

Forward guidance

@econcortex

2026-09-22

Abstract

Delphic versus Odyssean guidance, the Fed's calendar and threshold promises, and the puzzle that models predict effects far larger than the data show.

When the short rate cannot fall, the central bank can still move the *expected path* of short rates, and long rates with it. Forward guidance is communication about future policy used as an instrument in its own right. It had existed informally for decades; at the lower bound it became explicit, dated, and sometimes conditional on numbers.

Two kinds of guidance

Campbell, Evans, Fisher and Justiniano introduced a distinction that every later discussion uses (Campbell et al., 2012).

Definition 1 (Delphic and Odyssean guidance). **Delphic** guidance is a forecast: the central bank shares its view of the outlook and of how it will react, without binding itself. **Odyssean** guidance is a commitment: the central bank ties itself to a future path, as Odysseus tied himself to the mast, so that it will not re-optimize once the bound stops binding.

Only Odyssean guidance implements the Eggertsson–Woodford prescription from The effective lower bound. Delphic guidance can even be contractionary: if the announcement of low rates for longer is read as news that the outlook is worse than thought, expectations of income fall and spending with them. Distinguishing the two in the data is the central difficulty of the empirical literature.

The Federal Reserve's sequence

The Fed's statements after 2008 show the escalation from vague to precise.

- **Qualitative (December 2008):** rates would stay exceptionally low “for some time”, later “for an extended period”.
- **Calendar-based (August 2011):** exceptionally low rates “at least through mid-2013”, pushed to late 2014 in January 2012 and mid-2015 in September 2012.
- **Threshold-based (December 2012):** rates would stay near zero at least as long as unemployment remained above 6.5 percent and projected inflation stayed below 2.5 percent. This is guidance conditioned on the state of the economy rather than on a date, which is closer to a rule.

Calendar guidance has an obvious flaw: it does not say whether the date reflects a bad outlook (Delphic) or a promise (Odyssean). Threshold guidance is more informative, but thresholds are not triggers, a point the Fed had to explain repeatedly as unemployment approached 6.5 percent in 2014.

Does it work? The forward guidance puzzle

In the standard New Keynesian model of The Taylor principle and determinacy, guidance is extraordinarily powerful. The IS curve iterated forward makes today's output gap depend on the *sum* of all expected future real rate gaps:

$$x_t = -\frac{1}{\sigma} \sum_{k=0}^{\infty} \mathbb{E}_t (i_{t+k} - \pi_{t+k+1} - r_{t+k}^n). \quad (1)$$

A promise to hold the rate 25 basis points lower for one quarter ten years from now has the same effect on x_t as the same cut today, and the Phillips curve compounds the inflation response. Del Negro, Giannoni and Patterson named this the **forward guidance puzzle**: the model implies effects of announcements far larger than anything observed (Del Negro et al., 2023).

Two families of explanations followed. McKay, Nakamura and Steinsson showed that with incomplete markets and precautionary saving, households discount future income more heavily, which breaks the equal weighting in (1) and cuts the power of distant promises sharply (McKay et al., 2016). The other family relaxes rational expectations: if only part of the public pays attention to central bank statements, or if agents have bounded horizons, distant guidance is heavily discounted as well.

Measured effects

Swanson separated forward guidance from asset purchases in Fed announcements by their distinct signatures across the yield curve and found that guidance moved short- and medium-term yields with effects comparable to conventional rate changes, while purchases moved longer maturities (Swanson, 2021). Guidance is therefore a real instrument, with effects in the observed range rather than the model’s, and it fades when the horizon exceeds a few years.

Practical lessons

- Guidance is only as credible as the central bank’s willingness to deliver it later, which is why state-contingent language beats dates.
- It works best in combination with Asset purchases: channels, which signal the same commitment through actions.
- The ECB’s “lower for longer” language from 2013 and the SNB’s conditional inflation forecast are Delphic by construction; both banks avoided Odyssean commitments, which limits what guidance can do for them.

Campbell, J. R., Evans, C. L., Fisher, J. D. M., & Justiniano, A. (2012). Macroeconomic effects of Federal Reserve forward guidance. *Brookings Papers on Economic Activity*, 2012(1), 1–80. <https://doi.org/10.1353/eca.2012.0004>

Del Negro, M., Giannoni, M. P., & Patterson, C. (2023). The forward guidance puzzle. *Journal of Political Economy Macroeconomics*, 1(1), 43–79. <https://doi.org/10.1086/722734>

McKay, A., Nakamura, E., & Steinsson, J. (2016). The power of forward guidance revisited. *American Economic Review*, 106(10), 3133–3158. <https://doi.org/10.1257/aer.20150063>

Swanson, E. T. (2021). Measuring the effects of Federal Reserve forward guidance and asset purchases on financial markets. *Journal of Monetary Economics*, 118, 32–53. <https://doi.org/10.1016/j.jmoneco.2020.09.003>