FUNCTIONS OF THE CENTRAL BANK

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Introduction

Central banks in the past performed various functions and were often private entities. Today, as a rule, they are public institutions whose main purpose is most often to ensure monetary stability. To achieve this, central banks implement a specific monetary policy. However, this is not their only task. Usually the central bank also has the exclusive right to issue money.

The role of the central bank

It is assumed that the central bank is:

- an issuing bank - which means that it is an issuer of banknotes and coins, with which is indirectly connected the exclusive right of the central bank to conduct monetary policy, which in modern times is usually understood as a policy directed at taking care of the value of money by shaping the level of interest rates in the country;

- bank of banks - which means that it acts to ensure the stability of the entire state financial system, among other things, by regulating the liquidity of banks and has instruments to ensure the smooth functioning of the payment system;

- the bank of the state - within these functions, it usually maintains the accounts of the most important public institutions and conducts monetary settlements on these accounts, as well as manages the state's foreign exchange reserves.

All these functions show that the central bank is one of the key institutions in any country and has a very strong influence on its economy. The tasks of the central bank are often strongly interrelated and intertwine.

Stable value of money

The most important task of the central bank is to guard the stability of money. this means that the bank seeks to maintain a constant value of domestic money against other currencies (stable exchange rate). The effect of exchange rate stability is greater predictability of import and export prices. The central bank can stabilize the value of money by its purchasing power (purchase of a basket of goods). In the situation of exchange rate stabilization, we are dealing with external money stabilization, and in the case of price stabilization - with internal money stabilization. As for external money stabilization, the exchange rate is stabilized against the U.S. dollar or the euro, the currencies of the world's largest economies.

Inflation targeting strategy

Central banks, in carrying out their tasks, usually use an inflation targeting strategy. Such a strategy determines the level of inflation stabilization. It is usually very low. The main instrument that allows central banks to shape the strategy is the ability to change interest rates. Central banks take a great many factors into account when conducting monetary policy. But as a general rule, raising interest rates, or the cost of financing, makes it more expensive to borrow money, which in turn results in less spending in the economy. In contrast, lowering rates makes it cheaper to borrow money, so that spending in the economy increases, and this can result in a rise in inflation.

Ban on state financing

Despite what has already been emphasized that the central bank is the bubble of the state, it does not finance public sector spending. In many countries, the constitutions explicitly prohibit such action. This prohibition is primarily intended to curb the desire to increase public spending, which in turn could lead to higher inflation.

Conclusions

The existence of a central bank in a country, independent of the government, is a guarantor of effective monetary policy. The subordination of the state's monetary policy to current politics, could result in the unsettling of the state's finances and threaten monetary stability.

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