Written submissions

The Bank of Canada posted an open invitation on its website for Canadians to send formal submissions, such as official letters or papers, to express their views about the monetary policy framework and what they think the Bank's priorities should be. We received submissions from organizations, academics and economists:

- Competition Bureau of Canada
- Peter Dietsch, Université de Montréal and member of the Advisory Board of the Council on Economic Policies
- Greenpeace
- Erin Weir, Op Ed – Toronto Sun
- Edward Cheung, Author
- Guy Dauncy, Author
- Michel Darveau, Citizen

Submission by the Commissioner of Competition to Bank of Canada Consultation: Renewing Canada's Monetary Policy Framework

October 1, 2020

Introduction

I have read with interest, the Opening Remarks from the Bank of Canada's recent workshop on the renewal of Canada's Monetary Policy Framework.[1] In those remarks, Senior Deputy Governor Wilkins recognizes the important interaction between monetary policy and other public policy in supporting economic growth and price stability within the Canadian economy. This submission underlines the significant contribution that competition considerations can have in the broader economic policy context.

As Commissioner of Competition, I have a mandate to advocate for policies at all levels of government that support vibrant, competitive markets in this country.[2] This mandate flows from the long-understood principle that the competitive process is essential to ensuring a dynamic, resilient, and productive economy. My perspective is straightforward: to be at its best, Canada needs more competition.

Through this submission, I aim to reinforce that idea by focusing on three areas where competition supports better economic outcomes. The first is an explicit recognition of how the competitive process lowers inflationary pressures – bringing about the "good" disinflation that allows Canadians to access a wider range of products at lower prices. The second point is that greater competition is key to unlocking the type of productivity gains that matter so much to the continued wealth and prosperity of Canadians. Finally, the third is that, in a world of increasing marketplace concentration, we all need to adapt our approaches to preserve and maintain competitive vigour in the economy.

[1] Wilkins, C.A. (2020) "Opening Remarks of Carolyn A. Wilkins, Senior Deputy Governor" at the Bank of Canada Workshop: Toward the 2021 Renewal of the Monetary Policy Framework.

[2] See, for example, sections 125 and 126 of the Competition Act, R.S.C., 1985, c. C-34.

Competition Lowers Inflationary Pressures

At a basic level, competition is the rivalry between businesses that makes them work harder to win customers. However, competition is not just about delivering goods to market at the lowest possible price. Competition unlocks economic value by motivating entrepreneurs to re-imagine all aspects of a business: developing products that better address the desires of consumers, more efficiently producing and distributing goods, and retailing those products in innovative and valuable ways.

Businesses compete with each other along a number of different dimensions. While some businesses may choose to pursue a strategy of making products available for the lowest possible price, others may focus on marketing a product of the highest quality, or developing a product that is on the leading edge of technology. Competition benefits Canadian consumers through lower prices, greater choice, and increased levels of innovation.

Each of these outcomes has a deflationary effect on the economy. Through the competitive process, consumers receive lower quality-adjusted prices that are both measureable and impactful – an effect that is extensively studied.[3] As Governor Macklem noted in a 2014 speech, competition unlocks "good" disinflation in the economy.[4]

Competition Drives Productivity

International studies consistently link higher levels of competition with greater innovation and productivity.[5] The competitive process drives continuous improvement by ensuring that those businesses that can produce the most output with the fewest inputs will thrive, while releasing those less equipped to other productive uses in the economy. This effect ensures higher economic productivity, which increases the wealth and economic well-being of Canadians.[6]

[3] See, for example, Pryzbyla, M. and Roma, M. (2005) "Does Product Market Competition Reduce Inflation?" European Central Bank Working Paper No. 453.

[4] Macklem, T. (2014) "Flexible Inflation Targeting and 'Good' and 'Bad' Disinflation". Remarks at Concordia University, John Molson School of Business.

[5] OECD. (2014) "Factsheet on how competition policy affects macro-economic outcomes".

[6] See, for example, World Bank. (2019) "The World Bank Productivity Project".

The link between greater competition and higher levels of productivity is broadly understood. In 2008, the Canadian government enacted a review panel to study the nation's competition policy. In its final report, entitled *Compete to Win*, the review panel noted both that: "the primary drivers of productivity growth are the investment, innovation and adaptation fostered by openness and competition", and that "Canada must improve its productivity by increasing competitive intensity."[7]

These are not merely theoretical conclusions. In the 1990s, Australia embarked on a substantial overhaul of its competition policy. This initiative modernized Australia's economy by increasing competition policy scrutiny of some industries, and deregulating and extending competition in others. According to a subsequent National Inquiry, these reforms contributed significantly to a 13-year economic expansion in Australia.[8] Of particular note, this National Inquiry found that Australia's competition policy reforms were directly responsible for increasing GDP by 2.5 percentage points per year.

A Competition Culture Will Reinvigorate the Canadian Economy

Central bankers across the globe recognize the growing importance of pro-competitive policy-making. This interest has often focused on the impact of changing market structures resulting from the digitalization of markets, rising market concentration, and the rise of the "superstar firm".[9] Moreover, I would be remiss not to mention the significant contributions of Senior Deputy Governor Wilkins to this ongoing policy dialogue.[10]

As the digital economy disrupts and reshapes markets, authorities across the globe face a new set of challenges. For Canadian consumers and businesses to thrive in a digital economy, policy-makers need to seize opportunities to encourage competition and

[7] Competition Policy Review Panel. (2008) "Compete to Win". Final Report to the Minister of Industry.

[8] Government of Australia Productivity Commission. (2005) "Review of National Competition Policy Reforms". Inquiry Report No. 33.

[9] See, for example, Willis, J.L. (2018) "Changing Market Structures and Implications for Monetary Policy: An Introduction to the 2018 Economic Policy Symposium"; G7 Finance Ministers and Central Bank Governors. (2019) "Chair's Summary: G7 Finance Ministers and Central Bank Governors' Meeting"; and IMF. (2019) "Chapter 2: The Rise of Corporate Market Power and its Macroeconomic Effects" in *World Economic Outlook: April 2019*.

[10] See, for example, Wilkins, C.A. (2019) "Why Do Central Banks Care About Market Power?" and Wilkins, C.A. (2018) "At the Crossroads: Innovation and Inclusive Growth".

innovation in areas that matter to Canadians. That is why I have made it a top priority to emphasize vigorous law enforcement and competition promotion in digital markets.[11]

This links to a broader theme that I have championed in recent months. That is, if we truly want Canadians to thrive in the digital economy, we must develop a culture that embraces competition. Achieving a competition culture means that policy-makers will ensure that their policies actively support a competitive Canadian economy. To aid in realizing this goal, the Competition Bureau has recently published a toolkit that seeks to help policy-makers more explicitly consider competition in their policy processes.[12]

Conclusion

Canada needs more competition. Greater competition delivers better consumer results, and improves a broader range of macroeconomic outcomes. A greater focus on competition can act in concert with monetary policy in order to ensure the wealth and prosperity of all Canadians.

A nation does not inherit a strong competitive marketplace; it creates one by considering competition in the development of public policy. Canada has the potential to reap the real benefits of a strong culture of competition in our new economic reality, but it requires focus and collaboration. I encourage all levels of government to engage with us to work toward a better balance between regulation and competition.

Establishing a competition culture will neither happen overnight nor be achieved by any one organization on its own. I applaud the Bank of Canada for its ongoing work to highlight the role that pro-competitive policies can play in Canada's economic agenda. I hope that you will continue to consider competition as a key part of your research program going forward; the Competition Bureau is ready to do all that it can to deepen that focus.

Matthew Boswell
Commissioner of Competition

[11] Competition Bureau. (2020) "2020-2021 Annual Plan: Protecting Competition in Uncertain Times" and Competition Bureau. (2020) "Competition in the Digital Age: The Competition Bureau's Strategic Vision for 2020-2024".

[12] Competition Bureau. (2020) "Strengthening Canada's Economy through Pro-Competitive Policies".

CEP council on economic policies

Legitimacy Challenges to Central Banks: Sketching a Way Forward

Peter Dietsch

January 2020

Discussion Note 2020/2

Abstract

Delegation to independent agencies (IAs) can reap real benefits for policy making. In the case of monetary policy, it shores up the credibility of the central bank. However, it is generally accepted that the discretion of IAs needs to be constrained to ensure their legitimacy.

This paper aims to deepen our understanding of the link between delegation and legitimacy by considering the following challenge to the legitimacy of central banks: Their legitimacy is under threat due to the unintended consequences their actions have on inequalities in income and wealth on the one hand, and on the environment on the other. To frame these challenges, the paper builds on the distinction between input versus output legitimacy. The paper shows that this distinction highlights an important difference between the two policy contexts. It subsequently presents and analyses different strategies of institutional design to enhance the legitimacy of central banks vis-à-vis the two challenges.

Acknowledgements

This article is an expanded version of a letter published in the *American Political Science Review*, see Dietsch (2019). While the discussion of legitimacy in the face of distributional trade-offs is essentially the same as in that letter, the analysis of the influence of environmental sustainability issues on legitimacy is new. In addition, the discussion of the concept of legitimacy as well as of some of the potential institutional responses has been expanded. I thank Alexander Barkawi for his detailed and very helpful comments on the paper. I am also grateful to François Claveau, Clément Fontan, and Pierre Monnin for many discussions on the ethical dimensions of monetary policy.

About the Author

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One of the founding principles of democratic states is that citizens, at the ballot box, can influence who runs the country and how they run it. However, there is a clear trend in Western democracies in recent decades to deliberately insulate parts of decision-making from political influence by delegating them to independent agencies (IAs) (e.g. OECD 2002) and, thus, remove them by one step from democratic control.

The principal justification for this kind of delegation lies in its capacity to correct for political short-termism and to overcome the challenge governments face to credibly commit to certain policies. Next to the judiciary, one paradigmatic example of independent agencies today are central banks.

The promise of granting central banks operational independence lies in credibly committing to a lower inflation target compared to a monetary policy under direct political control. Yet, as in other contexts, central bank independence (CBI) comes at a potential cost. The double delegation to IAs – from the polity to government, and from government to the IA – can undermine their legitimacy.

The question of how we are to weigh the benefits and costs of delegation to IAs deserves more attention. Tucker (2018) argues that for the "unelected power" of IAs to be legitimate, a number of delegation criteria need to be respected.[1] For example, the policy objective of the IA needs to be one that can be specified; society's preferences with regard to the policy issue in question need to be reasonably stable, and so on (*ibid*.: appendix).

This article focuses on two kinds of challenge to the legitimacy of central banks in particular, both of them based on the observation that contemporary monetary policy has important spill-over effects that undermine societal objectives other than those included in central bank mandates. More specifically, the first challenge zooms in on one of the delegation criteria proposed by Tucker, namely the idea that "[t]he IA will not have to make big choices on distributional trade-offs" (*ibid*.). In the context of unconventional monetary policy, I argue, it is unrealistic to expect central banks to respect this constraint. Similarly, according to the second challenge, any monetary policy that undermines environmental sustainability, for instance by exacerbating rather than contributing to reduce carbon emissions, *a fortiori* weakens the legitimacy of the central bank. In both cases, the question arises of how to respond to these legitimacy challenges institutionally.

The argument proceeds in three steps. Section 1 rehearses the case for delegation to IAs as well as Tucker's account for why this delegation needs to be carefully designed to be legitimate. It spells out Tucker's delegation criterion barring central banks from making distributive choices, and extends the logic of Tucker's account to cover environmental sustainability issues. Section 2 fills in the empirical premises of the debate: If central bank actions today do indeed have significant spill-over effects on distribution and on

[1] For another recent contribution on the ethics of delegation to central banks and thus on their legitimacy, see van't Klooster (2019).

environmental sustainability, this raises important questions about central bank governance. Finally, section 3 sketches some preliminary responses to these questions. More specifically, I put forward a menu of institutional design options to allow independent central banks to meet the challenge that the spill-over effects of their policy pose to their legitimacy.

1 Why and how to constrain the discretion of central banks

The economic theory case for CBI rests on the argument of time inconsistency (Kydland & Prescott 1977; Barro & Gordon 1983). Any government agency that cares both about inflation control and about employment will be tempted to use inflation surprises to stimulate employment. Rational agents anticipate this and thus revise their inflation expectations and wage demands upward. The result is an unchanged level of employment with higher than necessary inflation. By contrast, an independent central bank is able to credibly commit to an inflation target.

While the details of the time inconsistency argument are subject to debate (e.g. Forder 1998; Goodhart 1994), there is consensus in theory and practice that monetary policy faces commitment problems,[2] and that granting independence to the monetary policy authority can help overcome them with the right institutional design (see Keefer and Stasavage 2003).

For an agency such as a central bank to be considered *independent*, several conditions need to be fulfilled. Those running the agency need to have job security, and the agency needs to have control over policy instruments as well as some autonomy in determining its budget (Tucker 2018: 11). Despite some institutional variation, modern central banks tend to meet these criteria.

From a systemic perspective, removing certain policy choices from elected officials can deliver substantive benefits. However, this strategy also bears risks. As highlighted in the introduction, the creation of independent agencies removes the policy choices in question by one step from democratic control. Whereas citizens can collectively change governments, independent agencies are not directly accountable to voters. As Jon Elster puts it, “very independent courts and banks may be a remedy more dangerous than the disease.” (Elster 1994: 66-7)

Two issues have to be distinguished here. First, as highlighted by the extensive literature on optimal principal-agent contracts, there is the question of when delegation to bureaucrats is

[2] Tucker (2018: 103) identifies “three manifestations of the problem of commitment [that] can be labelled (1) intrinsic time inconsistency, (2) electoral politics, and (3) sectional capture”, where the latter refers to the co-optation of decision-makers by vested interests. While the literature has traditionally focused on the importance of insulating central banks from *government* to overcome these commitment problems, the problem of sectional capture also points to the importance of insulating central banks from *financial markets*. (see Dietsch *et al.* 2018: chapter 3)

efficient in the sense of utility-enhancing for citizens (e.g. Alesina & Tabellini 2008).[3] Models in this category make assumptions about the incentives of politicians (e.g. re-election) and bureaucrats (e.g. career concerns) in order to then identify circumstances under which delegation tends to be or tends not to be preferable. Legitimacy is either not a concern in this literature, or quickly dealt with by requiring that the mandates of IAs remain subject to review and reform by elected officials (*ibid.*: 444).

The second issue, and focus of this paper, is precisely the question of under what circumstances the policy-making of an IA can be considered *legitimate*. To isolate this issue, I shall assume that we are dealing with a policy area where delegation to an IA is efficient, as is plausibly the case in monetary policy. The challenge at hand is thus to square the circle between the independence of institutions such as central banks on the one hand, and the need to ensure their legitimacy on the other.

For a political body, independent or not, to be legitimate, it needs to provide a justification of the coercive political power it exercises over citizens (cf. Peter 2017).[4] Different types of justification are eligible to play this role. For present purposes, let us distinguish two. First, the normative authority of the political body and thus its legitimacy may be grounded in the fact that its members are subject to direct democratic control. The slogan "no taxation without representation" is emblematic for this position. We believe that certain kinds of decisions need to be made by elected representatives in order to be legitimate. Second, the normative authority of the political body may be grounded in the broad social usefulness of the political outcomes that its actions promote. When we can ascertain this social usefulness without making important value judgements, direct democratic control seems less important. In fact, political influence may even be viewed as a hindrance. Let us call these two conceptions "input legitimacy" and "output legitimacy" respectively.[5]

Once we establish the link between the issue of legitimacy and IAs, two observations should be made up front. First, intuitively, for equal levels of coerciveness, an IA will need to answer to a higher standard of justification compared to elected officials, due to its independence.[6] Applied to the context of monetary policy, a justification that goes beyond the kind of efficiency-considerations discussed above is required for handing independent

[3] In these models, efficiency represents a placeholder for the value of utility maximization. This is not the only sense in which efficiency is used in the economic literature (see e.g. LeGrand 1990), but it is the use from which I wish to delineate the issue of legitimacy here.
[4] For important contributions to the literature on legitimacy, see for instance Buchanan 2002; Peter 2008.
[5] See Rosanvallon (2011: 8) for this distinction. Rosanvallon attributes it to Goodin (2003), but the latter arguably uses the distinction in a different sense.
For completeness sake, I should mention a third conception of legitimacy that, in a way, represents a more refined version of input legitimacy. It maintains that for a political body to be legitimate, it has to not only be subject to direct democratic control, but this control also needs to take a deliberative form (cf. Goodin 2003; Peter 2017). For simplicity, I shall set this third conception aside here.
[6] For a treatment of the legitimacy of IAs in political theory, see Rosanvallon 2011.

central banks the power to print money, influence interest rates, and – via inflation – effectively tax economic agents.[7]

Second, there is a clear affinity between the very purpose of IAs and the idea of output legitimacy: We create IAs precisely because we believe that they can deliver better results than the standard political process. By contrast, the nature of IAs is at odds with the idea of input legitimacy. One of the challenges at the heart of this paper is how to resolve the tension between the two conceptions of legitimacy in the context of central banks. An additional tension, this time within the paradigm of output legitimacy, can arise when pursuing the goals of an IA enters into conflict with policy objectives pursued by other government agencies. As van't Klooster (2019) points out, in such cases the legitimacy of the IA depends on the alignment of its policies with broader societal objectives. Incidentally, this idea was not lost on the authors of many current central bank mandates. For example, Article 127 (1) of the Treaty on the Functioning of the European Union (the Lisbon Treaty) states that "[w]ithout prejudice to the objective of price stability, the ESCB [European System of Central Banks] shall support the general economic policies in the Union with a view to contributing to the achievement of the objectives of the Union as laid down in Article 3 of the Treaty on the European Union."[8]

In short, a system of checks and balances is needed to ensure that the IA does not abuse its power but remains sensitive to the political preferences of the population despite not being up for re-election. Traditionally, these checks and balances include both *ex ante* measures such as limiting central banks' mandates to 'operational' as opposed to 'goal' independence and *ex post* controls such as parliamentary hearings.

In the remainder of this section, I shall provide illustrations of the two types of conflict described above in the context of central banking: a) input *versus* output legitimacy b) conflict between objectives of the central bank *versus* other policy objectives. The first case illustrates *both* of these tensions at the same time. The second, I shall argue, represents an instance of the latter tension alone. As we shall see, this has implications for the measures needed to restore central bank legitimacy.

1) Delegation to central banks and distribution

The important contribution of Tucker (2018) lies in providing a much more detailed framework for legitimate delegation to IAs, and to central banks in particular. Tucker's account has three components (2018: appendix): *delegation criteria* identifying a series of necessary conditions for such delegation to be legitimate – for example that delegation only occurs after wide public debate, that "society's preferences regarding the policy issue in

[7] For central banks with mandates that reach beyond price stability, similar justifications will have to be provided for the additional objectives in question (see e.g. Tucker 2018: chapter 20). This has become particularly relevant since the 2007-8 financial crisis, where many central banks have acquired regulatory and supervisory competences to promote the objective of financial stability.

[8] The "without prejudice" clause limits the impact of this article to that of a tie-breaker between two policies that are equally effective with regard to price stability. By contrast, the idea I shall defend in this article is that we should in some cases be prepared to make *compromises* on price stability if this allows us to better achieve our policy objectives overall.

question are reasonably stable", and that the "IA will not have to make big choices on distributional trade-offs or society's values"; *design precepts* detailing how delegation should be structured to ensure legitimacy over time – for example provisions concerning the specification of IA objectives, procedures to be followed, as well as the transparency of the IA's policy decisions; and *multiple-mission constraints* explaining why IAs should be given multiple objectives only under specific circumstances – for example that the objectives be "intrinsically connected", each subject to a commitment problem, and that combining them in one agency "will deliver materially better results."

Tucker's strategy is to create the conditions for the legitimacy of IAs *despite* their independence by imposing institutional constraints on the IAs themselves as well as on the process of delegation. Tucker's account is rich in detail and represents a welcome contribution to an under-researched question. However, the point of this paper is not to provide an overall assessment of it, but rather to zoom in on one central delegation criterion that strikes me as problematic in the context of central banks and that raises important substantive questions concerning the delegation to IAs and their legitimacy.

According to Tucker, a key precondition for IA legitimacy is that the agency does not make big choices on distributional trade-offs. The rationale for this constraint is that decisions that create winners and losers need to be subject to democratic control and, thus, should not be removed from elected officials. Implicitly, Tucker suggests that input legitimacy is required when it comes to distributive issues. By construction, IAs lack input legitimacy.

This paper accepts the plausibility of this argument but suggests that, at least in the context of central banking but potentially more generally, it presents us with a dilemma. Given that contemporary monetary policy has significant distributive consequences,[9] we either have to refrain from delegating monetary policy to an IA, thus potentially risking higher than necessary inflation, or we have to delegate anyway, violate Tucker's delegation criteria, and risk a monetary policy authority that lacks legitimacy.[10]

2) Delegation to central banks and environmental sustainability

The stakes in the debate concerning the relation between central bank policies and environmental sustainability are somewhat different. Here, the tension lies in the fact that an independent central bank might pursue policies that are in conflict with the policy objective of transitioning to a more sustainable economy (e.g. Matikainen *et al.* 2017). If we think that environmental policy does not require input legitimacy, because its central planks are based on scientific evidence rather than on democratic decision-making,[11] then the

[9] Incidentally, this is something Tucker recognizes (see Tucker 2018: 380-2 and 528-30).

[10] This dilemma represents the elephant in the room in Tucker's otherwise impressive book and remains unaddressed. A key objective of this paper is to point to the need for more research on how to resolve this dilemma.

[11] Note that I am not claiming that input legitimacy can be set aside because scientific evidence somehow produces a consensus on what needs to be done – the current political landscape illustrates that this is *not* the case. What I am claiming is that certain environmental questions, just like questions of monetary policy, are ones where paternalistic policies grounded in scientific expertise may be justified. You might of course disagree with this premise. We shall come back later to the question of whether, or to what extent, environmental policy also requires input legitimacy.

conflict here is not one between input *versus* output legitimacy, but rather a conflict between the output legitimacy of one public agency – central banks – and the output legitimacy of government more generally with regard to environmental issues. Mandating central banks to only care about one issue – price stability – or a subset of issues – price stability and financial stability, say – risks producing inefficient results with regard to our overall social welfare function. From the perspective of output legitimacy, this undermines the legitimacy of central banks.

In other words, the challenge in this case lies in balancing the benefits of delegation to central banks against the costs in terms of policy outputs outside central banking. The first important step lies in acknowledging the problem. Traditionally, the reflex of central bankers has been to point to their mandate and underline that this was not an issue for them. However, note that this in no way solves the problem, but merely deflects responsibility to governments. The second step, just as in the case of distribution, consists in accepting that we care about environmental sustainability not just for instrumental reasons but for its own sake.[12]

Against this backdrop, the challenge consists in identifying institutional arrangements that allow us to optimally balance the benefits of delegation to central banks against its costs in terms of policy outputs or, even better, to find ways of delegation that minimise those costs.

Before directly addressing, in section 3, the challenges just laid out regarding the impact of monetary policy on distribution as well as on environmental sustainability, the next section will underpin the empirical premises they rest on. In other words, I shall work to demonstrate that monetary policy decisions do indeed entail big choices on distributional trade-offs and impact environmental sustainability.

2 Two unintended consequences of monetary policy

2.1 Exacerbating inequalities in income and wealth

While monetary policy inevitably creates winners and losers, the nature and magnitude of these effects changed with the financial crisis of 2007. The distributive effects of conventional monetary policy pre-2007, at least outside of Japan, were limited to differentially affecting savers and debtors through the interest rate. The post-2007

[12] For a position limited to such instrumental considerations, see e.g. Coeuré (2018), who accepts that central banks should factor in environmental sustainability considerations when not doing so would undermine price stability or financial stability. See also Carney *et al.* (2019).

unconventional monetary policies, by contrast, have more significant distributive consequences.

Both so-called quantitative easing, that is, the outright purchase of financial assets by central banks from the financial sector, and low-interest loan programs such as the European Central Bank's (ECB) Long-Term Refinancing Operations (LTROs) have injected massive amounts of liquidity into the economy. Their intended effect, through the *portfolio balance effect*, is for this injection to stimulate investment and consumption. In practice, a substantive portion has been used to buy existing assets instead, thus leading to booms on real estate and stock markets and to unintended distributive consequences (e.g. White 2012; de Haan and Eijffinger 2016).[13] Many central bankers, including Tucker, acknowledge this. The Governor of the Bank of England, Mark Carney, for instance, has stated that "the distributional consequences of the response to the financial crisis have been significant" (2014).

The reactions of central bankers to this state of affairs are instructive, and show that they are well aware of the threat the distributive consequences of unconventional monetary policy pose to their legitimacy. Let me distinguish three types of response here.[14]

First, central bankers are quick to emphasize that distributive concerns do not figure in their mandate. This is correct, and some, perhaps most, of the blame for neglecting these unintended consequences should thus be directed at the politicians formulating the mandate instead. However, note that this issue is orthogonal to what concerns us here: Even if distribution is not part of central banks' job description, distributive side-effects of monetary policy can still undermine central bank legitimacy.

Second, central bankers say they had no choice (cf. Fontan *et al.* 2016: 336-7). The distributive consequences of unconventional monetary policy are the price we had to pay for saving the financial system from collapse. Note that this argument entails the claim that no other policy instruments were available that could have avoided financial meltdown *without* incurring the same level of inegalitarian consequences.

Third, several central banks have recently published papers that suggest the overall distributive effect of their crisis response has not exacerbated inequalities and has potentially even had an equalizing effect (Bunn *et al.* 2018; Ampudia *et al.* 2018). To understand this claim, we have to take a more detailed look at various *channels* of redistribution of monetary policy. While the literature identifies up to six such channels (e.g. Colciago *et al.* 2019, 5; Coibion *et al.* 2017, 81-85), what matters for our purposes is the distinction between two *kinds* of effects monetary policy has on distribution. "Direct effects include the impact of the

[13] Someone might object that the point of the portfolio balance effect is precisely to shift investment into riskier existing assets such as corporate bonds and, thereby, lower the costs of capital for the corporations in question. This point is well taken, but it raises the question of why and how a company that does not consider productive investment worthwhile with interest rates already at the zero-lower bound could be enticed to change its mind (see Dietsch *et al.* 2018: 28). As Keynes pointed out, it is unlikely that monetary policy will be effective in such a context. Its distributive side-effects, by contrast, are real and significant.

[14] For a detailed discourse analysis of central bankers on the issue of inequality, see Fontan *et al.* 2016.

different paths for nominal and real interest rates on households' savings incentives […] and on households' net financial income. […] The indirect effect operates through the general equilibrium responses of prices and wages, hence of labour income and employment." (Ampudia *et al.* 2018, 5).

Based on this distinction, central bankers argue that the *inegalitarian direct* effects of unconventional monetary policy on asset prices (see above) are compensated, or even outweighed by the *egalitarian indirect* effects on employment and growth. Note, however, that this line of reasoning accepts that monetary policy *does* have distributive effects. This turns the spotlight onto the second response above, claiming that monetary policy space was limited and that the precise configuration of distributive side-effects was inevitable. Yet, might there have been monetary policies that would have produced the desirable effects on employment and price stability with a lower level of undesirable asset-price-driven inequality? If so, then the central bankers' argumentative strategy fails. Both the second and the third response by central bankers ignore this relevant counterfactual. Pointing out that things could have been worse in terms of inequality *had central banks done nothing* does not establish that things could not have been better in terms of inequality without prejudice to price stability, or achieved a better compromise between the two objectives, *had they acted differently*.

Three observations are in order at this point. First, it can indeed be argued (e.g. Fontan *et al.* 2016: 336-7) that central bankers did not give serious consideration to ostensibly less inegalitarian policy alternatives, such as for instance helicopter money (e.g. Blyth and Lonergan 2014). Second, it is one thing to claim that monetary policy has no significant distributive impact, but quite another to claim that it has significant distributive consequences through various channels of redistribution, and that these different effects more or less cancel each other out. The latter strikes me as a rather ambitious empirical claim. Third, even if the empirical claim held for a certain monetary policy mix, choosing this policy mix over another still involves making choices with distributive consequences.

In sum, it seems fair to say that unconventional monetary policy of the kind we have seen since the financial crisis *inevitably* involves choices that have significant distributive consequences. Even if the precise direction and magnitude of these consequences is subject to an ongoing debate, it is in the very nature of the massive liquidity injections that central banks have resorted to at the zero lower bound of interest rates that they have an important distributive dimension. Incidentally, this holds for alternative policy instruments such as helicopter money, too, though their distributive impact would likely be very different.

Given that the present economic recovery has not been accompanied by a rise in interest rates, and given the difficulty in normalizing central banks' balance sheets, it is also plausible to anticipate that unconventional monetary policy and its significant distributive implications are here to stay.

Therefore, both in the present and for the foreseeable future, monetary policy is set to violate Tucker's delegation criterion that independent agencies should not make big choices on distributional trade-offs. How should one respond to this tension from an institutional design perspective?

2.2 SLOWING THE TRANSITION TOWARDS A SUSTAINABLE ECONOMY

The impact of contemporary monetary policy on environmental sustainability issues becomes evident once we compare what central banks currently do to what they could potentially do to support the transition to a greener economy. There is a sizeable gap between acknowledging that climate-related risks pose a threat to financial stability on the one hand, which nicely sums up central bank attitudes towards climate change today, and analysing the ways in which central bank policy might help to mitigate climate-related risks on the other. Consider the following illustration to make these rather abstract remarks more concrete.[15]

As part of their unconventional monetary policy, central banks have been buying financial assets at an unprecedented scale. Some of these quantitative easing programmes include corporate bonds, the ECB's corporate sector purchase programme (CSPP) being one example. When engaged in asset purchases of this kind, the question arises *which* assets to buy. The response to this question has important ramifications, since being included in such a purchase programme bestows tangible advantages on corporations by lowering their borrowing costs and thus stimulating investment.[16]

Mindful of these effects, the ECB chose to apply the principle of market neutrality to its corporate bond purchases. Rather than selecting specific bonds, they weight their purchases according to the current volumes outstanding of the bonds they buy. They are neutral, so the argument runs, in the sense that they do not depart from the *status quo* on capital markets. However, note that this veneer of neutrality cannot hide the inherently political decisions involved in these asset purchases (van't Klooster and Fontan 2019). Why buy corporate bonds rather than equities of small- and medium enterprises, for instance?[17]

More specifically, the policy of market neutrality, by reinforcing the *status quo*, also reinforces the dominant position of carbon-intensive industries (Matikainen *et al.* 2017). After all, in terms of bonds outstanding, fossil-fuel intensive sectors still represent an important share of bond volumes. This represents an opportunity missed to use monetary policy to promote the transition towards a more sustainable economy by giving preference

[15] The discussion in the next paragraph is based on Dietsch *et al.* (2018: 31-32).
[16] The case of Volkswagen and its benefits from being included in the ECB's asset purchases is instructive in this context (see Reuters 2016).
[17] Note, in addition, that the ECB restricts its purchases of corporate bonds to securities with an investment grade rating. This is understandable from a risk management perspective, but it does depart from the notion of market neutrality.

to greener assets (cf. Dietsch *et al.* 2018: 31-32). In fact, in light of article 127 (1) of the Lisbon Treaty mentioned earlier, one might wonder whether the ECB even has an *obligation* to promote environmental sustainability in this way, since there is no reason to think that doing so would undermine the effectiveness of its policy with regard to its primary objective, i.e. price stability.

In addition, the conservatism of central banks also manifests itself at a more fundamental level. There is growing evidence that financial markets underprice the risks related to climate change (e.g. Christophers 2017). As Monnin (2018a) points out, these skewed risk assessments subsequently feed into evaluations by credit rating agencies and into the monetary policy operations of central banks that rely on the latter. While this may be interpreted as a "mere" instrumental argument – better assessment of climate risks will promote financial stability – integrating "the monitoring of climate-related financial risks into day-to-day supervisory work, financial stability monitoring and board risk management" (Carney *et al.* 2019) would have the beneficial effect of promoting sustainable economic practices as well.[18]

3 Institutional devices to enhance central bank legitimacy…

We have seen that, in different ways, the insensitivity of central banks to the impact their policies have on the distribution of income and wealth as well as on our climate undermines their legitimacy. At first sight, one could react to this observation in one of three ways. First, someone might think that the unintentional side-effects of monetary policy are sufficiently worrisome to revoke the independence of central banks. This, I submit, would amount to throwing the baby out with the bathwater. Second, at the other extreme of the spectrum of possible responses, someone might hold that the current institutional configuration with an independent central bank and a narrow mandate centred on price stability represents a necessary condition to a well-functioning economy, and that we simply have to live with some negative side-effects. This, it seems to me, amounts to not taking seriously enough the challenge of legitimacy. It is hard to see how an illegitimate institution could successfully underpin any economy in the long term.

The third, more constructive kind of response lies in between these two extremes. Are there ways to hold on to the benefits of delegation to an independent central bank while at the same time shoring up its legitimacy? Given the general trend towards delegation to IAs, this question deserves considerably more attention than it has received thus far. The goal of this

[18] The Bank of England, for example, has included an exploratory climate change scenario in its 2019 stress tests for the insurance sector. See https://www.bankofengland.co.uk/prudential-regulation/letter/2019/insurance-stress-test-2019. Similarly, the "Dutch Central Bank recognizes climate risks as a significant long-term risk and aims to develop a stress test on climate." (High-Level Expert Group on Sustainable Finance 2018, 38)

last section will be to sketch a menu of available options of how our societies might manage the tension between delegation and legitimacy in light of the two unintended side-effects of monetary policy discussed in the previous section.

3.1 …IN THE FACE OF DISTRIBUTIVE TRADE-OFFS

Commentators on the role of IAs in democracies have often assumed "the possibility of separating efficiency and redistributive concerns because such a separation is crucial to the substantive legitimacy of regulatory policies." (Majone 1996, 296) Section 2.1 has demonstrated this assumption to be problematic when it comes to contemporary monetary policy. Even beyond monetary policy, the distributive dimensions of regulation are often neglected (see Robinson *et al.* 2016), though considering other policy fields in any depth lies beyond the scope of this paper.

What are the implications of this observation for delegation to IAs, and to central banks in particular? Can we overcome the dilemma identified at the end of section 1 between politicized and thus suboptimal monetary policy on the one hand and delegated but illegitimate monetary policy on the other and, if so, how? I shall sketch three potential strategies to do so.

First, one might envisage a more fine-grained division of labour and coordination between central bankers and elected officials when it comes to monetary policies that will foreseeably have significant distributive consequences. One example in this category is the establishment of joint committees composed of central bankers and representatives of the finance ministry, as were common in the post-war era. This would confront central bankers with other policy objectives and favour compromises between the narrow mandate of central banks and those other objectives.

Second, the mandate of central banks could be widened to incorporate the distributive side-effects of monetary policy into the decision making of central bankers. For instance, one might require that whenever unconventional monetary policies with a foreseeably significant distributive impact are adopted, this impact should receive a to be specified weight in the central bank's policy making (see Fontan *et al.* 2016: 342-43).[19] Advocates of narrow mandates focused exclusively on price stability are likely to object that such an arrangement would undermine the effectiveness of monetary policy, but the literature does not seem to support this objection (see Dietsch *et al.* 2018, chapter 2). Such a requirement would push central banks to give more serious consideration to innovative monetary policy instruments such as helicopter money, whose distributive side-effects are likely to be more benign.

[19] Note that there is room for such an arrangement in Tucker's account, given that multiple missions are acceptable provided the policy objectives are "intrinsically connected" (see section 2), and "will deliver materially better results." (2018, *appendix*)

The third option shifts our focus from central banks as agents to governments as their principals. Once governments are aware of the distributive side-effects of monetary policy, one might argue, it is *their* responsibility to respond to mitigate these effects. One way to ensure they live up to this responsibility would be to enact a *distributive neutrality commitment* on the part of the government. This commitment would require automatic fiscal corrections for any distributive consequences above a certain threshold that monetary policy might have. One argument against this option is that redistribution is always costly, and that it might be preferable to prevent the distributive side-effects of monetary policy from occurring in the first place. Another potential worry lies in the fact that redistributive fiscal policies are hard to implement, particularly so in a context of international tax competition (e.g. Dietsch 2015).

Interestingly, these three strategies differ in the ways in which they address the tension between input *versus* output legitimacy identified in section 1. The first strategy nudges central banks to coordinate with government agencies that, in contrast to central banks themselves, do have input legitimacy. In this sense, it takes the edge of the worry of input legitimacy vis-à-vis the central bank as an IA, but the worry does not disappear altogether. The second strategy, by requiring central banks to reduce the distributive footprint of their monetary policy, attempts to steer monetary policy back to a territory where input legitimacy is less of a problem to start with. As we have seen, our concern with input legitimacy is conditional: It only arises if an IA makes decisions touching on issues that we believe should be subject to direct democratic control. By explicitly asking central banks to avoid exacerbating income inequalities, the concern is alleviated. Finally, under the third strategy, the lack of input legitimacy of the agent (the central bank) is acknowledged and compensated for by an intervention of the principal (the government). Analysed through the narrow lens of legitimacy, it is not clear that one of these three strategies is preferable. Other concerns, such as for instance feasibility constraints, are more likely to be decisive here. Nonetheless, it is important to understand that these measures do not merely represent three different tools to the same end, but that they differ in how they address the challenge of legitimacy.

3.2 …IN AN ERA OF CLIMATE CRISIS

At first sight, it might seem as if we can simply draw up a parallel menu of policy options to enhance central bank legitimacy when it comes to their impact on environmental issues. However, we shall see that the different configuration of legitimacy concerns in the environmental context has repercussions for our choice between different options to alleviate them.

Briefly, the menu of policy options similar to the one sketched in the previous section would include: 1) Requiring central banks to coordinate with other branches of government, such as the ministry of environment or those responsible in the treasury for designing a carbon

tax for example. 2) Pushing central banks to respect the responsibilities to price in climate risks that are already part of their mandate (Monnin 2018a); give preference to low-carbon assets in asset purchase programmes (e.g. Dietsch *et al.* 2018: 31-32); and have central banks "introduce climate-related risk analysis into their eligibility criteria and haircuts of the collateral they accept." (Monnin 2018b: 14). 3) Let the environmental consequences of monetary policy play out, but compensate them through a more aggressive overall environmental policy. While this last option may seem even more unattractive than in the distributive case, bear with me to see that there is one noteworthy aspect to it.

What can we say about these options from the perspective of legitimacy? Note one important complication in this context that I have set aside thus far. In section 1, I suggested that when it comes to the impact of central bank actions on environmental policy, our concern is primarily one of *output* legitimacy. Looking at the policy menu just outlined, someone might object that the potential measures show that my assessment in section 1 was misguided. After all, these measures not only mitigate environmental impact, but they also create winners (green industries) and losers (carbon-intensive industries). Since I maintained that any policies with significant distributive consequences should be subject to direct democratic control, should we not conclude that central bank actions which, through their stance on environmental sustainability issues, affect distribution do require *input* legitimacy after all? In other words, the objection suggests that the legitimacy challenges presented by distributive and environmental issues are more similar than my analysis suggests.

This is an important objection, but I believe it fails and here is why. There is a difference in the normative status of the inequalities in income and wealth created by asset purchase programmes on the one hand, and the inequalities resulting from the different treatment of carbon-intensive and low-carbon industries on the other. Arguably, our tolerance to the former represents a value judgement that should be subject to democratic political procedures – it does indeed require input legitimacy – whereas *if* we are serious about the need to transition to a more sustainable economy, the idea that we should favour low-carbon industries is not a value judgement but a prudential judgement.[20]

This has implications for how we evaluate the three policy options from the perspective of legitimacy. Strategy 1, that is, the better coordination of monetary policy with environmental policy, will enhance output legitimacy by factoring in the unintended consequences of monetary policy. If I am right in suggesting that input legitimacy is not a desideratum here, then this amounts not just to an alleviation of our legitimacy concern (as in the case of distribution), but to restoring output legitimacy, period. As for strategy 2, including environmental sustainability concerns in central bank mandates, again, enhances output

[20] I acknowledge that one can extend this kind of reasoning to socio-economic inequalities, too. But it seems to me that, unfortunately, the antecedent of that argument – "*if* we are serious about a commitment to reduce socio-economic inequalities…" – still lacks the consensus that would allow us to free decisions about inequality from the requirement of input legitimacy.

legitimacy. There is a clear contrast here with the distributive case. In the latter context, strategy 2 encourages central banks to reduce their distributive footprint to reduce worries about *input* legitimacy; here, strategy 2 encourages central banks to take a clearer stance on environmental sustainability to increase their *output* legitimacy. Rather than having to constrain delegation, it turns out that we need to widen the delegation mandate to enhance legitimacy. From the perspective of the literature on the ethics of delegation, this is an interesting and somewhat surprising conclusion. Finally, as already indicated, strategy 3 might prima facie appear to be a non-starter. Since global warming is subject to partly irreversible threshold effects, letting it happen in order to subsequently attempt to reverse it is not an option. However, given the objection discussed in the two previous paragraphs, there is one aspect of strategy 3 that is worth preserving: Even if we think that the losers of a green new deal, i.e. the fossil-fuel industry, are disadvantaged for good reasons, there is a case to be made for governments to cushion the impact of this transition for them in the short term. This might include measures such as retraining programmes for workers in carbon-intensive industries.

4 Conclusion

Unintended side-effects of contemporary monetary policy undermine the legitimacy of central banks as independent agencies. More specifically, this paper has analysed legitimacy concerns in the context of the distributive consequences of unconventional monetary policy as well as with regards to their impact on the transition towards a more sustainable economy. I have suggested that the former by and large present a challenge of input legitimacy, where the latter should be viewed mainly as a challenge to the output legitimacy of central banks. This has implications for the normative and institutional responses in the respective contexts. For example, it implies that we will prefer independent agencies such as central banks to play a more passive role in the context of distribution – minimise their distributive impact – whereas we might be prepared to grant them a more active role in promoting the transition towards a more sustainable economy.

The list of potential ways presented above to reconcile independence and legitimacy in the face of distributive trade-offs and in an era of climate crisis is by no means exhaustive.[21] Furthermore, what I have presented here are mere ideas that will need to be fleshed out in theory and tested in practice to assess their merits. This is precisely the point of this paper: To highlight a serious gap in our theories about delegation to IAs when it comes to the side-effects of their policies. These side-effects undermine the legitimacy of IAs, including central banks. To reduce this tension, we can either reinforce the democratic control over IAs, albeit

[21] It notably brackets more fundamental reforms to the monetary regime that would presumably reduce distributive side-effects, such as for instance full reserve banking (Fisher 1935) or the constitutionalization of money (Buchanan 2010).

without undermining the initial rationale for delegation (see option 1 in sections 3.1 and 3.2), or attempt to directly mitigate the unintended side-effects of IA policies (see options 2 and 3).

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GREENPEACE

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October 8, 2020

Re: Formal Submission for the Bank of Canada's Monetary Policy Framework Review

Thank you for the opportunity to input on the Bank of Canada's Monetary Policy Framework Review.

The Bank of Canada has a broad mandate "to promote the economic and financial welfare of Canada."[1] Given the severity and growing urgency of the climate crisis, Greenpeace Canada believes that in order to effectively achieve its mandate the Bank of Canada must put climate change at the centre of its approach to monetary policy. To this end, we believe the Bank should explicitly include climate change, the mitigation of climate-related risks, and support for a green transition in its next framework agreement with the federal government. In its monetary policy review the Bank must carefully examine the connections between monetary policy and climate change, looking not only at how climate change impacts the conduct of monetary policy, but also at how monetary policy can impact climate change and any opportunities there may be for the Bank to support climate change mitigation.

The climate crisis poses a massive and growing threat to the Canadian economy and the wellbeing of Canadians. The Bank of Canada's own research indicates climate-related risks to the Canadian economy and financial system are severe.[2] Leading climate scientists have even warned that the physical risk of climate change presents "an existential threat to civilization."[3] The COVID-19 crisis has exposed some of the vulnerabilities of the Canadian economy to transition-related risks. As the CEO of Suncor has pointed out, "the temporary economic lockdown triggered by the 2020 pandemic is giving us a glimpse into a not-too-distant future where the transformation of our energy

[1] https://laws-lois.justice.gc.ca/eng/acts/B-2/page-1.html.
[2] Ens & Johnston (2020) *Scenario Analysis and the Economic and Financial Risks from Climate Change*, Staff Discussion Paper 2020-3, Bank of Canada, https://www.bankofcanada.ca/wp-content/uploads/2020/05/sdp2020-3.pdf, 13-14.
[3] Lenton et al (2019) Climate tipping points—too risky to bet against, *Nature*, 575 (7784), 592-5, https://www.nature.com/articles/d41586-019-03595-0, 595.

system could disrupt demand on a similar scale."[4] In fact, if climate risks are to be effectively managed, oil demand will be disrupted on an even greater scale by the coming energy transition. Liability risks could also be significant for Canada given our status as a significant fossil fuel producer.

Recovery from the COVID-19 crisis is a top concern of all economic policy makers, including at the Bank of Canada. The Network of Central Banks and Supervisors for Greening the Financial System (NGFS), of which the Bank of Canada is a member, has noted the urgent need to reduce greenhouse gas emissions, and stressed that "the economic response to the pandemic should therefore not be to re-build the old economy with the climate risks it presents, but to act now to lay the groundwork for an orderly transition to a more sustainable economy and climate-resilient financial system –a 'green' recovery."[5] Including climate change in the framework agreement with the federal government could give the Bank a clear mandate to pursue this goal. According to data compiled by Energy Policy Tracker, since the COVID-19 crisis began federal and provincial governments have poured twice as much money into fossil fuels as clean energy, indicating that we have done a poor job so far of following the NGFS guidance.[6]

The Bank of Canada has already taken a number of important steps to respond to the new climate reality. Former Governor Stephen Poloz has acknowledged that "the importance of climate-related issues for financial stability and monetary policy have become increasingly clear."[7] The Bank has identified climate-related risk as a key risk for the Canadian financial system, and is taking steps to better understand that risk.[8] However properly responding to the climate crisis requires more than simply trying to understand climate-related risks. It requires strong and urgent action to reduce them.

The Bank's current inflation targeting (IT) regime does give the Bank a certain amount of leeway to manage systemic risks through its monetary policy.[9] This leeway can and should be used to support climate change mitigation, for example by choosing a path to achieve the inflation target that helps minimize climate risks and supports the clean energy transition. It could also be argued that current IT regime does impel the Bank to act to address climate risks, because climate change threatens the stability of the financial

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[4] Lewis (June 1, 2020) Canada's Suncor CEO sees electric vehicles disrupting oil demand as much as coronavirus, *Reuters*, https://ca.reuters.com/article/businessNews/idCAKBN23823S.
[5] Network for Greening the Financial System (June 8, 2020) *Statement on the need for a green recovery out of the Covid-19 crisis*, https://www.ngfs.net/sites/default/files/medias/documents/green_recovery_statement_-_june_2020.pdf.
[6] https://www.energypolicytracker.org/country/canada.
[7] https://www.bankofcanada.ca/2019/03/bank-canada-joins-central-banks-supervisors-network/.
[8] Bank of Canada (2019) *Financial System Review-2019*, https://www.bankofcanada.ca/wp-content/uploads/2019/05/Financial-System-Review%E2%80%942019-Bank-of-Canada.pdf, 28-30.
[9] Bank of Canada (2016) *Renewal of the Inflation-Control Target: Background Information-October 2016*, https://www.bankofcanada.ca/wp-content/uploads/2016/10/background_nov11.pdf, 31-32.

system which is necessary for monetary policy to work properly.[10] However adopting these approaches runs the risk of giving the Bank too little scope of action to support climate change mitigation, and may result in a lack of clarity or disagreement as to whether mitigating climate risks is really within the mandate of the Bank. One of the Bank's own research papers on climate change states that policies for reducing emissions fall outside the Bank's mandate, suggesting the Bank does not currently see IT as implying a responsibility for mitigating climate risk.[11]

Incorporating climate change into the framework agreement would give the Bank a clearer mandate and larger operating space to act to reduce climate risks and support climate change mitigation.

Figuring out exactly how the Bank should act on such a mandate is something that would require additional research, discussion and experimentation, and we won't try to provide an answer to that question here. However at a bare minimum it should include:

1) Strengthening eligibility criteria for corporate debt purchase programs so that targeted companies must meet minimum sustainability standards, such as providing climate-related risk disclosures in line with TCFD recommendations. This would be in agreement with guidance from the International Energy Agency, which has said that "where central banks are expanding the supply of money through the purchase of assets, the introduction of appropriate eligibility criteria (for example, a preference to purchase corporate bonds that meet certain conditions), would help to ensure that the finance is directed towards sectors and technologies that are aligned with the goals of the sustainable recovery plan."[12]

2) Excluding fossil fuel companies and securities from asset purchasing programs. This would protect against monetary policy being used as an avenue for inappropriate fossil fuel subsidies, and as several researchers have noted, "purchase of carbon-intensive assets is in direct contradiction with, and may undermine, the signals that financial regulators are making about the risks associated with high-carbon investments."[13]

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[10] The Bank has explained its intervention in response to the COVID-19 crisis in these terms: https://www.bankofcanada.ca/markets/market-operations-liquidity-provision/covid-19-actions-support-economy-financial-system/.

[11] "Policies to prevent global warming—such as carbon taxes, emissions caps and spending on technological development—fall outside the mandates of central banks." Ens & Johnston (2020) *Scenario Analysis and the Economic and Financial Risks from Climate Change*, Staff Discussion Paper 2020-3, Bank of Canada, https://www.bankofcanada.ca/wp-content/uploads/2020/05/sdp2020-3.pdf, 1.

[12] International Energy Agency (2020) *Sustainable Recovery, World Energy Outlook Special Report*, https://www.iea.org/reports/sustainable-recovery, 112.

[13] Matikainen et al (2017) *The climate impact of quantitative easing*, https://www.lse.ac.uk/GranthamInstitute/wp-content/uploads/2017/05/ClimateImpactQuantEasing_Matikainen-et-al-1.pdf, 1.

3) Including climate risks in collateral frameworks, significantly increasing haircuts for fossil fuel and other high-carbon assets.

4) Reviewing and revising Bank policies and practices to ensure they take appropriate account of climate-related risks, help reduce those risks, and are supporting, not impeding, an orderly transition to a more sustainable, resilient, and equitable economy. To select just one of many possible examples, the Bank should look at how decisions about the policy rate could have differential impacts on green investments, which often have higher upfront costs and so may be more likely to receive less financing in a higher interest rate environment.[14]

It should be stressed that these are all actions the Bank of Canada can and should take regardless whether climate change is explicitly included in the new framework agreement with the federal government. What we are arguing here is that including climate change in the framework agreement will help ensure that the Bank does in fact take these and additional steps, and with the speed and urgency the climate crisis calls for.

Action on climate change by the Bank should also include researching and developing new policy tools to support climate change mitigation and management of climate risks. There is a growing body of research and practical experience in this area, and the Bank should both take advantage of and contribute to it. The IMF has published a review of financial and monetary policies for climate change mitigation.[15] The Asian Development Bank Institute has also released a study reviewing policies for green central banking.[16] Civil society organizations such as Reclaim Finance have put forward concrete proposals for how central banks can better respond to the climate crisis.[17] While not necessarily endorsing all the ideas presented by these authors, Greenpeace believes some of them could be useful in decarbonization efforts and deserve serious consideration. Where policy proposals do not strictly fall under the remit of the Bank, Bank staff could still provide research and other support for the relevant bodies (e.g. the Office of the Superintendent of Financial Institutions).

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[14] Monnin & Barkawi (2015) *Monetary Policy and Green Finance: Exploring the Links*, https://www.iisd.org/system/files/publications/greening-chinas-financial-system-chapter-7.pdf.

[15] Krogstrup & Oman (2019) *Macroeconomic and Financial Policies for Climate Change Mitigation: A Review of the Literature*, IMF Working Paper No 19/185, https://www.imf.org/en/Publications/WP/Issues/2019/09/04/Macroeconomic-and-Financial-Policies-for-Climate-Change-Mitigation-A-Review-of-the-Literature-48612.

[16] Dikau & Volz (2018) *Central Banking, Climate Change and Green Finance*, ADBI Working Paper 867, Asian Development Bank Institute, https://www.adb.org/publications/central-banking-climate-change-and-green-finance.

[17] See for example. https://reclaimfinance.org/site/en/2020/05/18/quantitative-easing-and-climate-the-ecbs-dirty-secret/ and https://reclaimfinance.org/site/en/central-banks-coronavirus-climate/. See also Greenpeace EU (2020) *Bankrolling the Climate Crisis*, https://storage.googleapis.com/planet4-eu-unit-stateless/2020/06/20200603-Report-ECB-coronavirus-bond-purchasing-bankrolls-fossil-fuels.pdf.

In the last review of the inflation-control target it was concluded that monetary policy should not focus on financial stability, in part because of concerns that monetary policy was "too blunt an instrument" for that purpose.[18] Developing new policy tools, and adapting old ones, in order to support climate change mitigation and risk management would help address this concern as it applies here. While the Bank should be mindful of how policy rate decisions impact climate change risks and mitigation, there's no reason to think the policy rate should be the only or even the primary monetary policy tool used to support a green transition.

While there may be nervousness at adapting and expanding the monetary policy toolkit to tackle climate-related issues, the history of monetary policy is a history of innovation geared towards addressing the economic challenges of the historical moment.[19] This can be seen most recently in the unconventional monetary policy tools developed to respond to the financial crisis of 2007-2008 and COVID-19.[20] Viewed from this perspective, expanding the goals and tools of monetary policy to help address the epochal climate crisis would not be a departure from standard monetary policy practice, but in keeping with it. And as Senior Deputy Governor Wilkins has noted, there was nervousness when IT was adopted too, but the Bank did it anyways and took a "leap of faith" because they knew there was a "dragon to slay" (inflation).[21] Today we have another much more dangerous dragon to slay: climate change.

It might be preferred that we not ask monetary policy to help decarbonize the economy, and that this job be left to other policy areas. But we will only achieve the deep, rapid, and sustained reductions in emissions needed to keep warming well below 2˚C if we use every tool available. In the words of one IMF economist defending the use of monetary policy for mitigation: "all hands are needed on deck, for, as Mark Carney of the Bank of England has warned, 'the task is large, the window of opportunity is short, and the stakes are existential.'"[22] Furthermore, Bank policy and actions may mitigate and/or enhance climate risk whether it wants them to or not. The Bank has a duty to understand these impacts and take responsibility for them.

On the question of whether the Bank should keep inflation targeting or replace it with average inflation targeting, price level targeting, or any of the other leading alternatives to

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[18] Bank of Canada (2016) *Renewal of the Inflation-Control Target: Background Information-October 2016*, https://www.bankofcanada.ca/wp-content/uploads/2016/10/background_nov11.pdf, 27.
[19] Williamson (2020) The Role of Central Banks, *Canadian Public Policy*, June 2020, 46, 2, 198-213, https://www.utpjournals.press/doi/full/10.3138/cpp.2019-058?mobileUi=0&.
[20] Poloz (2015) Prudent Preparation: The Evolution of Unconventional Monetary Policies, https://www.bankofcanada.ca/2015/12/prudent-preparation-evolution-unconventional-monetary-policies/. Poloz, (2020) Monetary policy in unknowable times, https://www.bankofcanada.ca/2020/05/monetary-policy-in-unknowable-times/.
[21] https://www.bankofcanada.ca/wp-content/uploads/2017/10/remarks-140917wilkins.pdf, 1.
[22] Oman (September 4, 2019) A Role for Financial and Monetary Policies in Climate Change Mitigation, https://blogs.imf.org/2019/09/04/a-role-for-financial-and-monetary-policies-in-climate-change-mitigation/.

GREENPEACE

IT that have been put forward, Greenpeace Canada does not take a particular position at this time. However we do think the Bank must consider very carefully how any change in the IT regime would impact climate risk, Canada's transition to a green economy, and the Bank's ability to fulfill a mandate to support climate change mitigation. It is imperative that monetary policy, like all aspects of government policy, support and not hinder a rapid transition to a sustainable, equitable, zero-carbon economy.

Inflation targeting was adopted in Canada in 1991 to address a particular problem of that historical moment: high inflation. Three decades later we are in a new historical moment where a different and far more serious problem is presenting itself: the climate crisis. Monetary policy in Canada must adapt to this new reality and turn its attention to reducing climate risks and supporting the transition to a green economy. That is why we believe climate change should be explicitly included in the Bank's framework agreement with the federal government.

I would be happy to discuss any of these issues further, including how the Bank of Canada could better incorporate climate change mitigation and consideration of climate risk into its work.

Thank you for your time and consideration of this submission.

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https://torontosun.com/opinion/columnists/weir-end-the-bank-of-canadas-fixation-on-inflation

WEIR: End the Bank of Canada's fixation on inflation

Author of the article:
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Governor of the Bank of Canada Tiff Macklem walks outside the Bank of Canada building in Ottawa, Ontario, PHOTO BY BLAIR GABLE /REUTERS

The Bank of Canada recently launched public consultations on its Monetary Policy Framework, which is scheduled for renewal next year. The COVID-19 pandemic and double-digit unemployment could finally end our central bank's fixation on inflation. An updated mandate should recognize that monetary policy must aim not only for low inflation, but also for high employment.

After struggling to manage inflation in the 1970s and 1980s, the federal Minister of Finance and the Bank of Canada unveiled inflation targeting in 1991 and entrenched the 2% target in 1993. Even in the midst of a major recession, the central bank committed to raising interest rates to limit borrowing, spending, investment and ultimately employment as much as needed to squeeze inflation down to 2%. Periodic interest rate hikes to

constrain domestic demand proved palatable because they coincided with, and were offset by, falling exchange rates and expanding export demand through the 1990s and early 2000s.

Since then, Canada's economy has been buffeted by the 2008 global financial crisis, the 2015 collapse of commodity prices, and the current global pandemic. In these three crises, inflation has not been a serious problem and Canada has not been able to rely on export growth. To its credit, the Bank of Canada responded to all three crises by cutting its overnight rate to near zero to facilitate borrowing, spending and investment. Lower interest rates and other monetary interventions helped to shore up domestic demand and save jobs.

But rather than embracing the obvious priority of safeguarding employment during economic crises, Canada's central bankers attempted to fit their policy responses into the paradigm of inflation targeting. In particular, they contend that the inflation target is "symmetric," meaning they are as concerned about inflation falling below 2% as about it rising above 2%. Everything the Bank of Canada did to enable borrowing, spending and investment during times of crisis is thereby rationalized as helping to raise inflation back up to the 2% target.

Few Canadians outside the central bank would accept boosting inflation from 0% or 1% to 2% as a more important goal than maintaining and creating jobs. But if our central bank ultimately pursued appropriate policies, why should Canadians care that these policies had to be oddly justified in terms of inflation targeting?

One concern was that the Bank of Canada's focus on inflation slowed its response to the global financial crisis. The U.S. Federal Reserve, which has a dual mandate to achieve stable prices and maximum sustainable employment, cut interest rates considerably sooner and deeper in 2008. However, both central banks were quick in responding to this year's economic disruption from COVID-19.

A more fundamental issue is that the Bank of Canada's "symmetric" rationalization only works for economic downturns that lower prices. While the

2008 global financial crisis and the 2015 collapse of commodity prices obviously reduced inflation, the current pandemic is more complicated. As outlined in the Bank of Canada's latest Monetary Policy Report, COVID-19 has reduced demand (and hence prices) for products such as gasoline, travel and clothing while increasing demand (and prices) for others such as cleaning supplies and non-perishable food. So far, the net effect has been lower inflation, which allows interest rate cuts to be cast as spurring inflation back up toward the 2% target.

However, it is easy to imagine the current pandemic or some future crisis evolving in ways that do not lower inflation. If economic stability and jobs were threatened while inflation remained at 2%, Canadians would still rightly expect our central bank to facilitate borrowing to finance spending and investment that support employment. But the Bank of Canada would be unable to justify such needed monetary policy as a means of restoring inflation to its target.

Central bankers understandably sought to fit monetary policy responses to recent crises into the paradigm of inflation targeting. But at some point, the accumulation of crises and responses that are not about controlling inflation must produce a paradigm shift.

During the global financial crisis, the collapse of commodity prices and the COVID-19 pandemic, the Bank of Canada has played an important role in encouraging borrowing, spending and investment that supports Canadian jobs. Next year's mandate renewal should officially recognize maintaining and creating employment as a key goal of monetary policy to ensure that our central bank can respond effectively to future economic challenges.

— ErinWeir was the Member of Parliament for Regina-Lewvan from 2015 to 2019.

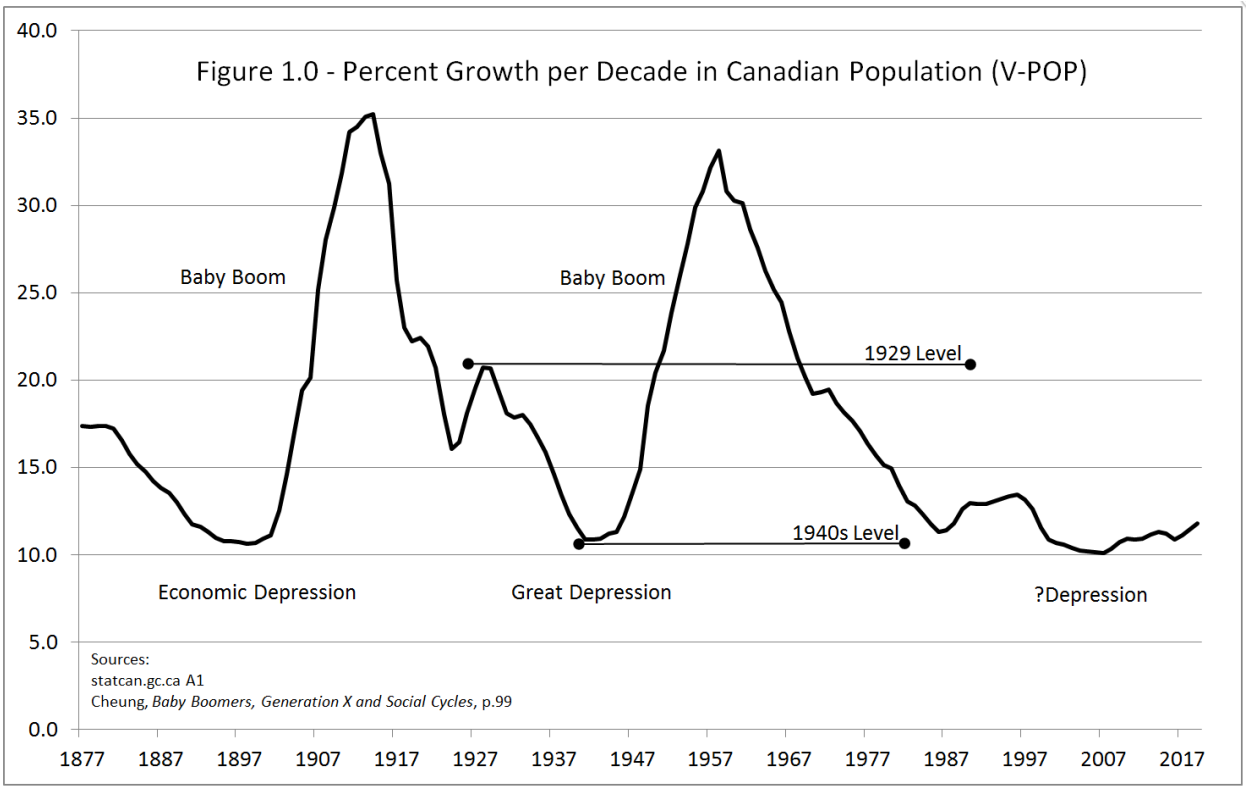
Demographics and Inflation in Canada

Bank of Canada Request for Consultation on Inflation Targeting and Alternative Frameworks

Author: Edward Cheung
Date: September, 2020.

Edward Cheung is the author of:
Baby Boomers, Generation X and Social Cycles: North American Long-Waves
Demographics and Fashion Trends, Medieval to Modern

Ebb and Flow in Population Growth



Like much of natural phenomena, there is an ebb and flow in the rate of growth of the population. Ebb and flow in nature is often described as being wave-like. Waves come in varying magnitudes and durations much like ocean waves or waves of bird migration. When the population increases through increasing birth-rate, there is a baby boom, and when the birth-rate drops, there is a natural decrease in population growth. Figure 1.0 shows the ebb and flow of Canadian population growth. Population growth increased in the early 1900s, in part due to increasing birth-rates, until 1914. The growth rate then declined into the Great Depression. During the Great Depression, the birth-rate started rising again. Population growth increased until 1958 then began another decline, reaching its lowest level in 2007. Within this population statistic are the dynamics of the many age groups. Baby boomers, being the largest generational group, have the largest impact on society. Over 50% of Canada's GDP is from consumer spending and the economic activities of baby boomers, from youth to maturity to old age, are reflected in all the economic statistics. As baby boomers entered schools, more schools and teachers were needed. As baby boomers entered the labour force, became independent consumers, and bought cars and homes, there were pressures on resources and productive capacity. The economy expanded and inflation flared. When productive capacity reached the levels required to support the consumption of baby boomers, inflationary pressures eased. With their new-found wealth, baby boomers invested their earnings, and equity inflation could be seen in rising stock markets. As baby boomers retire, the economy enters a period of slowing or declining consumption and businesses are left with excess capacity.

Labour Force

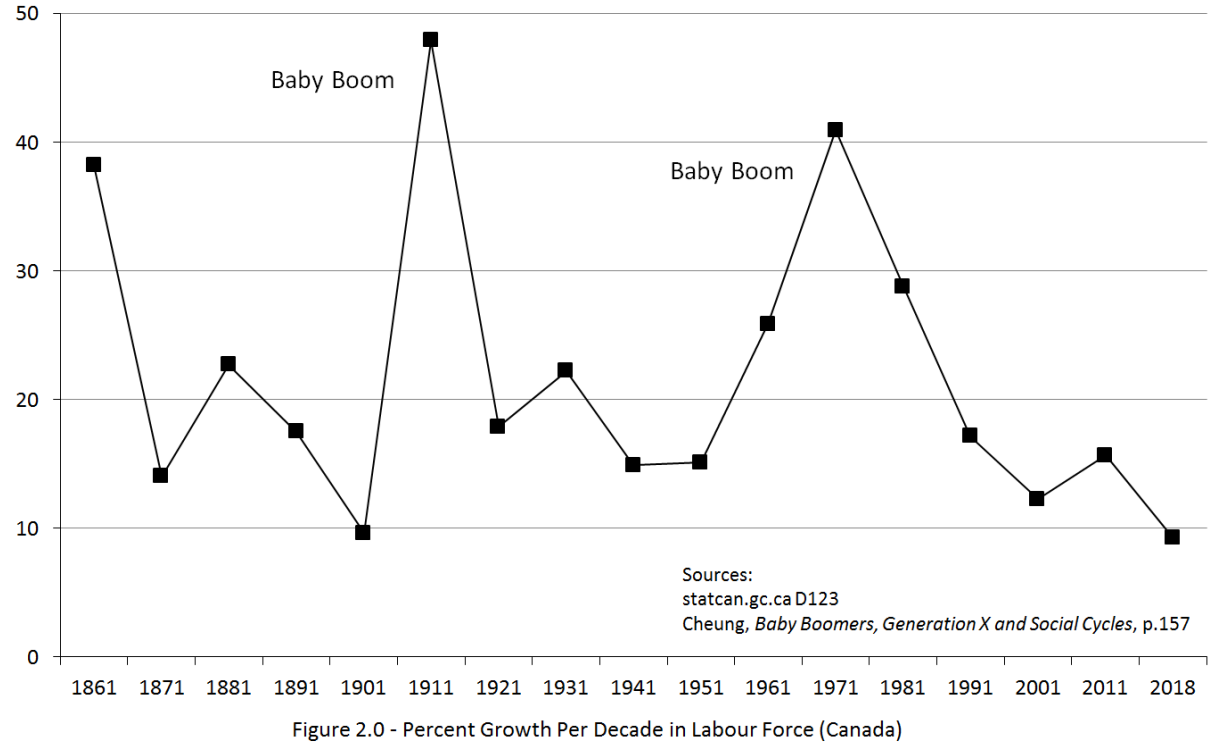


Figure 2.0 - Percent Growth Per Decade in Labour Force (Canada)

Figure 2.0 shows the percent growth per decade in labour force. The same ebb and flow seen in population growth can be seen in labour force growth. Population growth rate peaked in 1958. Labour force growth rate peaked in 1971, with the decadal data, as baby boomers were growing up and entering the labour market. Labour force growth reached its lowest level on the 160 year record in 2018, two years before the coronavirus pandemic.

In recent years there has been quite a bit of news about how, when baby boomers retire, there would be a smaller labour force, there would be a shortage of workers, and that the shortage of workers would put pressure on wages. The labour force is growing at record lows, yet there has been no pressure on wages. Instead, wage increases are at the same low rates as when the world had just come out of the Great Depression of the 1930s.

Growth per Decade

Transforming the data to a rate of change per decade, decade over decade, brings the data down to a scale that can be visualized, brings out longer term trends over shorter fluctuations, and makes all the data directly comparable. Transforming the data to per decade rate of growth allows us to compare annual population data with the decadal labour force data.

Inflation, Wage Gains, Interest Rates

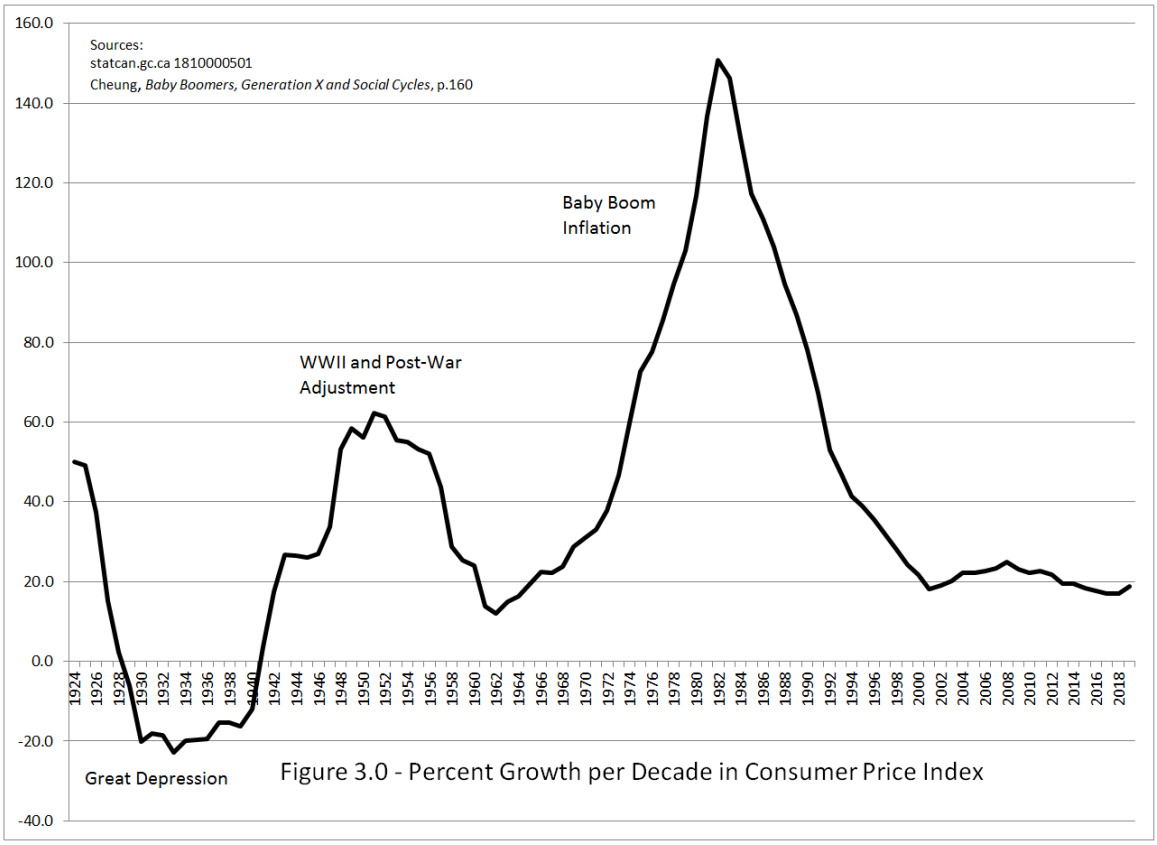


Figure 3.0 - Percent Growth per Decade in Consumer Price Index

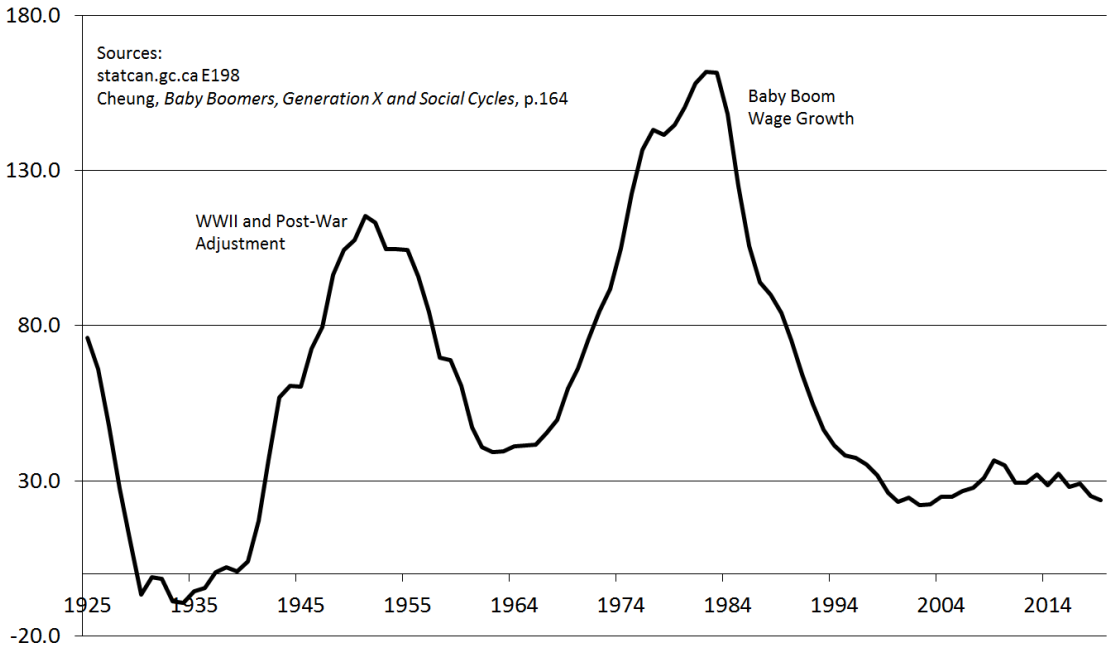


Figure 4.0 - Percent Growth Per Decade in Wages (Canada)

Figure 3.0 and figure 4.0 show the percent growth per decade in consumer price index and wages. Inflation and wage growth peaked a decade after the labour market growth peaked, that is after a large number of baby boomers had entered the labour market and became independent consumers. There were two major impacts on consumer prices and wages. World War II and the post-war adjustment was one major impact. A rapidly growing population was the other major impact. In the 1960s and 1970s, demographics had no role in the field of economic study. Inflation was viewed as a significant threat to the stability of the economy. Consumers were told to consume less and price and wage constraints were enforced. A family of two now had three to eight children to feed and that played no part in economic theory. The consumer market increased with population growth, but productive capacity had not caught up to consumer demand. Tight monetary policy and high interest rates set by central banks deterred industry from increasing productive capacity. Food and commodity shortages encouraged hoarding and speculation as prices spiraled out of control. Fears of resource depletion developed as prices soared.

After the 1980s, inflationary pressures declined and by the 2000s, the rate of inflation settled around the 2% range. Wage increases had declined to about the same rate as the early 1940s when the Great Depression ended.

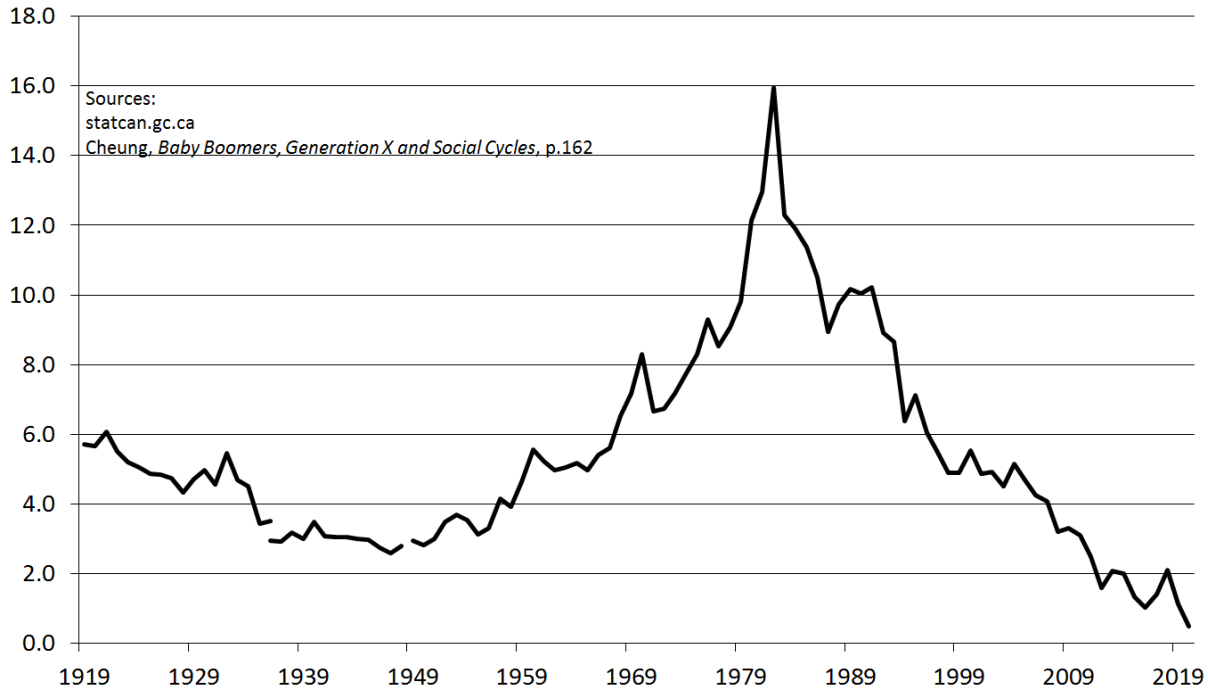


Figure 5.0 - Interest Rates on 10 Year Government Bonds (Canada)

Interest rates peaked at about the same time that inflation peaked with 10 year bonds reaching 16% in 1982. By 2011 interest rates on 10 year bonds declined to the lowest level on the 100 year record. In mid-2020 interest rates on 10 year bonds went below half a percent.

GDP

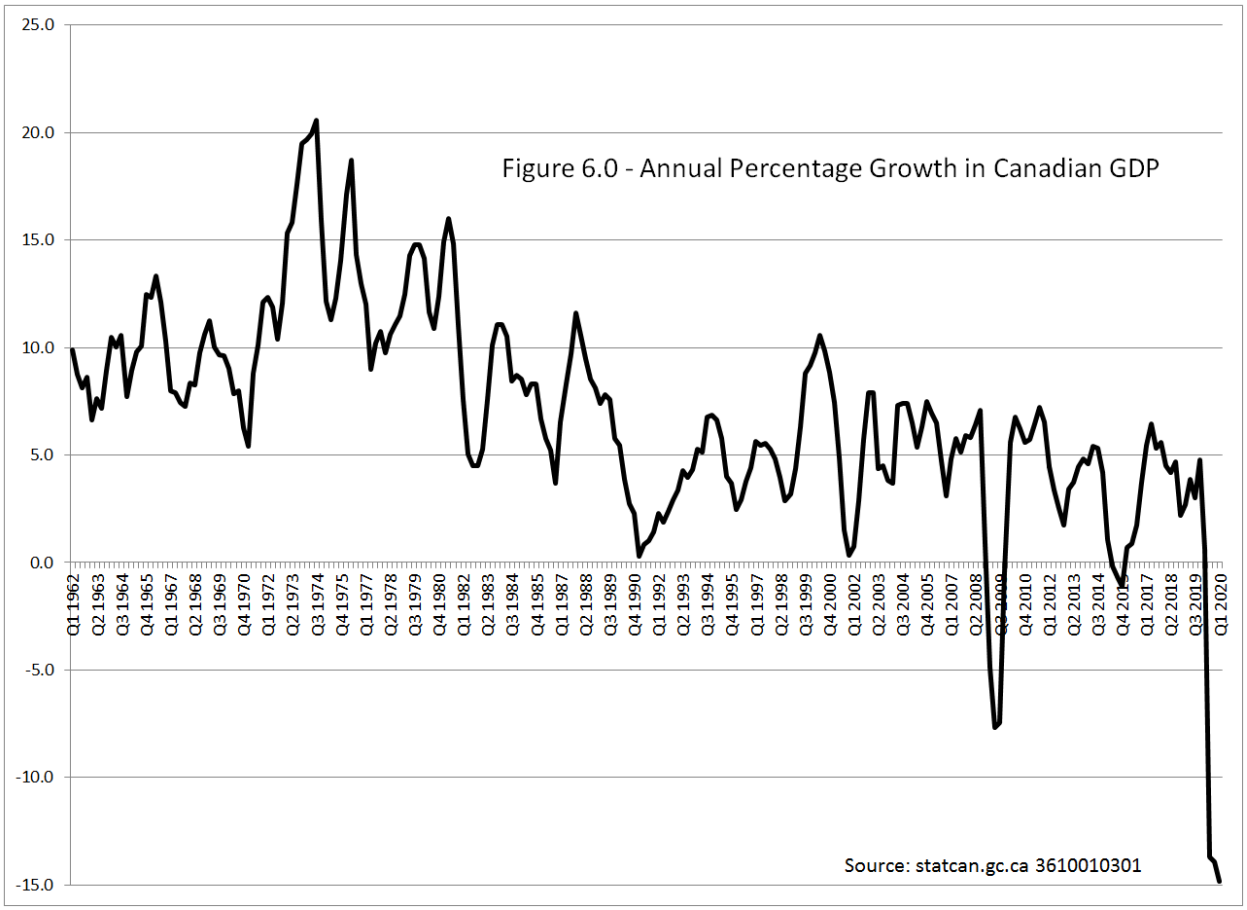


Figure 6.0 shows the annual percentage change in GDP. Annual growth rate peaked in 1974 at 20%. Annual growth rates have been on a declining trend for almost 50 years. GDP growth nearly entered negative territory in 1991 and 2001, but did so with the recession that came after the stock market peak of 2007. With the coronavirus isolation, the 2nd quarter GDP of 2020 was down 15% from a year before. The severity of economic downturns has been increasing since 1974.

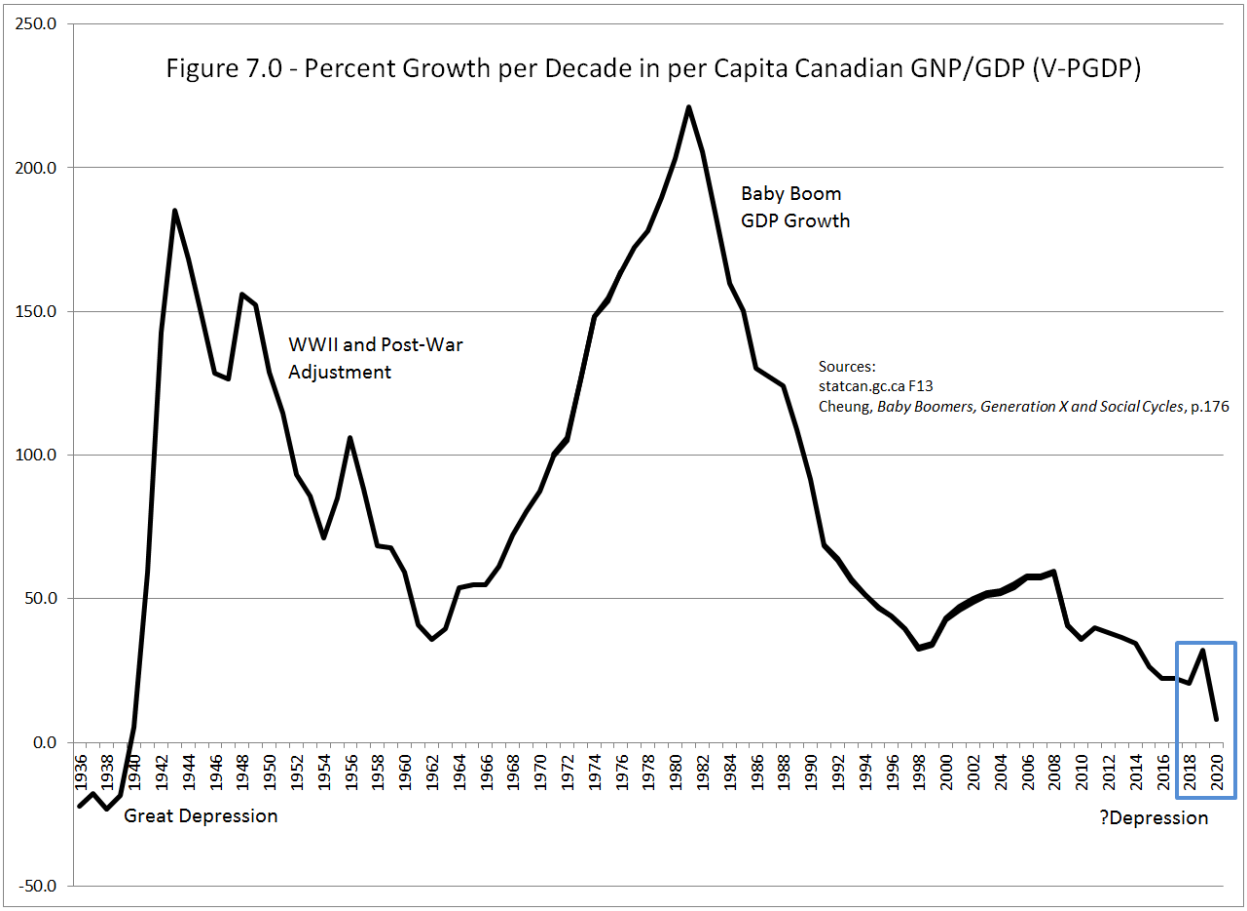


Figure 7.0 shows the percent growth per decade in per capita Canadian GDP (V-PGDP). The decadal growth rate peaked in 1981. Decadal growth rates have been declining for the last 40 years. The two significant impacts on economic growth - World War II and the baby boom induced economic growth - are similar to those in the inflation and wage gains charts (Figures 3.0 and 4.0). GDP growth mirrors the growth of the maturing baby boomers entering the workforce and the consumer population. The Great Depression of the 1930s is apparent on the left side of the chart. There is no formal definition of an economic depression, but this chart shows a natural definition of an economic depression. When the per capita GDP growth per decade is negative, there is an economic depression. The V-PGDP reached the lowest level since the Great Depression in 2018, rose in 2019, and has continued its downward trend in the first half of 2020. If Canadian GDP continues the downward trend to the end of 2020, then economic growth per decade will be at depression levels.

The complete lifecycle of the baby boom generation from the time that they were born to the time that they retire is reflected in the economic statistics. After 80 years of economic growth, with 60 of those years intent on fighting inflation, the Canadian economy faces the prospect of returning to the economic conditions that started the Keynesian economic revolution that was credited to giving us the tools to prevent recessions and depressions. Over 50% of Canada's GDP is from consumer spending, yet few saw this coming because demographics has an obscure role in economic theory.

Outlook

With an aging population and slowing population growth, there is slowing consumer demand. The economy becomes sluggish and downturns take longer to recover. Japan, the U.S. and many industrialized nations are facing similar demographic and economic situations. Despite pushing $7 trillion dollars into the financial system and accumulating assets valued at 34% of GDP, the U.S. Federal Reserve reached its inflation target of 2% only four times in the last decade. With the current economic downturn, the Chairman of the U.S. Federal Reserve has announced that it will let inflation run hot. The likelihood of inflation reaching past 2% for any sustained length of time is low, unless the money that the FEDs have pushed into the financial system makes its way to consumers, or government finances enter a period of unrestrained printing of money. The Bank of Canada should set its sight on sustaining employment and economic growth. Those will be the challenges for the next decade and possibly beyond.

Transforming Finance: A New Role for Central Banks

By Guy Dauncey

A chapter of my forthcoming book on The Economics of Kindness

Banking is an amazing example of cooperation at work. By enabling some people to pool their savings, banking enables other people to buy a house, start a business, or embark on an initiative that will benefit millions. Like everything, however, it can be done with kindness or with dominating self-interest.

How can we transform the world's financial institutions so that they enable us to build a new ecological civilization, rather than destroy our existing civilization through the ignorance and selfishness of capital-maximizing greed? This is a critical question that takes us to the core of our troubles.

We need to understand how money is created. In the beginning, among our primate ancestors and later among our hunter-gatherer ancestors, it was created by acts of kindness. Within their circles of trust and mutual dependency chimps and humans remember the kindnesses they receive on an invisible spreadsheet, and we feel the need to repay them. They become debts, which cease to exist when they are repaid.

When food surpluses became common, people began to accumulate possessions, awakening the impulse to achieve, perhaps to dominate. A would-be dominator could throw a huge feast. If someone could not respond in kind he might borrow, but if the harvest failed his family could become trapped in debt-slavery. When the élites changed the rules to permit the passing-on of inheritances, relationships of cooperation gave way to relationships of power. Unpaid debts became crimes against power.

When bankers sat behind their benches in 12th century Florence and Venice they started lending with pieces of paper that said "I promise to pay", but to hedge their bets they charged interest. They also discovered that they could issue more promises than they had money in reserve, trusting that their backers would not all demand their money back on the same day.

When you invest your personal savings, a dollar is a dollar. But when a financial institution invests it creates the new money out of thin air, limited only by Bank of International Settlements rules on how much it must keep in reserves. For every $10 in the vaults it might be allowed to create $100. To lend to other banks, it might be $50.

This is how all money is created. It happens whenever a financial institution issues a loan. It is neither exogenous (created by demand) nor endogenous (created by supply). It is mutualogenous, created by mutual cooperative agreement. The purpose of most banks and hedge-funds is no longer kindness, however, but self-interest.

A brief story. On Vancouver Island, before the white settlers arrived, the forest was ancient and huge. The early settlers persuaded the indigenous First Nations to sign treaties, tricking them out of land they had occupied for millennia and converting it to private ownership. In the 1990s a forest company in the Oyster River Division near Courtenay on Vancouver Island had harvested most of its old-growth forest, and was now cutting second growth. Its owners signed a sustainability agreement with the government limiting the cut to 400,000 cubic metres a year, which is around 10,000 logging trucks of timber. Then the owners converted their company into an income trust, which required it to provide an 8% return to investors. This required the cut to be tripled, so they dumped their sustainability commitments and began cutting up to 1.2 million cubic metres a year, stripping the mountainsides bare, causing dismay among the public and

the forest workers' union. The clearcut land no longer slowed the heavy winter rains. Rivers flooded, and the local water supply became so contaminated with silt and mud that local tax-payers had to spend $125 million dollars on a water treatment plant. All because of the desire of the investors to extract their pound of forest flesh. The investors win. Everyone else loses, including the trees, bears, cougars, elk, beavers, and the vast store of ancient forest carbon.

In 2018 the global Financial Stability Board estimated the total assets of all financial institutions to be $379 trillion,[1] including $247 trillion in credit/debt, every dollar of which is expecting a return.[2] In just eleven years between 2005 and 2016 the debt increased by 73%, requiring repayment by governments, non-financial corporations and private households.[3] Pandemic debt has increased this yet further.

Who is creating all this debt? If the interest is 5%, that's some $12 trillion a year, against a global GDP of some $90 trillion, causing almost 14% of all money to flow to the owners of capital as interest every year. And we wonder why there is such inequality.

The money has been created by some 220,000 financial institutions,[4] including 25,000 licensed banks, 80,000 mutual investment funds,[5] 89,000 credit unions,[6] 25,000 shadow banks,[7] savings cooperatives, building societies and public banks,[8] and tax-avoiding offshore institutions. Of the $247 trillion some $32 trillion (13%) is either being screened for socially responsible investment (excluding such things as fossil fuels, tobacco and armaments), impacted by corporate commitments to environmental, social and governance goals, or loosely impacted by corporate engagement or shareholder actions.[9] 87% is still chasing selfish returns, including investments that are financing ecological collapse, climate disaster, inequality, rising personal debt, unaffordable housing and resentful populism. Less than 1% is being invested in the renewable energy transition. Most of the finance for illegal fishing and rainforest destruction is channeled through tax havens.[10] And we wonder why we are in such trouble.

> *"This hidden tide of money flows constantly from the tired, the weak, the vulnerable, the huddled masses and victims of discrimination and abuse, from across London and Britain, through an immense filigree of financial pipelines to a relatively small number of mostly white European or North American men in Mayfair, Chelsea, Luxembourg, Jersey, Geneva, the Caymans and New York. This is the finance curse in action."* – Nicholas Shaxson[11]

The global financial system is not only inherently selfish: it is also inherently unstable. In *Rethinking Money* Bernard Lietaer showed that between 1970 and 2010 there were 145 banking crises and 208 monetary crashes. In 2008, gambling by the banks would have crashed the entire global system if it were not for state socialism in the form of central bank bail-outs. In America the banks' actions cost the economy $22 trillion. Housing prices collapsed. Ten million people lost their homes. Almost nine million people lost their jobs.

In *The Finance Curse: How Global Finance is Making Us All Poorer* the British tax-avoidance campaigner Nicholas Shaxson describes how between 1995 and 2015 Britain's financial sector caused a £4.5 trillion loss to the economy (£67,500 for every person in the UK) due to a combination of skills and resources being misallocated away from their most productive uses, the 2008 crisis, and excessive profits and bankers' pay.[12] Far from being the goose that lays the golden egg, Britain's banks are a cuckoo that is crowding out the fledgling sectors of the economy that could make Britain more prosperous.

In *Overcharged: The High Costs of High Finance*, the Roosevelt Institute found similarly that between 1990 and 2023 America's financial system will have imposed an excess cost of around $18 trillion on the economy ($54,500 for every person in the US).[13] The private equity mogul Wilbur Ross, commerce secretary under Donald Trump, muscled his way to control of a big chunk of the US steel industry. In

2005 he walked away with $4.5 billion, which was about how much the steelworkers and retirees lost in their health and pension plans.[14] And we wonder why people are angry.

During the opening months of the 2020 pandemic the wealth of American billionaires increased by $584 billion, while American households lost $6.5 trillion and 45.5 million people filed for unemployment.[15]

Even the New York Stock Exchange has fallen prey to predatory investors, who use supercomputers to catch a steal on other brokers and trade in dark pools of money through billions of orders a day, replacing the previous good governance with bad governance that rewards bad behavior.[16] Neoclassical economists claim that market-fixing such as this should not occur, but in the real world the impulse to dominate seizes every opportunity to crush the cooperative impulse. 70% of financial industry participants in America believe that today's capital markets are no longer fair to investors. Only 28% of millennials trust the banks to be fair and honest.

In a cooperative society money is a measure of reciprocal kindness. In a dominating society it is a measure of non-reciprocal obedience, backed by the threat of debtors' prisons, debt-collecting thugs, bankruptcy and eviction. Our financial system developed under the rule and culture of dominance societies, however, so most people's understanding of it exists in a mental box shaped by dominating power. When we climb up and look outside the box, however, a completely different world reveals itself. Starting in the 18th century, people with compassionate hearts and a cooperative impulse have created:

- Public money, based on trust in America's colonies and their economic growth.
- Public banks, creating money for the common good.
- Cooperative banks and credit unions.
- Ethical banks, such as Triodos and Bolivia's BancoSol.
- Methods of investing savings for the common good.
- Community currencies, such as the WIR in Switzerland.
- Interest-free banking.
- Mutual benefit, building and insurance societies.
- Central banks that use their money-creating powers for the common good.

We need to re-organize the entire financial system along cooperative lines. As soon as there is democratically strong political support, this can be done in nine giant steps, but it will require tens of thousands of financially-literate activists to work together globally. The urgency is dire, and the need is great, but the task is achievable.

Nine Steps to a Compassionate Financial System

1. Legislate a Ten-Year Transition to Socially Purposeful Finance

The first step is the same Ten-Year Transition proposed for business. Voluntary initiatives are never going to achieve what's needed: legislation is required. It will need a political party with the courage and a winning majority to propose it, but this is what all big change requires. By the end of the transition every financial institution (FI) in a nation that adopts the transition would be required to sign onto these ten commitments:

1. To adopt a Social Purpose Charter that states the FI's purpose, including a legally binding intent to pursue social and ecological purpose as well as financial purpose, creating a fiduciary duty to ensure social and ecological sustainability as well as profitability.

2. To use Integrated Reporting to track the use of natural, social and human capital as well as financial capital, and to publish climate and ecological risk assessment scorecards on all loans above a certain size.[17]
3. To respect central bank credit guidance and not invest in or lobby for any Red-Listed activities that will cause climate or ecological harm, or for any tax-avoiding company. (See below)
4. To prioritize long-term investing, in keeping with credit guidance from the Central Bank.
5. To embrace profit-sharing, offering an equity stake in ownership to all long-term employees, and to cap the pay and bonuses of executives at a negotiated ratio of the lowest worker's pay.
6. To strive to have at least 50% women and racial diversity on the board of directors.[18]
7. To encourage workplace democracy, allowing long-term workers to elect 50% of the directors.
8. In the event of sale, closure or impending bankruptcy, to grant first right of refusal to workers, community organizations or governments that may wish to buy the institution.
9. To pay taxes fairly, and not engage in transfer pricing, offshore banking or the use of tax havens.
10. For financial institutions with above $100 million in annual revenue, to appoint a public board of trustees to be accountable to the public good.

In return, financial institutions would receive three public benefits: $100,000 deposit insurance; daily procedural assistance from the Central Bank and access to the government bond market; and *in extremis* a public bail-out, subject to partial or total public ownership. Social purpose banking would become the norm. Non-compliant banks would be denied a license to operate.

The Sovereign Money school of thought says that banks should be stripped entirely of their power to create money, and be able to lend only their reserves. The argument is that the power to create new money should belong to the government. My view is that humans have an inherent right to trust someone and to offer a loan that sets up a reciprocal debt, but not in a way that causes harm to humans or Nature.

By the end of the transition banks would operate as public utilities providing a much needed service, following democratically determined credit guidance that would govern their ability to create money. Some financial institutions might choose to leave the country, but the data shows that socially responsible loans are less risky and perform better, so most banks might go along with the transition, once they get over the shock to their self-importance. For those that do walk away we will need global change.

2. Support Cooperative, Community and Ethical Banks

The second step is legislation enabling the development of many more cooperative banks, community banks, ethical banks and credit unions to meet the everyday needs of the economy. After the transition they would share the market with social purpose private banks.

The Indian state of Kerala, with 11,000 cooperatives, has a state-wide cooperative bank that supports Kerala's network of 980 cooperative banks and 1,647 agricultural cooperative credit societies. In Britain, the Community Savings Bank Association plans to launch a similar network of eighteen regional cooperatively-owned banks.[19]

Members of the Global Alliance for Banking on Values, who share $163 billion in assets, wants to change the entire banking system so that it supports full spectrum sustainability. Its members include Vancity Savings in British Columbia, Rabobank in Holland, Triodos Bank in Europe, Merkur Cooperative Bank in Denmark, First MicroFinance Bank in Tajikistan, Banca Etica in Italy, BancoSol in Bolivia, and Muamalat Bank in Malaysia.[20] This is a worldwide movement. In 2013, the ILO's *Resilience in a Downturn: The Power of Financial Cooperatives* found that community-based financial institutions out-performed investor-owned banks during the 2008 financial crisis on almost every rating.[21]

Social purpose banks can also offer interest-free loans, as the cooperative JAK Bank does in Sweden. Established in 1997, it enables members to borrow without interest based on personal savings. In 2016 their 36,000 members shared $277 million in assets and the bank earned a 92% ecological sustainability rating.[22] A member who wants to take out a loan must first save, usually on a monthly basis. In effect, members are borrowing from their future selves. Members can also provide loans for local enterprises, which are guaranteed but don't receive interest.[23]

Jewish Free Loan Toronto does much the same, with 800 active loans in the community worth over $3 million.[24] In the Jewish tradition lending money without interest is the highest form of charity, better than giving money.[25] Interest-free banking also happens in the Islamic world, where a lender participates in the risk and return on investment instead of receiving interest, and where a bank provides 100% of the capital and shares the profits with the entrepreneur, but in the event of loss carries it all.

Money created by a bank ceases to exist when the loan is repaid - but where does the money for the interest come from? As long as there is economic growth, borrowed dollars hopefully fuel business innovation, earning the money to pay the interest. In an economy without economic growth, however, the interest must come from the borrower's personal wealth. Debt of this kind therefore quickly becomes a guarantor of rising inequality. In ancient agricultural times, before economic growth, rulers felt it wise to announce occasional jubilees when all debts were forgiven, not out of the kindness of their hearts but to protect themselves from being murdered and their palaces looted by starving peasants.

Interest has a positive function if it inspires loans that will leverage innovation to increase productivity and growth. Without such loans, the railways would never have been built and the industrial revolution would never have happened. Loans have a negative function, however, when increased productivity pours fuel on the climate and ecological fires, or when they create non-productive debt, increasing the likelihood of a crash. Logically, it might appear to have no place in an economy that is ecologically stable without growth. When the economists Tim Jackson and Peter Victor tested the hypothesis that an interest-based money system necessarily requires growth, however, they found that a stationary economy was quite compatible with interest-bearing debt and commercial credit creation, throwing a question mark into the debate about the compatibility of interest-bearing debt and a steady-state economy.[26]

3. Establish Public Banks

The third step is legislation enabling the establishment of a public bank in every city, state and province. Public banks create money too, but they do so with social purpose, guided by democratically chosen preferences. In Germany, Sweden, Denmark, Italy, Spain and France community and state-owned public banks serve as much as 64% of the banking market. In France, the Caisse des Dépôts et Consignations, founded in 1816 with $200 billion in assets, is now a major source of financing for the construction of affordable housing. It also manages pension funds, provides finance to small to medium businesses, and emphasizes long-term investing.

In *Banking on the People*, the American financial visionary Ellen Brown writes that Germany's public Sparkassen banks have a return on capital that is several times greater than Germany's private bank sector. Kreditanstalt fur Wiederaufbau (KfW) has been the main source of financing for building retrofits to tackle the climate crisis. As well as financing Germany's small and medium-sized businesses, public banks have provided 72% of the financing for Germany's solar and wind installations. In Bangladesh, the publicly-owned Infrastructure Development Company provided the capital to install more than three million solar panels in rural areas.

In Britain and America, public banks are still pretty much unknown. The Bank of North Dakota was formed in 1919, followed by the Alberta Treasury Branch, but that is pretty much it. The defaulting of the

slavery-based banks of Mississippi, which were backed by the state legislature, may be responsible for their absence.

By 2020 twenty-five initiatives to establish public banks were being pursued by both progressives and conservatives. When California's Public Banking Act 587 passed a critical stage Assemblywoman Lorena Gonzales said, "This is long overdue. We need to take the profit out of banking in order to invest in our communities that have been left behind by Wall Street."[27] Americans and Canadians are also campaigning to turn post offices into local savings banks,[28] liberating people from the perils and greed of payday lenders who charge an average interest of 400% pa, sometimes as high as 700%.[29]

4. Take Failing Banks into Public Ownership

In 2008 the Royal Bank of Scotland was saved from collapse by a £45.5 billion government bailout. Sir Fred Goodwin, the bank's CEO, was fired and retired on a pension of £703,000 a year, after being called a benefit scrounger and a cataclysmic failure. He later gave up £200,000 a year to appease public anger and was stripped of his knighthood.[30] The bank remained in private hands, however, and in 2014 it was fined for rigging the foreign exchange markets. In 2020 it was still technically 62% owned by the government, which has made little effort to change the way it operates.

The fourth step, therefore, is to place failing banks in public ownership and give them a social purpose mandate. This is what the Belgian government did with Dexia, their fourth largest bank, when it bailed it out, renaming it Belfius and giving it a public interest mandate that emphasizes social and climate goals, governed by a democratic structure with considerable decision-making power at the local level.[31]

In 2014 Britain's New Economics Foundation proposed breaking the Royal Bank of Scotland into 130 public banks supervised by citizen stakeholders, arguing that this would boost Britain's GDP by £30 billion over the next three years. The new banks would increase credit for the real economy by lending to small and medium enterprises, improve the diversity and resilience of Britain's banking system, offer a current account to every British citizen, rebalance the economy by increasing investment in regions outside London, and provide greater financial support for local social, cultural, and sporting activities.[32] What's not to like?

5. Support Socially Responsible Investment

Step five is to change the investment playing field to incentivize socially responsible investment (SRI), making it eventually the only kind of investment that exists. SRI has made vast leaps since it started in the 1980s. By 2017, $12 trillion was being screened in the US for socially responsible concerns,[33] and 1065 institutions had divested themselves of $8.77 trillion, thanks to the persuasiveness of the student-led fossil fuel divestment movement.[34] Swiss Re, one of the world's largest re-insurance companies, is shifting its $130 billion investment portfolio to ethical sources;[35] Norway's $1 trillion Sovereign Wealth Fund is disposing of most its fossil fuel investments, directing the money instead to renewable energy. Many investment companies have joined Climate Action 100+, a five-year initiative that is working to ensure that the world's largest corporate carbon polluters tackle the climate emergency. By 2019, 370 investors with $35 trillion under management had signed a statement of climate intent.[36]

Do such investments pay? In 2017 a study of 10,000 mutual funds found that most sustainable equity funds had an equal or higher median return and equal or lower volatility than traditional funds. Another study found a positive relationship between sustainability and the financial performance of stock prices in 80% of the 41 studies reviewed.[37]

What about a big player like BlackRock, with $6.5 trillion under management? BlackRock's CEO, Larry Fink, has written to the CEOs under his watch that "every company must show how it makes a positive contribution to society." The intention can be applauded, but Blackrock invests more money in climate-destroying companies than any other investor, and its board consistently votes against shareholder demands for transparency and climate action. Its investments in the Tar Sands, the Arctic, the Amazon and Indonesia are making the climate emergency worse.[38] BlackRock invests in Golden Agri-Resources, for instance, which in turn invests in Golden Veroleum Liberia, which bought a 65-year concession to clearcut 260,000 hectares of Liberia's Upper Guinea Forest to grow palm oil for processed foods, chocolate, baked goods, cosmetics, soap and cleaning products. The Upper Guinea is the largest intact forest in west Africa, home to 2,000 species of flowering plant, 1,000 different insects, 240 varieties of tree and 150 mammals, including the endangered pygmy hippopotamus. This is where global finance bites into the fabric of nature and spits it out, transforming forests full of wildlife into dead numbers on a spreadsheet. BankTrack found that Golden Veroleum has had "a devastating impact on people and the environment … and a consistent record of land degradation, human rights violations and disregard for community land rights."[39] Were it not for organizations like BankTrack and the Rainforest Action Network, profit-chasing finance would quickly wipe out all of the world's rainforests.[40]

How can investments be directed towards social responsibility? To support the Ten Year Transition, we need a legislated Red/Amber/Green taxonomy of investment opportunities, creating a scorecard for social and environmental benefit or harm that could be used in the assessment of investment opportunities. This is not a fantasy: the European Union is deep into the weeds of developing just such a taxonomy.[41] In the meantime, a ban on fossil fuel and rainforest destroying investments could be imposed on all public pension funds, and tax reductions could be created for income from socially responsible investments.

- Green-Listed investments would pay less tax and have access to a lower interest rate from the Central Bank.
- Amber-Listed investments would pay higher tax on profits. Banks would have higher reserve and margin requirements, imposed interest rate ceilings, and greater supervisory pressure.
- Red-Listed investments in activities deemed harmful to future generations or the nine planetary resilience boundaries would not be allowed.

If the Ten-Year Transition was enacted in America BlackRock would have to decamp to another country, or be unable to invest in Red-Listed activities, including non-certified palm-oil plantations. The challenge would be in monitoring and enforcing the certification, which currently falls to the Roundtable on Sustainable Palm Oil, whose members are responsible for only 19% of global palm oil production.[42]

What of ordinary people who want to invest in their local communities? Locally-owned businesses represent between 60% and 80% of most economies. They are highly profitable and competitive, yet disconnected from the trillions of dollars that are invested in mutual funds, pension funds, and insurance funds that control long-term retirement savings. If that proportion of people's savings was invested in local communities, in America (for instance) between $34 and $45 trillion would shift to local companies, instead of going to the big corporations that are monopolizing our economies. Each community of $10,000 people would have $1 billion to invest. A city of 100,000 people would have $10 billion.

In America, Michael Shuman has shown how this is possible in *Put Your Money Where Your Life Is: How to Invest Locally Using Self-Directed IRAs and Solo 401(k)s*, and the website www.thenextegg.org. Nova Scotia has a law allowing community groups to set up local investment funds, as a result of which $100 million has been invested locally through 60 funds. If America had similar legislation it could have 21,000 such funds, and local brokerages would flourish.

6. Embrace Credit Guidance

The sixth big step is to embrace central bank credit guidance. Neo-classical economists view any interference in the free market process of credit creation as an unwarranted disturbance of the holy laws of economics. They preach that any unfortunate side-effects pertaining to the use of credit, such as the climate or ecological emergencies, should be treated as externalities, and left in purgatory.

In the real world, many governments work with their central banks to issue credit guidance, directing money-creation towards the common good. In the post-war period the governments and central banks of Europe, Canada, the US, Japan, Taiwan, South Korea and China all used credit guidance to direct loans towards productive industries for exports and manufacturing, away from consumer purchases. In the period 1945-1980 credit guidance was used to support economic growth, shaping markets by means of credit ceilings, quotas, interest rate ceilings, portfolio restrictions, collateral requirements, supervisory pressure, moral suasion, subsidies for home purchases, mortgage guarantees, and credit subsidies for exports, agriculture and small-to-medium enterprises.

In *Credit Where It's Due: A historical, theoretical and empirical review of credit guidance policies in the 20th century*, Dirk Bezemer and his coauthors have written a fascinating history of credit guidance in the postwar years and its abandonment due to neoclassical theology in the 1980s, leading to an excess of debt creation for private purposes, the US sub-prime mortgage crisis, the financial crisis of 2008, the worldwide housing price bubble, the affordable housing crisis, and the private debt crisis.[43] Bezemer shows that the abandonment of credit guidance permitted banks to reduce money-creation for productive purposes from 60% to 40% of their loans, and to increase loans for purely financial purposes from 40% to 60%, providing the financial fuel that has enabled financialization, housing price inflation, and the increase in personal debt. His conclusion is that governments should adopt credit allocation policies that support sustainable economic growth in priority sectors, as India, Bangladesh and China have done.

Credit creation could also be directed towards long-term investments that reduce systemic risk. Loans for fossil fuel development and rainforest destruction would be Red-Listed (banned), and money-creation would be directed instead towards loans for sustainable Green-Listed ventures.

7. Suppress Domination

The seventh big step reflects the fifth principle of the economics of kindness: suppress domination. In the financial sector the dominating impulse reveals itself as predatory private equity, vulture funds, corporate raiders doing hostile takeovers with borrowed money, payday lenders, deceitful derivatives, banks that are 'too big to fail' gambling with risky ventures and accepting vast public bail-outs when they do fail, and executives who revolve in and out of the regulatory agencies, corrupting the process of good governance, lobbying to protect their influence and bribing political parties with campaign donations to blunt their desire to enforce change.

If a bank is too big to be allowed to fail, it should be broken up. A cooperative economy needs fair competition, not foul collusion, which requires the break-up of monopolies and oligopolies. As well as the initiatives outlined above, a cooperative financial system will need regulations to control lobbyists and limit executive pay and bonuses, using words in plain English.

8. Central Banking for the Common Good

Central banks are another great demonstration of cooperation at work. They are an insurance system for the banks that benefits us all. The eighth step is to change their mandate, enabling them to extend their powers to tackle national and global emergencies.

In countries that control their own currency, central banks create money. They use this power to increase the money supply, using euphemisms such as increasing the credit supply, injecting liquidity, monetizing the deficit, open market operations, buying securities, expansionary monetary policy, expanding the balance sheet, or quantitative easing.[44]

Private money creation has its origin in personal gifts, where the giver expects the gift to be reciprocated, the debt repaid. Central bank money creation has a different origin. When an elder or child is sick, the clan members give of their time and effort without any expectation of a return. Seen through the lens of self-interest, it makes no sense, but the clan knows that the wellbeing of one requires the wellbeing of all. It is a social gift. The giving expresses trust in their culture as a whole, and the knowing that if they were to neglect their children or their elders the spiritual weakness created by this unkindness would weaken them all. It is a practice saved for emergencies, not done every day.

Seen through this lens, central bank money-creation should be kept for emergencies, and not used purely to keep profits flowing to the owners of private capital.

Knowing that greedy kings and rulers have often abused their power to manipulate the money supply, central bankers understand the importance of independence, and their need to support the stability of the economy regardless of the government's wishes. Their thinking exists in their own mental bubble, however, in which it seems natural to support their fellow bankers and financiers, who are assumed to hold the key to economic stability.

Thus when the central banks of America, Britain, Japan and Europe injected $9 trillion into their economies to stave off the 2008 financial meltdown, calling it quantitative easing (QE), they did so by purchasing toxic and effectively worthless assets off the banks, giving them a massive injection of liquidity (cash). Their intention was that the new money would lower interest rates and increase the banks' reserves. The banks would lend to companies, which would invest in new ventures, creating growth and jobs for all. That's not what happened, however. Because of economic uncertainty, businesses didn't want to invest; their animal spirits were feeling bearish. So the banks lent much of the new credit into the housing market, where it caused inflation, contributing to today's appalling housing crisis. They also lent for stock market purchases, contributing to inflation in the Dow Jones and other financial indexes. In both instances they created more private debt, charging interest on every dollar.

What if they had acted differently? Governments could have issued climate bonds and affordable housing bonds and central banks could have bought the bonds off them, pumping the money directly into affordable housing, transit, bike lanes, renewable energy and regenerative farming, putting wages in workers' pockets and stimulating aggregate demand. It achieves the same goal as Milton Friedman's proposal to drop money out of a helicopter, and Keynes' tongue-in-cheek proposal "to fill old bottles with bank notes, bury them at suitable depths in disused coalmines ... and leave it to private enterprise on well-tried principles of laissez-faire to dig the notes up again", but it does so with more wisdom and purpose. In Europe, Positive Money Europe has proposed just this, calling it 'QE for People'.

As well as creating social gift money, a central bank can issue interest-free loans for affordable housing, renewable energy, building retrofits and the electrification of transit, with loans that pay for themselves. Being a public entity, a central bank does not need to charge interest. In addition, a public bank can raise the money for such investments as green bonds, with the central bank becoming the buyer of last resort, guaranteeing their market price, as the economic historian Adam Tooze recommends.

The former is what the Bank of Canada did during the 1950s and 60s, providing zero-interest loans to finance the construction of the St. Lawrence Seaway, the TransCanada Highway and various hospitals and schools. They continued doing so until 1973, when the Bank of International Settlements got the

Gospel of Neoliberalism and demanded that Canada, France and other countries cease printing money to meet their public investment needs and borrow the money instead from the private sector, paying interest on every dollar.

In China, where they do not care about the Bank of International Settlements any more than Luther cared about the decrees of the Pope, the use of credit guidance and public banking have enabled massive investments in green technology:

- 99% of the world's electric buses are in China.
- Shenzheng has completely electrified its fleet of 16,000 buses.
- In 2018 China's people bought over a million electric vehicles, compared to 410,000 in Europe and 360,000 in the US.
- In 2018 China installed 44 GW of solar PV, increasing cumulative capacity to 175 GW, compared to 50 GW in the US and 11 GW in Europe.

In today's old economy, most central bankers assume that their role is to manage monetary policy by juggling inflation rates, economic growth, employment and currency stability. In a cooperative economy they would embrace **a democratically-guided five-fold mandate**:

1. To be the ultimate repository of financial trust, preventing and resolving financial crises.
2. To regulate the volume of money in the economy to meet the needs of economic growth, limit inflation, limit unemployment and stabilize the currency.
3. To regulate the volume of interest-bearing debt, distinguishing between productive and parasitic debt, managing public debt, and controlling the risk of high private debt relative to GDP.
4. To issue credit guidance regarding the democratically determined purposes for which banks can create money as debt.
5. To create gift money to assist in the resolution of emergencies, including the climate and biodiversity emergencies and the affordable housing crisis.

In Japan, the Central Bank has been quietly acting on part of #3 for several years, creating money to transfer the Japanese government's vast federal debt to its books, effectively retiring it. No inflation has been forthcoming.

Clearly, a central bank can't print whatever money a government might demand. If a country is flooded with money its value will collapse, causing hyperinflation. In happened in Germany in 1921, Hungary in 1946, Zimbabwe in 2018, and Venezuela in 2019. Michael Hudson, Professor of Economics at the University of Missouri–Kansas City, has pointed out that inflation need not follow if an economy has the ability to absorb the money. It was not the printing of money that caused Germany's hyperinflation, but Germany's need to pay reparations abroad. Following their defeat they were ordered to print Deutsche Marks to obtain foreign currency to pay the Allies, so that the Allies could pay for the arms they had bought from the United States. It was the collapse of Germany's foreign exchange that caused the hyperinflation, not domestic spending.[45]

In Britain and Canada the new mandate could be approved if the governments were to say so. In Europe it would need a ruling by the European Commission. In America, the Feds would first need to be democratized, becoming "a new public institution that truly understands that its obligation is to society, not money markets," as William Greider puts it. Congress would then be able to harness the Fed's money creation powers to finance major public objectives.[46]

The World Future Council's chief economist Matthias Kroll has proposed that the world's central banks work together to buy $300 billion a year in climate bonds annually, leveraging private investments of $2

trillion a year for the transition to renewable energy. In her April 2019 speech to the Bank of England, Sarah Breeden, Executive Director of International Banks Supervision, spoke to the estimated $90 trillion that will be needed to finance the climate transition by 2030, and the opportunity for the financial sector to make green finance mainstream:

> "Climate change poses significant risks to the economy and to the financial system, and while these risks may seem abstract and far away, they are in fact very real, fast approaching, and in need of action today (…) We can already hear distant thunder, but we must not wait for the storm to hit. We need to work together internationally and domestically, private sector and public sector, to achieve a smooth and orderly transition. The window for that orderly transition is finite and closing. And our work to seize that opportunity could not be more important. Indeed it is not an overstatement to say that the future of our planet depends on it. All hands on deck."[47]

9. Global Financial Agreements

Ah, the freedom of unregulated global capital. Today, it's in Thailand. Tomorrow, based on an algorithmic decision by a Wall Street computer, it's in Indonesia financing the development of a new coal mine. It is capital's ability to go wherever it wants that the British financial author and activist Ann Pettifor targets as the biggest obstacle to climate solutions in *The Case for The Green New Deal*. If a nation is to be in charge of its investments, she argues, it must be in charge of its exchange rates, its credit creation, and its interest rates, and it must find a way to bring offshore capital back onshore. Otherwise, whenever a financial difficulty arises and footloose capital flees the country governments will have to raise interest rates to lure capital back into the country, raising the cost for every business that has a loan or a line of credit. Worse, governments will be obliged to sell off assets, or go cap in hand to the IMF for a loan in return for conditions that make it even easier for capital to come and go, even though that was the cause of the problem in the first place.

This freedom of capital is written into thousands of trade agreements, prohibiting countries from pursuing their own economic development strategies. "These prohibitions are particularly strong for countries that have agreements with the United States," she writes. "The imperial power of the United States is used to enforce both the reality and the ideology of unfettered, globalized capital mobility."

Capital controls are common in China, which uses them to restrict investment in foreign companies and overseas real estate, although if you live in Vancouver it's hard to believe it. Step nine would be the use of capital controls to restore financial control in other countries around the world.

How could a government respond to the financial temper tantrums which would likely follow any such action? Even a minute's notice of restrictions can cause electronically nervous computerized capital to flee. Step nine therefore also requires a global treaty to close down the offshore world, and prevent a rush to the bottom, with banks moving their head offices to countries whose governments don't give a damn. It will be politically hard, but it is not technically complicated. As Sarah Breeden says, all hands on deck.

About the Author

Guy Dauncey is an anthropological economist who works to develop a positive vision of a sustainable future, and to translate that vision into action. He lives on Vancouver Island. He is founder of the BC Sustainable Energy Association, co-founder of the Victoria Car Share Cooperative, and the author or co-author of ten books, including *The Climate Challenge: 101 Solutions to Global Warming* and *Journey to the Future: A Better World Is Possible*. He is currently completing his 11th book, titled *The Economics of Kindness: A Ten-Year Transition to a Green Cooperative Economy*. He is President of the Yellow Point Ecological Society, and a Fellow of the Royal Society for the Arts. His website is www.thepracticalutopian.ca.

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From: Michel Darveau <michel.darveau@videotron.ca>
Sent: October 7, 2020 11:37 AM
To: Stakeholder Relations <stakeholderrelations@bank-banque-canada.ca>
Subject: {External} Politique monétaire et inflation

Bonjour,

Dans la discussion sur l'inflation, je crois qu'il est important de définir ce qu'on entend par ce terme.

Je crois que la plupart des économistes s'entendent pour dire que l'inflation représente la hausse, au cours du temps, du prix d'un certain panier de biens. Le panier étant fixe, du moins à court terme.

Par contre, la plupart des gens y voient la hausse du coût de la vie, ce qui tient compte de l'évolution du panier de base au cours du temps. Il y a plusieurs décennies, personne n'avait de téléphone cellulaire, d'ordinateur personnel, de connexion Internet et de nombreux autres gadgets qui sont maintenant essentiels à la vie courante. De plus il n'y avait généralement qu'un véhicule par famille alors que la norme est maintenant d'en avoir deux. Ceci fait en sorte que les familles dépensent de plus en plus et leur revenu disponible ne suffit plus. Ce phénomène fut compensé par l'arrivé massive des femmes sur le marché du travail, mais ceci étant fait, il n'y a plus beaucoup d'options pour augmenter le revenu familial.

Les ménages canadiens ayant de plus en plus de difficulté à équilibrer leur budget ne comprennent pas comment la Banque du Canada peut prétendre que l'inflation n'est que de 0.3% ou 0.5%. Ils sont donc convaincus qu'on leur ment et qu'on trafique les chiffres.

Pour ce qui est de la croissance économique, il ne faut pas confondre l'effet et la cause. Il est connu qu'une économie en croissance crée de l'inflation. Mais il est faut de croire que l'inflation crée de la croissance. De même, l'absence d'inflation ne crée pas la récession.
L'idée que les consommateurs retardent des dépenses en l'absence d'inflation est fausse. Ils n'attendront pas de possibles baisses de prix avant d'acheter. Si c'était vrai, personne n'achèterais jamais d'ordinateur, de téléphone ou autre appareil électronique. Ils n'ont pas cessé de baisser de prix depuis les dernières décennies et se sont vendus quand même en grand nombre.

Baisser les taux d'intérêts pour créer de l'inflation est une fausse solution. Le but étant de créer de la croissance économique, la solution adoptée devrait directement affecter la croissance. Ceci inclus des subventions directes aux entreprises créant de l'emploi ou de l'aide directe aux consommateurs pour stimuler certaines dépenses.

De moins en moins de canadiens disposent de fonds de pension à prestation déterminées. Ils sont donc de plus en plus nombreux à devoir économiser pour la retraite. Les bas taux d'intérêts impliquent un faible rendement des épargnes ce qui réduit l'augmentation du capital à long terme et augmente le capital requis pour obtenir le même objectif de revenu. Ces deux facteurs se combinent et impliquent une hausse importante du taux d'épargne requis pour le même revenu de retraite.
C'est autant d'argent non disponible pour alimenter la croissance économique. Les faibles taux d'intérêts ont donc l'effet de réduire la croissance économique, du moins chez ceux qui sont prévoyants et qui économisent.

Une autre façon fréquemment citée pour stimuler la croissance est une augmentation de la population. C'est aussi une fausse solution. D'un point de vue global, la population actuelle excède déjà les ressources disponibles. Il est certainement possible d'encore augmenter ces ressources mais cela aura des effets délétères sur le climat et les milieux naturels. Il serait plus approprié de limiter l'augmentation de la population mondiale et éventuellement de la réduire à un niveau plus acceptable. Les pays existent de toutes les tailles et il n'y a pas de corrélation entre la taille et leur prospérité. Si la taille n'est pas un indicateur de prospérité, pourquoi la croissance de la population devrait-il en être un? De toute façon, aucun système ne peut croître à l'infini. Il est impératif de trouver un mode d'opération qui peut générer de la croissance économique avec une population constante. La croissance économique se traduira par une augmentation du revenu disponible pour les ménages. Ce qui implique une hausse de productivité des travailleurs.

Il serait plus approprié que la Banque du Canada favorise des taux d'intérêts qui fournissent un rendement adéquat aux épargnants et qui tiennent compte du niveau de risque encouru par les investisseurs. Il est anormal que des entreprises au seuil de la faillite réussissent à vendre des obligation à long termes à des taux de 2% ou 3%. Plusieurs d'entre elles feront éventuellement faillite ce qui pénalisera grandement ceux qui ont acheté ces obligations.

Un autre effet pervers des bas taux d'intérêts est la hausse vertigineuse du prix des maisons. Elles sont maintenant inaccessibles pour la majorité des ménages canadiens. Évidemment, les paiements mensuels ne sont pas trop élevés aux taux actuels, mais personne ne devrait s'engager avec une hypothèque à long terme aux taux actuels car cela est beaucoup trop risqué si les taux venaient à augmenter dans le futur. Si au moins les banques pouvaient offrir des hypothèques de 25 ans à taux fixe, cela éliminerait le risque pour l'acheteur en cas de hausse de taux. Mais aucune institution canadienne n'offre ce type d'hypothèque.

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