

Central Bank Communications

By

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Background

- 1) Central Bank's forecasts, e.g. of its own future interest rates [Goodhart and Lim, IJCB, 2011], or of unemployment, etc., are not good, (though no worse than others), outside the relatively short-term future. No crystal ball; no reason to believe such forecasts are better than, say, those of the market beyond a short horizon.

- 2) The form of a Central Bank's communication is considerably influenced by the structure and form of its decision-making process:-
 - Single Governor,
 - Small CB Management team,
 - Committee with externals.

Collegial vs Individualistic.

What can be communicated?

	Mean	Variance
Current Decision	Everyone	Minutes [Collegial vs Individualistic]
Reaction Function	Most	? [Hawk/dove analysis]
Interest Rate Path (Conditional)	NZ, Nordics [Problem for Committees]	FOMC [Dots]
Interest Rate Path (Pre-commitment)	Forward Guidance	? [Scenarios. UK?]

Forward Guidance

Contra: Forecasts unreliable [Reaction function changes].

So either,

- a) Take wrong policy, or
- B) Renege

Revealed preference is (b), so limited credibility.

Pro: Clarity and Reach of communication.

Conclusion

Despite weaknesses, will be done in foreseeable future.

Rationale: To limit upwards move in long rates as short rates re-normalise.

N.B. Will not have much effect on bets about date of first move, though communication of reaction function may have limited effect.