IMPROVING U.S. MONETARY POLICY COMMUNICATIONS

June 4, 2019

Stephen G. Cecchetti and Kermit L. Schoenholtz
FOMC Communications

• Enormous progress since 1993
  • Transparency fosters accountability and enhances credibility
  • Level and uncertainty of inflation declined markedly

• Communications reinforce commitment to mandate
  • Price stability
  • Maximum sustainable employment
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• Communications reinforce commitment to mandate
  • Price stability
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Can we find further improvements?
Improving Communications

• Interviews

• Objectives
  • Link key communications to annual statement on goals
  • Simplify public statements (while conveying divergences of view)
  • Clarify how policy will react to changing conditions
  • Highlight policy uncertainty and risks
Improving Communications

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Our Analysis

• Interviews
• What we learn from the SEP
• Recommendations
Interviews

• Three open-ended questions
  1. What do you see as the primary objectives of FOMC communication?
  2. How do you think FOMC communication should evolve over the next five to ten years?
  3. What do you view as the greatest challenges to effective FOMC communication?

• 24 respondents in writing and oral interviews
• Policy reaction function
• Uncertainty and risks
• Dot plot/matrix
• Transparency as a tool
• Communicating w/ public in plain English
The Survey of Economic Projections (SEP)

• Information in the median
• Incremental value of the matrix
• Unavoidable policy uncertainty
The Median Projections

• Assume representative policymaker
• Interpret simple reaction function
• Estimate annual equilibrium real rate
SEP Median Implied Equilibrium Real Rates

Long run $r^*$ falls:
+2.15% to +0.90%

Short run $r^*$ rises:
–0.31% to +0.44%
The Matrix

• Infer individual reaction functions
  • Meeting by meeting, unless there are names
  • Without names, people will infer identities

• Assess stability of the median

• Foster systematic policy and enhance deliberations
Uncertainty and risks

• Historical projection error ranges
• Published in the full SEP (with a lag)
• Severely underutilized
## March 2019 Survey of Economic Projections for 2021

<table>
<thead>
<tr>
<th></th>
<th>Median Projection (%)</th>
<th>70 percent range (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Inflation</strong></td>
<td>2.0</td>
<td>0.9 to 3.1</td>
</tr>
<tr>
<td><strong>Growth</strong></td>
<td>1.8</td>
<td>−0.1 to 3.7</td>
</tr>
<tr>
<td><strong>Unemployment</strong></td>
<td>3.9</td>
<td>2.2 to 5.7</td>
</tr>
<tr>
<td><strong>Federal Funds Rate</strong></td>
<td>2.6</td>
<td>0.1 to 5.1</td>
</tr>
</tbody>
</table>

Federal Funds Rate Projection Fan Chart
(with 70% confidence, March 2019 SEP)

Median projection and confidence interval based on historical forecast errors

Federal funds rate
- Midpoint of target range
- Median of projections
- 70% confidence interval*

Recommendations

- Focus on objectives to improve communications
  - Link all key communications to annual statement on goals
  - Simplify public statements (while conveying divergences of view)
  - Clarify how policy will react to changing conditions
  - Highlight policy uncertainty and risks
Recommendations

• Focus on objectives to improve communications
  • Link all key communications to annual statement on goals
  • Simplify public statements (while conveying divergences of view)
  • Clarify how policy will react to changing conditions
  • Highlight policy uncertainty and risks

• Two Examples
  • Post-Meeting Statement
  • Concise Inflation Report
  (Other possibilities include the minutes)
Recommendations

• Post-Meeting Statement
  • Elements
    • Statement of the decision, including votes
    • Rationale for the decision, including the reason for dissents
    • Discussion of uncertainties and risks
  • Principles
    • Readable by a high-school senior
    • Link to the Statement on Longer-run Goals and Monetary Policy Strategy
    • Foster group accountability (use first-person plural pronouns)
## A Simpler Post-Meeting Statement

<table>
<thead>
<tr>
<th>Date</th>
<th>Number of Words</th>
<th>Flesch-Kincaid Grade Level</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Original</td>
<td>Alternative</td>
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<tr>
<td>Dec 2017</td>
<td>427</td>
<td>270</td>
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<tr>
<td></td>
<td>16.3</td>
<td>12.5</td>
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<tr>
<td>Mar 2019</td>
<td>303</td>
<td>300</td>
</tr>
<tr>
<td></td>
<td>16.4</td>
<td>10.7</td>
</tr>
</tbody>
</table>
Recommendations

- Post-Meeting Statement
- Concise Inflation Report
  - Elements
    - Fan charts for inflation, growth, unemployment and the interest rate
    - Short narrative describing modal outcome, uncertainty and risks
    - Data appendix: medians, dot plot, error ranges, and matrix
  - Principles
    - Readable by a high-school senior
    - Link to the Statement on Longer-run Goals and Monetary Policy Strategy
    - Foster group accountability (use first-person plural pronouns)
Recommendations

• Post-Meeting Statement
• Concise Inflation Report
• Benefits
  • Emphasizes link to longer-run goals
  • Broadens public access
  • Shifts focus to uncertainties and risks
  • Coordinates external communication
  • Improves quality of internal debate
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