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NOTES AND CONTRIBUTIONS

INTRODUCTION TO THE SPECIAL ISSUE ON 'CURRENT ISSUES IN CENTRAL BANKING'

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Abstract
The recent surge in inflation has led to an increase in research by academic economists into various aspects of central banking: in particular, central bank communication and trust in central banks. In addition, the move towards introducing Central Bank Digital Currency has increased the need for research in this area. This Special Issue of the *National Institute Economic Review* brings together some of this recent research and includes contributions from academic and policy-oriented researchers and leading experts on these recent developments in central banking research.

Keywords: central banks; central bank digital currency; central bank communication; trust in central banks

JEL Codes: E42; E51; E52; E58

When the New Labour government were elected in 1997, one of the very first things they did was to grant operational independence to the Bank of England. Between 1997 and 2022—the 25th anniversary of this event—the Monetary Policy Committee of the Bank of England kept inflation very close to the target. Indeed, over the 25 years from the second quarter of 1997 to the first quarter of 2022, CPI inflation averaged 2.00%! However, since then, CPI inflation surged to a peak of 11.1% in October 2022 before falling back to 1.7% in September 2024. This poor performance has led some to question the independence of the Bank of England as well as strongly criticise the bank's communication. In addition, this has brought to the fore the recent academic research into central bank communication and trust in central banks.

While this was happening, the Bank of England has also been investigating the case for issuing the Central Bank Digital Currency (CBDC), specifically, the 'digital pound'. In essence, a digital pound would be like a digital form of cash. The Bank of England would issue it directly, and individuals would be able to hold their digital pounds in a digital wallet and spend them in shops or online. The Bank of England published a consultation paper in 2023, and a response to the more than 50,000 responses they received to the consultation in January 2024. Currently, the Bank has moved into the 'design phase', where they will look at the technology required for a digital pound, how its introduction might affect monetary policy, and how it would work in a practical sense. Having done that, they will make a decision as to whether to introduce it or not. Other countries have moved faster than the Bank of England with, for example, the Bahamas, Jamaica and Nigeria having already introduced a CBDC and countries such as China and India running CBDC pilot schemes. However, there are big questions around the introduction of a CBDC, including what it might mean for the monetary transmission mechanism, how payments using CBDC will be cleared, how providers of digital wallets might be compensated, and to what extent transactions made using CBDC will be private. In addition, such questions have proved to be a fruitful area for academic research.

This Special Issue of the *National Institute Economic Review* brings together some of the recent research on CBDC, central bank communication and trust in central banks, and includes contributions from academic and policy-oriented researchers and leading experts on these recent developments in central banking research.

In their contribution to this Special Issue, Ramon Adalid, Lorenzo Burlon and Maria Dimou (European Central Bank) examine the potential impact of adopting a CBDC on the monetary transmission mechanism. Although the central bank balance sheet identity ensures that the introduction of CBDC will not create a funding scarcity for the banking system as a whole, it could still lead to a less favourable funding mix for banks, which in turn could to restrictions in credit supply, which could adversely affect the monetary transmission mechanism. Specifically, if the demand for CBDC is large, and the banks experience adverse funding conditions, resulting from, say, collateral constraints or liquidity shortages, then bank lending conditions could be adversely affected, with implications for the monetary transmission mechanism. However, the authors argue that the central bank can limit the negative effects of the CBDC rollout by carefully designing and implementing it, as well as through careful communication. Furthermore, the central bank could maintain its desired monetary policy stance by taking specific actions to prevent or neutralise these unwarranted impacts. Finally, the authors argue that a CBDC could encourage digitalisation and competition within the banking sector.

In their contribution to this Special Issue, Alfred Duncan and Joao Pedro de Camargo Mainente (University of Kent) review two important questions relating to the introduction of CBDC. First, they ask how providers of digital wallets might be compensated for this service. They consider two possibilities. In the first case, the Central Bank remunerates their holdings of wholesale CBDC at Bank Rate, whereas retail CBDC is unremunerated. In the second case, the wallet provider would simply charge a fee for each transaction made using CBDC. They find little difference between the two cases in the effort that wallet providers would exert to prevent fraud. They then consider how CBDC payment might be cleared. One case would be that, similar to traditional interbank clearing, reserves are transferred from the paying bank to the digital wallet. However, this would leave banks open to a high risk of a 'run' unless CBDC payment values were strictly limited. Alternatively, the central bank could fill the gap in the paying bank's reserves at the same time as crediting the digital wallet. However, this would leave the central bank exposed to individual bank risks.

In their contribution to this Special Issue, Michael McMahon and Lovisa Reiche (University of Oxford) use data from the Bank of England's 'Inflation Attitudes' survey to examine differences between men and women in inflation perceptions, inflation expectations, and attitudes towards inflation. They find little difference between men and women in inflation perceptions and expectations, although women seem to be more uncertain about inflation and care more about it. During periods of high inflation, men push for higher wages, whereas women increase their savings. The authors do find differences between men and women in their financial knowledge and trust in the Bank of England, suggesting that there may be a case for the Bank of England to tailor its communications towards men and women differently. Specifically, they suggest that the Bank could improve women's financial understanding and increase their satisfaction with the Bank through diverse messaging.

In her contribution to this Special Issue, Carolina Garriga (University of Essex) also uses data from the Bank of England's 'Inflation Attitudes' survey to assess the determinants of trust in the Bank of England. She finds that aggregate public trust in the Bank of England fell with the poor inflation performance of recent years. However, for individuals, trust depends on the level of the individual's knowledge about the Bank, whether they own their house or rent, how old they are and whether they are male or female.

In their contribution to this Special Issue, Cristina Bodea and Andew Kerner (Michigan State University) and Masaaki Higashijima (University of Tokyo) examine whether there is a difference as to how central bank communication is received based on whether the person delivering the message is male or female. They used an online survey experiment to test this, sending participants in the experiment Bank of Japan communications, but randomly assigning these communications to either a male or a female member of the Monetary Policy Board. They found that participants in the survey were less likely to trust the Bank of Japan and its ability to deal with inflation if it were represented by a female policymaker rather than a male.

Finally, in their contribution to this Special Issue, Nicole Baerg (University of Essex) and Carola Binder (Haverford College) explore the use of factual versus emotional statements within central bank communication. They develop a new method for classifying statements made in central bank speeches into those which are factual and those which are emotional, which enables them to assess how much central bankers rely on emotional appeals to their audience as part of their communication strategies. The method they use results in a customised classification, but this only slightly outperforms more traditional methods based on supervised learning approaches, while the results of applying these older approaches are easier to interpret.

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