Mario Draghi: Accounts and accountability

Speech by Mr Mario Draghi, President of the European Central Bank, at the Euro50 Group Roundtable on "Monetary Policy in Times of Turbulence", Frankfurt am Main, 31 March 2015.

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Dear Edmond, dear members of the Euro50 group,

Thank you for inviting me to speak to you this evening. It is a great pleasure to be here.

Our monetary policy meeting in January this year was marked by two innovations. The Governing Council decided to expand its asset purchase programme to include public sector securities. And for the first time, a summary of that meeting's deliberations was published.

These decisions had the appearance of watershed moments – we had never before made purchasing government bonds a central tool of monetary policy,[1] nor had we provided accounts of our monetary policy meetings. But both decisions were in fact the logical extension of our monetary and communication policies over several years, and in particular when our interest rates reached the effective lower bound.

With interest rates at the lower bound, both the tools and the communication of monetary policy have to change. Asset purchases become the logical next step to expand the monetary policy stance; and enhancing transparency becomes the logical way to steer expectations and ensure accountability in an unprecedented new environment.

In other words, what took place in January was not a revolution but an *evolution*. And what I would like to talk about this evening is how our policy has evolved in particular in terms of transparency and accountability, with a special focus on the publication of our accounts.

Transparency as a source of accountability and effectiveness

The ECB has a primary objective of maintaining price stability which is given to us by the Treaty. Achieving that objective requires independence. Independence in turn requires accountability. And accountability requires transparency.

Central banks no longer subscribe to the dictum attributed to Montagu Norman, Governor of the Bank of England from the 1920s to the 1940s: "never excuse, never explain". We are not only accountable for achieving our mandate ex post, but we have an obligation to explain the decisions we are taking in real time to deliver price stability over the medium-term. For this a high degree of transparency is essential.

And transparency also has a second key benefit. To the extent that it facilitates a better understanding of monetary policy, it reinforces the transmission of our policy signals. A monetary policy strategy that is well communicated and well understood by markets and the public at large can support credibility and harness market expectations, which in turn makes it easier for us to attain our objective.

The more complex the environment in which monetary policy operates, the more important both these dimensions of transparency – accountability and effectiveness – become.

First, while policy decisions are never mechanical, in complex circumstances there is inevitably a greater role for judgement. This in turn means that there is a greater obligation to explain to the public why one course of action was chosen over another.

[1] The Securities Markets Programme was aimed at addressing specific frictions in financial markets that were hampering the transmission of standard monetary policy.

Second, complex circumstances increase uncertainty about how our monetary policy strategy is applied, which makes it harder for the central bank to steer expectations. So, more transparency and more active communication on our "reaction function" is needed.

Of course, the environment the ECB has faced in recent years has been anything but simple. Our approach to transparency has therefore naturally had to evolve.

This began with the forward guidance we introduced in mid-2013. As central banks reach the effective lower bound, and so can no longer use changes in short-term rates as a policy signal, communicating directly about the future path of rates and their response to a changing economy becomes more important. By introducing forward guidance we were able to increase our influence over the shape of the yield curve and, in doing so, partly shelter euro area money markets from developments elsewhere in the world, notably the US.

Through 2014 we continued to enhance our transparency by conveying our "reaction function" in broad terms – i.e. how we would respond to specific scenarios materialising over time. In particular, in a speech in Amsterdam in April last year I set out a number of contingencies and their corresponding monetary policy responses. The monetary policy measures taken through the year were fully consistent with the roadmap laid out then, culminating in the decision in January to expand our asset purchase programme.

This episode provides a clear example of the importance of transparency in establishing credible expectations and thus increasing the impact of monetary policy.

Anticipation of further easing measures had started to set in from the summer of 2014, in line with a progressive deterioration in the price outlook and the contingency plans we had laid out. Long-term nominal interest rates declined by around 100 bps from then until our January decision, precisely because we had communicated our reaction function and markets understood it. This is one reason why we have already been seeing positive effects, even though large-scale purchases of government securities only began in March this year.

To clarify our reaction function going forward, in my remarks at the European Parliament last week I discussed the conditions that will determine the duration and intensity of our expanded asset purchase programme, above and beyond our expressed intention to carry out our purchases until end-September 2016.

I stressed that the Governing Council will take a holistic perspective when assessing the path of inflation. We will evaluate the likelihood for inflation not only to converge to levels that are closer to 2%, but also to stabilise around those levels with sufficient confidence thereafter. When doing this assessment, the Governing Council will follow its monetary policy strategy and concentrate on inflation trends, looking through any surprise in measured inflation (in either direction) if judged to be transient and with no implications for the medium-term outlook for price stability.

This remains in line with our tradition of conveying the Governing Council's assessment in qualitative terms, also in the case of our forward guidance, rather than in quantitative terms, e.g. using numerical thresholds.

Opening up our monetary policy meetings

Perhaps the greatest innovation in our transparency and communication, however, has been the decision to publish an account of our monetary policy meetings – an issue that has been debated since the ECB was founded in 1999.

This is not to say that we have been opaque about our deliberations in the past. The ECB was a pioneer in establishing, from day one, monthly press conferences immediately following the Governing Council meeting, where the President and Vice-President face questions in real-time. The Federal Reserve only adopted this practice in April 2011 and at quarterly frequency.

However, we have taken the view that with transparency “more is not always better”. Especially in the early days of the ECB, when our credibility and the collegial nature of our decisions still had to be established, we put a premium on speaking to the public with one voice. Our concern was that published minutes or accounts could have compromised this – and I do not think this was unfounded.

At the time, even slight differences in messages between Members of the Governing Council were criticised by commentators as a “cacophony”, while differences of opinion within the Monetary Policy Committee (MPC) of the Bank of England, with its external members, were often praised as reflecting the richness of its discussion!

The point is that context matters. It is not enough just to communicate; the conditions also have to be in place for that communication to be well understood. In the view of the Council those conditions were not present then.

So what has changed now?

The main contextual change is that since late 2008 we have been, like all major central banks, increasingly resorting to unconventional measures to meet our mandate. Compared with conventional monetary policy (i.e. interest rates), these measures are less easy for the market to anticipate and their effects are less well understood.

This is because, first, unconventional measures can take many different forms and operate through different transmission channels. And second, there is no historical or statistical track record from which the market could deduce our policy reaction to a given set of circumstances.

Moreover, while monetary policy always has side effects, the unprecedented nature of some unconventional measures makes those effects more uncertain. For example, there are questions about possible trade-offs with financial stability and – uniquely for the ECB – potential distributional effects across countries. All this required more explanation.

So we decided that we needed to be more open with the public about how we reached our decisions. And, to better influence expectations, we needed to provide clearer guidance to the market about the rationale and impact of our measures and the factors that influence our decisions going forward. In other words, with the account we wanted to support both dimensions of transparency: accountability and effectiveness.

At the same time, we felt that the passage of time had put the Governing Council in a position where differences of views could be communicated without compromising the credibility and singleness of our monetary policy. Such differences are quite normal and should exist in any meaningful and diverse committee. And in any event, Council members can and do communicate their views individually through speeches and interviews. In our judgement there is no longer a reason to fear that reasonable debate will be confused with unhealthy division and unnecessary discord.

Still, transparency also has limits. Effective communication requires clarity and structure rather than merely the release of maximum information. As Einstein reminded us, one should “make things as simple as possible, but no simpler”, and the same applies to transparency: as much as possible, but no more. In particular, transparency must not come at the expense of clarity of communication and quality of decision-making.

In keeping with this, we have combined the move to publishing accounts with a decrease in the frequency of our monetary policy meetings. This enables a more thorough analysis of the medium-term implications of the flow of incoming data between meetings. And it is also more aligned with the schedule of economic projections prepared by the Eurosystem staff.

A lower frequency of meetings will not affect our ability to respond to new information in a timely manner. And it will in fact increase the value of information generated by each discussion, thereby ensuring that our communication contains more signal and less noise.

The specific features of our accounts

In general terms, our accounts are similar to established practice at other major central banks. They are intended to provide a richer summary and convey the flavour of the discussion among Governing Council members. But we have also made some specific decisions about the way we present our accounts that stand us out from other central banks.

Here there are three issues in particular that I want to focus on: why we do not attribute positions to individual Council members; why we publish accounts instead of minutes; and why we do not provide vote tallies.

First, the explanation for non-attribution lies in the specific institutional setting of the euro area and the unique communication challenges in a multi-country monetary union. This implies that in reporting on our monetary policy deliberations the independence of the members of the Governing Council must not be put at risk. They act in a personal capacity in the interest of the euro area, rather than as representatives of their countries of origin.

There is an argument that, in this context, attributing positions could actually be helpful, as it would act as an antidote against Governing Council members being overly influenced by national considerations. But our concern was the opposite: that any attribution of names to policy positions could all too easily be misconstrued or misinterpreted through a national prism.

We also felt that insulating members from such national scrutiny would be more conducive to maintaining an open and frank exchange of views, which is essential for the effectiveness of our collegiate decision-making. With similar reasoning the Warsh review commissioned by the Bank of England recommended for the MPC to preserve a “safe space” for discussions of a more explorative nature.

The inaugural edition of our monetary policy accounts was well-received. In the words of one observer, it clearly showed that the Governing Council had a thorough, serious and “sincere” exchange of views. And as those who have read the accounts will have seen, this way of presenting our discussions does not hide the different assessments and judgements of members on the course of action being proposed.

Still, while we see differences of views within the Governing Council as part of a healthy decision-making process, it is also very important to us to preserve the collegiality of its deliberations. This is why we have chosen to publish accounts of our monetary policy discussions rather than minutes.

Decision-making by committee reflects more than the sum of the pre-established views of its individual members. Views during the discussion can be “fluid” – which is after all exactly the purpose of discussing. Moreover, once a decision is made, what matters is the shared commitment of the Governing Council, in its entirety, to fully implement all decisions that have been taken. We did not want the publication of the accounts to detract in any way from these two crucial aspects of collegial decision-making.

In our view, providing a fair and balanced summary of the main arguments put forward was the best way to achieve this. And indeed, from this perspective our first attempt was successful. As the account of the January discussion shows, the final decision taken in the light of the discussion slightly modified the initial proposal under consideration. The Council decided to accelerate and frontload the impact of asset purchases by increasing the monthly asset purchase volume to EUR 60 bn, from the EUR 50 bn considered initially.

You will have noted that the language we use reflects our collegiate, consensus-oriented mode of discussion and decision-making. This includes qualifiers such as “broadly agreed” and “widely shared” which convey in broad terms the balance of opinion behind the assessment and arguments put forward. There is however no information to be extracted from the particular form of words used. The language should not in any way be construed in quantitative terms or linked mechanically to our policy decisions.

Finally, why do we not provide a vote tally?

In line with our collegial approach, the Governing Council has an established tradition of taking monetary policy decisions by consensus, without recourse to formal voting and without qualifying the decisions in any particular way. There are of course occasions when forging a consensus is not possible, and then the Council can take decisions by majority, be it small or large, as was the case with the January decisions. Nevertheless, not publishing a voting record allows members to support the decision of the committee, even if they may have personally preferred a different course of action.

Conclusion

Let me conclude.

Enhancing transparency is a logical step for central banks facing an increasingly uncertain environment. In different ways all major central banks have moved in this direction during the crisis, be it through forward guidance on their policy or enhancing communication with the public. And this is in my view a thoroughly welcome development. The days of central banks acting as opaque and secretive institutions should be consigned to the past.

More transparency benefits central banks by making them more accountable and effective. And in our case it also helps deal with the particular challenges of setting monetary policy in a multi-country monetary union.

Throughout the crisis citizens in some parts of the euro area have been calling on the ECB to do more, while elsewhere we have been called to do less. This is inevitable in a monetary union. But I trust that by publishing our account we can help the public to understand how all viewpoints are reflected and respected in our decisions, and how in the end we strive to take the decision that best serves the euro area as a whole.