



## The Czech National Bank's monetary policy in the media

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### ABSTRACT

This is an analysis of the favorableness and extent of the media coverage of the Czech National Bank's (CNB) monetary policy decisions in the period of 2002–2007. An extensive set of articles published in the four most relevant Czech daily broadsheets is used along with parameters of the CNB's actual monetary policy decisions, related communication and variables characterizing the economic environment. The most appealing results are that those CNB decisions that surprised financial markets were not negatively perceived by the media and that interest rate changes increased both favorableness and extent of media coverage. Therefore, from the media coverage point of view, there was no need for too much smoothing when setting the interest rates.

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### 1. Introduction

Transparency and communication are particularly important for those central banks that conduct their monetary policies within the inflation targeting framework. The Czech National Bank (CNB) has been applying this regime since 1998 and since then it has become one of the most progressive institutions concerning the openness of monetary policy among its peers. The CNB's efforts to become more and more transparent in terms of monetary policy decisions and their background have intensified recently, with some changes having been introduced to the existing set of communication tools. Filáček et al. (2007) present the reasons underlying the CNB's decision to start publishing interest rate forecasts in 2008. Moreover, the CNB has been publishing the votes cast by individual board members on interest rate decisions by name starting in 2008. And very recently, the CNB has decided to disclose the exchange rate trajectory consistent with its quarterly macroeconomic forecast as well.<sup>1</sup>

All these steps taken have been primarily oriented toward the financial markets and analysts, who are naturally the main target group of the CNB's communication on monetary policy decisions. As a matter of fact, inflation-targeting central banks are in general particularly highly dependent on the market perception of their policy decisions and

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<sup>1</sup> See the press release at: [http://www.cnb.cz/en/public/media\\_service/press\\_releases\\_cnb/2008/081106\\_nom\\_exchange\\_rate.html](http://www.cnb.cz/en/public/media_service/press_releases_cnb/2008/081106_nom_exchange_rate.html) (last accessed on 11 November, 2011) or the box in Inflation Report I/2009, pp. 6–7, available at: [http://www.cnb.cz/en/monetary\\_policy/inflation\\_reports/2009/2009\\_I/index.html](http://www.cnb.cz/en/monetary_policy/inflation_reports/2009/2009_I/index.html) (last accessed on 11 November, 2011).

communication.<sup>2</sup> A credible, accountable and transparent central bank should, however, also take account of the general public's perception of its monetary policy decisions.<sup>3</sup>

Unlike the sophisticated audience (markets, analysts), which is directly influenced by announcements made by the central bank (available, for example, on its web site), the general public is indirectly reached by the bank primarily through the media. The media's perception of monetary policy decisions and communication is thus important for the extent and quality of the central bank's influence on the general public and people's view of the credibility of the bank's monetary policy. Inversely, from the general public's point of view, monetary policy reflection in the media is undoubtedly crucial for assessing the role the central bank plays in the country's macroeconomic and monetary developments.

Taking the aforementioned into account, we find it appropriate and useful to take a look back at the media's perception of the CNB's monetary policy decisions in the period of 2002–2007. In doing so, we closely follow the methodological approach suggested by [Berger et al. \(2011\)](#), which can be considered pioneering work in this research area. In other words, our study is a national application of their novel multi-country oriented research and both their approach and their results serve as an obvious benchmark for us.

The above-mentioned time period seems very convenient for the purposes of our research, its results and their interpretation for at least two reasons. First, that period of time was characterized by quite smooth economic developments (see basic facts and figures on the past Czech economic developments in the Appendix, [Fig. A.1](#)) And second, in the above-mentioned period there were no major regime changes in either the conduct of the CNB's monetary policy (stable inflation targeting framework with forward-looking monetary policy reaction function incorporated in the forecasting model) or its communication (the initial level of transparency set in 1998–2002 prevailed roughly unchanged until 2008 where important steps substantially increasing transparency started to be taken).<sup>4</sup> The improvements in communication recently made in the CNB's communication – despite being oriented toward a rather sophisticated audience – could have somehow modified the pattern of the CNB's reflection in the media. From this point of view, it will be interesting to see how the results of potential future research on the topic will be influenced by including the communication changes made as well as the global financial and economic crisis and related negative tone recently prevailing in the media's reporting of economic events.

To unwrap our major results in brief, we can list the following. First, the media did not perceive negatively the fact that the CNB from time to time surprised financial markets with its interest rate decisions. And in turn, such decisions attracted the attention of the media, which led to more/longer/title page articles. And second, interest rate changes regardless of their direction were appreciated by and deserved special attention of the media. This is in our view the most appealing result of our research indicating that from the media coverage point of view there was no need for too much smoothing in interest rate setting.

As a matter of fact, monetary policy decision makers usually smooth interest rates when setting them in reaction to economic developments. As mentioned for instance by [Woodford \(2003\)](#), interest rate changes typically occur through a series of small adjustments in the same direction with only rare reversals of directions.<sup>5</sup> By doing so, central bankers aim at avoiding instability in financial markets and limit the number of large policy rate changes that could lead to a loss in credibility. As we see it, the extent of any central bank (including the CNB) boards' inclination to smoothing might be in this respect increased by its worries that big and frequent interest rate changes could potentially be negatively reflected in the media. These considerations, however, proved to be groundless based on the results of our research.

The remainder of the paper is organized as follows. The second section provides an overview of literature relevant to the topic of our research. The third section describes the data used and defines the variables we employ to characterize the media's coverage of the CNB Board's decisions on interest rate settings. The fourth section displays the results of our estimations, interprets them and discusses robustness issues. The last section summarizes and concludes.

## 2. Literature review

The growing importance of communication in monetary policy has initiated a substantial amount of research in this area over the last decade. In their survey, [Blinder et al. \(2008\)](#) suggest dividing the available literature into two main strands. The first strand analyzes the impact of communication on the financial markets, while the second one links the differences in monetary policy communication strategies across countries to differences in inflation performance in these countries.

Research on the impact of central bank communication on the financial markets has received relatively strong attention over the last decade. Typically, empirical studies examine how central bank statements move the financial markets. [Guthrie and](#)

<sup>2</sup> This is the case because longer-term interest rates, determined, inter alia, by market expectations of future monetary policy, play a key role in the actual decision-making of economic agents. And, accordingly, these longer-term rates (rather than the short-term ones under the direct control of a central bank) co-determine the ultimate macroeconomic outcomes the central bank aims to influence.

<sup>3</sup> This can be backed not only by the aim of a typical inflation-targeting central bank to affect the formation of people's inflation expectations, wage-bargaining and other price-setting processes. Another reason is that many central banks deal with challenges stemming from the fact that over time they have become almost fully independent of governments (even being sometimes accused of getting out of democratic control) and some form of accountability to the public is perceived as necessary.

<sup>4</sup> Simultaneously, Mr. Zdeněk Tůma was the only governor representing the CNB in the period of time under our scrutiny.

<sup>5</sup> This smoothing has traditionally had a reasonable background and has been examined widely and deeply in recent literature. For instance [Rudebusch \(2006\)](#) reminds us of two types of smoothing (short-run smoothing versus over the course of several quarters dynamic adjustment). Simultaneously he presents two sources of such an interest rate inertia, being either endogenous meaning deliberate gradualism (central bankers seek to smooth) in delivering the desirable monetary response, or exogenous, i.e. reflecting slow cyclical fluctuations in the key macroeconomic variables driving monetary policy.

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