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Dissent in monetary policy decisions

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ABSTRACT

Voting records indicate that dissents in monetary policy committees are frequent and predictability regressions show that they help forecast future policy decisions. This paper develops a model of consensual collective decision-making and dissent, and estimates it using individual voting data from the Bank of England and the Riksbank. Regressions based on artificial data simulated from the model show that decision-making frictions help account for the predictive power of current dissents.

1. Introduction

Dissents are a key feature of the minutes and voting records of monetary policy committees. Data from the committees at the Bank of England, the Riksbank, and the Federal Reserve show that dissents occur frequently: At least one member dissents in 63, 38, and 34 percent of meetings, respectively. On the one hand, it is not obvious that dissents should matter for policy decisions. By definition, a dissenting vote does not prevent the implementation of the policy preferred by the majority of members. On the other hand, in a setup where members interact repeatedly, a dissenter may have an effect on the future actions of fellow members and, hence, on policy.

In this paper, we report empirical evidence that a current dissent by a committee member is helpful in forecasting the future votes of other members. For instance, a current dissent in favor of an interest rate cut is a predictor of votes for an interest rate cut by other members in the next meeting. Then, it is not surprising to find that dissents are helpful in forecasting the policy decision of the committee as a whole, as was first pointed out by Gerlach-Kristen (2004) for the Bank of England, and is documented here for the Riksbank and Federal Reserve.[1] Also, we examine how the predictive power of dissents depends on the seniority and previous dissent rate of the dissenter. More specifically, we construct measures of dissent where dissenting votes are weighted according to either the tenure or the previous voting record of the dissenter. Results show that neither seniority nor "serial" dissent increases the predictive power of equally weighted dissenting votes. This latter result may be due to other members discounting dissents by members that have often dissented in the past.

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[1] In contrast, Meade (2002) uses FOMC dissents, both official ones in the minutes and verbal ones inferred from the transcripts, for the period 1992 to 1996 and finds that dissents do not help predict future policy changes. Andersson et al. (2006) analyze the effect of dissents on the yield curve in Sweden and find that the minority view, as reflected in the minutes published a few weeks after the policy meetings, has a quantitatively large but statistically insignificant effect on investors' expectations about future Repo rate decisions.

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This paper examines mechanisms through which dissent may help forecast future policy decisions. In particular, we focus on two frictions: (1) decision-making frictions arising from a desire to reconcile—by means of consensus—different views about the appropriate interest rate; and (2) size frictions arising from the fact that, in practice, the policy space is not continuous, but consists instead of interest rate changes in multiples of 25 basis points. Methodologically, we pursue the following approach. First, we formulate a model of committee decision making under consensus (or supermajority rule) where the policy space is discrete and current decisions are independent of dissents in the previous meeting. Using data from the Bank of England and the Riksbank, we estimate the model with both frictions. Then, we use simulations to study whether current dissents help forecast future policy decisions in regressions using artificial data generated from the model. Under the null hypothesis, the coefficient of our dissent measure would be statistically different from zero a proportion of times equal to the nominal size of the t-test. However, we find that the test over-rejects, suggesting that our mechanism is at play and can account for the predictability results; we provide an intuition for this mechanism and show that shock persistence magnifies its effect.

In order to disentangle the contribution of the two frictions considered, we estimate and simulate a version of the consensus model where the policy space is continuous (there are no size frictions) and a version where decisions are made by the median committee member but subject to size frictions (there are no decision-making frictions). Comparing results from the different models indicates that size frictions alone cannot account for the predictability in the data and counterfactually predicts a large positive autocorrelation in dissent.

Other mechanisms that could potentially account for the forecasting power of dissents are heterogeneity in preferences for interest-rate smoothing, and members' concerns for choosing the "right" decision and/or increasing their reputation. Regarding the former mechanism, we report statistical evidence that there is essentially no heterogeneity in smoothing preferences across members (Jung, 2013). Regarding the latter one, we develop a heuristic argument based on our ongoing research that suggests that in an environment with uncertainty about the state of the economy and private information, reputation concerns may not, but decision concerns could, generate predictability of future policy decisions on the basis of dissents. Given the preliminary nature of our work, we interpret this finding as a suggestion that decision concerns may complement decision-making frictions in accounting for the predictability found in the data.

The model of committee decision making extends the consensus model in Riboni and Ruge-Murcia (2010) in three directions. First, we relax the assumption that the composition of the committee is fixed over time. This is important for realism and because changes in composition imply changes in the identity of the key members under the consensus protocol. In turn, this means that the inaction interval—the set of status quo policies where policy changes are not possible—varies over time. Second, we assume that committee members can choose only among a discrete set of interest rate changes. Finally, the model incorporates a simple rule for registering dissents. This extension allows us to study the possible implications of dissents for monetary policy under a well-defined benchmark.

2. Empirical regularities

In this section, we examine the voting records of the monetary policy committees in our sample, propose measures of dissent that aggregate individual dissents into a time series, and study the power of those measures to forecast the votes of individual members and the decisions of the committee.

2.1. Voting records

The analysis is based on the voting records from three central banks, namely the Bank of England, the Swedish Riksbank, and the U.S. Federal Reserve.

For the Bank of England, we use the voting records of the Monetary Policy Committee (MPC) for the 148 meetings between June 1997 and August 2009.[2] The MPC consists of nine members of which five are internal, that is, chosen from within the ranks of bank staff, and four are external appointees. Internal members are nominated by the Governor, while external members are appointed by the Chancellor. Meetings are chaired by the Governor and take place monthly. Decisions concern the target value for the Repo Rate and are made by simple-majority rule on a one-person, one-vote basis. Prior to November 1998, the records report the interest rate preferred by assenting members and whether dissenting members favored a tighter or a looser policy. Thereafter, the records report the interest rates preferred by each member, including dissenters. These records are available at www.bankofengland.co.uk.

For the Riksbank, we constructed the voting records of the Executive Board (EB) using the minutes of the 81 meetings between February 1999 and September 2009. The minutes are available at www.riksbank.com. Under the Riksbank Act of 1999, the Executive Board consists of the Governor and five Deputy Governors. Meetings of the EB are chaired by the Governor and take place about seven times a year. Decisions concern the target value for the Repo Rate and are taken by

[2] Since the data were collected in the Fall of 2009, the samples for all central banks end in August/September of that year. We considered extending the sample beyond this period but, since monetary policy in the aftermath of the financial crisis has been implemented by means other than interest rate adjustments, it is not clear that recent voting records adequately capture the policy stands of committee members.