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Jan F. Qvigstad

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Monetary policy committees and communication¹

Jan F. Qvigstad

with Ingimundur Fridriksson and Nina Langbraaten

A country has only one central bank. It is therefore logical to compare it with central banks of other countries. There is broad agreement on the objective of monetary policy – price stability – and on central bank independence in the use of policy instruments to reach that objective. According to international best practice, monetary policy decisions should be made by committee², but neither theory nor practice provides any clear answers as to which committee type is the right one or which form of work practice is best. There is broad international agreement that monetary policy decisions should be transparent. However, the way transparency and central bank communication work in practice will depend among other things on whether the monetary policy committee is collegial or individualistic.

1 Introduction

Monetary policy has undergone major changes over the past decades, both internationally and in Norway.³ Central banks are now largely independent of political authorities in their conduct of monetary policy. The most common monetary policy objective is price stability, but the definition of price stability may vary across countries. The organisation of monetary policy decision-making internally at central banks has also changed in many countries. Generally, these decisions are now made by committee. There have also been considerable changes in the degree of transparency and in communication. Today, most central banks are open about the objective of monetary policy, their strategy for reaching that objective and the background for and the process behind interest rate decisions (see Qvigstad (2009)). Yet despite common trends, differences remain in the way central banks organise and communicate monetary policy decisions. These differences are likely due to different histories and different social and political structures. Neither theory nor empirical research provides clear answers as to what is the best solution.

In the interest of democratic governance and monetary policy effectiveness, transparency and communication of monetary policy are important. Since 2005, Norges Bank has published forecasts of the key policy rate. As a result of the financial crisis, pronouncements regarding future key rates are now used by many central banks.

This paper will examine in more detail differences in the organisation and communication of monetary policy.

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² “Monetary policy committee” refers in this paper to the monetary policy decision-making bodies in central banks irrespective of these bodies’ official name or authority in other respects.

³ These changes were described in an article in Norges Bank’s journal *Economic Bulletin* in 2007. See Claussen et al. (2007).

2 Why monetary policy committees?

Delegating monetary policy – independence

A number of considerations warrant that the government set objectives and delegate tasks to public sector institutions. This can provide a more solid basis for decision-making and depoliticise decisions and measures. Furthermore, management by objectives and delegation of tasks can improve predictability for other economic agents. This arrangement may be viewed as an institutional solution to the problem of avoiding making serious mistakes. By giving agencies clear objectives and the instruments to attain them, governments can deter them from shirking responsibilities.

Nevertheless, from a democratic point of view, delegating the operational conduct of monetary policy to an independent body may be considered problematic. It is therefore important for the central bank to have a clear mandate and to be transparent, so that elected representatives, the press and the public can always verify that the central bank is conducting monetary policy in line with its mandate (see e.g. Blinder (1998)). Even if the central bank is independent in the conduct of monetary policy, it needs to be accountable to the principal. It must be evaluated on results, and also on its assessments and decisions (see Qvigstad (2009)).

With regard to economic policy, it is usually argued that some long-term objectives can be attained only if short-term considerations are not allowed to determine the use of instruments (see Kydland and Prescott (1977)). This is the case for monetary policy and inflation targeting. There may be a desire to use a low interest rate to attain higher growth in output and employment than the level that is sustainable in the long term. However, economic agents are aware of this temptation. If they cannot trust that the key policy rate will be set to ensure stable inflation, they will expect higher inflation over time. The long-term cost may be high, and the short-term gain limited, as Norway and other countries experienced in the 1970s and 1980s. An independent central bank is better poised to give priority to long-term considerations over short-term gains.

Just as Ulysses had himself tied to the mast to resist the song of the Sirens,⁴ government authorities can, by setting targets and delegating tasks, prevent themselves from carrying out policies that are pernicious in the long run. Relinquishing the opportunity to break a promise makes that promise more credible. Being accountable for one's promises in the form of reporting and follow-up can ensure that one is tied to the mast (see Qvigstad (2008)).

In some countries, central bank legislation sets out provisions that give the political authorities power of instruction over the central bank with respect to monetary policy.⁵ These provisions ensure that any instructions be given within a framework that is made known in advance and with full disclosure. Central bank legislation in the UK, New Zealand, Canada and Australia contains such provisions. The formulation of the power of instruction varies to some extent. The Norges Bank Act is a part of this tradition. The King in Council (the government) may issue instructions to Norges Bank, but only in accordance with clearly defined and special procedures that depart from ordinary administrative procedures. The Bank of England Act requires the existence of “extreme economic circumstances” before the Treasury may give the Bank directions. In Sweden, the political authorities do not have a statutory power to instruct the central bank with respect to interest-rate setting. The Swedish

⁴ See Elster (1979).

⁵ Political authorities will always be able to give instructions to the central bank by amending legislation. However, this is a cumbersome process, and the threshold for initiating such a process will normally be high.

Constitution states: “No public authority may determine how the Riksbank shall decide in matters of monetary policy”.

Nor may the ECB seek or take instructions. Article 130 of the *Treaty on the Functioning of the European Union* states:

“When exercising the powers and carrying out the tasks and duties conferred upon them by the Treaties and the Statute of the ESCB and of the ECB, neither the European Central Bank, nor a national central bank, nor any member of their decision-making bodies shall seek or take instructions from Union institutions, bodies, offices or agencies, from any government of a Member State or from any other body.”

Collective bodies often make better decisions than individuals

Independence alone will not result in good decisions. Even if an independent central bank is better positioned to avoid allowing short-term concerns and fickle preferences to dictate the key rate, decisions must be made under considerable uncertainty (see Qvigstad (2010)).

By delegating decision-making responsibility to a collective body, it is possible to avoid that the special interests of individuals dominate. It may also provide assurance against serious misjudgements, which is important when decisions need to be made under uncertainty.

Mervyn King⁶, the Governor of the Bank of England, said the following:

“The best way to make technical judgements under uncertainty is by making use of the accumulated wisdom of a committee whose members can pool their knowledge and expertise”.

Another benefit of decision-making by committee is that decisions will be based on a broader range of assessments than those of an individual. Having more members means greater access to varied knowledge and opinions, but it also means that more persons must have a say in the final decision.

Having to reach a consensus decision does not always or necessarily make the decision a better one, however. When committee members share a set of views and thought processes, so-called “groupthink” may lead them astray, and few diverging opinions may be expected in its discussions. Thus, a collective body may be convinced that its common stance must be right (see Qvigstad (2010)).

Democratic arguments may also suggest that decisions by an independent central bank should be made by committee. If the mandate for monetary policy is expressed in general terms, this leaves room for interpretation. It may, therefore, be an advantage for monetary policy not to be shaped by just one person’s interpretation. Moreover, the underlying analyses and forecasts may be interpreted in varying ways and the weight given to the relevant considerations may also vary.

The literature does not provide a clear answer as to the optimal composition and work methods of monetary policy committees. Nor is it clear what might be the correct division of duties between central bank staff and the monetary policy committee. The staff are subordinate to central bank management, which also sit on decision-making bodies.

⁶ See King (2007)

Nevertheless, in the monetary policy decision-making process, it is clear that the staff are a stabilising element. This makes the central bank robust to changes in bank management and the monetary policy committee. In order for the staff of economists to perform their role effectively, high professional standards are important. The staff will be able to influence the work of the monetary policy committee in several ways. Their analyses are important for the effectiveness of the committee. The staff must also be a staff for the entire committee. Even if individual committee members should be assigned their own resources, as is the case at the Bank of England, such resources would still not be of the same scale or have the breadth of expertise that the central bank staff in its entirety has. But having own resources at their disposal can assist individual committee members in communicating with the staff.

Apel et al. (2013) conducted a survey of the members of Sveriges Riksbank's Executive Board and the members of Norges Bank's Executive Board⁷ to ascertain their views on their work on the monetary policy committee. The survey revealed that members believed that the staff were more important as a source of information than the other committee members. In particular, the staff appeared to have more influence with regard to the projections for economic developments.

Various types of committee

There is considerable variation in the way committees conduct their meetings. At some central banks, the chair of the monetary policy committee submits a recommendation for the key policy rate, while at other central banks, the governor does not signal his views in advance. Blinder (2006) distinguishes between two types of committees: a *collegial committee* and an *individualistic committee*.

Members of a collegial committee emphasise the importance of appearing unanimous to the outside world. There may be a vote. However, consensus should not be mistaken for unanimity. Even if the members may be in agreement on the decision, or at least agree not to oppose it, the degree of support may vary. A collegial committee may work in several ways. Blinder (2006) distinguishes between two opposites. One is a *genuinely-collegial committee*, where the members may argue for their own points of view behind closed doors, but they ultimately arrive at a joint decision. Each member takes ownership of that decision, and there are no public disagreements. An example of such a committee may be the Governing Council of the ECB.

Lorenzo Bini Smaghi, a former member of the ECB Executive Board and ECB Governing Council, wrote the following in a feature article in the *Financial Times* on 4 September 2012:⁸

“National politicians, media and the wider public have not yet fully understood that the ECB Council members do not represent the interests of their respective countries. They often associate the names of the members with their nationality, forgetting that each member participates in the ECB Council on a personal basis. The exercise of accountability in a collegiate way aims to protect the ECB Council members from the possible pressure coming from their own countries. As a result, the discussions – sometimes quite animated – take place within the ECB Council, but only the decision is made public. The members of the ECB Council are expected to loyally support and defend in public whatever decision is taken”.

⁷ The survey was conducted only among external members of the Norges Bank Board for the period between 1999 and April 2011.

⁸ See Bini Smaghi (2012).

However, the President of the Deutsche Bundesbank and member of the ECB Governing Council Jens Weidmann chose to make public the fact that on 6 September 2012, he was the only Council member to vote against the ECB's programme for the unlimited purchases of government bonds from states that are either in a full macroeconomic adjustment programme or a precautionary programme under the European Financial Stability Facility/European Stability Mechanism, known as Outright Monetary Transactions (OMTs). In an interview in *Neue Zürcher Zeitung*,⁹ he gave the following justification for going public:

"The general public are well informed – we owe it to them to be frank. A central bank is credible if it takes people seriously and provides them with truthful information. There is no point in trying to dress up the facts".

When asked how he now saw his future role on the ECB Governing Council, Weidmann replied:

"Despite all the commotion about government bond purchases, it would be very wrong to imagine that I'm always in the minority within the Eurosystem. The majorities on many other issues are very different, and on some there is no dissent within the Council at all. That is precisely why I find it so important to garner support for my position on controversial issues".

The second type of collegial committee is referred to as an *autocratically-collegial committee*, where the chairman largely determines the committee's decision. Blinder (2009) believes that the FOMC under chairmen Burns, Volcker and Greenspan is a clear example of this type of committee, but claims that this is not the case under Bernanke, the current chairman.

Members of an individualistic committee do not attach importance to presenting an outward appearance of unanimity. The committee reaches its interest rate decision by vote. Unanimity is not expected. Examples of central banks with individualistic committees are Sveriges Riksbank and the Bank of England. Decisions are made by majority vote, and each member is individually accountable for his or her vote. The potential challenges linked to this type of committee are that the central bank may speak with many voices and the outside world may be uncertain of the intended direction for monetary policy. The result may be a cacophony of voices, according to Blinder (2006). An example of this is Sweden, where in 2012 there was a debate on whether Sveriges Riksbank clearly communicated its monetary policy and there was "general criticism that the Riksbank's communication has not always made it easy to understand exactly why certain decisions have been made and why these decisions have been seen as being better than conceivable alternatives", as formulated by the Deputy Governor, Per Jansson.¹⁰ In a feature article in 2012, Lars Calmfors wrote that "oenigheten i Riksbankens direktion har fått stor uppmärksamhet [disagreement within the Executive Board has drawn considerable attention]".¹¹

An advantage of an individualistic committee is that purely individual accountability can provide positive incentives. There are no other committee members to hide behind. At the same time, such a system usually requires more analytical work and preparation of individual assessments and thus a full-time position at the central bank. In that case, external committee

⁹ See *Neue Zürcher Zeitung* (2012)

¹⁰ See Jansson (2012).

¹¹ See Calmfors (2012).

members may quickly assimilate to the internal culture, and the bank loses the counterweight to the internal milieu. The view from outside disappears, and the central bank may lose the control function that external members provide. On the other hand, there is a risk that purely external members would not be sufficiently heard.

Blinder (2009) believes that members of monetary policy committees should be full-time employees, but at the same time underscores that as insurance against groupthink it is probably best if only a minority of the committee comprise “bank careerists”. To avoid groupthink, there may be an advantage to have external committee members, who are not as strongly influenced by the central bank's internal viewpoints. In Blinder's view, it may be difficult to completely insulate part-time committee members, who also have outside jobs, from conflicts of interest. For that reason, he argues that it can be advantageous for potential external member of a monetary policy committee to be a full-time public servant. This is not completely without drawbacks, because it may be difficult to keep them fully occupied.

In many countries, legislation sets out qualification requirements for the members of the monetary policy committee, but the requirements are often formulated in fairly general terms. They may include experience in macroeconomics, financial markets and monetary policy. Mendzela (2012) is of the view that the qualifications required in the business sector should also apply for monetary policy committees. These requirements are business acumen, integrity and common sense. He argues that non-technical discussions force specialist to think in broader terms and challenge technocratic and theoretical assumptions. They generate fresh thinking, earlier action and better outcomes.

One argument in favour of unanimous endorsement of monetary policy decisions by committee members is that central banks are important social institutions that should not be linked too closely to individuals but should have a collective identity. It is the institution and its mandate that should have precedence, not the persons filling the roles for brief periods (see e.g. Issing (2005)).

A disadvantage of a collegial committee is that individual members can hide behind the collective, avoid taking responsibility and in this respect become free-riders.

Committee size

The literature does not provide clear answers as to the appropriate size of a monetary policy committee. Considerations that must be balanced include a sufficiently diverse and experienced membership that gives rise to value added discussions. Moreover, the committee must be able to make decisions. Committees with functions other than solely the conduct of monetary policy will need more members with a broader background than committees with a single task. The design of a committee will also depend on the desired degree of efficiency in the decision-making process. The greater the number of members, the more difficult it will be and the more time it will take to reach a decision. The exchange of views will be more difficult. Professor Anne Sibert has suggested that the committee should be “dinner party size” (see Qvigstad (2010) and Blinder (2008)). Among a sample of 84 central banks, Berger et al. (2006) find that the average size of a monetary policy committee is 7-9 members. The size of the committee appears to increase with the size of a country and diversity of its population (see Berger et al. (2006)). This indicates that the size of the committee is affected by information management requirements.

One reason to limit committee size is that individual members may take less responsibility when the committee is large. Each member has less influence and it becomes more difficult for outside parties to verify the efforts of individual members when the committee has many members. The size will also depend on the type of committee. With an individualistic committee, it may be difficult to have 20 members whose views are to be stated and recorded in minutes, as in the case of the Executive Board of Sveriges Riksbank. Another reason is that learning internally within the committee becomes more difficult when the committee is large (see Claussen et al. (2004)). Among OECD countries, committee size varies between three members in Switzerland and 23 at the ECB.¹²

Appointment procedures

Members of monetary policy committees are usually appointed by a country's government or parliament, though in some cases, the central bank also plays a role in their appointment. One example is the US, where the regional Federal Reserve Bank presidents are appointed by their respective regional boards.¹³ These boards comprise representatives of banks and different industries, and are intended to reflect a broad cross-section of the providers and users of banking services in each district. The other seven members of the Federal Open Market Committee (FOMC) are nominated by the US president and confirmed by the Senate. In Sweden, the six members of the Executive Board are appointed by the Riksbank's General Council which is appointed by the parliament. In the UK, the four external members of the Monetary Policy Committee (MPC) are appointed by the Chancellor of the Exchequer.

One way to ensure central bank independence from political authorities is to appoint members of a monetary policy committee for periods longer than the terms of elected members of parliament. Lybek and Morris (2004) examined 101 central banks, and found that at 66 percent of them, members are appointed for four or more years. To ensure continuity in monetary policy, appointments of committee members can be staggered, so that not all members are replaced at the same time. On the other hand, it may be advantageous to limit the number of terms or years of members to promote renewal and development.

Participation of other government bodies

A number of central banks allow representatives of the central government authorities to be present at meetings of the monetary policy committee (see Claussen et al. (2007)). Usually, they do not have the right to vote. This includes the Bank of England, where a representative of the Treasury sits in on meetings and can participate in the discussion, and at the ECB, where the chairman of Ecofin¹⁴ and a member of the European Commission may attend meetings of the Governing Council. At the Bank of Japan, representatives of both the ministry of finance and the Cabinet Office may attend monetary policy meetings. They may make motions, but are not entitled to vote.¹⁵

¹² There are currently 23 voting members of the Governing Council, but that number will be reduced to 21 once the number of euro area states reaches 19 (as at today's date, 17 EU member states have introduced the euro).

¹³ Five of the twelve regional presidents are members of the FOMC, and the remaining seven may attend meetings, where they have a right to speak, but not to vote. Except for the Federal Reserve Bank of New York, there is an annual rotation among regional Federal Reserve Banks for membership of the FOMC.

¹⁴ The Economic and Financial Affairs Council, which comprises the ministries of finance of EU member states.

¹⁵ They may also request that a vote on monetary policy be postponed to the following meeting. If such a request is made, the Policy Board is to vote on whether to accede to the request.

3 Communicating the committee's monetary policy decisions

The terms “transparency” and “communication” are often used interchangeably. However, it may be useful to reserve the term “communication” for those cases when the central bank uses its transparency actively as a tool to influence market participants (see Claussen et al. (2007)).

Effective communication should satisfy three criteria (see e.g. Winkler (2000)). First, communication should be *clear*. There should be no room for misinterpretation by the recipient agent and the information should not be imprecise to the extent that it is not given any weight.

Second, communication should be *efficient*. This means that agents should not spend much time on finding and interpreting relevant information. The information must be adapted to the target group.

Third, communication must be *honest*. External communication should reflect the internal decision-making process (see Qvigstad (2009)).

A fourth criteria may apply – *good bureaucratic craftsmanship*. The committee must explain the premises and produce solid analyses that facilitate the assessments. It should be communicated whether the conclusion was easy or difficult to reach and whether alternative conclusions existed.

A number of central banks publish minutes of monetary policy committee meetings. However, how the actual discussion of the monetary policy committee appears in the minutes varies. Most minutes contain a detailed account of the economic situation, financial markets and international developments, but the account of the actual discussion is often limited and it is often impossible to determine the viewpoints of individual members. Blinder (2006) believes that a central bank's decision-making system affects what it is possible for a central bank to communicate externally. In his opinion, where there are individualistic committees, voting results can be published, possibly, with a high degree of detail in the minutes. Sveriges Riksbank is an example of a central bank that goes to great lengths with respect to the degree of detail in the minutes and in identifying discussion participants by name.

Frequent among central banks that publish minutes and voting results is that monetary policy decisions are made by committees whose members are employed at the central bank or work full-time on monetary policy issues. The structure of the minutes varies to a large extent. The Riksbank in Sweden and the Bank of England both operate with individualistic committees, but the minutes are very different. The Riksbank's minutes include an extensive account by each member. The minutes from the meeting on 24 October 2012 numbered 32 pages. The Bank of England produces minutes for the committee as a whole and does not cite the views of individual members by name, but the minutes may indicate differences in the weight given to arguments, which may result in divergent conclusions.

Detailed meeting minutes increase accountability among committee members. This may give rise to positive incentives. On the other hand, such transparency may inhibit the actual discussion. Members may come to meetings with pre-drafted statements, which may impair the quality of the exchange of views.

Detailed minutes also entail a risk of moving the real discussion from the official meeting into closed rooms. This does not provide genuine transparency.

Central banks are increasingly communicating their key rate expectations. Communication procedures vary among central banks. In the same way as Norges Bank, the Reserve Bank of New Zealand and Sveriges Riksbank communicate their projections of economic developments and the key rate ahead in their monetary policy reports. Other central banks, such as the ECB, indicate the direction of the key rate in press releases after monetary policy meetings, or the direction can be inferred from the deliberations of the monetary policy committee, as is the case for the Bank of England. After the financial crisis, the Fed started indicating in its press releases after monetary policy meetings how long it intends to keep policy rates unchanged and which conditions must be satisfied for policy rates to be raised.

A more detailed account of the procedures of other central banks is provided in the Appendix.

4 Norges Bank's framework

The Executive Board – Norges Bank's monetary policy committee

Norges Bank's monetary policy decisions are made by its Executive Board, which has seven members: the governor, the deputy governor, and five external members. With the exception of Australia and Iceland, Norway differs from the other countries discussed in the Appendix in that five of seven members are not full-time employees of the central bank. The survey conducted by Apel et al. (2013) showed that the members of the Executive Board supported the current framework. The Executive Board of Sveriges Riksbank has a different composition, comprising full-time internal members, but its members were also satisfied with the arrangement. Apel et al. (2013) point out that this may indicate that the choice between whether members are external or internal is not a self-evident one.

The governor and deputy governor are chairman and deputy chairman respectively of the Executive Board. They are appointed to full-time positions for a term of six years. The governor and deputy governor may be reappointed for an additional six-year term. The remaining members are appointed for a term of four years that are staggered so that every other year either two or three members' terms expire. Members may be reappointed for an additional two four-year terms. Two alternates are appointed for the five external members of the Board. In the interest of continuity, alternates also attend meetings of the Board..

Members of the Executive Board are appointed by the King on the recommendation of the Ministry of Finance. According to Proposition to the Odelsting No. 81 (2002–2003)¹⁶, when appointing members importance is to be given to ensuring that the Executive Board reflects a breadth of background and expertise, with particular insight into economic issues. The Proposition states that the Executive Board should be composed of persons with different backgrounds in order to ensure that it is capable of critically reviewing its assessments. Political authorities are not represented on Norges Bank's Executive Board.

The Executive Board also plays an important role in providing feedback on the quality of the background documentation compiled by Norges Bank's staff as the basis for the Board's decisions. For the staff to perform its role effectively, it is crucial for this material to be of

¹⁶ Proposition to the Odelsting No. 81 (2002–2003) Bill amending the Norges Bank Act and the Financial Institutions Act and repealing the Currency Control Act and the Money and Credit Control Act.

high professional quality. Norges Bank has a strategic management team that regularly discusses the conduct of monetary policy.

The Executive Board is not only responsible for Norges Bank's monetary policy decisions, but also the Bank's other operations, including the Government Pension Fund Global (GPFG).

Consensus-based

Norges Bank's Executive Board can be designated as a collegial committee. This means that the committee takes decisions by consensus and that members collectively stand behind the final decision.

External members are not full-time employees of Norges Bank, i.e. their primary occupations are outside the central bank. External members can act as a counterweight against any internal culture of like-mindedness that might arise, and hence have an important control function.

Norges Bank Act – the power to instruct the Bank

The Norges Bank Act makes no reference to objective of monetary policy. The Bank shall conduct its operations in accordance with the economic policy guidelines drawn up by the government authorities, according to the Norges Bank Act. The following is stated in the recommendation from the Standing Committee on Finance and Economic Affairs concerning the Act relating to Norges Bank and the Monetary System etc. (Recommendation No. 50 (1984-85) to the Odelsting: “A new Norges Bank Act should be able to be adapted to various scenarios. In line with this, the Committee proposes a general clause for the Bank’s activities and that the Council of State be authorised to lay down further guidelines in a number of areas”.

Pursuant to Section 2 third paragraph and Section 4 second paragraph of the Norges Bank Act, the Government issued a new Regulation on Monetary Policy on 29 March 2001. An inflation-targeting regime was introduced. At the same time, new guidelines were issued for fiscal policy and the phasing-in of oil revenues into the Norwegian economy.

A typical characteristic of recent central banking legislation in other countries is an objects clause stating that the primary objective of the central bank is to ensure that the value of money is stable. In Norway, the inflation target is set out in a regulation pursuant to the Act, as an operational and more intermediate target.

The Norges Bank Act provides the government with a general power to instruct the Bank. Former Norges Bank Governor Svein Gjedrem¹⁷ stated the following:

“The instruction section does not prevent Norges Bank from setting the interest rate independently of pressures from the central government authorities. It is difficult to conceive today that this could change.”

Gjedrem (2010) points out that Norges Bank has a special position in public administration. While ministries in Norway can easily issue instructions to their subordinate agencies, this provision sets strict and specific formal requirements for instructing the Bank. This power cannot be delegated by the Council of State to the Ministry of Finance. The Bank shall be consulted in advance and the Storting shall forthwith be notified of the reason for the instruction. The only time the power of instruction was exercised was when the inflation target was introduced in 2001.

¹⁷ See Gjedrem (2010)

Norges Bank is accountable

Norges Bank is required to provide an annual account of the implementation of its mandate. Norges Bank reports on the conduct of monetary policy in its annual report, which is submitted to the Ministry of Finance and communicated to the King and the Storting. Every year, the governor attends an open hearing on monetary policy in the Storting. In addition, the Ministry of Finance obtains an independent assessment of monetary policy in the form of yearly reports, called Norges Bank Watch.¹⁸ The assessments in Norges Bank Watch are also presented annually in the Government's *Finansmarknadsmeldinga* (Financial Market Report).

At the same time, Norges Bank is open about its activities and work processes. Norges Bank's work processes and professional standards are evaluated by external experts on a regular basis.¹⁹ There are no Norwegian benchmark institutions against which Norges Bank can be assessed – there is only one central bank. Norges Bank must therefore be assessed against the practice of other central banks.

Communicating monetary policy

Norges Bank's communication of monetary policy is adapted to the Executive Board's work methods. The governor and the deputy governor are chairman and deputy chairman, respectively, and only they speak on behalf of the Executive Board.

The degree of transparency regarding Norges Bank's interest rate decisions has increased gradually since inflation targeting was formally introduced in 2001. From an international perspective, the Bank has been a pioneer in many areas. For example, since 2005, Norges Bank has published three-year ahead key rate forecasts. Through such communication, the Bank indicates the interest rate path that it deems to provide an appropriate balance between the different monetary policy considerations. When the interest rate forecast reflects a monetary policy stance that strikes a reasonable balance, it enhances the predictability of interest rate policy. Norges Bank is open about the basis for its monetary policy decisions. The Bank's understanding of its mandate and of the framework for the implementation of monetary policy is documented and has been made public. The well-known economist John B. Taylor²⁰ has said the following about Norges Bank:

“The [sic] Norges Bank is a remarkably transparent central bank. As with the Swedish Riksbank, it announces not only its most recent interest rate decision, but also the likely path for its interest rate decisions in the future. While some have criticized publishing future interest rate forecasts, the experiences in Norway and Sweden show that there are advantages of such increased transparency.”

In its *Monetary Policy Report*,²¹ Norges Bank publishes forecasts for key macroeconomic variables for the next three years, including the Bank's own forecasts of its key policy rate.

¹⁸ The reports from Norges Bank Watch are available at: <http://www.bi.edu/research/research-centres/Centre-for-Monetary-Economics-CME/Norges-Bank-Watch/>. Norges Bank Watch is funded in part by the Ministry of Finance.

¹⁹ See e.g. Longworth and Rødseth (2003), Genberg et al. (2003) and Fridriksson (2010).

²⁰ See Taylor (2010)

²¹ Traditionally, Norges Bank has reported on monetary policy and discussed the outlook for financial stability in separate reports. The experiences of the financial crisis demonstrated that developments in the real and financial economy are closely interwoven. The Bank has concluded that it is of benefit to incorporate these analyses into a joint report with a view to their further development. From 2013, Norges Bank will publish four reports per year,

But the interest rate forecast is a forecast, and not a promise. The future is uncertain. Actual interest rate developments may therefore deviate from the Bank's forecasts.

Transparency about Norges Bank's reaction pattern is a necessary element in the interaction with fiscal policy. It is important that the Government and the Storting know the central bank's response pattern when the size of government budgets is decided. It is an advantage that the social partners also take this into account (see Qvigstad (2009)). One way the response pattern for monetary policy is communicated is through the "the criteria for an appropriate interest rate path".²² The criteria have been formalised by a mathematical loss function. The loss function must be viewed as a monetary policy tool.

Transparency surrounding the Executive Board's discussions has increased. The *Monetary Policy Report* contains the Executive Board's assessments and reflects its discussion of the monetary policy strategy.²³ This is in line with what is referred to as minutes by other central banks. The actual discussion of monetary policy takes place in an Executive Board meeting around two weeks prior to the publication of the *Monetary Policy Report*. On the basis of this discussion, a draft of the Executive Board's assessment is circulated among the members for their comments. These comments are incorporated into the final version. The Executive Board's assessment is available the same day that the *Monetary Policy Report* is published and the interest rate decision is announced, i.e. approximately two weeks after the actual monetary policy discussion took place. This is consistent with what other central banks' practice. They publish minutes two to three weeks after the monetary policy meeting. A press release is published after each monetary policy meeting, providing an account of economic developments of importance for the interest rate decision and of the Executive Board's assessments. After each monetary policy meeting, a press conference is held, led by the Governor or the Deputy Governor.

5 Summary

Recent decades have brought major changes in monetary policy, both in Norway and other countries. Central banks have become independent in the conduct of monetary policy. Decisions are made by a committee. There is no formula for deciding whether a collegial committee is better than an individualistic committee. Each system has its strengths and weaknesses.

There is now greater transparency surrounding the conduct of monetary policy. In the interest of democratic governance, this is important. A central bank must also communicate its expectations concerning interest rates and economic developments in order to make monetary policy more effective. The form this communication takes is likely to depend on how decisions are made in individual central banks.

The organization of monetary policy frameworks varies across countries. There is no internationally accepted best practice for communicating monetary policy. For example, how

which will form a decision basis for monetary policy and advice on countercyclical capital buffers, see <http://www.norges-bank.no/en/about/news-archive/2012/reports-on-monetary-policy-and-financial-stability/>

²² See *Monetary Policy Report* 1/2012 for a more detailed account of the criteria.

²³ See "The Executive Board's assessment" in *Monetary Policy Report* 3/2012.

detailed published minutes should be depends to a large extent on whether the monetary policy committee is collegial or individualistic.

However, there are also considerable differences in the structure of the minutes within each group. For example, there are greater differences in structure between Sveriges Riksbank and the Bank of England, which both have individualistic committees, than between Norges Bank with a collegial committee and the Bank of England with an individualistic committee.

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Appendix: Practice in other central banks²⁴

An account of various countries' frameworks for monetary policy committees, processes and communication is provided below.

Australia

The Reserve Bank of Australia has a target of 2–3 percent annual inflation on average in the medium term. The Reserve Bank Board has the decision-making authority for monetary policy. The Board has nine members, two internal members, the governor and the deputy governor, the Secretary of the Treasury and six external, non-executive members. The Board meets eleven times each year. Decisions are consensus-based and are published in a written statement by the governor, in which the governor provides a brief account of the background for the decision and the Board's assessment. Relatively brief minutes of the monetary policy meeting is published two weeks after the meeting, with an analysis of the economic situation and outlook and a short summary of the monetary policy discussion. The minutes do not include the views of individual members and do not disclose whether the decision was unanimous. No press conference is held. Four times a year, the bank publishes a *Statement on Monetary Policy*, which contains a detailed analysis of the economy and financial markets. The bank does not publish policy rate forecasts.

Canada

The Bank of Canada aims to keep the annual rate of inflation at the 2 percent midpoint of a control range of 1–3 percent. Interest rate decisions are made by the Bank of Canada's Governing Council, which is composed of the governor and five deputy governors. The bank has eight monetary policy meetings per year. Interest rate decisions are consensus-based and are announced in a press release, which is a summary of the background for the decision. Minutes are not published. Press conferences are held four times a year in connection with the publication of the Bank of Canada's *Monetary Policy Report*, which includes analyses and projections of economic developments. The bank does not publish forecasts for its policy rate.

New Zealand

The inflation target in New Zealand is between 1 and 3 percent annual rate of inflation on average in the medium term. Formal decision-making authority rests with the governor alone. In practice, the governor makes interest rate decisions after consultations with the Official Cash Rate Advisory Group, whose members include the two deputy governors and two part-time external advisers. There are eight assessments of the policy rate each year. Decisions are announced in a brief press release. Minutes are not published. Press conferences are held four times a year on the occasion of the publication of the bank's *Monetary Policy Statement*, which includes analyses and projections of developments ahead and the policy rate.

Sweden

The inflation target in Sweden is an annual inflation rate of around 2 percent. Sveriges Riksbank's Executive Board has decision-making authority for monetary policy matters. The Board is also responsible for the bank's entire operations. It comprises six full-time employed internal members: the governor and five deputy governors. The Board holds six monetary

²⁴ Source: The websites of the respective central banks. - Denmark's Nationalbank and Finland's Bank are not included. Denmark operates a fixed exchange rate policy, which means that monetary and exchange rate policy are geared towards maintaining a stable Danish krone against the euro. The formal policy framework is ERM2. Finland is a member of the euro area and as such Finland's Bank does not conduct an independent monetary policy.

policy meetings per year. Interest rate decisions are announced in a press release followed by a press conference. The press release contains a summary of the background for the Board's decision. Minutes of the monetary policy meetings are published two weeks after the meeting. The Board is an individualistic committee that does not attach weight to presenting a consensus view, nor does it. The minutes contain detailed information on the economic situation and outlook, as well as a detailed account of the Board's deliberations in which individual members are named. The decisions are made by vote, and the views and votes of individual members are disclosed in the press releases and in the minutes. Three times a year, the bank publishes the *Monetary Policy Report*, containing analyses and forecasts. In addition, three briefer *Monetary Policy Updates* are published in between the main reports. Sveriges Riksbank publishes policy rate forecasts.

UK

The inflation target is an annual inflation rate of 2 percent in the UK. At the Bank of England, decision-making authority rests with the Monetary Policy Committee. It has nine members, five internal and four external. The internal members comprise the governor, two deputy governors, the bank's chief economist and the executive director for markets. The Committee holds twelve meetings a year. Decisions are made by vote and published in a very short press release that only reports the actual decision. Minutes are published two weeks after the meetings. They provide a description of the economic situation and outlook and include a summary of the discussion at the monetary policy meeting, but do not link views to named individuals. However, individual members' votes are published. The Monetary Policy Committee also makes decisions on the scope of quantitative easing. Four times a year (six days after the monetary policy meetings), the Bank of England publishes its *Inflation Report*, containing analyses and forecasts. Press conferences are held in connection with publication of the *Report*. The bank does not publish policy rate forecasts.

Euro area – ECB

The ECB's target inflation rate is below but close to 2 percent over the medium term. Decision-making authority rests with the Governing Council, which currently has 23 members. Six of the members, including the president, sit on the ECB Executive Board, while the remaining 17 are governors of the central banks of euro area member states. The Council holds twelve monetary policy meetings a year. In practice, decisions are consensus-based. The decision is announced in a press release, and a press conference is held after the monetary policy meeting. Minutes are not published, but the ECB has gradually increased transparency about cases where there was not full agreement concerning certain decisions. Twelve times a year (one week following each monetary policy meeting) the ECB publishes a monthly report containing analyses of economic developments and financial markets. Four times a year, the report includes economic forecasts for the euro area. The ECB does not publish policy rate forecasts.

US

One of the monetary policy objectives of the Federal Reserve is price stability.²⁵ The Fed does not have a formally defined inflation target, but the Federal Open Market Committee (FOMC) has stated that “[t]he Committee judges that inflation at the rate of 2 percent, as measured by the annual change in the price index for personal consumption expenditures, is most

²⁵ According to the Federal Reserve Act, the Federal Open Market Committee shall seek “to promote effectively the goals of maximum employment, stable prices, and moderate long-term interest rates.”

consistent over the longer run with the Federal Reserve's statutory mandate.”²⁶. Decision-making authority rests with the FOMC, which has twelve members, all full-time employees of the Fed. The members include the chairman, the six other members of the Board of Governors and five regional Federal Reserve Bank presidents (the president of the New York Fed is a permanent member, the others serve on a rotating basis). The FOMC holds eight monetary policy meetings per year. Decisions are by vote and announced in a short press release with information on individual members’ votes. Four times a year (as from 2011), interest rate decisions are followed by a press conference. At the same time, the Fed publishes economic forecasts. After three weeks, the Fed publishes minutes containing extensive background information and an anonymised summary of the discussion, but which disclose members’ votes. A verbatim transcript is published after five years. As from 2012, the bank also includes policy rate indications as part of its economic projections.

Iceland

The Central Bank of Iceland operates with an annual inflation target of as close as possible to 2½ percent. Decision-making authority rests with a monetary policy committee with five members, the governor, deputy governor, the chief economist of the central bank²⁷ and two external members. The committee holds eight meetings per year. Interest rate decisions are announced in a press release, followed by a press conference. The press release includes the committee's assessments behind the decision. The background information for the committee's decision and a brief summary of the decision is published two weeks after the meeting. The decision is made by vote. The summary does not link views to named individuals, but states the number of votes for and against the decision, as well as abstentions. An overview of individual members’ votes during the previous year is published once a year in the bank's annual report. Twice a year, the bank publishes *Monetary Bulletin*, which includes analyses and forecasts. In addition, brief updates of the forecasts are published twice a year. The bank published policy rate forecasts in 2007 and 2008, but has not done so since autumn 2008.

All eight of these central banks publish the analyses and forecasts underlying their decisions. At three of the banks, the decisions are consensus-based, while four make decisions by vote; three of these disclose individual members’ votes. New Zealand is a special case, where decision-making authority formally rests with the governor alone. All eight announce decisions in press releases, seven hold press conferences, three after each monetary policy meeting, one after every other monetary policy meeting, and three in connection with publication of an inflation or monetary policy report, four publish minutes, with varying degrees of detail, one bank publishes complete minutes identifying discussion participants by name and two publish policy rate forecasts. Moreover, the senior executives of all the banks give speeches and lectures on different topics, including the conduct of monetary policy.

²⁶ See Board of Governors of the Federal Reserve System, Press release January 25, 2012. In December 2012, the FOMC announced the following in a press release: “In particular, the Committee decided to keep the target range for the federal funds rate at 0 to ¼ percent and currently anticipates that this exceptionally low range for the federal funds rate will be appropriate at least as long as the unemployment rate remains above 6½ percent, inflation between one and two years ahead is projected to be no more than a half percentage point above the Committee’s 2 percent longer-run goal, and longer-term inflation expectations continue to be well anchored.”

²⁷ Under the Act on the Central Bank of Iceland as amended, the third internal member shall be a senior monetary policy expert (i.e. it does not necessarily need to be the chief economist).