Abstract

This paper employs bivariate GARCH methodology to investigate the existence of tradeoff of relationship between output growth and inflation variability in Nigeria and to ascertain whether monetary policy regime change from direct control regime to indirect or market based regime affected the nature of the volatility tradeoff. The paper also investigates if changing the weight attached to each of the variables in a particular regime altered the magnitudes of monetary policy effects on output growth and inflation. The findings reveal the existence of short run tradeoff relationship between output growth and inflation in both regimes and across the two regimes. However, no strong evidence of long run volatility relationship could be established making it difficult to evaluate the long run impact of monetary policy on output and inflation volatility. The results further reveal that regime change affected the magnitude of policy effects on output and inflation. Thus, monetary policy had stronger effect on output growth than on price stability during the period of direct control regime when rapid and stable output growth was the primary objective of monetary policy. On the other hand, monetary policy has much larger impact on inflation during the current period of indirect control regime when the primary objective of monetary policy has tilted to price stability objective. Finally, our study reveals that volatility of output and inflation became more persistent during the period of indirect control regime compared to the direct control regime period.