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Communication and transparency – The example of the ECB

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ABSTRACT

Communication by central banks has two goals to fulfill: One is to be accountable and transparent to the public for its policy. The other is to make monetary policy by guiding expectations as effective as possible. Diversity of views inside the bank is instrumental for appropriate monetary policy decisions, but creates a tremendous challenge for communication. Central banks dispose of a variety of communication tools. Forward guidance seen as a revolution in central banks' communication raises new questions. Not maximum, but optimal transparency should be the final stage to strive for.

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1. Introduction

Preliminary remark

I would like to thank the organizers for having invited me to this fascinating conference. I admire John Taylor for his outstanding research. But, on top of that I will remain grateful that he accepted my invitation and came to Frankfurt to the ECB before the start of the euro to discuss problems of monetary policy for a new currency, the euro.

Andy Levin has presented a stimulating paper. The key message is that the monetary policy strategy and communication should be a joint design. I could not agree more. The challenge is to reconcile two time dimensions of steering expectations. One is short-term indications about policy intentions in the next meeting(s) of the policy-making body. The other is to make the sequence of individual decisions consistent over time with the strategy and the mandate of the central bank. If this challenge is met, monetary policy is predictable in the short-term and credible in the longer-term.

Communication has two goals to fulfill. One is the obligation to be accountable to the public for its policy. In this sense, accountability is the counterpart of independence of the central bank. The other goal is to make monetary policy as effective as possible. Monetary policy can only fix the central bank interest rate(s) thereby controlling the very short end of the interest rate spectrum. The influence of the central bank on the long end depends on market expectations regarding future central bank decisions (and their impact on inflation etc.). Woodford (2005) goes so far to say that very little else other than expectations matters.

Whereas for a long time central banking was surrounded by a “peculiar and protective political mystique” and presented as an “esoteric art” (Brunner, 1981), transparency has become a kind of mantra for central banks.

Following Andy's presentation I will discuss a few issues of the complex subject “communication and transparency”.

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2. Diversity of views

There is a vast literature concluding that committees are superior to a “one person” statute to assess the situation properly and take the appropriate monetary policy decisions. This result is based on the reasoning that a diversity of views is conducive to cover different aspects and weighing them against each other before taking decisions. “Competition” of views within the central bank among staff and board members is requested to achieve the best policy (Svensson, 2013). As member of the Executive Board of the ECB in charge of economics and research I regularly organized informal discussions especially with academic critics of our strategy and policy as a fundamental element in this process.

However, diversity causes a tremendous problem for communication. Should the central bank make all the different views transparent? Should all members of the decision making body present their views to the public? Would this not end in a cacophony, a disaster for communication undermining the credibility of the central bank?

At the ECB on monetary policy decisions we followed the consensus principle (Issing, 2008). This was often misunderstood as a procedure by which the decision was delayed until the last member agreed. The reality was very different. Consensus must not be misunderstood as unanimity. Consensus as it was practiced by the Governing Council means no more and no less than that at the end of an extensive discussion in which every member could express his or her view and policy preferences, the president could announce the decision. Consensus also means that one or more members who at the time might have preferred a different decision are able to live with the consensus that is, acknowledge the power of the argument in favor of the decision. This is essential when it comes to communication and general support of the decision. In a multi-national environment as the euro area it is crucial that the ECB's decision is explained and defended by all members of the council “at home” to avoid any suspicion of national bias. It is obvious that this is easier achieved when nobody is regarded as being “defeated” in a voting. Insofar the consensus principle could be seen as a means to reconcile internal diversity of views with the need to communicate monetary policy decisions in a clear and convincing manner.

Diversity is not only an issue inside the central bank but also on the side of the receivers of the central bank's communication. Here, the central bank has to deal with a diverse world of audiences (Issing, 2005). Academics mistakenly often see the monetary policy process as a kind of seminar and expect corresponding research based communication. Beyond this specific group there exists a complex world reaching from bank economists to journalists and the general public. Experience has shown how difficult it is to communicate all information relevant to the decision making process in a way that is not only exhaustive but also clear and comprehensible. Psychological research has pointed to the limits of human information processing skills (Kahneman, 2003). This research has shown, e.g. that the weighing of information greatly depends on its intuitive accessibility. Furthermore it is generally simplified and categorized before it is collated. Altogether this implies a huge challenge for central bank communication. A too sophisticated approach could easily create confusion rather than providing clarity.

3. Communication tools

For us in the ECB, the youngest central bank in the world, responsible for the stability of the euro, a totally new currency for a large group of countries, it was obvious that good communication was an indispensable condition for success. Already in October 1998, less than 3 months before the start of monetary union, we informed the public about our monetary policy strategy and explained that maintaining price stability as our mandate we would keep the inflation rate below two percent over the medium-term. (At an early stage we also published a book with detailed background research, see Issing et al. (2001)).

From the start of the euro in January 1999 the ECB used a broad spectrum of communication tools: The press conference of the president and vice president after every monetary policy decision meeting beginning with an Introductory Statement followed by questions and answers; a week or so later the Monthly Bulletin provided encompassing information on the economic and financial background for the decision taken.

After a period of gaining experience the ECB decided to publish the projections of the staff four times a year. In the remaining eight editions of the Monthly Bulletin (mostly) two articles are devoted to research on key aspects of monetary policy and the economy in general. A number of special reports as e.g. the Financial Stability Review are also published regularly. The research oriented Working Paper series in quality and numbers have soon become a tremendous success. Occasional Papers present analysis on relevant topics.

The members of the Executive Board and the governors of the national central banks give speeches all over the place. The accountability towards the European Parliament is mainly the task of the president.

The ECB has also established a special relation with academia, bank economists and the media. Three watchers groups were formed even before European Monetary Union started. In 1999 as a reaction to critical reports the ECB started a conference in cooperation with the Center for Financial Studies at Frankfurt Goethe University and with all watchers involved. This conference since has taken place every year and the list of participants reads like a roll call of eminent names from academia, banking and the media. The interaction with leading representatives of the ECB has developed as a special communication tool involving directly the main “multipliers” on issues of central banking. The conference has contributed to a better understanding of the ECB's policy and at the same time has also stimulated research.

It is difficult to measure the effectiveness of communication. In guiding inflation expectations, probably the most important challenge – the ECB does not stand behind other major central banks. Despite of this anything but self-evident

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