



# SPEAKING POINTS

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## What role for monetary policy in achieving inclusive and sustainable growth?

- I intend to say a few words about the role of monetary policy in achieving inclusive and sustainable growth.
- I would like to start by saying that in general, a well-balanced monetary policy, including a price stability target, contributes to sustainable growth, and that sustainable growth is normally positive for equality.
- Achieving the monetary policy goal of keeping inflation low and stable leads indirectly to positive effects on equality, as households with low incomes don't have the possibility to shield themselves from the costs connected with high and volatile inflation.
- The press release from 15 January 1993, when the inflation target in Sweden was announced, stated: "Price stability is a prerequisite for sustained economic growth as well as full employment and it prevents an arbitrary redistribution of income and wealth".
- If inflation is higher than expected, borrowers benefit because the value of their debts declines, while lenders and those with large savings lose out. This type of large, arbitrary redistribution between lenders and borrowers was common in Sweden during the 1970s and 1980s, but is now history.
- On the other hand, households with low incomes also suffer if inflation is too low due to low aggregate demand. These households are usually very exposed to the business cycle and, more often than not, face unemployment and lower living standards when there is a trough. So, again, low and

stable inflation is an important contribution from monetary policy.

- When looking at effects on equality, there are different channels from monetary policy at play.
- These include the exchange rate, effects on stock prices, house prices and the labour market.
- Low interest rates increase demand and are often associated with higher share prices and house prices. As shares are typically owned by high income earners, this increases the capital income for those at the upper part of the income distribution<sup>1</sup>. House ownership is normally more evenly distributed than shares<sup>2</sup>, so higher house prices would have smaller effects on equality.
- The labour market channel is sometimes ignored when analysing the monetary policy effects on equality. This effect is not easy to calculate, but it is an important channel.
- When attaining an inflation target, this normally goes hand in hand with an economy avoiding too much of booms and busts in the business cycle and less swings in unemployment. Less uncertainty over economic developments and economic policy is good for investment, and hence for growth and labour market outcomes. So, labour market developments are important for income equality.
- In recent years, in order to meet their price stability targets, many central banks have pursued a very expansionary policy, including low or even negative policy rates, as well as purchase programmes of securities. These policies have attracted criticism, saying they increase inequality, but I disagree.
- Given the weak trend in growth in many countries, a less expansionary monetary policy than pursued during recent years would have led to higher unemployment than was the case. In that sense, monetary policy could be argued to have contributed to lower income inequalities, as unemployment could lead to large negative effects on household income. Many of those households, who would have experienced unemployment, would then have fallen to lower income deciles, contributing to higher income dispersion. Most studies that include the labour market effect come to the conclusion that the overall effect of expansionary monetary

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<sup>1</sup> See Deutsche Bundesbank (2016).

<sup>2</sup> See Deutsche Bundesbank (2016).

policy on inequality is that it slightly decreases it. Or in short, the dampening effect of lower unemployment offsets the effects from higher share prices. But the overall effect seems, if any, to be small.

- To sum up, the very expansionary monetary policy conducted during recent years in some countries could be argued to have had a positive net effect, albeit small, on equality. The positive employment effect normally seems to dominate over the negative effects<sup>3</sup>.
- We at the Riksbank don't per se take equality into consideration when taking monetary policy decisions. It is not part of our mandate. This is more effectively done by fiscal policy. I don't believe any other central bank specifically takes this into account either.
- But going forward, the Swedish parliamentary committee on finance has asked the Riksbank to evaluate the distributional effects of the expansionary monetary policy in recent years. So this is an area we are working on now and will continue to do so.
- As the theme of this conference is "reshaping globalisation" I would like to end by adding some words about my views on the global perspective on equality and the possible explanations for increased inequality in many developed economies during recent decades. As I have said, the contribution from monetary policy to equality should in my view in general be minor.
- I do not think you can talk about globalisation without also talking about technology. Some argue that increased inequality in many countries is due to the latest technological progress having been skills biased, resulting in a rise in the skill premium and the decline of some labour market institutions in advanced economies, emerging markets and developing countries<sup>4</sup>. The decline of labour market institutions includes lower trade union membership, which reduces the relative bargaining power of labour, and more flexible labour market institutions that can pose challenges

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<sup>3</sup> See, for example, the effects of the monetary policy pursued by the Federal Reserve in connection with the financial crises in Bivens (2015), the effects of monetary policy in the USA since 1980 in Coiboin (2016), the effects in advanced economies since 1990 in panel data-analyses in Furceri et al. (2016) and effects of the monetary policy conducted by the ECB in connection with and after the financial crises, with a focus on Germany in Bundesbank (2016).

<sup>4</sup> One example is that a decline in trade union membership (union rate) reduces the relative bargaining power of labour, exacerbating wage inequality (Frederiksen and Poulsen 2010). Another is that more flexible labour market institutions (although positive for reallocating resources to more productive firms and enabling firm restructuring) can pose challenges for workers, especially those with low skills, and hence play an important role in explaining inequality developments (Alvaredo et al 2013).

for workers with low skills. Technological progress combined with globalization seems to have played at least some role in increasing inequality within countries.

- The discussion of the effects of globalization is interesting. Globalization has for long been a natural part of the Nordic economies. Our dependency on foreign trade is much higher than the global average. There is among the Nordic countries an acceptance on the positive long term net effects on productivity, growth and employment. Globalization creates opportunities for new jobs.
- The reason for the positive view on globalisation in the Nordic countries might be a broader social security net and public policy that help people who lose their jobs due to trade as well as technology. Training and education improve employability and reasonable replacement ratios in unemployment benefit and other social benefits can mitigate the negative short-term effects of globalization. These are all fiscal or structural policy issues, outside the scope of monetary policy, but still important in a global perspective.
- To summarize: Globalisation and technology are strong forces that rapidly shape the world. Policymaking is needed to facilitate the changes that ensue for individuals, companies, the public sector and countries as a whole. In that policymaking, I want to stress that each and every policy area should do what it does best to make good contributions when the changes are being managed.
- Thank you!

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