**Comments on
Dale, Orphanides, and Österholm,
"Imperfect Central Bank Communication:
Information versus Distraction"**

Lars E.O. Svensson
Sveriges Riksbank

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Paper's main point

- If
(1) Central bank (CB) forecast is worse than private-sector (PS) forecast **and**
(2) PS incorrectly believes CB forecast is good,

then releasing CB forecast may be bad

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My main points

- (1) **and** (2) unlikely combination
- If either (1) or (2) does not hold, releasing CB forecast is good

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My main points

- (1) is often wrong: CB forecast is likely to be at least as good as PS forecast
- In (1), CB forecast has to be sizably worse than PS forecast
- In (2), PS has to put a very high weight on bad CB forecast for the release of CB forecast to be bad

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Simple signal-extraction problem

- PS forecast, precision p
$$x_t = \pi_{t+1} + \varepsilon_t, \quad E[\varepsilon_t] = 0, \quad Var[\varepsilon_t] = \sigma_\varepsilon^2 = 1/p$$
- CB forecast, precision q (ε_t, η_t independent)
$$y_t = \pi_{t+1} + \eta_t, \quad E[\eta_t] = 0, \quad Var[\eta_t] = \sigma_\eta^2 = 1/q$$
- Optimal (linear) combination of forecasts, precision $p + q$
$$z_t = \alpha^* y_t + (1-\alpha^*)x_t, \quad \alpha^* = \frac{q}{p+q}$$
$$Var[z_t - \pi_{t+1}] = \frac{1}{p+q} < \min[\sigma_\varepsilon^2, \sigma_\eta^2]$$

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Simple signal-extraction problem

- If PS knows p and q, releasing CB forecast is never bad, no matter how poor
- For release to be bad, we need poor CB forecast **and** poor choice of α

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(1) is often wrong: CB forecast is likely to be at least as good as PS forecast

- CBs have and use more resources for analysis and forecasts than any single PS forecaster
- CBs know more about their own intentions than PS observers (instrument-rate path!)

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Regarding (2), PS need not choose poor α

- CBs indicate uncertainty in their forecasts (including instrument-rate paths), for instance by uncertainty intervals
- PS weight α on CB forecast has to be very high for the communication of poor CB forecast to be bad
- If precision q of CB forecast < precision p of PS forecast, optimal weight α^* on CB forecast < ½. For precision of combined forecast z_t to be lower than precision of PS forecast, weight α on CB forecast has to exceed $2\alpha^*$

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Simple model-averaging normally good

- Let α = ½, equal weight on CB and PS forecasts
- For release of CB forecast to be bad, we must have
$$q < p/3,$$
precision of CB forecast must be less than 1/3 of precision of PS forecast
- Simple model-averaging normally good

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Another point: Morris-Shin 2002 is pro-transparency, not con

- In Morris-Shin model, coordination motive makes PS put larger weight on CB forecast. Then releasing CB forecast may deteriorate welfare if CB forecast is poor
- Svensson 2006: Precision of CB forecast (q) has to be very bad, less than 1/8 of precision of PS forecast (p), for welfare to deteriorate

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Conclusion

- Arguments against transparency not convincing: Unlikely combination of
(1) CB forecast much worse than PS forecast, and
(2) PS incorrectly believes CB forecast good
- Uphill battle to find good arguments against more transparency, especially against publishing instrument-rate paths
- Experience so far: More transparency has (almost?) always been better (Blinder et al., *JEL* forthcoming)

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