Summary of Audience Q&A
Session #4: Federal Reserve Communications

Date: June 4, 2019

Moderator: Hyun Song Shin (Bank for International Settlements)

Presenters: Stephen Cecchetti (Brandeis International Business School) and Kermit Schoenholtz (NYU Stern School of Business)

Discussant: Jón Steinsson (University of California, Berkeley)

Summary Prepared by: Ellen E. Meade, Special Adviser to the Vice Chair and Senior Adviser in the Division of Monetary Affairs, Board of Governors of the Federal Reserve System

Following the presentation of "Improving U.S. Monetary Policy Communications" by Stephen Cecchetti and Kermit Schoenholtz, and discussion by Jón Steinsson, the authors responded to the points raised by their discussant.

Professor Schoenholtz followed up regarding the distinction between communications about the economic outlook and communications about the future path of policy. He noted that if the FOMC's reaction function is understood by the public, then news about the economy will be appropriately interpreted in the context of the reaction function. However, if the policy interest rate is at its effective lower bound (ELB), then the FOMC would likely want to communicate about the future path of the policy rate—that is, use forward guidance. In normal times, with policy rates above the ELB, if the Committee's reaction function is clearly understood, then the public will be able to interpret what incoming information implies for monetary policy.

With regard to the Summary of Economic Projections (SEP) and releasing the individual names associated with each projection, Professor Schoenholtz cited research pointing to the advantages associated with greater transparency in central bank communications.

Finally, he agreed with Professor Steinsson that it is difficult for the FOMC to commit to a reaction function and noted that, given changes in the economy, appointments of policymakers, and rotating membership of the FOMC, it would be hard to make a commitment that lasted longer than a few years. In this context, Professor Schoenholtz noted that reaffirmation of the Committee's Statement on Longer-Run Goals and Monetary Policy Strategy every January is helpful because it links the changing members of the FOMC together and would permit the communication of a change in the reaction function, if warranted.

The moderator then turned to the audience for comments and questions. Stan Fischer (BlackRock) commented about policymakers' reluctance to add fan charts to the SEP because they pointed to considerable uncertainty about the economic outlook. With regard to the authors' suggestion to release a matrix linking the economic projections in the SEP by individual, Mr.

Fischer noted that to make this information most useful it would be necessary to know the forecasts that had been submitted by voting members of the FOMC.

Donald Kohn (Brookings Institution) indicated his general agreement with the authors' recommendations for Fed communications: make better use of the Statement on Longer-Run Goals and Monetary Policy Strategy; simplify the FOMC postmeeting statement; highlight the rationale for policy and uncertainty/risks to the economy; reduce the cacophony of views coming from FOMC participants. Mr. Kohn saw a tension between the simplication of the statement and the highlighting of the rationale and uncertainty/risks. He disagreed with the authors about the merits of publishing the matrix of SEP projections because it would focus attention on the differences across individual policymakers.

Larry Meyer (Monetary Policy Analytics) asked whether the FOMC speaks to the financial markets or the broader public. He noted that he agreed with the authors' suggestion to publish the SEP matrix but that he would not identify policymakers by name. He also noted that he doesn't find the fan charts useful and doesn't need them to understand how much uncertainty there is. Instead, he would prefer a reminder in the SEP that forecasts are subject to considerable uncertainty and are almost never correct. Finally, Mr. Meyer noted that the Chair should use the SEP projections to a greater extent in his press conferences to explain the rationale for the FOMC's policy decisions.

Ben Friedman (Harvard University) observed that the paper accurately conveyed the importance of language and words. For that reason, he hoped the FOMC didn't follow the authors' recommendation to create an "Inflation Report" because such a name could convey to the Congress and general public that the FOMC doesn't take the dual mandate seriously and that maximum employment is not important.

In response to these comments and questions, Professor Cecchetti said it was important for the FOMC to convey uncertainty in a way that was productive; he saw the fan charts as helpful in doing that. He also noted that the FOMC should communicate to the public that it will adjust policy quickly as warranted in response to incoming information. With regard to the SEP, he noted that the medians of a variable over time and across variables are not generated by a single policymaker's projection, and agreed with Mr. Kohn that publishing the matrix would provoke an effort to identify each policymaker's interest rate path.

Professor Schoenholtz commented that the FOMC should speak broadly to financial markets, the Congress, and the public, which was the reason for recommending a simplification of the language in the FOMC's postmeeting statement. Professor Cecchetti added that the *Fed Listens* effort was a two-way communication with the general public and the official policy statements should be as well.

Alan Blinder (Princeton University) pointed out that the Fed has to communicate to at least three audiences: experts in the financial markets and press; the Congress; the broader public. He remarked that it would be impossible to communicate to those three audiences using an identical communication vehicle. In particular, he noted that the FOMC's postmeeting statement is for experts, who understand Fed policy and know what to look for; therefore, writing the statement at the level of a ninth grader was unnecessary. Professor Blinder saw communicating with the general public—for example, Chairman Bernanke's appearance on 60 Minutes in 2009—to be very different and very challenging. He observed that when he came to the Fed in 1994 as a policymaker, he was told that most Americans think the Federal Reserve is a national forest. If it were his task to revise the FOMC statement, he would include information on the nature of the debate; the arguments made; which side won, which side lost and why.

Brian Sack (D.E. Shaw) noted that a makeup strategy would be very challenging to communicate. Such a strategy, to be successful, would require that in response to disappointing news about inflation, the public would revise up its expectations of inflation 3-7 years hence. Because expectations don't usually behave that way, the Fed would have a big job to communicate such a strategy to the public. He asked whether there was any reason to be optimistic that makeup strategies would work?

Roberto Perli (Cornerstone Macro) disagreed with Professor Cecchetti's assertion that the Fed should not be too concerned about surprising financial markets. Mr. Perli commented that monetary policy is most effective if financial markets understand policy. He observed that the Fed's current policy framework is working fairly well except at turning points in the business cycle. He was therefore not surprised that the most frequently mentioned item in the survey that Professors Cecchetti and Schoenholtz conducted was understanding the Fed's reaction function, although he was surprised that scenario analysis did not receive more attention.

William Dudley (Princeton University) asked how the FOMC's postmeeting statement should evolve from meeting to meeting—should there be a high threshold for change or a low threshold for change? A high threshold would be associated with little change and the statement could become stale; a low threshold would be associated with greater change. He asked the authors: What regime is the Fed in now? What regime should it be in? If the Fed is in the wrong regime, how can it move to the right one?

Tobias Adrian (International Monetary Fund) observed that the fan charts that display uncertainty around the SEP projections do not change materially over time. He asked whether there was a better way to communicate about uncertainty and risks to the outlook?

Yuriy Gorodnichenko (University of California, Berkeley) echoed Professor Blinder's comments about the challenges of communicating with the general public. He asked, who is the Fed's audience? Whose expectations is the Fed trying to influence? He noted that forward guidance and other policy tools worked by influencing the expectations of consumers and pricesetters in the economy but that the Fed focuses its communications on the financial markets, which are only a small part of the economy.

Peter Hooper (Deutsche Bank) asked the authors to what extent the recommendations in their paper reflected the views of the people who were surveyed as opposed to their own.

Lewis Alexander (Nomura Securities International) agreed with Tobias Adrian that the fan charts did not provide much information from meeting to meeting, and indicated he would prefer to have the SEP include policymakers' subjective views about uncertainty and risks.

James Bullard (President, Federal Reserve Bank of St. Louis) observed that the paper didn't get at a central issue, which is that the FOMC's postmeeting statement reflects the consensus of the Committee whereas the SEP dot plot is the views of individual policymakers about appropriate policy. The statement and SEP are released at the same time but can send different messages. He asked, would it be better to have the FOMC agree on the dot plot? At present, the dots are interpreted as a forecast of what the Committee will do when the dots reflect what participants think the Committee should do. He cautioned against simplifying the FOMC statement and relying on the Chair to explain in the press conferences.

Professor Cecchetti agreed with Professor Blinder that there were three main audiences for Fed communications, indicating he was uncertain about their sophistication and saw simple language as a good disciplining device. In answer to Mr. Sack, Professor Cecchetti noted that if the FOMC adopted a makeup strategy then it would necessitate a revision to the Statement on Longer-Run Goals and Monetary Policy Strategy. He agreed with Professor Gorodnichenko that the Fed is broadly accountable and its audience has to be everyone. He also commented that with regard to financial markets, what is important is the longer run response to Fed communications, not the immediate response over a short window of time.

Professor Schoenholtz pointed Mr. Hooper to a figure in the paper summarizing topics that survey respondents highlighted, and noted that the paper's recommendation about the dot plot did not reflect the survey responses. On the issue of uncertainty and risks, he pointed to the histograms of uncertainty and risks in the SEP as displaying subjective assessments.

Professor Steinsson disagreed with those who said that the FOMC should communicate with the general public. He commented that if experts in the financial markets are confused about Fed policy and monetary policy is transmitted to the economy through the bond markets, then the FOMC should focus its efforts on better communications with that audience.