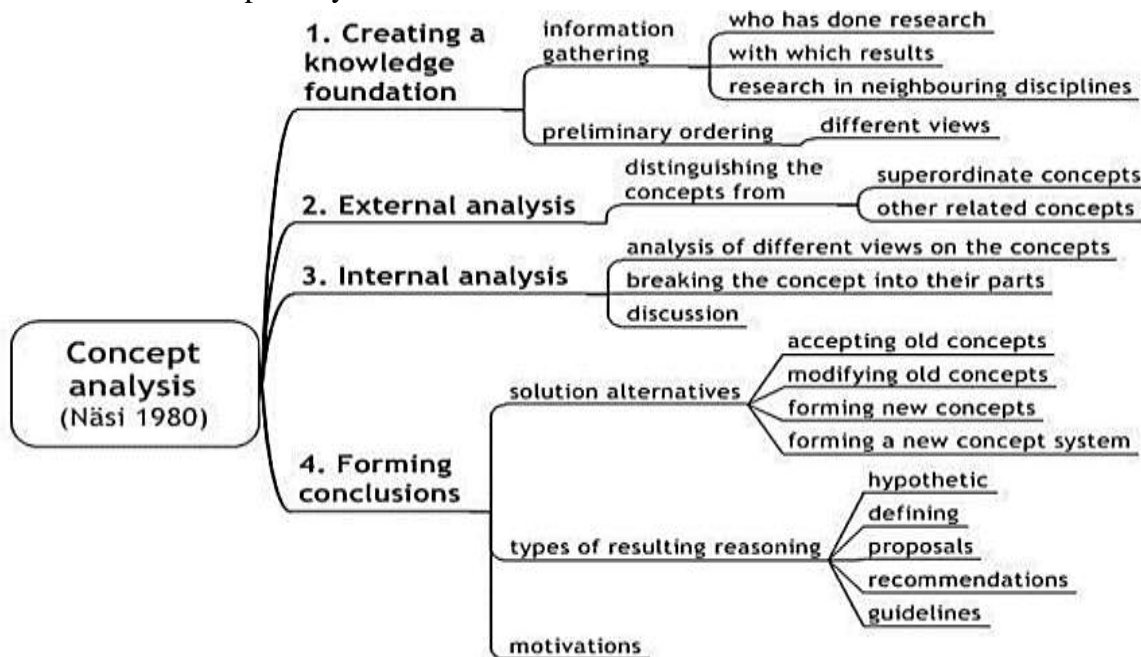
Methodology

This study employs a concept analysis approach to investigate the intricate interplay between Central Bank independence, adherence to the golden rule in fiscal policies, and the occurrence of dynamic inconsistency in Nepal's monetary policy. Näsi (1980) stated that

concept analysis is a vital research activity aimed at enhancing conceptual clarity by dissecting, understanding, and defining the attributes and relationships of key concepts.

Näsi's Four Elements of Concept Analysis

Näsi's model comprises four interwoven elements: information gathering, external analysis, internal analysis, and conclusion. These elements provide a flexible yet systematic framework for concept analysis.



Note. Nuopponen (2010) and Näsi (1980).

Analysis and Discussions

Creating a Knowledge Foundation

Dynamism

Kydland and Prescott (1977) claimed and sought a policy that was compatible with the temporal aspect. According to them, the monetary rule is a promise that policymakers strive to keep so that the public's expectations match the actual rate of inflation. However, discrete decisions deviate from the laws of monetary policy and follow their own rules (Romer, 1976).

Equation Outlook and Assumptions

Consider an economy in which aggregate demand disturbances have actual impacts and inflation expectations influence aggregate supply. AS (Aggregate Supply is given by Lucas Curve).

Flexible Price Level (FPL) of output < Socially Optimal Level (SOL) of output:

$$y = \hat{y} + b (\pi - \pi^e) \dots\dots\dots (i)$$

Where, $b > 0$, $y = \log (\text{output})$ and $\hat{y} = \log (\text{FPL})$

The FPL is lower than the SOL due to either positive marginal tax rates (preventing common people from fully benefiting from increased labor supply) or imperfect competition (preventing firms from fully benefiting from increased output).

Inflation above a certain level is costly. To account for all of the assumptions, let the social welfare function be quadratic in both output and inflation. The

policymaker minimizes the loss function.

$$L = 1/2 \{ (y - y^*)^2 + a (\pi - \pi^*)^2 \} \dots \dots \dots \text{(ii)} \quad \text{Where, } y^* > \hat{y} \text{ and } a > 0$$

External Analysis

Analysis of the model

Consider two possible approaches to determining monetary policy and projected inflation.

First situation. Before determining the projected inflation, the policymaker makes a binding pledge as to what it will be. Now, in a binding commitment, expected inflation equals actual inflation, hence equation (i) yields the output equal to the normal rate. Now, the policymaker must choose ' π ' to minimize 'L'. The solution is simply ' $\pi = \pi^*$ '.

Second situation. The policymakers choose inflation based on expectations (E). This may happen if projected inflation is estimated before money growth, or if ' π ' and ' π^e ' are determined concurrently.

Minimization. Substituting equation (i) and equation (ii), the policymaker's problem would be:

Minimize: $1/2 [\{ \hat{y} + b (\pi - \pi^e) - y^* \}^2 + a (\pi - \pi^*)^2]$ The First Order Condition (FOC) is:

$$b \{ \hat{y} + b (\pi - \pi^e) - y^* \} + a (\pi - \pi^*) = 0 \dots \dots \dots \text{(iii). Solving for } \pi, \text{ we get; } \pi = \{ b^2 \pi^e + a \pi^* +$$

$$b (y^* - \hat{y}) \} / (a + b^2) \dots \dots \dots \text{(iv)}$$

$$\pi = \pi^* + \{ b / (a + b^2) \} (y^* - \hat{y}) + \{ b^2 / (a + b^2) \} (\pi^e - \pi^*) \dots \dots \dots \text{(v)}$$

Graphic Analysis

Figure 1

Inflation Determination (In Absence of Commitment)

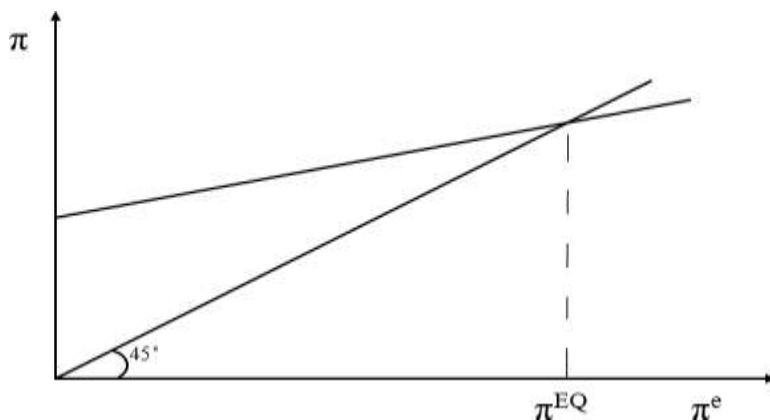


Figure 1 and equation (v) show that the policymaker intends to pursue an expansionary policy. If the public expects policymakers to adjust the optimal inflation rate ' π^* ', the marginal cost (MC) of slightly higher inflation is positive. In this case, the policymaker chooses an inflation rate higher than ' π^* '.

If there is no uncertainty, equilibrium requires that expected and actual inflation are equal. If we impose ' $\pi = \pi^e$ ' in equation (v), we get,

$$\pi^e = \pi^* + (b/a) (y^* - \hat{y})$$

$$\pi^e = \pi^{EQ} \dots \dots \dots \text{(vi)}$$

If the expected inflation surpasses this amount (π^{EQ}), the actual inflation is less than individuals expects and the economy turns to be in disequilibrium. Likewise, if ' π^e ' is less

than π^{EQ} , π exceeds π^e . Hence, the only equilibrium for π and π^e is π^{EQ} and for y to be equal with \hat{y} . The expected inflation rises to the point where the policymaker, taking π^e as given chooses to set $\pi = \pi^e$. In a nutshell, the policymaker's discretion is to increase inflation without affecting the output.

Internal Analysis

Barro and Gordon (1983) Analysis of Dynamism

When it comes to dynamic inconsistency, the notion established by Barro and Gordon is also important. Barro and Gordon discussed the two equations that represented both sides of the monetary mechanisms. Their model focused on the two main educational outlooks. They were:

Utility of the Central Monetary Policy Authority

$$U_t = \phi (Y_t - Y_n) - \pi_t^2/2 \dots \dots \dots (vii)$$

Where; Y_t = the actual rate of output (change in output)

Y_n = the natural rate of the output (this is consistent with the absence of any business cycle shocks)

π_t = Inflation

Since this equation is dependent on the ' ϕ ', we must ensure that it is positive, i.e. $\phi > 0$. The term ' ϕ ' refers to the Central Monetary Authority's assessment of deviations from the natural rate of output. When ' ϕ ' becomes positive and ' Y_t ' exceeds ' Y_n ', the central bank's utility grows.

The General People

Assume that the average person has the following output function:

$$Y_t = Y_n + \alpha \{ \pi_t - E(\pi_t) \} + \mu_t \dots \dots \dots (viii)$$

This equation (viii) is what public faces. The ' $\{ \pi_t - E(\pi_t) \}$ ' is the deviation that is defined as the actual inflation deviation from the expected inflation. The predicted inflation rate, denoted as ' $E(\pi_t)$ ', is based on the general public's expectations at a certain moment. These expectations are influenced by the central monetary authority's policy statements.

' ϕ ' indicates people's sensitivity to deviations from inflation expectations, while ' α ' is also positive. ' μ_t ' is a disturbance term with a zero serially uncorrelated error term, representing all sorts of economic shocks. When the value of ' μ_t ' is positive, the output increases; when it is negative, the output decreases. In equation (vii), the central monetary authority maximizes its utility when there are higher variances in the output. However, when the ' π_t ' value increases, the case changes. The central monetary authority must make a trade-off between output and inflation. While output cannot be directly impacted, inflation can be. The rate of ' $\{ \pi_t - E(\pi_t) \}$ ' can be chosen, but not ' Y_t '.

Actually, the abstractness of equation (viii) is undefined because it describes the general public's perception, which is also the Aggregate Supply (AS) curve. The equation (viii) represents the Expectations Augmented Phillips curve for output, which also correlates with inflation. The Phillips Curve is an AS curve that shows a positive correlation between price changes ($\{ \pi_t - E(\pi_t) \}$) and output changes (Y_t). The central monetary authority seeks to maximize their utility in a way that, hopefully, raises output above the natural rate, so boosting aggregate supply. As Because the central monetary authority can only select ' π_t ' and

not 'Yt', in equation (vii), 'πt' is indirectly proportional to the utility of the central monetary authority. The central monetary authority maximizes utility under equation (vii) by selecting the ideal inflation rate of 'πt* = φα'. The '*' denotes the optimal option. The central monetary authority considers a mixture of two things, namely

- a) Preferences (stated by 'φ') - as 'φ' shows that how much the central monetary authority cares about the changes in output from inflation.
- b) The influence of the supply – this is stated by 'α', nonetheless, if the value of 'α' is small that too rules out.

When the value of the 'φ' is modest, the central monetary authority is less concerned with the increase in output (Yt) compared to inflation. When the 'φ' value is high, the central monetary authority prioritizes output over other factors. This can be expressed as whether the central monetary authority is a "inflation hawk" or a "inflation dove".

The predicted rate of inflation, 'πt* = φα'; 'φ', 'α > 0', indicates that inflation will be positive. The central monetary authority will issue "zero" inflation rates, indicating that the general public's expected inflation is zero. i.e. 'E (πt)'= 0.

However, there are two distinct possibilities in terms of public expectations and assumptions.

Adaptive Expectations

Under adaptive expectations, the general public knows more things and is better off with the information set. When the general public believes that inflation will be zero. In equation (viii), the central monetary authority prefers 'πt* = φα' and 'φ', 'α > 0' rather than 'E (πt)'=0.

$$Y_t = Y_n + \alpha (\phi\alpha - 0) + \mu_t$$

$$Y_t = Y_n + \alpha^2 \phi \dots \dots \dots (ix) [E (\mu_t) = 0]$$

Since people's inflation expectations are '0', output can be increased in the first period by 'α²φ' over the natural rate of output. In the first period, we receive equation (ix) as output, which means that actual output exceeds the natural rate, which is where the central monetary authority is smart enough.

Now let's look at the other side of the tale. Assume the general public updates the inflation expectation for tomorrow as 'E (πt + 1) = φα'. In this instance, the general public does not trust that the central monetary authority's 'E(πt + 1)' = 0. Assuming one period ahead in equation (viii), we get:

$$Y_{t+1} = Y_n + \alpha \{ \pi_{t+1} - E (\pi_{t+1}) \} + \mu_{t+1}$$

Because 'Yn' is the natural rate of output, it remains constant over time (at least for short durations). 'πt + 1' refers to the non-monetary oscillations (shocks) in the business cycle. The central monetary authority continues to optimise when 'πt* + 1= φα'.

Now, putting the values, $Y_{t+1} = Y_n + \alpha (\phi\alpha - \phi\alpha) + \mu_{t+1}$

$$Y_{t+1} = Y_n + \mu_{t+1}$$

$$Y_{t+1} = Y_n [E (\mu_{t+1}) = 0]$$

This means that the output over time and the natural rate are similar, as most people are now aware. However, high inflation causes economic inefficiency and diminishes the utility of the central monetary authority. When utility and output are average and inflation is low, it is preferable to a single period of high output followed by high inflation.

Rational Expectations

The public is familiar with the central monetary authority's policy, which is expressed as 'E (μ_t) = 0'. They know the authority will set ' $\mu_t = \phi\alpha$ ', therefore they think it's detrimental to set 'E (μ_t) = $\phi\alpha$ '. In the first period it is:

$$Y_t = Y_n + \alpha (\phi\alpha - \phi\alpha) + \mu_t Y_t = Y_n + \mu_t$$

$$Y_t = Y_n [E (\mu_t) = 0]$$

In the second period where 'E (π_{t+1}) = $\phi\alpha$ ';

$$Y_{t+1} = Y_n + \alpha (\phi\alpha - \phi\alpha) + \mu_{t+1}$$

$$Y_{t+1} = Y_n + \mu_{t+1}$$

$$Y_{t+1} = Y_n [E (\mu_{t+1}) = 0]$$

It follows under this scenario; the central authority cannot increase output above its natural rate. Most significantly, if the central bank sets ' $\pi_t^* > \phi\alpha$ ', the ' Y_t ' grows, but the utility of the central monetary authority decreases dramatically. Thus, there is always a limit to "monetary expansion". Thus, Barro and Gordon described the dynamic of monetary expansion. It is evident that it is the "expectations" that define the ' π^* ', and if individuals are reasonable enough, and the central monetary authority is not interested in increasing inflation above the optimal amount, the utility of itself will decrease.

Forming Conclusions

Rule and Discretion

When a policymaker has discretion, they can design policies based on contingencies or conditions. However, if they are bound by a law, the central authority must maintain inflation ' $\pi_t^* = 0$ '. It is well known that Milton Friedman stated that the central authority could be bound by a rule that increased the monetary base by 2% and 3% each year, as well as another rule that forced the nominal interest rate to zero, resulting in the real interest rate equaling the rate of deflation in the economy.

When a policymaker follows a rule, they are required to stabilize inflation, and monetary policy cannot be employed solely to influence the business cycle. The central bank utility is defined as follows:

$$U_t(\text{RULE}) = -\pi_t^2/2$$

If ' $\pi_t = 0$ ', only ' $U_t(\text{RULE})$ ' is maximized. This means that if projected inflation is zero, utility is maximized.

How do Policymakers Promote Social Welfare?

Carlin and Soskice (2006) have stated the policymaker has discretion; the root of the specific problem is beyond discretion. It would be unusual if people believed that the policymaker could commit to a strategy while also having discretion. In this situation, the policymaker can declare inflation equal to ' π^* ' and cause predicted inflation to be equal to ' π^* '. However, policymakers can set inflation using the equation (v). As equation (v) solves the problem of minimizing the social loss function given expected inflation, this commitment improves social welfare.

General Solutions to Dynamic Inconsistency

- a) Replacing discretion by a rule: Commitment
- b) Delegation of monetary policy to an independent central bank by the

government.

- c) Reputation: Building a reputation for being tough on inflation.

In essence, the situation is increasingly leading to a debate about the merits of strictly following rules vs using discretion. As a result, the central bank must operate within limits that allow it to lower inflationary pressures while optimizing overall welfare results (Relovsky, 2004).

Dynamic Inconsistency and Golden Rule

The monetary rules are set as promises to align public expectations with actual inflation rates, discrete decisions often deviate from these rules. This deviation is attributed to the dynamic nature of economic conditions and the temptation for policymakers to pursue alternative courses of action. Understanding this dynamic inconsistency is crucial as it sheds light on the complexities of implementing a consistent and effective monetary policy, especially when policymakers may be inclined to diverge from established rules.

The golden rule, or adherence to a rule rather than discretionary policymaking, can lead to optimal outcomes, especially when the rule entails stabilizing inflation at a specific level. This is significant because it highlights the trade-off between discretionary policymaking and rule-based approaches, as well as insights into the possible benefits of committing to a preset set of norms for the central bank. Evaluating the golden rule's application might help policymakers choose between discretion and commitment when developing monetary policy options (Jones, 2019).

Implications for Nepal

It is crucial for a comprehensive analysis of these concepts as they provide a conceptual foundation for understanding the complexities of monetary policymaking, the potential benefits of rule-based approaches (such as the golden rule), and the need for a country-specific assessment to inform policy decisions in the context of Nepal.

In the dynamic landscape of Nepal's economic governance, the autonomy of the Central Bank plays a crucial role in shaping the nation's financial trajectory (Smith, 2021). Analogous to a conductor directing an orchestra, the Central Bank orchestrates monetary policies that have far-reaching impacts on interest rates, inflation, and employment (Coats, 2019). However, this autonomy introduces a nuanced challenge—the dynamic inconsistency of monetary policy, akin to navigating a chessboard where each move triggers a cascade of effects (Brown, 2020). The Central Bank must strategically plan its actions, grappling with the intricacies of short-term gains versus long-term stability (BIS, 2012).

Amidst this economic chess match, the Golden Rule serves as a guiding beacon, casting its enlightening glow on the decisions of the Central Bank (Jones, 2019). This rule encapsulates the delicate balance between economic growth and inflation, urging policymakers to navigate the narrow channel where excessive inflation or overly restrictive policies can lead to adverse consequences (Williams, 2020). The Golden Rule thus functions as both a compass and a warning, steering policymakers through economic waters while avoiding the perilous reefs of instability (Davis, 2021).

Determining the optimal monetary policy framework for Nepal necessitates a careful examination of the country's economic landscape and priorities. Firstly, an in-depth assessment of the current economic conditions is crucial, encompassing factors such as

inflation rates, growth prospects, and overall economic stability. If Nepal is grappling with immediate concerns related to inflation control and economic stability, adopting a monetary policy targeting approach may be prudent. This strategy allows the central bank to utilize interest rates and other monetary tools to manage inflation and stabilize the economy in response to short-term fluctuations. Conversely, if the focus is on establishing a long-term commitment to a specific inflation level for sustained economic stability, the golden rule might be a viable option. This rule involves a credible commitment to maintaining a predetermined inflation target, fostering confidence among the public and investors.

The decision-making process must factor in the institutional capacity of Nepal's central bank. An evaluation of the institution's capabilities in implementing monetary policies effectively is essential. This includes an examination of transparency, communication strategies, and the ability to respond flexibly to economic shocks. If the central bank possesses the necessary tools and flexibility required to navigate uncertainties, a monetary policy targeting approach might align well with the country's needs. On the other hand, if there is a focus on building a credible commitment and ensuring a stable, rule-based approach, the golden rule may be more suitable. Additionally, considering public perception and understanding of the chosen framework is critical. Clear communication about the selected monetary policy approach is essential for garnering support and cooperation. Ultimately, the decision-making process should align the chosen approach with long-term economic goals, weighing the trade-offs between short-term flexibility and sustained stability. Engaging with experts, stakeholders, and thorough analysis will contribute to a well-informed decision that accommodates Nepal's unique economic circumstances.

Conclusions

Nepal's assessment of the optimal inflation rate proposed a way to target an inflation was accompanied by significant operational independence for the Nepal Rastra Bank (NRB), has thrust critical considerations into the limelight. This research paper sought to unravel the complex interplay between central bank independence, the Golden Rule of fiscal policy, and the looming threat of dynamic inconsistency. The decision to anchor monetary policy around an inflation target was a response to the pursuit of price stability, a cornerstone for sustainable economic growth. While the autonomy granted to the NRB aimed to insulate monetary decisions from short-term political pressures, concerns linger about potential vulnerabilities to political influence and the steadfast commitment to long-term inflation targets. Understanding how central bank independence shapes the NRB's effectiveness in achieving inflation objectives becomes paramount in navigating Nepal's economic landscape.

The research underscores the significance of addressing the ever-present specter of dynamic inconsistency, where policymakers may succumb to short-term temptations, jeopardizing both monetary and fiscal stability. Through a thorough concept analysis, this study sheds light on the complexities of policymakers' decision-making, emphasizing the role of expectations and commitment. The literature review revealed a positive correlation between central bank independence and monetary policy credibility in Nepal, but a notable research gap persists. This study highlights the necessity for future research to delve deeper into the intricacies of central bank autonomy within Nepal's context, emphasizing the conceptual relationship between the Golden Rule and central bank independence. As Nepal

charts its economic trajectory, this research offers critical insights that can inform robust policy frameworks, strengthen institutional development, and contribute significantly to the nation's long-term economic stability and prosperity.

Implications for Future Researchers

This study calls for further research to bridge the existing gap in understanding how dynamic inconsistency, central bank independence, and the Golden Rule apply to Nepal's unique circumstances. Future researchers should delve deeper into the intricacies of Central Bank autonomy within the Nepalese context and conceptualize the relationship between the Golden Rule and central bank independence with different methods of quantifications and with the use of the econometric tools. Exploring policy frameworks that reduce inconsistencies and enhance the effectiveness of monetary policy is imperative for future researchers for Nepal's long-term economic stability and prosperity.

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