Challenges and Opportunities for Central Bank Communications

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Explaining monetary policy with simple rules

"Let's begin using simple monetary policy rules as benchmarks to explain our policy decisions."

(Loretta Mester, The Federal Reserve and Monetary Policy Communications. Rutgers University, Jan. 18, 2018.)



An illustration: Two simple rules from the Fed's Tealbook

• Level rule: Classic Taylor rule $i = r^* + \pi + \theta(\pi - \pi^*) + \theta y$

• Difference rule: Natural Growth Targeting $\Delta i = \theta(n - n^*)$

- π : Inflation
- y : Output gap
- *n* : Nominal income growth
- Variants of alternatives, based on Fed staff projections with θ = 0.5, presented in Bluebook/Tealbook starting with January 2004 FOMC meeting. To date, real-time prescriptions have been disclosed to the public until end-2018.



Two simple rules from the Fed's Tealbook: 2004–2018



Fed funds target (or midpoint of target range). Rule prescriptions constrained by ZLB. Post-2018 Tealbooks not yet available to the public.

Natural growth rule: Tealbook and SPF-based variants



SPF variant for each quarter t based on SPF median projection of year-over-year nominal GDP growth ending in t + 3.

Avoiding the forward guidance trap



1-year ex-ante real interest rate reflects the 1-year OIS rate minus the 1-year inflation swap rate.