Abstract

Central banks worldwide have become more transparent. An important reason is that democratic societies expect more openness from public institutions. Policymakers also see transparency as a way to improve the predictability of monetary policy, thereby lowering interest rate volatility and contributing to economic stability. Most empirical studies support this view. However, there are three reasons why more research is needed. First, some (mostly theoretical) work suggests that transparency has an adverse effect on predictability. Second, empirical studies have mostly focused on average predictability before and after specific reforms in a small set of advanced economies. Third, less is known about the effect on interest rate volatility. To extend the literature, I use the Dincer and Eichengreen (2007) transparency index for twenty-four economies of varying income and examine the impact of transparency on both predictability and market volatility. I find that higher transparency improves the accuracy of interest rate forecasts for three months ahead and reduces rate volatility.