

Towards more clarity in central bank communication

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Central banks and the Common Good
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**Views are my own and do not represent the position of the Banque de France or the Eurosystem.*

From secrecy to transparency

- ▶ In the late 1980s, the practice was **secrecy and opacity**:
 - ▶ The Fed did not communicate explicitly its target
 - ▶ Greenspan (Senate Committee, 1987):
"Since becoming a central banker, I have learned to mumble with great incoherence. If I seem unduly clear to you, you must have misunderstood what I said"
- ▶ Over the past 25 years, revolution towards **extensive communication**
 - ▶ CBs hold press conferences after each decisions (ECB since 1999, Fed quarterly since 2011/ each meeting since 2019)
 - ▶ They publish a monetary policy statement explaining their decisions, the state of the economy, and provide information about future policy (Fed since 1994, ECB 1999)
 - ▶ Some even publish minutes of their meetings with votes (Fed since 2005) or accounts (ECB since 2015) [▶▶ CB practices](#)

Why communication and transparency?

- ▶ Increase in **central bank independence** in the 1990s called for **accountability**, need to explain how actions serve objectives CBs are entrusted with
- ▶ CBs adopted **inflation target** (e.g., Bank of Canada, Reserve Bank of New Zealand earlier than ECB or Fed)
 - ▶ Policy framework giving a central role to the communication of their objectives and policy decisions to **manage expectations**
 - ▶ Households and firms decision depend on long-term rates, affected by expectations of future short-term rates
- ▶ Soaring inflations in the 1970s called for managing inflation expectations
- ▶ Introduction of unconventional monetary policy and communication as a primary tool, **forward guidance**

From an audience of financial markets to the general public

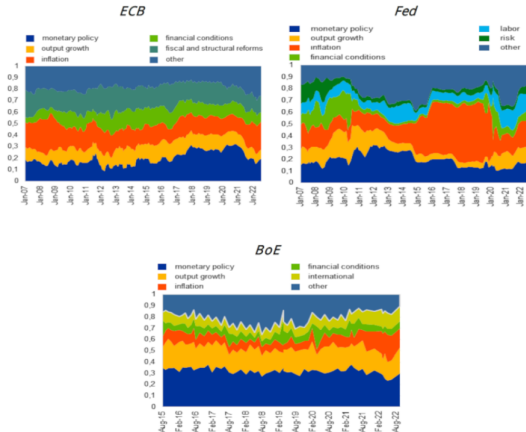
- ▶ CBs in the forelight with the GFC and Covid-19, increased complexity of unconventional monetary policy and controversy around these news tools
- ▶ Increased use of **social media, listening events**
- ▶ Some CBs supplement the publication of their policy statements with summaries and a simpler language: **multi-layered communication**
- ▶ Initiated by the BoE in 2017, and followed by the ECB after its 2021 strategy review, with the **idea of explaining also in simple terms why decisions are taken and what it means for their lives**

Multi-layered communication

Layers of complexity: example

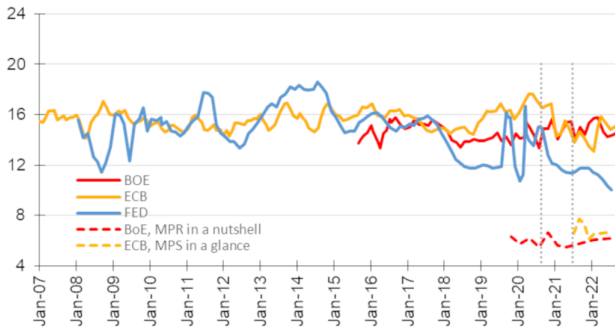
- ▶ Different layers targeting different audiences of the population
- ▶ Since November 2017, the BoE accompanies the policy decision each quarter by a Monetary Policy Report, in 3 layers:
 1. a first layer explaining interest rate decision in an abbreviated format with icons
 2. a second layer **“in a nutshell”**, a visual summary of the monetary policy report, brief analysis with the main factors behind the interest rate decision
 3. a third layer: the MPR, in-depth analysis with a technical language
- ▶ The ECB has 2 layers:
 1. Monetary policy statement **“at a glance”**
 2. Monetary policy statement

Topics in monetary policy statements



- ▶ Wide array of topics, but 4 common across central banks: inflation, output growth, monetary policy and financial conditions
- ▶ Topic of inflation picking up coinciding with **increase in policy rate, commitment to return to target**

Effective lower complexity



- ▶ According to the **Flesch-Kincaid readability measure**, MPSs require 15 years of education (20-21 years old)
- ▶ The “nutshell” and “at a glance” versions require around 8, hence 13-14 years old.
- ▶ MPS are lengthier

Clarity at all times?

Clarity and state-dependent communication

In presence of externalities, there are incentives to design communication strategically and **not to reveal fully certain states** (e.g., inefficient shock) to bias the private sector's actions upward

"I wasn't willing to use the r-word in public at that point, even though the risk of a downturn was clearly significant. [...] I didn't want to add **unnecessarily to the prevailing gloom** by talking down the economy."

— Bernanke, The Courage to Act (2015)

"It is not always and everywhere the case that greater openness and transparency is a good thing. **Had we been fully open and fully transparent** about what was going on during the financial crisis, it would, let me tell you, **have been a lot, lot worse.** "

—Haldane, FT (2017)

"And while the robust recovery is supporting underlying inflation trends, what we are seeing now is mostly a phase of **temporary inflation** linked to reopening"

— Lagarde 2021, ECB

State-contingent communication

In Herbert (2022), I formalize this idea of communication to a general audience, and derive 2 key features of state-dependent communication with an heterogeneous audience:

1. Some **opacity in both states** (e.g., recession, expansion) is optimal
 - ▶ Communication is going to play a moderating role: the CB never reveals the state with full precision, even the good state
 - ▶ With a homogeneous audience: the CB wants full transparency in the good state of the economy

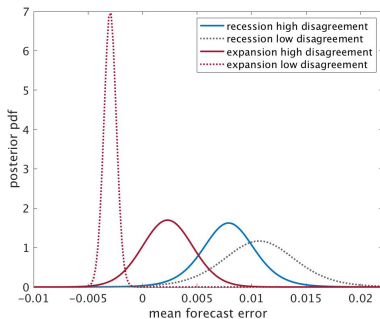
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2. **More beliefs disagreement** in the economy leads to **greater transparency**

▶▶ model

FOMC's unemployment rate forecast biases



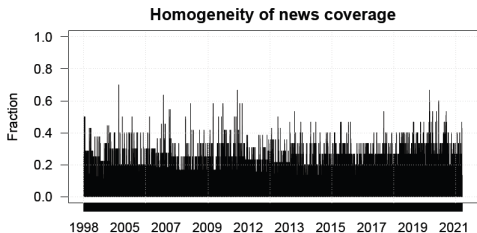
Notes: Sample 1979-2016. Bayesian estimates with Jeffrey's prior.
Sources: Monetary Policy Report, Survey of Professional Forecasters,
author's calculations.

1. FOMC forecast errors are systematically biased in opposite directions in recessions and expansions statement
2. Less bias during periods of high disagreement in each state
 - ▶ E.g.: Richmond Fed forecasts within TVP-VAR, VAR boundaries
 - ▶ Looking at the difference with SPF forecasts, no distinct behavior

Communication to non-experts and the media

Newscoverage about central banks

- ▶ Newspapers **focus on different topics** related to the Fed
- ▶ But at times, they vary their coverage and all agree on what's the most important topic → **homogeneity is high**
- ▶ The general public is more likely to read the same information, improved efficacy of monetary policy



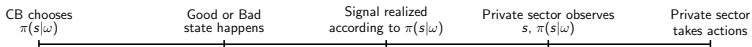
ANNEX

Central bank common practices

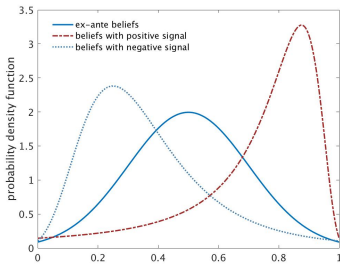
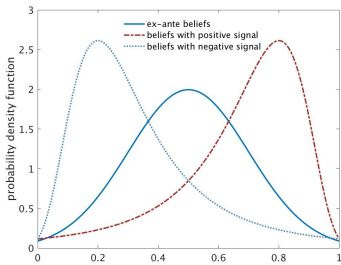
| | Meetings | Press Release | Minutes | Press Conference |
|-----------------|---|--|---|---|
| ECB | 8 per year since 2015 12 per year pre-2015 | Decision notice released at 13:45, less than 1h after the meeting Monetary Policy Statement released at the same time as the Press Conference | Published about 4 weeks after the Governing Council | Starts at 14:30, with the reading of the Monetary Policy Statement (former introductory Statement) |
| Fed | 8 per year | FOMC statement released at 14:00, about 3h after the meeting | Released 3 weeks after the date of the policy meeting | Starts at 14:30, at every meeting since January 2019 From 2011-2019: 4 times a year with the FOMC's quarterly economic projections |
| BoE | 8 per year since 2017 12 per year before | Monetary Policy Summary published at 12:00, less than 1h after the meeting Released since August 2015 Before 2015: short media release | Released at the same time as the Statement | Starts at 12:30 4 times a year following the publication of Monetary Policy Report (previously Inflation Report) |
| BoJ | 8 per year | Statement on Monetary Policy published a few minutes after each meeting | Published at 8:50 am according to a published schedule (usually 3 business days after the next meeting) | Starts at 3:30 |
| Riksbank | 5 meetings per year since 2020 (used to be 6) | Monetary Policy Report published at 9:30 am | Approximately 2 weeks after the meeting, at 9:30 (calendar is published) | Starts at 11:00 am |
| BOC | 8 per year | Decision notice released at 10:00 am | No dissemination | Starts at 11:00 am |
| RBA | 11 per year, 1 st Tuesday of each month except January | Released at 2:30 (prior to 2007 only when cash target was changed) | 2 weeks after the meeting First published in December 2007 | Occasionally |

State-contingent communication policy

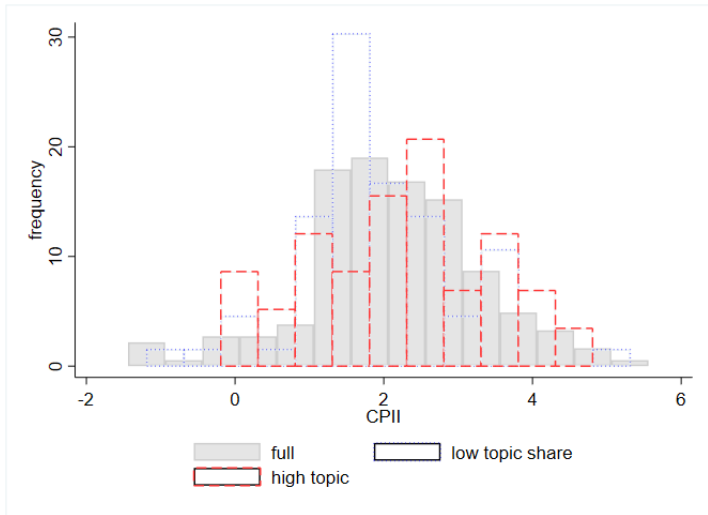
- ▶ The communication strategy about the two states ($\omega = \{0, 1\}$) is *public*: both communication policy and signal are observed



- ▶ CB may choose how often to say it's a good state when it's bad ($\pi(s = 1|\omega = 0)$) differently from how often to say it's bad when it's good ($\pi(s = 0|\omega = 1)$) (different opacity) to bias beliefs upwards [▶ back](#)



State-dependent topic composition of statements





New focus and homogeneity

Based on Nimark and Pitschner 2019, we build the following measures:

▶ News focus

$$d_{m,k} = \frac{p_{m,k} - p_k}{p_k}$$

- ▶ $p_{m,k}$: probability that newspaper m reports on topic k
- ▶ $p_k = \frac{1}{M} \sum_{m=1}^M p_{m,k}$: corresponding average across all M newspapers

▶ Homogeneity

$$H_t \equiv \frac{\sum_m \mathbb{1}(\operatorname{argmax}_k F_{t,m,k} = \operatorname{argmax}_k F_{t,k})}{M}$$

- ▶ $F_{t,m,k}$: fraction of news coverage devoted to topic k by newspaper m on date t
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