Discussion of "Risk Management in Monetary Policy: A Review with Asset Pricing Implications"

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What the Paper Does

- Monetary policy *tilt*: forward-looking component of monetary policy, over and above current policy actions. Generally in the form of directional bias (towards tightening or easing). Revealed through communication.
- Empirical properties of two language-based measures of the tilt: the HD score (Hawkish minus Dovish statements) and an LLM-based indicator (+1,0,-1).
- Key findings

(i) MP tilt explained by perceptions of risk and uncertainty, over and above expectations $\Rightarrow$ risk management
(ii) MP tilt has an impact on financial markets: a tightening tilt reduces the term premium

- Two case studies in risk management: 1990s productivity miracle and 2000s post-covid episode

General Comments

1) Review of a very interesting research program, with some new results

2) Focus: risk management and the tilt

- But risk management factors can also drive *current* policy actions, and *current* policy actions can presumably influence risk.
- So why a (nearly) exclusive focus of the paper on the "tilt"?

3) Languaged-based measures from FOMC transcripts (5 year lag).

- Why not real-time communications? (press conference, speeches, etc.)

4) Missing: financial crises

- Key aspect of risk management in monetary policy
- Woodford (2012), Svensson (2017),..., Boissay-Collard-Galí-Manea (2025)

5) Presentation

- Long list of empirical findings, new and old. *All* interesting.
- But the order of presentation may not be the most logical

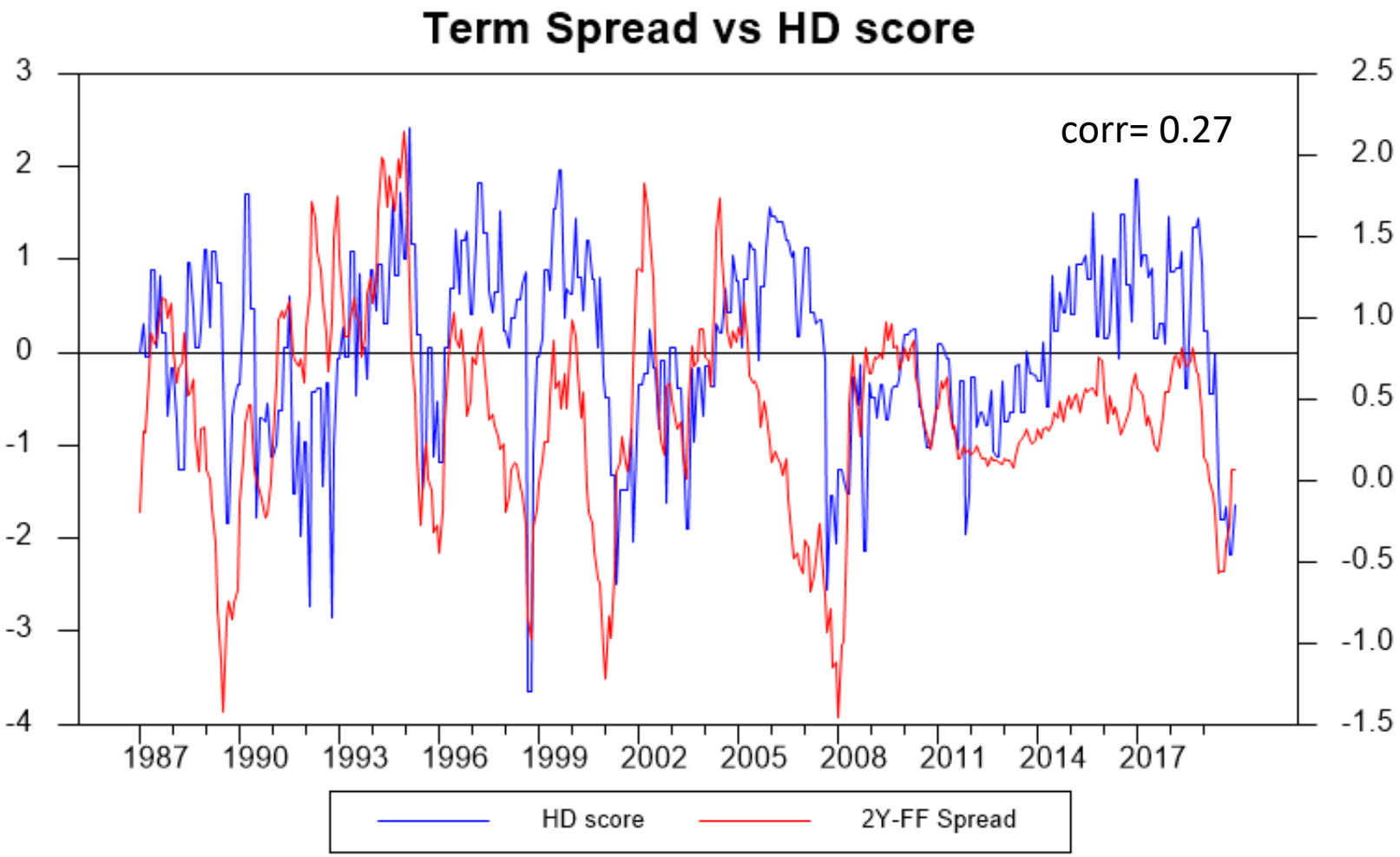
Empirical Findings

1) HD score explains the "official tilt" (83-99)

- Both reflect intentions.
- Not much surprising, but sanity check

2) HD score explains future changes in Federal Funds rate

- Fed tilt is informative, not just verbal noise.
- Not addressed: Are language-based measures of the tilt reflected in corresponding *market-based* measures? Intended vs perceived
- Evidence: HD score vs 2Y-Yield minus FFR Spread


Term Spread vs HD score
corr= 0.27
3
2
1
0
-1
-2
-3
-4
2.5
2.0
1.5
1.0
0.5
0.0
-0.5
-1.0
-1.5
1987
1990
1993
1996
1999
2002
2005
2008
2011
2014
2017
HD score
2Y-FF Spread

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- Evidence: HD score vs 2Y-Yield minus FFR Spread
- Forecasting policy rate changes:

$$f_{t+12} - f_t = \underset{(0.07)}{-0.70^{**}} + \underset{(0.09)}{1.29^{**}} spread_t \quad ; \quad R^2 = 0.31$$

$$f_{t+12} - f_t = \underset{(0.06)}{-0.16^{**}} + \underset{(0.07)}{0.44^{**}} HD_t \quad ; \quad R^2 = 0.09$$

$$f_{t+12} - f_t = \underset{(0.07)}{-0.67^{**}} + \underset{(0.09)}{1.19^{**}} spread_t + \underset{(0.06)}{0.25^{**}} HD_t \quad ; \quad R^2 = 0.34$$

Empirical Findings

3) HD score explains Romer-Romer monetary policy shocks

- Interesting, but not obvious interpretation
- Consistent with *exogenous* MP shocks being persistent, with MP driven by first moments and disconnected from risk factors
- Suggestion: explore whether RR shocks are explained by uncertainty and tail risk factors

4) Inflation uncertainty and real economy sentiment explain HD score and LLM-based measures of tilt

- Key finding of the paper
- But LLM-based tilt also explains *current* policy actions (Table 1)

A. Dependent variable: FOMC policy action, ΔFFR_t or $ActionLLM_t$

	$\Delta FFR_{t-1,t}$		$ActionLLM_t$	
	(1)	(2)	(3)	(4)
$BoRLLM_t$	0.12***		0.29***	
	(5.45)		(7.59)	
$InfPMU_t$		0.045**		0.096**
		(2.48)		(2.32)
$EcoSent_t$		0.052**		0.11**
		(2.31)		(2.47)
Controls	Yes	Yes	Yes	Yes
R^2	0.43	0.39	0.39	0.36
ΔR^2	0.073	0.053	0.12	0.11
N	259	259	259	259

B. Dependent variable: FOMC policy tilt, $TiltLLM_t$

	$TiltLLM_t$					
	(1)	(2)	(3)	(4)	(5)	(6)
$BoRLLM_t$	0.68***	0.60***	0.58***			
	(11.15)	(7.58)	(7.96)			
$ActionLLM_t$		0.22*	0.017			
		(1.67)	(0.13)			
HD_t				0.42***		
				(7.09)		
$InfPMU_t$					0.32***	0.27***
					(4.26)	(4.38)
$EcoSent_t$					0.30***	0.16**
					(4.25)	(2.46)
$F_t(\pi_4) - \tau_t$			0.49***	0.31***		0.48***
			(5.66)	(3.08)		(3.89)
Controls	No	No	Yes	Yes	No	Yes
R^2	0.49	0.51	0.62	0.50	0.40	0.51
N	259	259	259	259	259	259

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- Suggestion: explore whether RR shocks are explained by uncertainty and tail risk factors

4) Inflation uncertainty and real economy sentiment explain HD score and LLM-based measure of tilt

- Key finding of the paper
- But LLM-based tilt also explains *current* policy actions (Table 1)
- Suggestions:

(i) show corresponding evidence for HD score
(ii) use same explanatory variables in regressions for current action as used for tilt
(iii) show increase in R^2 resulting from uncertainty and sentiment variables

Empirical Findings

5) A tilt towards tigthening reduces the term premium

- Authors' interpretation: $\uparrow$ policy credibility, $\downarrow$ uncertainty, etc
- Interpreted as suggesting effectiveness of MP tilts...
- ... but it works against policymakers' intentions!

Why would a Fed in an easing mood (e.g. ZLB) want to see an increase in term premia?

Concluding Remarks

- Great paper
- Big picture and detailed findings about a very interesting research program
- I look forward to further instalments!