**Discussant remarks on 'Trust in Central Banks' by Michael Ehrmann**

**RBA Annual Conference 2024 – Central Bank Communications**

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## 1. Introduction

In recent years, trust in central banks has declined significantly, a trend that has been particularly pronounced since the COVID-19 pandemic and the subsequent inflation surge. As inflation exceeded targets worldwide, many central banks, including the European Central Bank (ECB) and the Federal Reserve, were perceived as slow to respond, leading to a substantial erosion of credibility. This issue, however, is not entirely new; the Global Financial Crisis marked a pivotal point where public confidence in these institutions began to wane. Trust in the ECB fell from over 60% in its initial years to just 30% by the mid-2010s, and today, only about half of euro-area citizens express trust in the institution.

Michael Ehrmann's recent survey, *Trust in Central Banks*, brings together a wealth of research findings and practical insights on the evolving dynamics of public trust in central banking, offering a timely contribution as these institutions navigate heightened scrutiny. By presenting both an overview of existing literature and concrete strategies, Ehrmann provides central bankers with valuable guidance on policy execution and communication aimed at restoring and maintaining public trust. This discussion builds on Ehrmann's analysis and offers my perspective on the important role that central bank trust plays in shaping inflation expectations.

## 2. Inflation Expectations as a Measure of Central Bank Credibility: Benefits and Challenges

When assessing trust in central banks, we often turn to one fundamental question: is the central bank achieving its mandate? For most central banks, the key element of this mandate is price stability, typically defined by keeping inflation near a specific target. Thus, inflation expectations have become a primary gauge of central bank credibility, as they reflect the public's belief in the bank's ability to fulfill its inflation mandate.

The dominant approach involves comparing short-term inflation expectations—often one-year ahead—to the central bank's inflation target. This metric is popular partly because of the availability in household surveys, and the public is presumed to have a more tangible sense of near-term economic developments. Yet, as Ehrmann emphasizes, this reliance on short-term inflation expectations, while convenient, has its drawbacks.

In today's complex economic landscape, using short-term inflation expectations to judge credibility can be problematic for several reasons. First, inflation dynamics have and will continue to become more persistent due to structural shifts in the global economy, such as deglobalization, decarbonization, demographic changes, high debt levels, and rapid digitalization. These factors mean that inflation shocks can linger longer in the economy than in the past. During periods of economic stress, such as inflation surges or recessions, it may be unrealistic for individuals to anticipate a return to target within just one year—even if they ultimately believe in the central bank's capability to stabilize inflation over time.

Second, unconventional monetary policy frameworks that incorporate history-dependence, like Average Inflation Targeting (AIT) pursued by the Federal Reserve in 2020-2021, further complicate the use of short-term expectations as a credibility measure. With history-dependence, central banks commit to "making up" for past inflation deviations from the target by allowing inflation to overshoot or undershoot in subsequent periods. For these policies to be effective, the public must expect inflation to deviate from the target for a period longer than one year. Thus, a credible central bank might actually intend for inflation to remain above target temporarily, which short-term expectations could misinterpret as a lack of credibility.

To address these and other issues, Ehrmann and his coauthors have developed an alternative approach to measuring central bank credibility. In Ehrmann et al. (2023), they ask survey respondents a more direct question: "How likely do you think it is that the ECB will maintain price stability in the Euro area economy over the next three years?" This question has several advantages. First, it directly assesses whether people trust the central bank to achieve its mandate, rather than inferring credibility from inflation expectations alone.

Additionally, this three-year horizon is better suited to address the persistence of modern economic shocks, which may disrupt inflation targets for extended periods. A longer timeframe aligns more realistically with public perceptions of central banks' capacity to manage inflation in the face of enduring structural challenges. Furthermore, this approach is more accessible to individuals who may not be financially literate or comfortable with inflation forecasting and probabilities, providing a simpler and potentially more inclusive measure of credibility.

Finally, this more direct measure of trust is more adaptable to changes in central bank targets. If central banks revise their inflation goals in the future—a possibility that many are currently contemplating—this measure offers greater continuity, allowing us to compare data over time without recalibrating to a new target.

## 3. Broadening the Scope of Public Trust in Central Banks Beyond Inflation Management

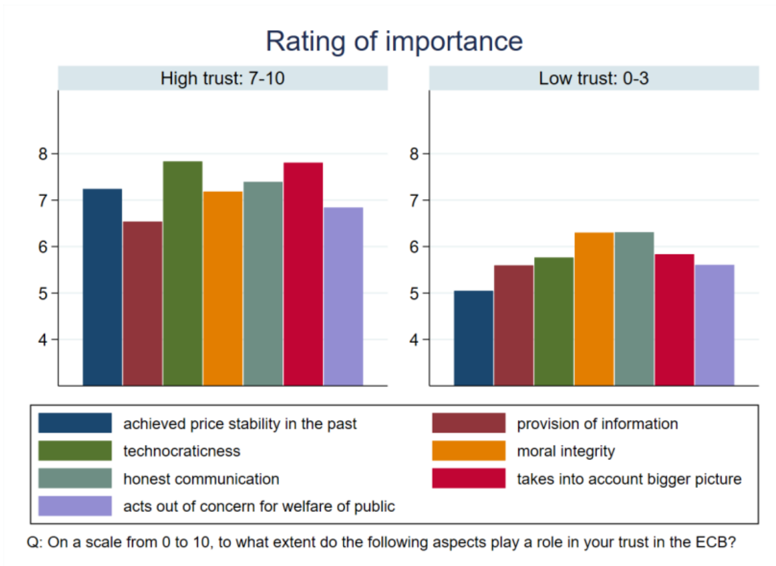
While inflation management is a critical aspect of central bank mandates, public trust in these institutions often depends on more than just inflation outcomes. Recognizing this, some central banks and researchers have adopted broader approaches to assess public trust, examining aspects of central bank performance that extend beyond inflation control alone.

For example, the Bank of Canada's surveys ask respondents to evaluate the central bank's ability to fulfill various elements of its mandate: its ability to maintain low and stable inflation, ensure the financial system works well, and contribute to successful management of the economy. Similarly, Bulutay (2024) investigates public perceptions of the European Central Bank (ECB) across multiple dimensions of its responsibilities, assessing not only inflation performance but also the central bank's broader roles and efforts.

In Eickmeier and Petersen (2024a), we explore the factors shaping German households' trust in the ECB. Our study asks respondents to rate their overall trust and to assess the importance of different factors that influence their view. Figure 1 presents the mean rating of each factor for low- and high-trusting respondents. Interestingly, we observe notable differences in what drives trust.

High-trust respondents, who are often highly educated, tend to care about nearly every aspect of the ECB's performance. However, they place particular emphasis on the ECB's past performance in managing inflation and the technocratic nature of the institution. This group values expertise, consistency, and the technical competence of central bankers, reflecting a more institutional view of trust.

*Figure 1. Factors influencing trust in the ECB.*




In contrast, low-trust respondents place relatively less importance on inflation management. Instead, they are more concerned with the people behind central banks—their integrity, honesty, and the transparency of their communication. This finding implies that, for low-trust groups, central banks might foster trust more effectively by enhancing transparency, communicating in more accessible ways, and demonstrating integrity rather than focusing solely on inflation performance. However, we note that low-trust respondents give low ratings on all attributes, suggesting that additional, unmeasured factors may be contributing to their mistrust.

Both high- and low-trust respondents report that the ECB's technical expertise[1] weighs more heavily in their institutional trust than its past success in achieving price stability. This technocratic aspect of central bank credibility can be assessed by comparing respondents' expectations to their published projections (Mokhtarzadeh and Petersen 2021; Coibion et al. 2024; Kostyshyna and Petersen, 2024). Using a different approach, Kril et al. (2016) ask surveyed respondents to assess the credibility of the Bank of Israel by rating, on a scale of 1 to 9, "to what extent do you believe that the Bank's forecast will be realized?" This method gauges institutional credibility without directly involving respondents' own inflation expectations, much like the approach of Ehrmann et al. (2023), but focuses specifically on respondents' confidence in the bank's technical proficiency.

**Implications for Central Bank Communication Strategies**

The ways we measure central bank credibility can significantly influence institutional communication strategies. If we rely solely on deviations of inflation expectations from target as an indicator of credibility, we may conclude that communication should focus on aligning the public's inflation expectations with targets.

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[1] Technocraticness of the ECB is described to respondents as "It makes its decisions on the basis of previously defined rules, technical analyses, scientific evidence, and facts."

However, by adopting broader measures—such as those that capture the public's views on technocraticness, transparency, integrity, and other institutional qualities—we gain insights into additional dimensions where trust may be faltering. These alternative approaches reveal specific avenues where central banks could engage with the public more meaningfully. Indeed, there is ever-growing evidence discussed in Ehrmann's survey that demonstrate the improved responsiveness of the public to more holistic communication.

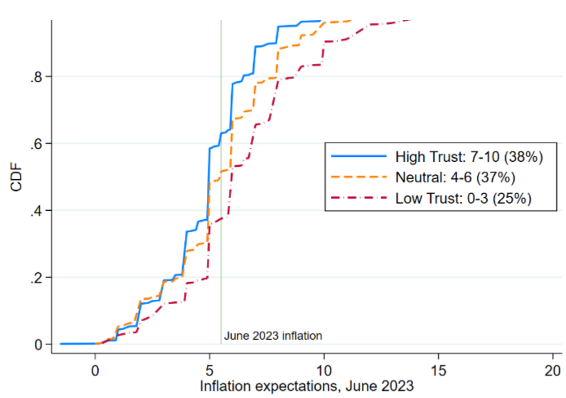
**The Role of Central Bank Credibility in Influencing Inflation Expectations**

A central assumption in central banking is that building public trust will help the institution achieve its inflation goals more effectively. Many studies report a negative correlation between trust in central banks and inflation expectations, suggesting that, to manage inflation, central banks need to cultivate public trust.

To examine this further, for this discussion I compare households' rating of trust in the ECB and one-year ahead point inflation expectations from the June 2023 (Wave 42) Bundesbank Survey on Consumer Expectations (BoP-HH). Empirical cumulative distribution functions of inflation expectations for high and low trust respondents are presented in Figure 2. Consistent with the literature, individuals with higher trust in central banks tend to report lower inflation expectations. Yet, the differences are often modest—typically around 1-2 percentage points across most of the distribution. Much of this difference can be attributed to education and numeracy skills, as people with higher trust might also be more familiar with inflation concepts.

Moreover, inflation expectations among the public are highly dispersed, regardless of trust levels. Among both high- and low-trust respondents, a wide range of inflation expectations persists, with many high-trust individuals still holding high inflation expectations. Almost no one, high-trust or otherwise, was predicting inflation exactly at the target rate of 2% within one year (or within 3 years), and few anticipated the actual inflation rate in June 2024 (2.5%). These patterns suggest that central bank credibility might not be as influential on inflation expectations as commonly assumed.

*Figure 2. Distribution of household one-year ahead inflation expectations (BoP-HH June 2023).*



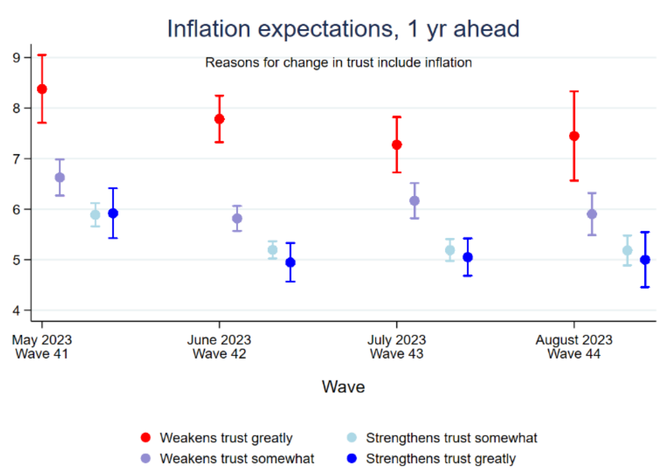

**Mixed Evidence from Causal Studies**

While correlation studies indicate a significant negative relationship between trust and inflation expectations, findings from experimental and intervention studies are more varied. Communicating about central bank tools, explaining mechanisms, or providing purely technical information may temporarily shape expectations but tends to fall short of building meaningful trust (Brouwer and De Haan, 2023; Bulutay, 2024). From my read of the literature, it seems that fostering household trust effectively often involves evoking an emotional response. Interventions that integrate inflation information with an emotional appeal have shown greater success in generating a trust-mediated impact on inflation expectations. For example, Bulutay (2024) finds that correcting German households' misperceptions about the ECB's forecast performance by informing them that "The ECB's projections for the euro area inflation rate deviated by less than one percentage point on average from the actual inflation rates in the period from 2001 (when the projections began) to 2021." can simultaneously increase trust and lower inflation expectations. Similarly, Niizeki (2023) shows that in June 2022 Japanese households' trust in the Bank of Japan declined, and inflation expectations rose following a controversial statement by then-Governor Haruhiko Kuroda: "Japanese households' tolerance of price rises has been increasing." This statement, made amid widespread hardship from inflation, was widely criticized and eroded public trust.

In Eickmeier and Petersen (2024b), we discuss results from an information intervention conducted in Wave 42 of the BoP-HH survey aimed at increasing trust in the ECB by highlighting its climate-related activities. We informed German households that the ECB is actively managing climate-related risks, supporting the green transition, and incorporating climate-relevant measures within its mandate. We then asked respondents two questions: (1) To what extent does the ECB's involvement in climate change affect your trust? and (2) Why has the ECB's involvement in combatting climate change strengthened or weakened your trust? By connecting these responses with participants' prior inflation expectations and observing changes over subsequent survey waves, we aimed to assess whether shifts in trust would correspond to changes in inflation expectations.

Our results revealed considerable heterogeneity in changes in self-reported trust in the ECB, based on its climate-related activities, with respondents providing various rationales for their increases or decreases in trust. However, respondents whose stated trust in the ECB increased or declined following the intervention did not significantly adjust their inflation expectations when resurveyed in subsequent waves of the survey. The same pattern emerges for respondents who reported that their change in trust was specifically related to the ECB's perceived ability or inability to fulfill its mandate (Figure 3), and when we alternatively consider three-year ahead inflation expectations.

*Figure 3.* Distribution of household inflation expectations, by wave and self-reported change in trust in the ECB.




These findings, together with the earlier work by Brouwer and De Haan (2023), puts into question the robustness of the relationship between central bank credibility and inflation expectations. While trust and credibility may bolster the central bank's reputation and encourage long-term acceptance of its policies, they may not consistently influence inflation expectations, especially when trust-enhancing strategies are not directly related to inflation itself. The persistence of inflation expectations, even when individuals report changes in trust—particularly among those attentive to central bank actions—indicates that other factors might play a more substantial role in shaping expectations.

## Concluding Remarks

Extensive experimental research, in the lab and through surveys, indicates that communicating inflation projections can serve as a highly effective guide for household inflation expectations, proving more relevant than information on inflation targets or past inflation (Mokhtarzadeh and Petersen 2021; Coibion et al. 2022; Kostyshyna and Petersen 2023, 2024; Hoffmann et al. 2024). While trust is important, it only becomes meaningful for inflation management when central banks demonstrate a strong commitment and track record in meeting their targets. The public needs to see evidence of competence and reliability through visible progress on inflation targets and successful forecasting. Past performance, especially recent successes, is critical to building and maintaining credibility (Rholes and Petersen 2021; Ahrens et al. 2023; McMahon and Rholes 2023; Bulutay 2024). This involves not just sharing projections but also showcasing achievements—demonstrating to the public that the central bank is "doing a good job."

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