

Celebrity central bankers

Kenneth Rogoff | Harvard University | 10 November 2014

Why do the comments of major economies' central bankers command outside attention nowadays? It is not as if they change interest rates all of the time. Nor have they developed new, more robust models for analyzing the economy. On the contrary, major central banks' growth and inflation forecasts in the years since the financial crisis have consistently overestimated both growth and inflation – and by wide margins.

There are many good reasons for the attention lavished on monetary policymakers, including the rise of central-bank independence, public acceptance of the need to appoint highly competent technocrats to oversee the money supply, and the deepening of financial markets. And, many central bankers have been rightly lauded for their role in preventing a global meltdown during the financial crisis.

Even so, given the numerous uncertainties surrounding macroeconomic forecasts and the effects of policy instruments (not least quantitative easing), many academics find it puzzling that central bankers' speeches and statements generate so much fanfare. And, for all of their heroics during the financial crisis, many central bankers have been far too inflexible in the aftermath, worrying too much about overshooting inflation targets, and too little about deflationary dynamics. Moreover, central bankers bear a share of the blame for the crisis in the first place, mainly owing to lax regulatory policy.

Many central bankers portray former US Federal Reserve Chairman Alan Greenspan (who served from August 1987 until January 2006) as the culprit, saying that he projected an image of central-bank omnipotence that is not warranted in theory or practice. But this critique is overblown. Greenspan is long gone, but the focus on central-bank pronouncements is greater than ever.

What, then, is going on?

I would argue that, in addition to all of the factors listed above, three further considerations should be noted.

For starters, the public perception that central bankers are omniscient makes them an attractive whipping boy for politicians. Moreover, the digital revolution in media has elevated the role of business news, one of the few profit centers for print and broadcast journalism in many countries. Central bankers' pronouncements are of interest to business people – especially in the financial sector – and business people are of interest to advertisers.

Finally, and perhaps least appreciated, is the fact that central-bank policy pronouncements are almost unique in having clear and predictable effects on financial markets, at least in the

very short run (which can be a day or less). If Fed officials surprise markets by making more hawkish statements (suggesting an upward bias to policy interest rates) than investors were expecting, the US dollar will usually appreciate, long-term dollar interest rates will usually rise, and the US stock market typically will decline.

True, these effects may be small and transitory. But, unlike most of the reams of macroeconomic information with which we are bombarded every day, central bankers' speeches and opinions have relatively foreseeable effects, especially when the bank's chair, president, or governor speaks, or other officials speak in concert. And, with trillions of dollars swirling around global financial markets, this predictability creates a fat target, with investors willing to make massive bets when they are pretty sure they are right, even if the profit per dollar is small.

If you think I am exaggerating, consider the coverage of other economic news – say, unemployment, GDP, or the trade balance. Virtually every story quickly shifts its focus to what the data mean for monetary policy.

Some economic indicators, such as unemployment or inflation data, are indeed immediately important for central banks, because they may directly concern their mandates, and therefore have rather predictable effects. But much information is simply noise. This makes policy opinions that come straight from the horse's mouth almost uniquely valuable.

In short, there are many good reasons why central bankers receive so much media focus, including their relative independence and generally solid performance. But, there are also other reasons having to do with politicians' need for scapegoats, the media's struggle to reinvent itself in the Internet age, and central-bank pronouncements' predictable short-term effects on financial markets. These other factors have combined to create a bubble around central-bank pronouncements and decisions that grossly exaggerates their economic significance.

Is this a bubble that central bankers should worry about? The answer is clearly yes. The news bubble is of particular concern, because it reinforces the idea that central bankers somehow care disproportionately about financial markets, which is generally not the case.

Most central bankers really are targeting growth, inflation, and financial stability, if not necessarily in that order. The political bubble is an inevitable product of central-bank independence, and preventing monetary policy from becoming a target for elected officials requires constant effort. The predictability bubble is perhaps the trickiest to navigate, though my instinct is that less would be more. Exaggerated importance is one kind of bubble that central bankers should always be eager to burst.

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