Monetary Policy & Central Banking

Central Bank Communication

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Today, there are 3 questions:

1. Why do central banks communicate?
2. How do central banks communicate their policy decisions?
3. How do central banks communicate the economic outlook?

1. Why do Central Banks communicate?

- Why is communication part of monetary policy rather than simply public relations?

Two reasons to communicate

- 1. Accountability
  - Central banks have been delegated considerable authority over monetary policy.
- 2. Policy effectiveness
  - Monetary policy depends partly on expectations about the future.

- These are distinct reasons for communication:
  - One is about **legitimacy**, the other about **how monetary policy works**.

Communication and accountability

- We already discussed:
  - Elected authorities set monetary-policy objectives.
  - Central Banks are made independent to achieve them.
- How can the public judge if the central bank is doing a good job?
- Communication allows the central bank to explain:
  - What did we decide?
  - Why did we decide it?
  - How does the decision relate to our mandate?
  - How do we assess the economic outlook and risks?
- Independence and transparency act as complements.

Monetary policy works through expectations

- Today's policy rate is not the only thing that matters
- A household considering a mortgage, a firm considering a five-year investment project, or an investor pricing a bond all care about future conditions.
- Expectations about future interest rates, future inflation and future economic conditions affect decisions today.
- Central Bank communication can impact these expectations.

Communication can affect monetary conditions today

- Longer-term interest rates depend partly on expectations of future short-term interest rates:

$$i_t^{(n)} \approx \frac{1}{n}\sum_{j=0}^{n-1} E_t\left(i_{t+j}\right) + TP_t^{(n)}$$

- Where $TP_t^{(n)}$ is the term premium (the extra return investors require for holding a longer-term bond rather than repeatedly investing in short-term bonds.)
- Central-bank communication → expectations of future policy rates → longer-term interest rates today → spending and investment

Phillips Curve

- From Phillips (1958).
- What is the relationship between (wage) inflation and unemployment?
- Can a central bank exploit this relationship to keep unemployment low (or output high)?

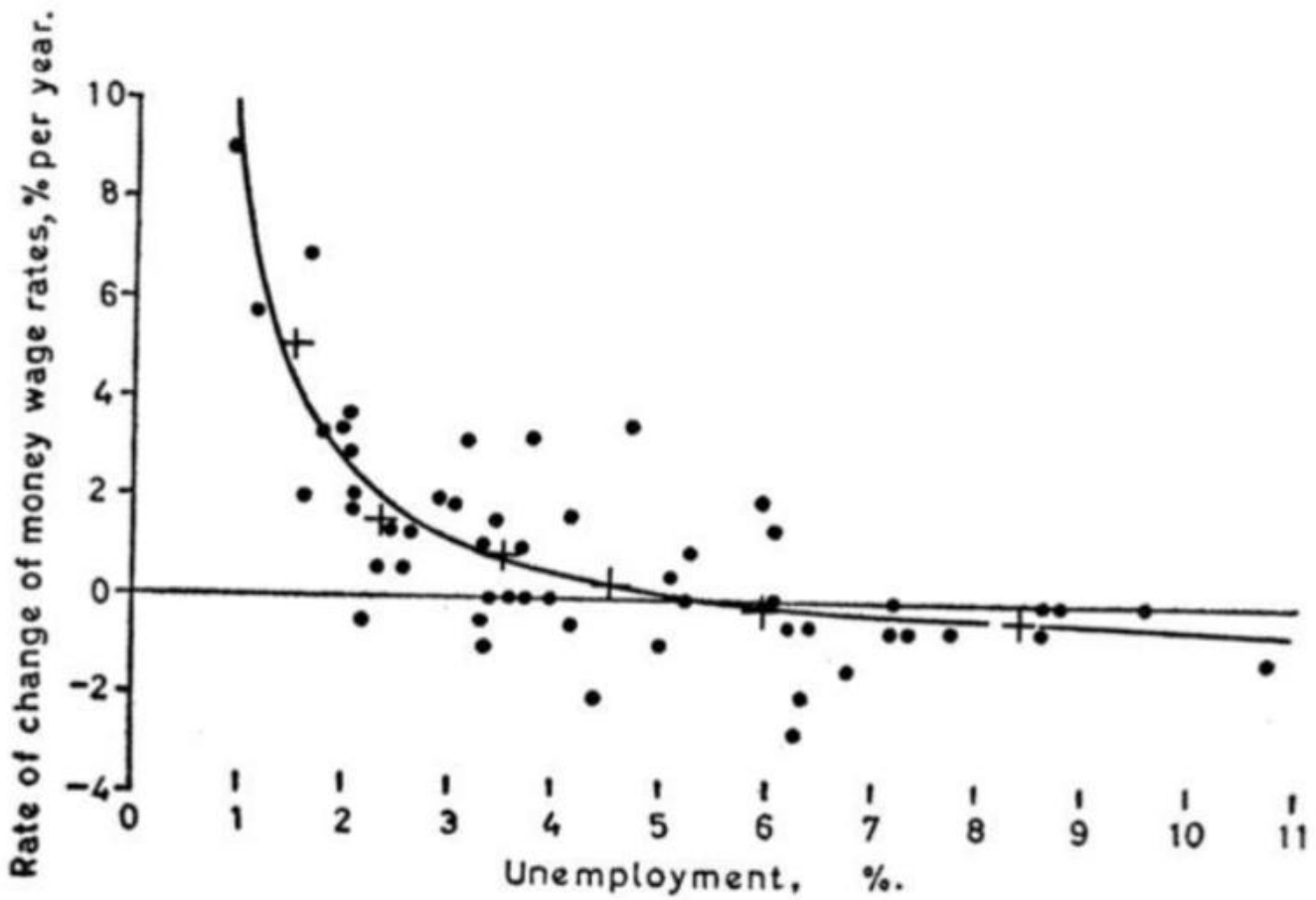


Fig.1. 1861 – 1913

Expectations-augmented Phillips curve

- Expectations-augmented Phillips curve:

$$\pi_t = \pi_t^e + \alpha(y_t - y^n)$$

- Where π_t is inflation, π_t^e is expected inflation, y_t is output, and y^* is potential output.
- Rearranging:

$$y_t - y^* = \frac{\pi_t - \pi_t^e}{\alpha}$$

- What does this imply?
- $\pi_t > \pi_t^e \Rightarrow y_t > y^*$
- $\pi_t = \pi_t^e \Rightarrow y_t = y^*$
- $\pi_t < \pi_t^e \Rightarrow y_t < y^*$

- It is unexpected inflation, not just higher inflation, that can temporarily increase output.
- Once inflation expectations are set, a Central Bank has the incentive to create unexpected inflation
- Kydland and Prescott (1977) time consistency problem

Kydland and Prescott and time-inconsistency

- Once inflation expectations are set, a Central Bank has the incentive to create unexpected inflation
- But monetary policy is a repeated game:
  - Households and firms come to anticipate the Central Bank's incentive
  - They revise their inflation expectations upwards
  - The central bank can no longer generate a systematic inflation surprise.
- Inflation bias: output returns to potential, but inflation remains higher:
- $\pi_t = \pi_t^e > 0, \qquad y_t = y_t^*$
- Key point: Without a credible commitment, discretionary monetary policy can produce higher inflation without a lasting increase in output.

Communication only works if it is credible

- A central bank can affect current financial conditions and macroeconommic outcomes through what it says (expectations), as well as through what it does with today's policy rate.
- But a central bank cannot determine expectations simply by announcing what it wants people to believe.
- For communication to influence expectations, people must believe that the central bank:
  1. Intends to act consistently with what it says.
  2. Is able to do so.

2. How do central banks communicate their policy decisions?

- What channels of communication do central banks use?

What do Central banks communicate?

- Central banks communicate different kinds of information:
  - What have we decided, and why?
  - How do we expect the economy to evolve?
  - What might this mean for future policy?

- How certain are we? Do policymakers agree?

Communicating the policy decision

- The policy announcement tells us what the central bank has done, but the statement also begins to explain why.
- When a central bank announces its decision, markets and the public want to know:
  - What has it decided?
  - Why has it made that decision?
  - What does it think is happening to the economy?
  - What might affect future decisions?

Example: Bank of England

Monetary Policy Summary, November 2026

At its meeting ending on 4 November 2026, the Monetary Policy Committee (MPC) voted by a majority of 8–1 to increase Bank Rate by 0.25 percentage points, to 4%. One member voted to increase Bank Rate by 0.5 percentage points, to 4.25%.

The conflict in the Middle East is now in its ninth month. Global energy prices have continued to rise from an already elevated level. UK CPI inflation increased to 3.5% in September. It is now expected to rise to around 5% by the middle of next year. It is then projected to fall as the impact of rising energy prices on 12-month inflation rates fades, and still restrictive monetary policy bears down on inflation.

While the direct effects of higher energy prices are clear, and will continue to feed into firm and household energy bills, there remains limited evidence of knock-on effects on other prices and wages. However, the degree of inflationary pressure in the pipeline is now sufficient to warrant an increase in Bank Rate. Activity data in recent months have generally been stronger than expected, adding to the case for modestly tighter monetary policy.

Monetary policy is not on a pre-set path. The Committee will continue to assess the evidence at each meeting, in particular how likely high energy prices are to feed through to other prices and the economy more broadly, by monitoring the evolution of underlying pay, pricing behaviour, and slack. The Committee will adjust Bank Rate as necessary to ensure CPI inflation returns to the 2% target in the medium term.

Interest rates and Bank Rate: our latest decision | Bank of England – the UK's central bank

Why have a press conference?

- If the central bank has already published a statement, why hold a press conference?
- A written statement is controlled and concise.
  - But that means there will be things it doesn't fully explain.
- The press conference allows the central bank to elaborate on the reasoning, etc
  - And it allows journalists ask questions to clarify it.

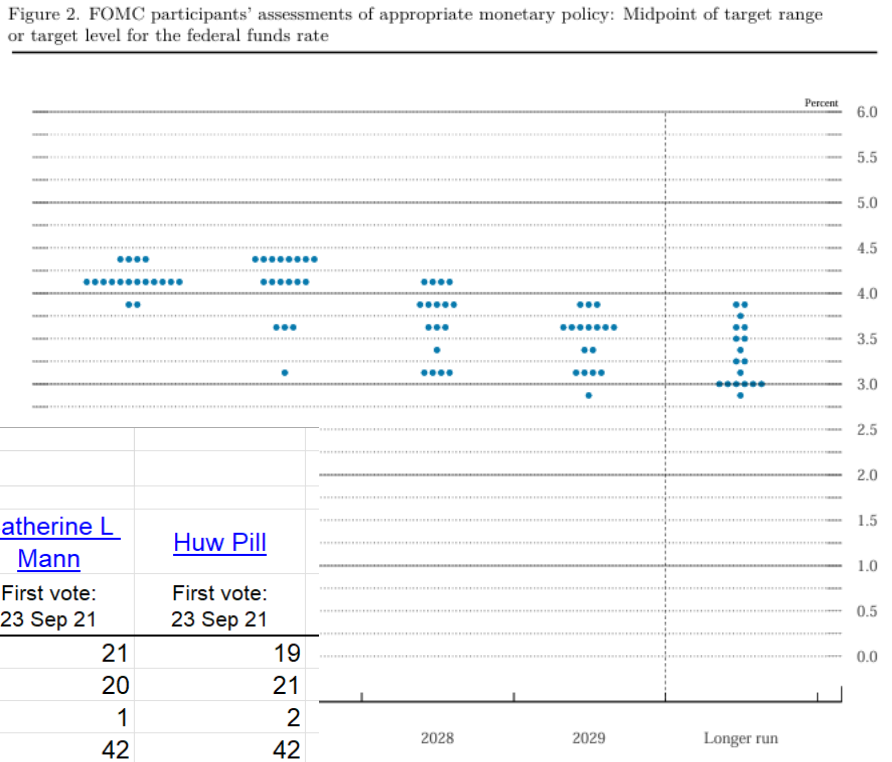
- See the latest Bank of England press conference here: Press conferences | Bank of England – the UK's central bank

Minutes and votes: revealing the deliberation

- Does the policy decision tell us whether policymakers agreed?
- Minutes/accounts can reveal:
  - Arguments considered in reaching the decision
  - Alternative views within the committee
  - How finely balanced the decision was
  - The considerations that might change the decision later
- When individual votes are published, the voting record gives a particularly clear indication of disagreement.
  - Does a 5-4 decision communicate something different from a 9-0 decision, even if the policy decision itself is identical?

Disagreement: Minutes, accounts, dot plots, voting record

- Federal Reserve publishes “dot plots”.
- ECB publishes “Accounts” which are anonymised.
- Bank of England publishes voting record.



		Monetary Policy Committee voting history - Bank Rate						
	Current members	Andrew Bailey First vote: 19 Mar 20	Sarah Breeden First vote: 2 Nov 23	Swati Dhingra First vote: 22 Sep 22	Megan Greene First vote: 3 Aug 23	Clare Lombardelli First vote: 1 Aug 24	Catherine L Mann First vote: 23 Sep 21	Huw Pill First vote: 23 Sep 21
Voted to increase		15	1	3	8	1	21	19
Voted to maintain		33	16	14	16	14	20	21
Voted to reduce		7	8	17	3	4	1	2
Meetings		55	25	34	27	19	42	42
	Bank Rate							
18 June 2026	**3.75%**	3.75%	3.75%	3.75%	4.00%	3.75%	3.75%	4.00%
30 July 2026	**3.75%**	3.75%	3.75%	3.75%	4.00%	3.75%	4.00%	4.00%
17 September 2026	**3.75%**	3.75%	3.75%	3.75%	4.00%	3.75%	4.00%	4.00%
05 November 2026	**4.00%**	4.00%	4.00%	4.00%	4.00%	4.00%	4.25%	4.00%

Explaining the decision requires explaining the outlook

- Monetary policy is forward-looking: so the economic outlook affects the policy decision.
- Therefore, explaining the policy decision requires explaining the outlook.
- Central banks therefore communicate forecasts/projections for inflation, growth, etc.
- But a forecast is an assessment of an uncertain future - not a statement of what will happen.

Why is the outlook uncertain

1. Uncertainty about the current state of the economy

- Data are published with lags, can be revised, and some important concepts are not directly (e.g., output gaps).

2. Uncertainty about future shocks

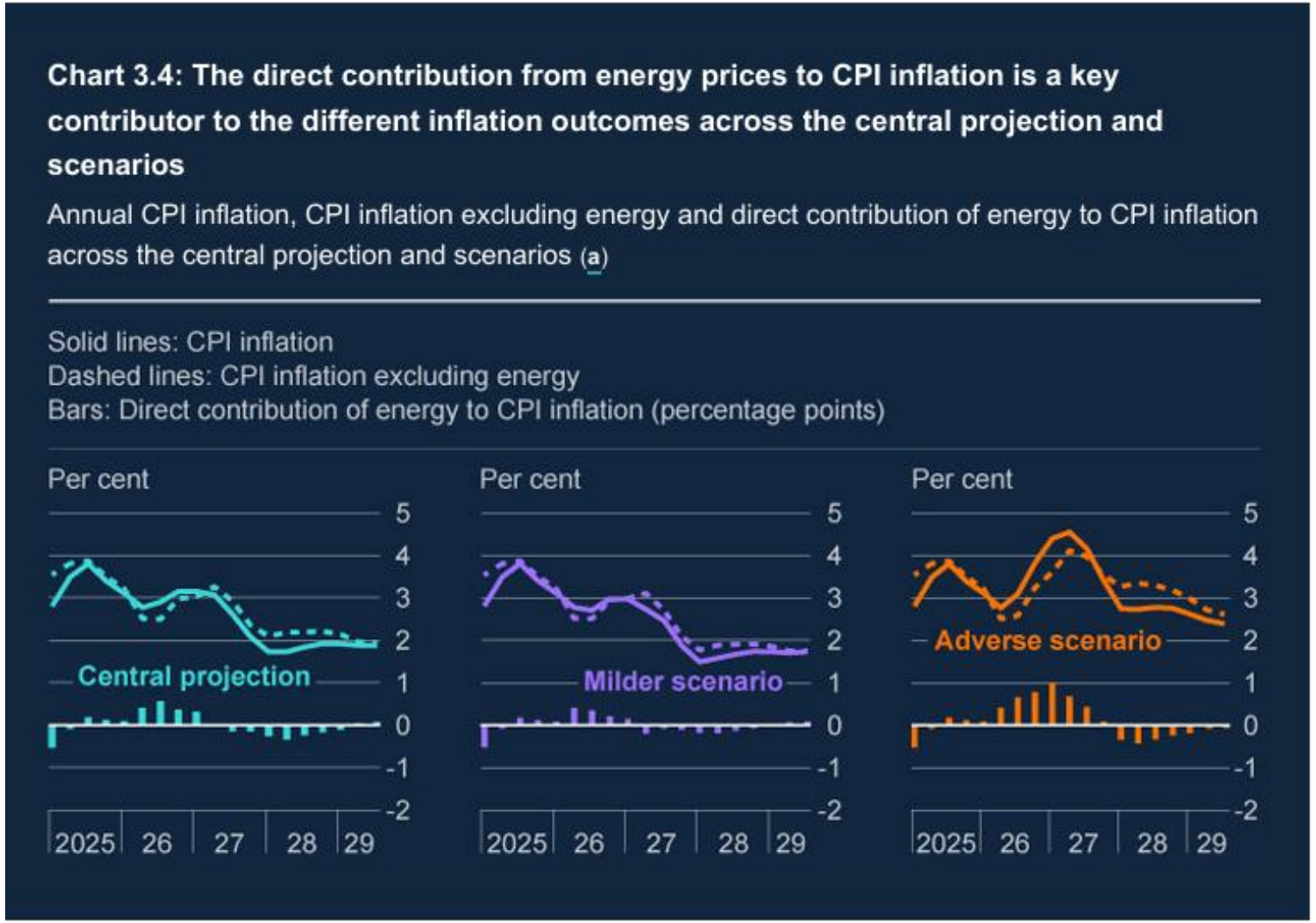
- The central bank cannot know what will happen to energy prices, global demand, financial markets, geopolitics, etc.

3. Uncertainty about how the economy works

- There is uncertainty about the strength and timing of relationships within the economy.

How can central banks explain uncertainty?

- Monetary Policy Report - July 2026 | Bank of England – the UK's central bank



Communicating uncertainty is difficult

- There is a tension between: Clarity vs false precision.
- A precise statement can be easy to understand but convey too much confidence.
- **A detailed representation of uncertainty can be more accurate but harder to understand.**

3. Who do central banks communicate with?

- Who should a Central Bank communicate with?

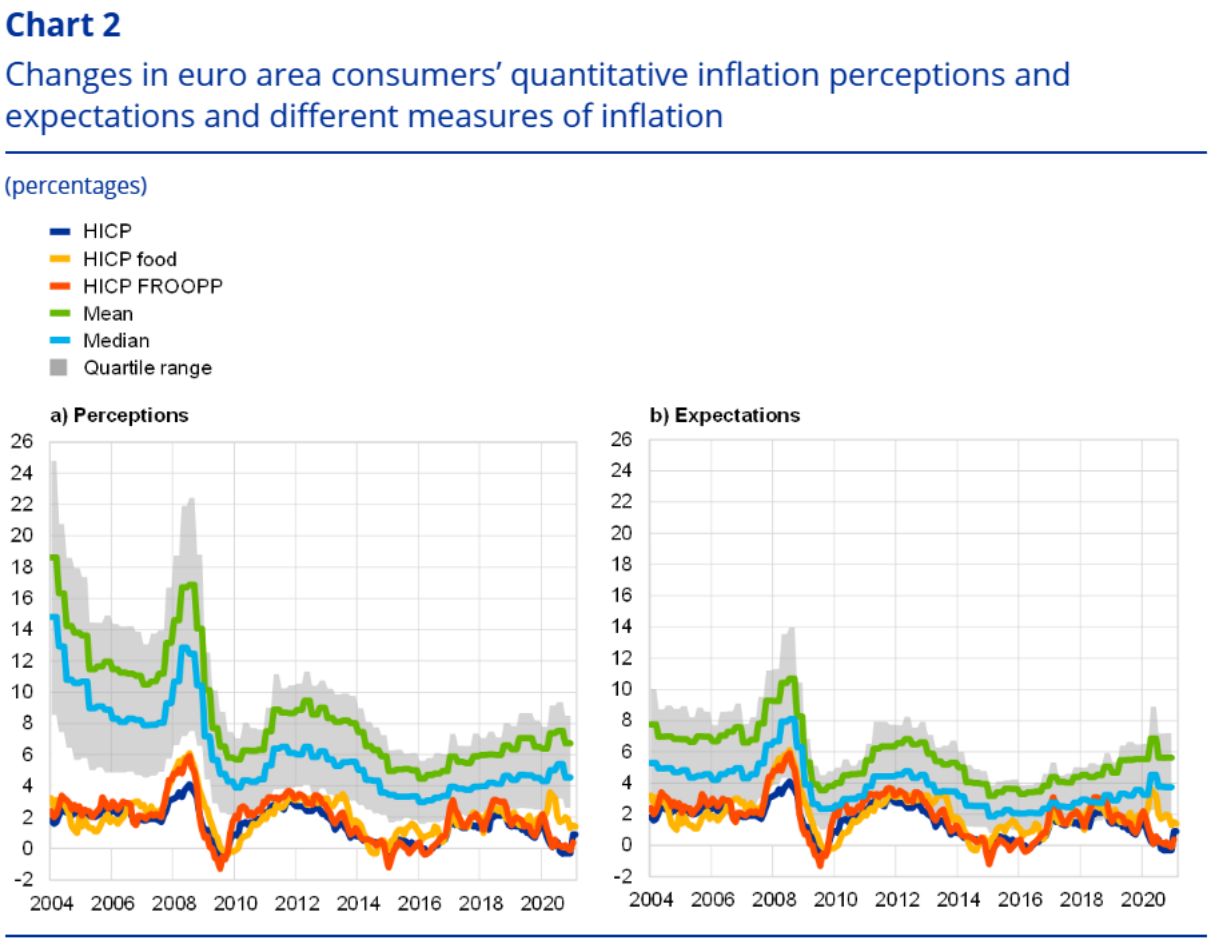
Who do central banks communicate with?

- Accountability: Government
- Expectations: Financial Markets, firms, households

- Should the Central Bank communicate in the same way with everyone?

What does the public know about inflation?

- Cœuré (2019) noted that a European Commission survey people asked people about the current inflation rate.
- From 2004 to 2018, the average response was approx. 9%.
- In fact, it was about 1.6%.
- However, households still recognise broad changes in inflation over time.



Meyler and Reiche (2021)

Writing a review of an academic paper

A critical review doesn’t simply summarise a paper - it evaluates how convincing the research is.

- Research question: What are the authors trying to establish, and why does it matter?
- Method and evidence: How do they investigate the question? What data and methods do they use?
- Main findings: What do the results show? Distinguish the evidence from the authors' interpretation.
- **Critical evaluation:** What are the strengths and limitations of the approach? Why do these matter for the conclusions?
  - Don't just identify a limitation! Try to explain why it matters for interpreting the findings.
- **Overall assessment:** How far does the evidence support the authors' claims, and what remains uncertain?

Ehrmann, et al., (2025), “Credibility gains from central bank communication with the public”

1. Research question and motivation

- What are the authors trying to find out? Why might central bank communication with the general public matter for monetary policy?

2. Measuring credibility

- How do the authors measure central bank credibility? Do you think this is a good measure? What might it capture, or fail to capture?

3. Research design

- How does the information experiment work? What are the different treatment groups, and why is there a control group? What are the strengths and potential limitations of this approach?

4. Findings and evaluation

- Using Table 1, what are the main findings? Which type of communication appears most effective, and how persistent are its effects?
- How convincing is the evidence that central bank communication can improve credibility among the general public? What conclusions can – and cannot – be drawn from the experiment?

Next week: policy briefing – advance prep

- **Read the latest monetary policy decision and accompanying statement** from your chosen central bank.
- **Identify the key economic indicators** that the central bank uses to assess economic conditions and inform its interest-rate decisions. Use the bank's monetary policy statement and supporting publications to identify these indicators.
- **Find the original sources of these data.** Identify where the indicators are first published, for example by the central bank, Eurostat, the Office for National Statistics (ONS), or another official statistical agency. Locate the exact time series.