The Central Bank Crystal Ball: Temporal information in monetary policy communication
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Abstract
Effective central bank communication provides information that the public does not have but wants to learn. Rather than arising from private information per se, we argue that the public's information deficit reflects three main channels: (i) an updated evaluation of the state of the economy based on past data, (ii) a different projection from the state to the likely future evolution of the economy, and (iii) differences in the reaction to the economic outlook. This paper provides a methodology to quantify the temporal information in the text of central bank communication. Both the backward-looking evaluation and forward-looking projection channels significantly improve the ability to explain the news in yields around ECB announcements compared with topic-based text analysis. We also show that speeches generate greater news in yields the larger the information deficit remaining after the previous ECB Governing Council press conference.