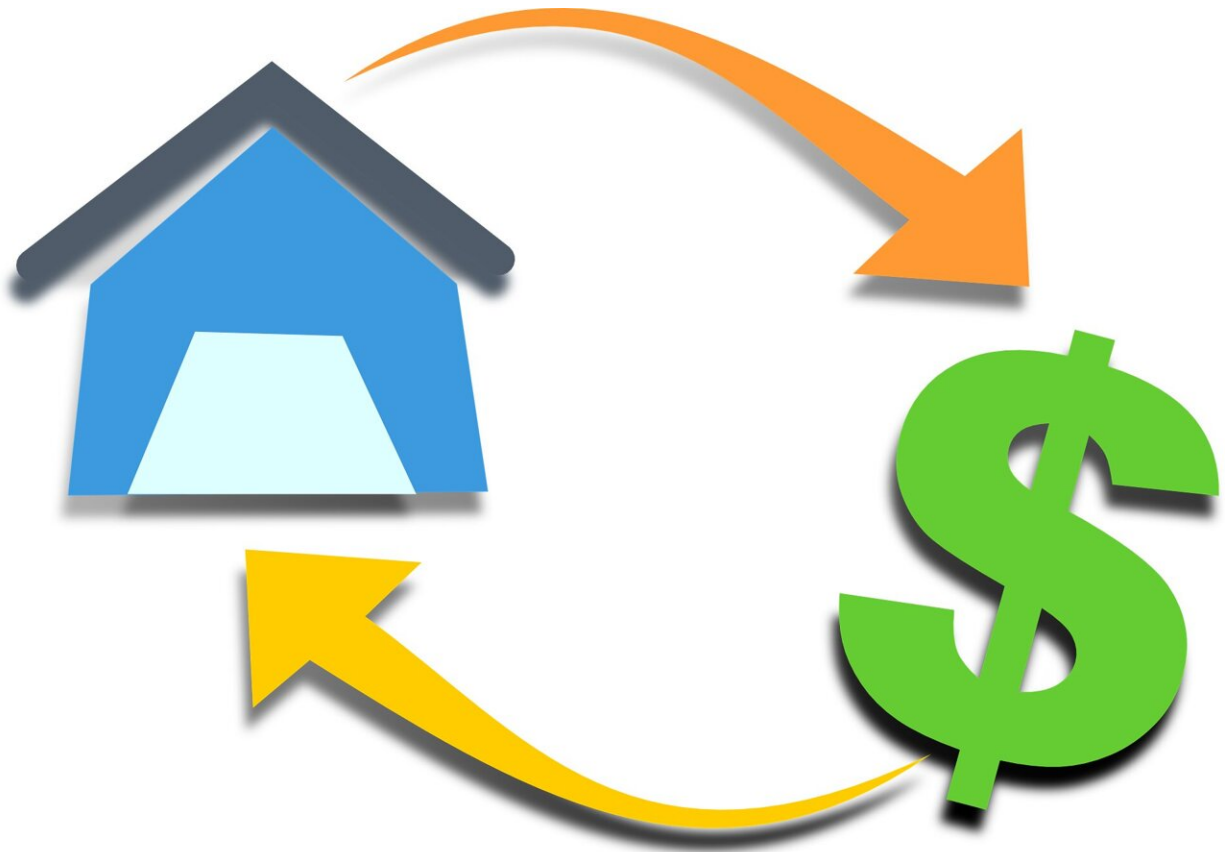


# When the Fed announces a new monetary policy strategy, do households listen?

May 5 2023

---



Credit: Pixabay/CC0 Public Domain

In August 2020, Federal Reserve Chair Jerome Powell announced a change in the Fed's inflation strategy: they would be implementing a strategy called average inflation targeting (AIT), which allows inflation

to move above and below the target rate of 2% so that it averages out to 2% over time. This differs from the previous strategy of traditional inflation targeting, in which the intent is to return inflation to the 2% target regardless of how long it has deviated from that rate.

But the impact of such a change depends on [households](#) and firms understanding the policy and acting in response to it. In the paper "Average Inflation Targeting and Household Expectations," published in the *Journal of Political Economy Macroeconomics*, Olivier Coibion, Yuriy Gorodnichenko, Edward S. Knotek II and Raphael Schoenle find that the Fed's new AIT strategy had little impact on household expectations—in fact, many people had not even heard of it.

The authors utilize data from a daily [survey](#) of consumers that has been running since March 10, 2020, weighting the [respondents](#) to ensure their sample is representative of the U.S. population. Among standard demographic questions, the survey asked respondents about where and how frequently they saw news about [monetary policy](#) or the Fed, about their understanding of the Fed's economic objectives, and what they thought the Fed would do under hypothetical economic scenarios.

The survey questions sought to determine if respondents understood that the Fed was using an AIT strategy and how such a strategy worked.

In the days following Powell's August 2020 announcement, the authors documented that only 33% of survey respondents reported hearing news about the Fed, with less than half of those people reporting they heard specifically about the Fed's new policy. This increase dropped off shortly thereafter. "Despite extensive coverage in the [news media](#), Chair Powell's speech apparently did not reach or register with the vast majority of the population," the authors write.

Along those lines, people who reported hearing news about the Fed in

the days after the announcement were no more or less likely than prior respondents to mention AIT as the Fed's monetary strategy. Only about 23% of survey participants correctly identified the strategy after the announcement. And households' broader economic outlooks were the same after the announcement, the authors report, with their expectations about [inflation](#), [personal income](#), and output growth remaining unchanged.

The authors wondered if it could take time for households to grasp the Federal Reserve's promise of a new strategy, so they repeated the same survey questions one year later in August 2021. While the percentage of respondents correctly identifying AIT as the Fed's current course of action rose slightly to 30%, "it remained the case that more households believed the Fed was pursuing IT than AIT," Coibion, Gorodnichenko, Knotek, and Schoenle report.

Finally, the researchers tested how being presented with information on monetary policy changed individuals' economic outlook. They divided their sample into three groups, giving one information on AIT, one information on IT, and another no information, and then questioned each individual on their economic expectations.

The authors find no difference between the responses of the groups who received the AIT or IT information. "Even when information about the new inflation strategy is presented directly to households and the strategy is clearly explained to them, it does not lead to discernibly different expectations than traditional inflation targeting," they write. "This finding suggests that AIT is unlikely to provide many of the economic benefits that theory often attributes to it."

**More information:** Olivier Coibion et al, Average Inflation Targeting and Household Expectations, *Journal of Political Economy Macroeconomics* (2022). [DOI: 10.1086/722962](https://doi.org/10.1086/722962)

Provided by University of Chicago

Citation: When the Fed announces a new monetary policy strategy, do households listen? (2023, May 5) retrieved 26 June 2024 from

<https://phys.org/news/2023-05-fed-monetary-policy-strategy-households.html>

This document is subject to copyright. Apart from any fair dealing for the purpose of private study or research, no part may be reproduced without the written permission. The content is provided for information purposes only.