# COMMUNICATION AND THE BELIEFS OF ECONOMIC AGENTS

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UC Berkeley and NBER

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Mario Draghi (2015): "*When inflation expectations go up with zero nominal rates, real rates go down. When real rates go down, investments and the economic activity improves. That's the reasoning [of QE].*"

# Standard Mechanisms

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ALL OF THESE MECHANISMS RELY ON MANAGING EXPECTATIONS OF THE "GENERAL PUBLIC"

# SOME QUESTIONS

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- How far can central banks go in communicating with the general public?

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Jerome Powell (2018): *"[B]ecause monetary policy affects everyone, I want to start with a plain-English summary of how the economy is doing, what my colleagues and I at the Federal Reserve are trying to do, and why."*
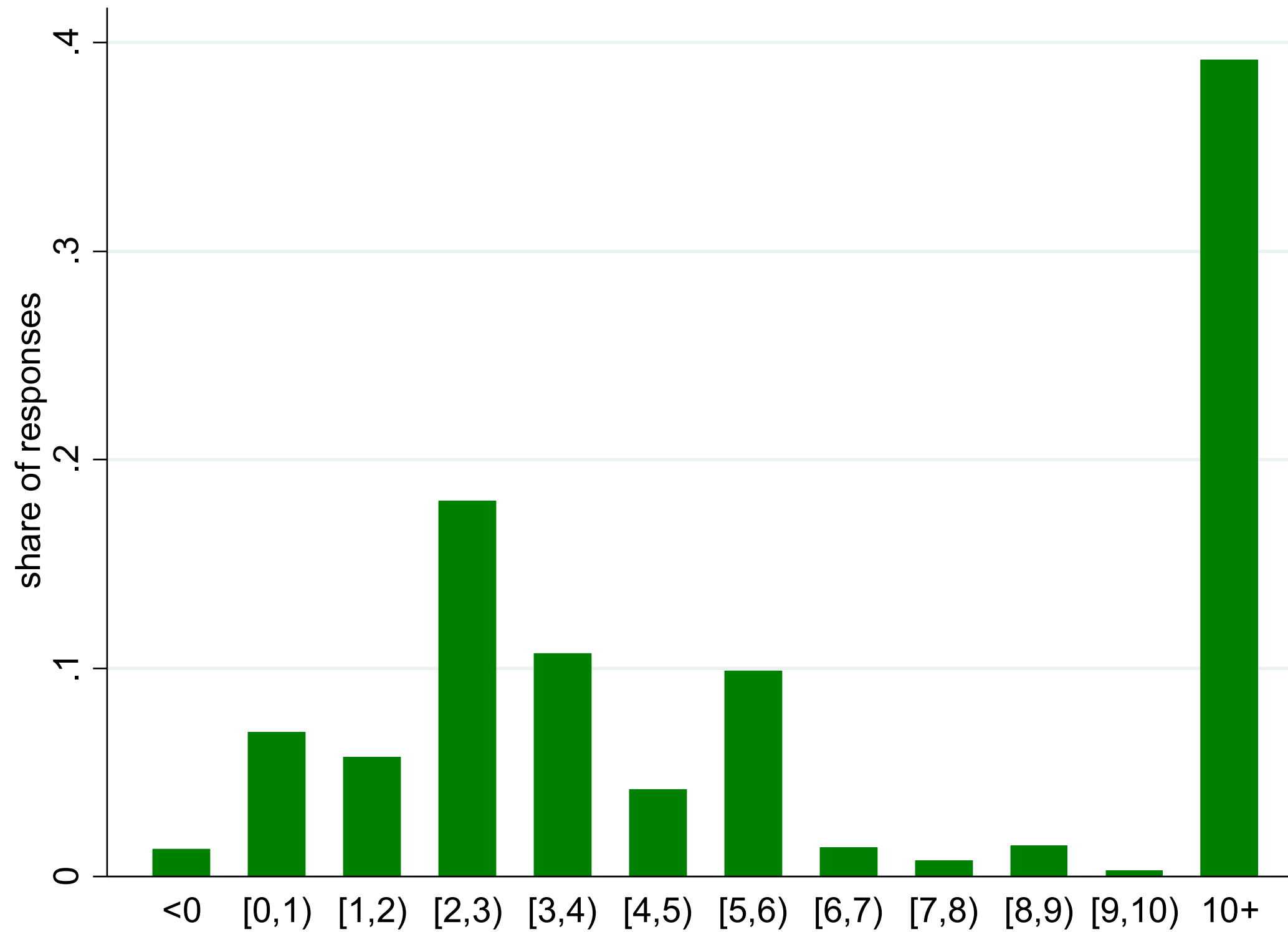
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Christine Lagarde (2020): *"After all, it is the everyday economic decisions of people and companies that we seek to influence with our policy and communication. If our language is not accessible, our policy will be less effective."*

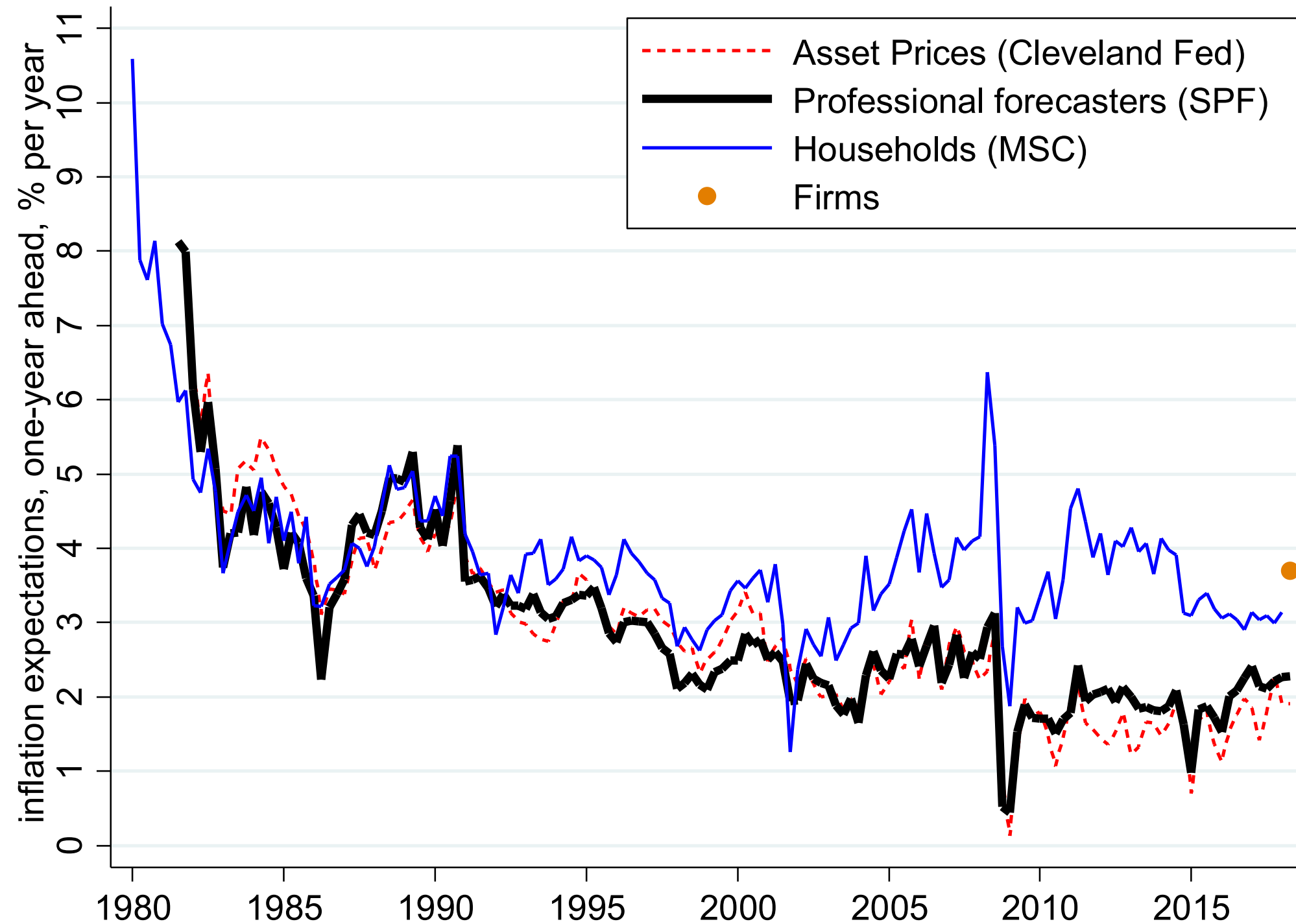Ben Bernanke (2020): *"The limits to forward guidance depend on what the public understands, and what it believes."*

# WHAT DOES THE PUBLIC KNOW?



share of responses

source: Coibion,
Gorodnichenko
and Weber (2019)

Little knowledge about the inflation target in the U.S. (sign of success?)

# WHAT DOES THE PUBLIC PREDICT?



source: Coibion et al. 2020

Households and firms are really different from professional forecasters and markets.

# HOW DOES THE GENERAL PUBLIC FORM EXPECTATIONS?

- Inflation expectations is a key object for central banks:
  - Alan Greenspan, "I am not saying what [inflation expectations] is a function of. We know it's a very difficult issue, but that is the key variable. It's important, but just because we can't make a judgment as to what these driving forces are in an econometric sense doesn't mean that it's not real."

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- Janet Yellen (2016): "Perhaps most importantly, we need to know more about the manner in which inflation expectations are formed and how monetary policy influences them."

# HOW DOES THE GENERAL PUBLIC FORM EXPECTATIONS?

Predictors of inflation expectations in low inflation economies.

- Perceptions of recent inflation (strong)

- Shopping (strong)

- Media (intermediate)

- Policy (weak)

- Incentives (strong)

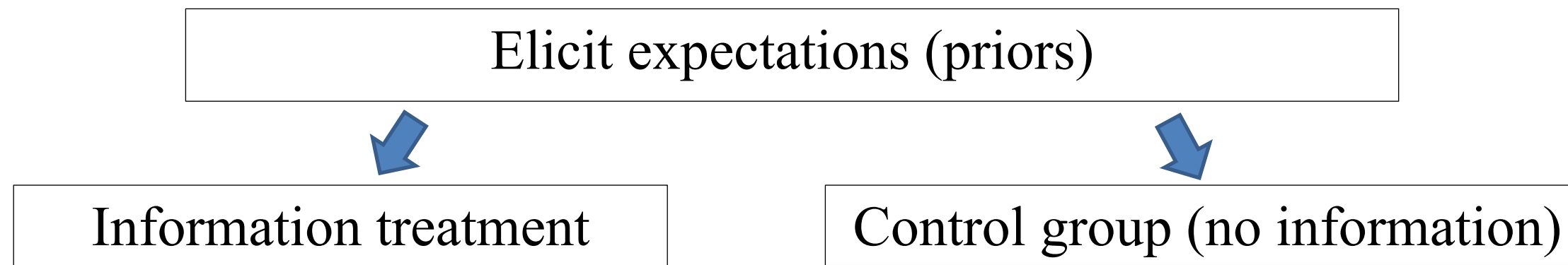# CAN WE CHANGE INFLATION EXPECTATIONS?

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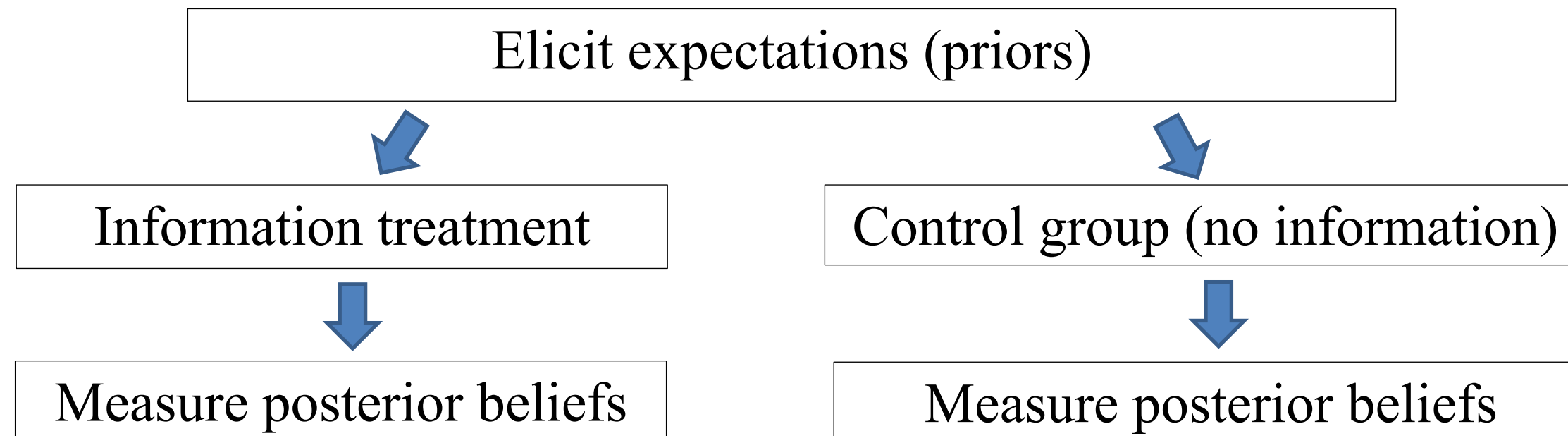| Information treatment | | Control group (no information) |
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| Treatment groups (coefficients are relative to the control group) | |
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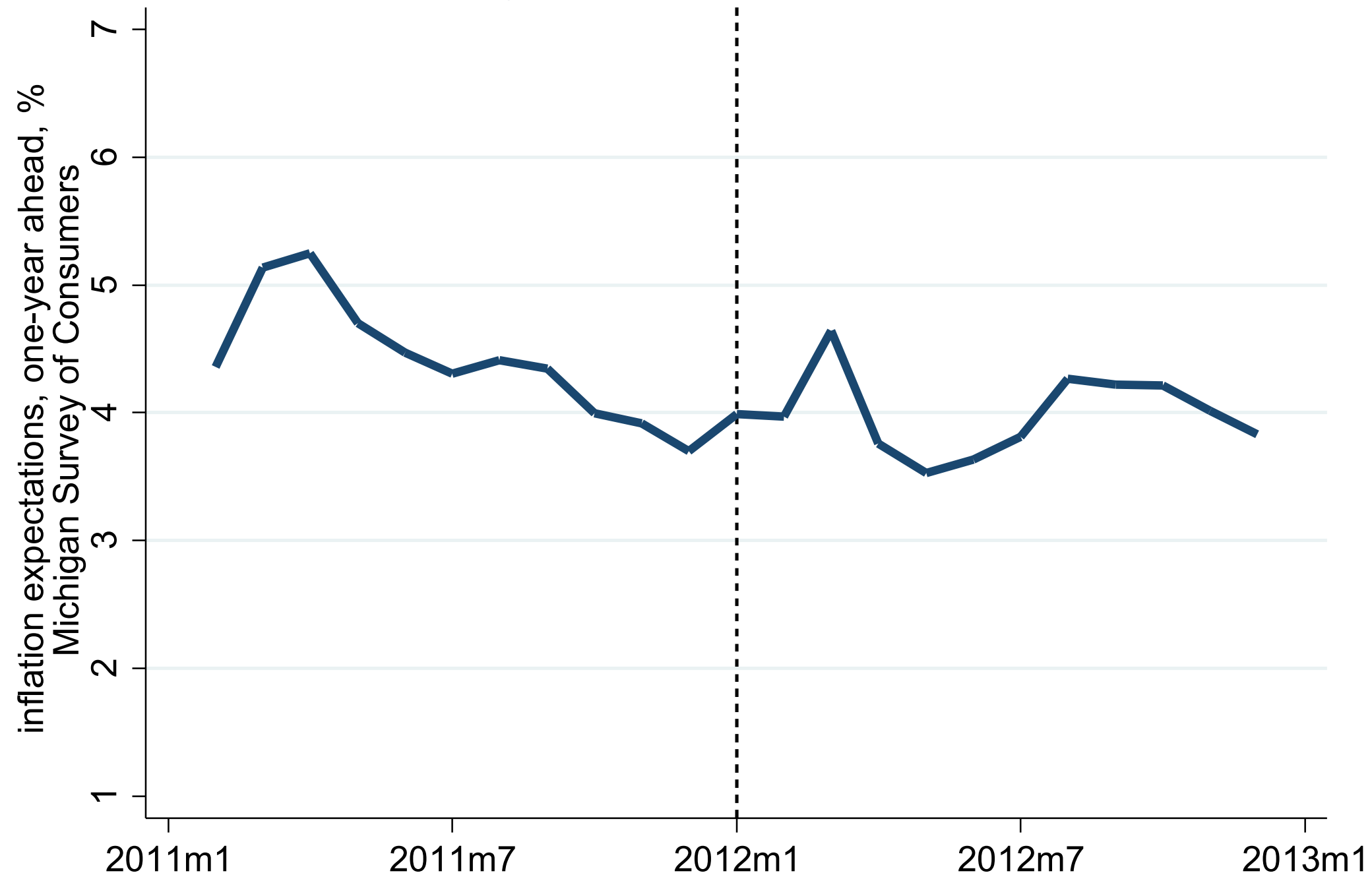| Dependent variable: Revision of one-year-ahead inflation forecasts of U.S. consumers | |
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**IT WORKS IN THE SHORT RUN BUT THE EFFECTS ARE GONE AFTER 6 MONTHS.**

# BREAKING THROUGH THE VEIL OF INATTENTION



The announcement of a 2% inflation target by the Federal Reserve had no discernible impact on U.S. household expectations of inflation.

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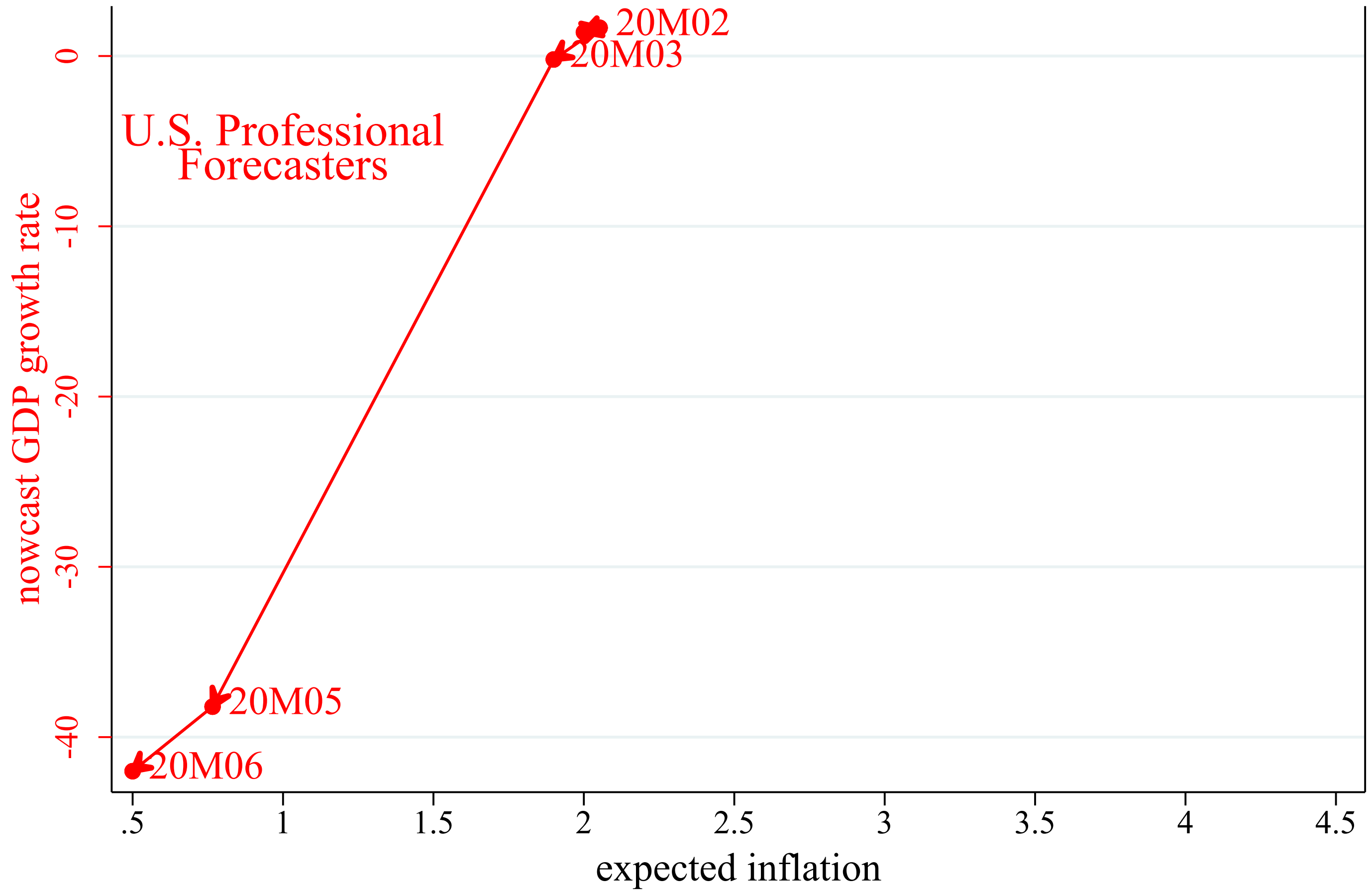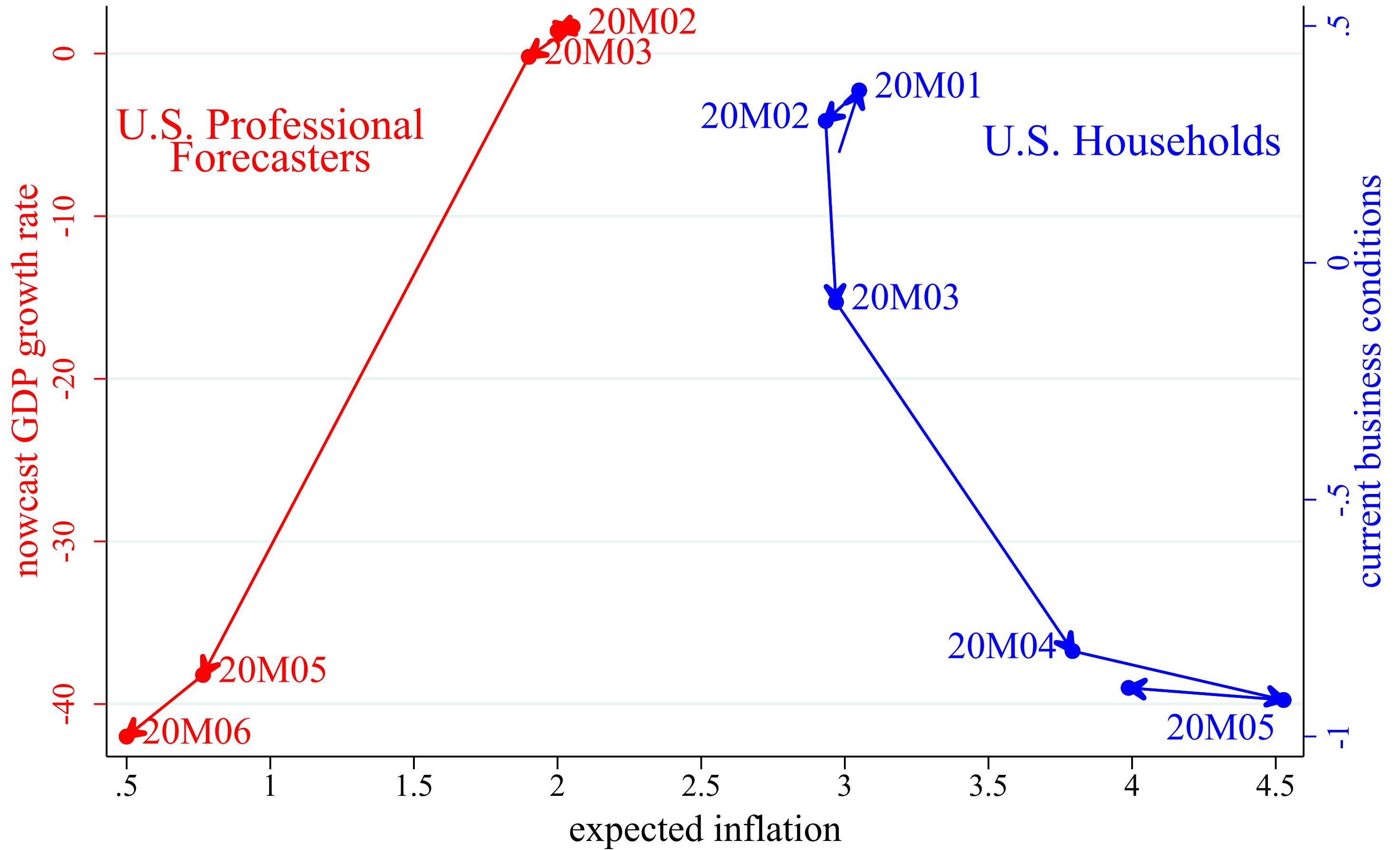- Repeat the message

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  • Potentially differentiate messages across audiences
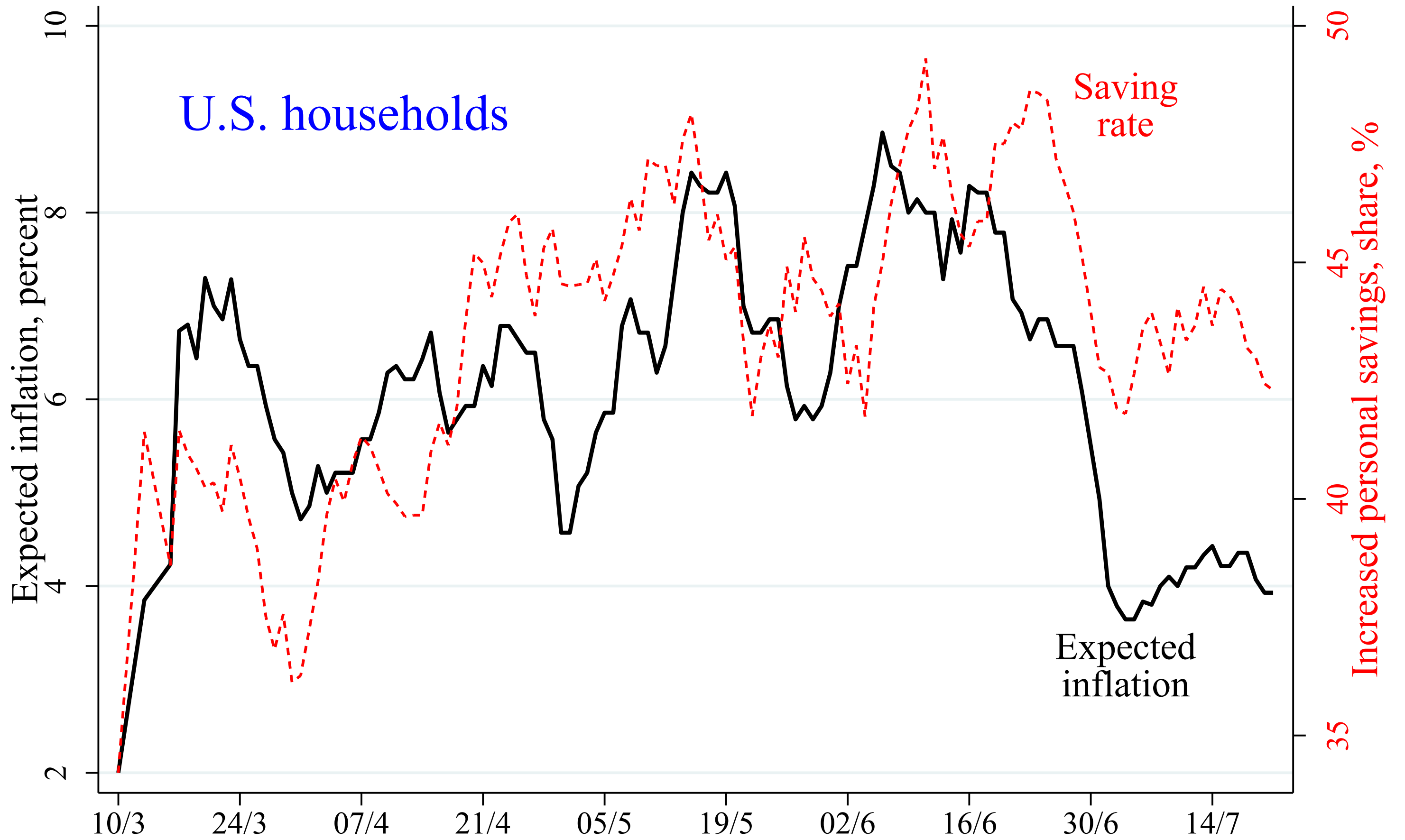
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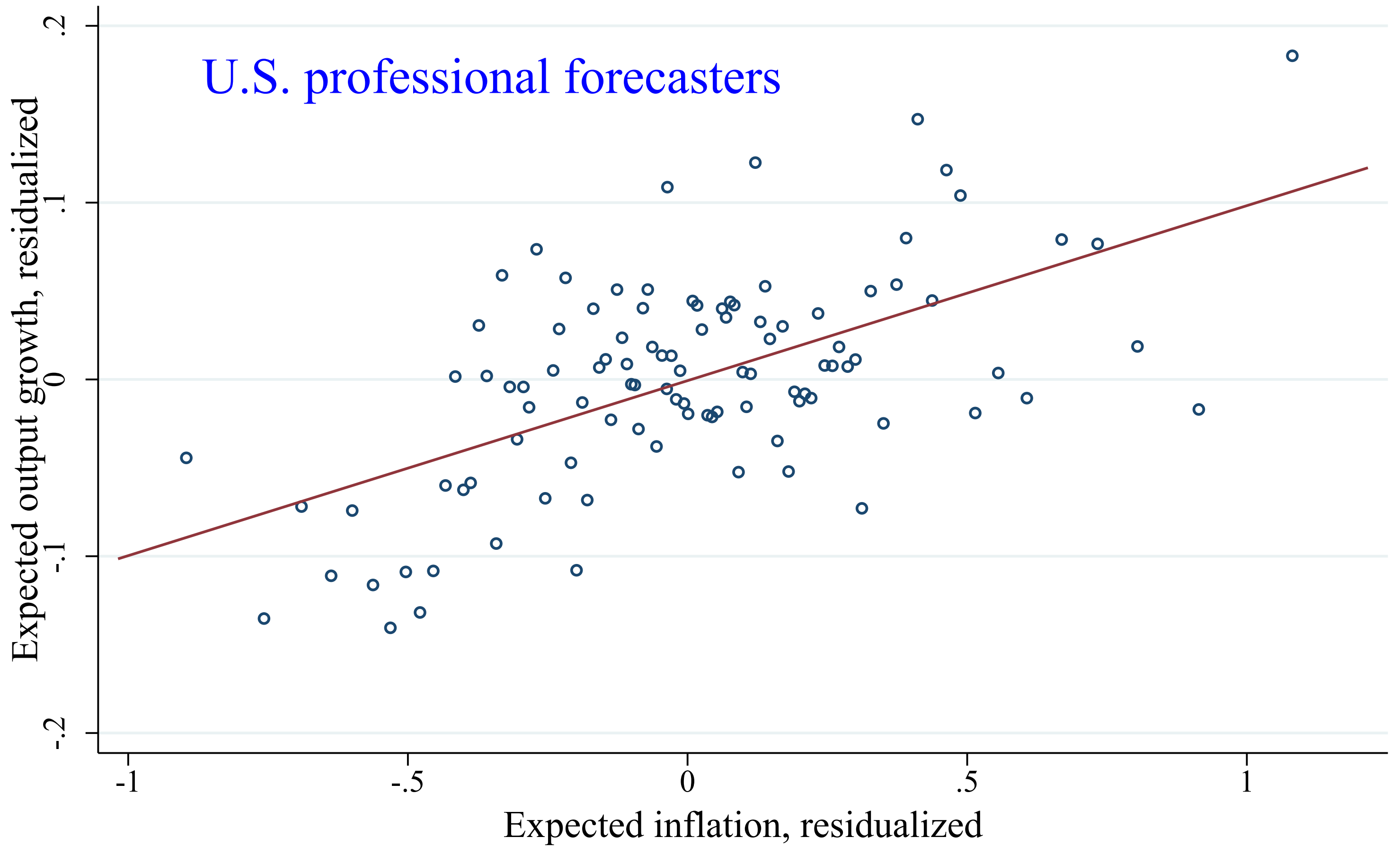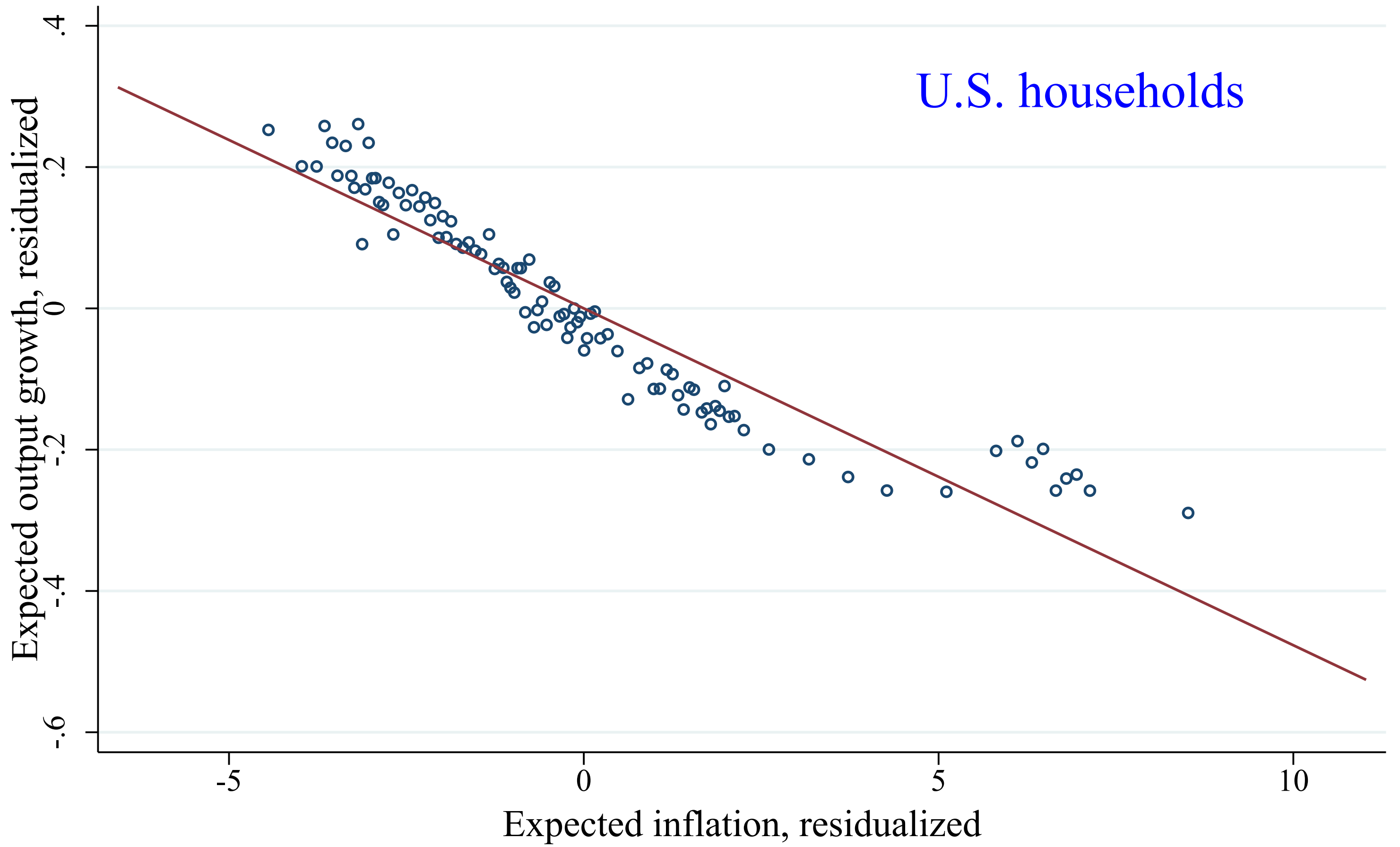
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- How/what information should be communicated is key!
  - Should we raise inflation expectations of households and firms?
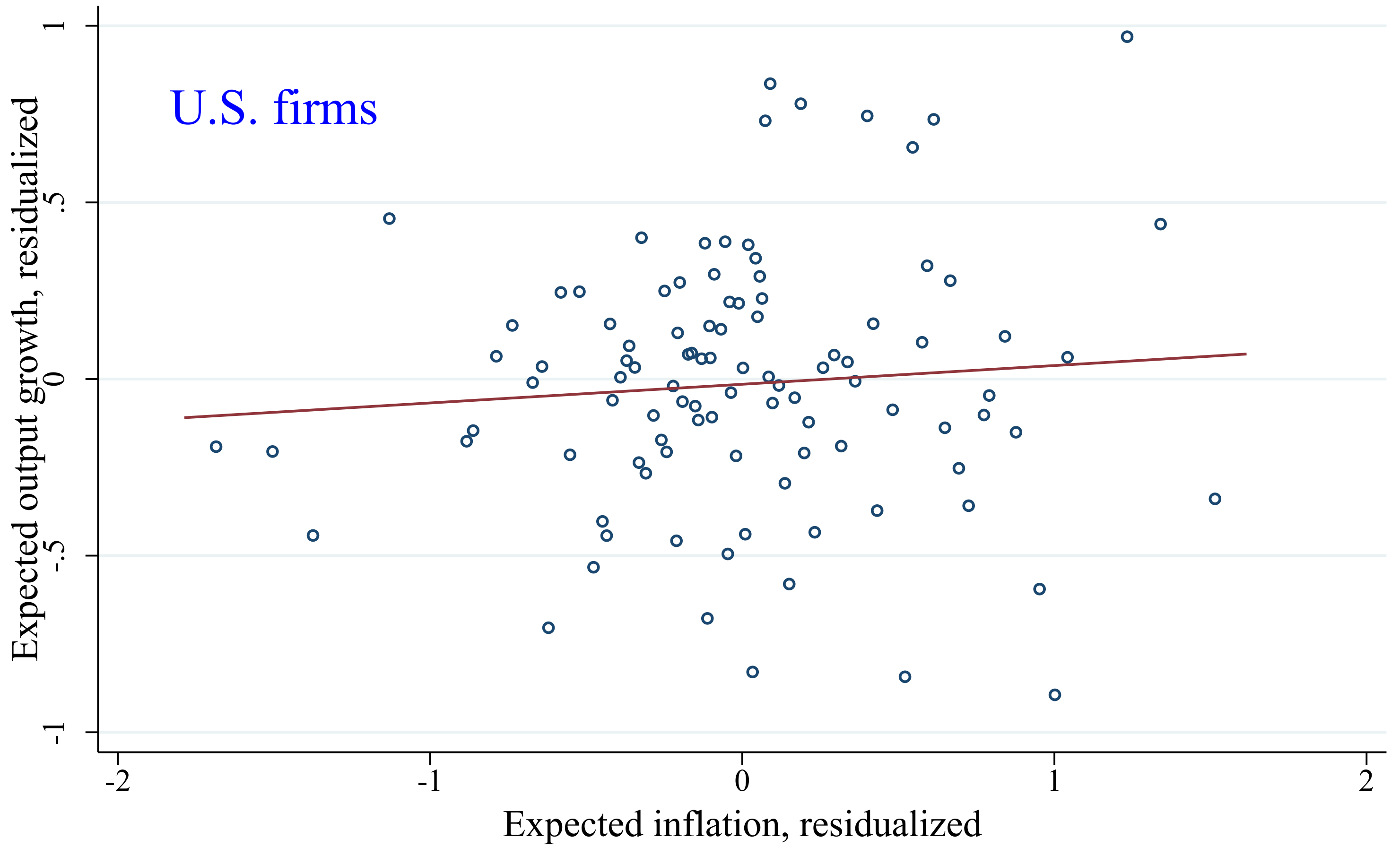  - Does the public think that inflation is desirable?

U.S. households

Saving rate

Expected inflation

Expected inflation, percent

Increased personal savings, share, %

Source: Cleveland Fed

U.S. professional forecasters

Expected output growth, residualized (y-axis)

Expected inflation, residualized (x-axis)

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- Prepare sustained information campaigns