General Discussion: Crisis Management in the COVID-19 Economic Shutdown

Chair: Susan M. Collins

Ms. Collins: Our panelists have provided three nuanced perspectives on crisis management. While quite different, each thoughtfully took into account key longer-term trends that we're seeing—from structural trends to issues of trust. There were a number of comments, as well, related to public engagement, which of course harkened back to the discussion that started this morning's session. I'll begin with some questions of my own. Listening to the three presentations made me think about what each of you sees as the legacies, the long-term impacts of the kinds of adjustments that are being made in each of your monetary authorities right now. In addition to hearing more about that, I also think it would be quite interesting to hear perspectives from Canada, and from the ECB, about the concerns related to the small and medium-sized firms that Tharman (Shanmugaratnam) mentioned toward the end of his remarks.

Ms. Swonk: I wanted to ask a question on communication. I think we really do need to be talking to the public more but I wanted to get your thoughts on two areas. One is bridging the gap between what consumers and the broader public see as inflation and what Wall Street sees as inflation. The public reports higher inflation, while Wall Street has lowered inflation expectations. How does the Fed square those with the public? Second, I think that we all agree that the pandemic is largely a disinflationary event, but there is a risk we suffer a supply shock much of like we have already seen in the food supply chain. How do those complicate this messaging?

Mr. Rehn: Thank you Susan and many thanks for the great panel. Picking up from Philip Lane's excellent remarks I'd like to ask a question on the effect of the strong policy stimulus on productivity. I very much agree with Philip that setting up the PEPP program at the very early stage of COVID-19 expressed and resulted from the commitment of the ECB Governing Council to react quickly and forcefully to the crisis. It is important to emphasize the flexibility of PEPP as a key determinant of its success. So, it was not only about size, but also about design. This flexibility sent a strong signal to the markets of the Governing Council's commitment to prevent the widening of spreads in the euro area.

Now, against this backdrop, let me pose a longer-term question on the impact of QE like PEPP on productivity. As some recent research maintains, would you conclude as Option A that the strong monetary and fiscal stimulus today could damped or even water down the restructuring effect in the economy, support so-called "zombie" firms, and thus have a negative impact on productivity? Or rather as Option B, would you consider that, as the policy stimulus reduces the hysteresis effect, it thus helps maintain long-term productive capacity, which should be good for long-term productivity? So, are you in the camp of A or B? I'd very much like to hear your views on this essential analytical dilemma.

Ms. Collins: There are many issues and views on the floor including the questions that have just been posed. I would ask each panelist to offer their final comments. Please reflect on what you see as the highlights from the session, as well as responding to things that you might have heard from another panelist and to questions from the audience.

Mr. Lane: I think this year, of course the ECB, to some degree we have innovated, but we were building on an already pretty extensive program in terms of we already had a corporate bond purchase program; we already had targeted lending to firms through the banks. And let's make a point there too: by keeping the corporate bond market working, by extending it to include commercial paper to the extent larger firms can rely on it, it allows the SMEs to have more access to bank lending. That is a very important transmission channel for corporate bond purchases, from a holistic point of view. But the bigger architecture issue has been in relation to fiscal policy. The EU Recovery Fund has changed the nature of the European fiscal architecture, at least in relation to large negative shocks. There is now more shared fiscal response: I think that is very important and has positive long-term implications.

I think in relation to the issue of inflation expectations, there's a recognition that all sorts of expectations matter. This includes those households where the salience of, for example, food inflation is relevant. We have a new area-wide consumer expectations survey which is helpful in having very quick comprehensive readings of how households are developing their beliefs. Maybe the last point I'll make is just that I liked Tharman's remarks about the future of jobs. Absolutely, I think this issue should be at the forefront everywhere, given the global trend before the crisis with the rise of low-wage employment and the issues about retraining, investment in human capital and so on. Looking beyond monetary policy, the rising importance of these issues will be very important. And I think–I didn't talk about it today very much–a lot of the ideas about direct communication with the public that Tiff (Macklem) was highlighting, we would share about our point of view of the ECB.

Mr. Macklem: I'll start by addressing the question on communication. I think as you were suggesting Susan (Collins), we do see a bit of a disconnect measuring inflation. Canada is running around zero but the perception of any individual is that inflation hasn't gone down and in some cases it's even gone up. And there is some reason for that. People's consumption baskets have dramatically–the cost of airline travel may have fallen a lot, but people aren't flying much. What they are doing–and people's perceptions of inflation tend to be heavily influenced by the things they buy very frequently like food. So one of the ways we are addressing that is we are working with a statistical agency in Canada–Statistics Canada–and have done a survey of household spending patterns during the crisis and created an alternative version of the CPI with these new weights to see how much is, when you reweight to reflect what people are actually buying now, what does inflation do? And what we have seen is it actually still falls a lot. Not quite as much as the official CPI, but quite a lot. And in the latest numbers we are already seeing that as the economy reopens and people's spending patterns go back to something that's a little closer to normal, that gap is narrowing. By trying to address the issue head on and communicating, I think that is one way we are trying to address that.

The other part that you mentioned is that this is as much a supply shock as it is a demand shock. And we have even more trouble measuring supply than demand. So, there is a little bit of uncertainty. I think our approach to that one is to try to be as transparent as we can about our estimates of the supply impact. In our monetary policy report we put a whole box on the supply versus demand impacts. We don't have it all figured out and that is something we are going to have to assess on an ongoing basis and keep revising going forward. But, yes, we do have to keep in mind that it is both demand and supply. And then finally I will just say a word about SMEs. Monetary policy is not well suited to targeting particular segments of the economy. We are certainly concerned about that. The reality is Canada has done a reasonably good job of controlling the virus, the economy is reopening, but not all SMEs are going to be able to reopen. And in particular, ones that are in sectors–restaurants or hospitality, where people need to be close together–it is going to be very difficult for them for a long time. And I think that really reflects our view of the broader pattern of this recovery. We are seeing now some very impressive rebound numbers as the economy reopens and that is a really good thing, but not all parts of the economy are going to be reopened for some time. We expect after this first phase it is going to be a pretty long, bumpy phase and as Tharman, as Chair Powell emphasized, it is going to be really important for monetary policy to support through the whole long recovery.

Mr. Shanmugaratnam: Three quick points. First, it was bad enough that we've had a few decades in very advanced economies of the growth of jobs that were low wage, low productivity and low security. What's worse, is not having enough of such jobs. And what we have to do is to both get people back into work, but also get them into something better than the bottom end of a barbell structure. And it is not going to happen if we simply leave things to the market.

I think the scope for monetary policy to address this is limited. What monetary policy has to do is to try its best to achieve a tight labor market. But as implied in Chairman Powell's comments earlier on, if we leave it only to monetary policy, monetary policy is also going to be much less effective. It can also have some counterproductive effects over time. We're far from an optimal mix of monetary and fiscal policies today. And I'm not just talking about the size of fiscal deficits, or about how much government debt we tolerate. We have to move away from thinking about the aggregate fiscal stimulus, which might be appropriate when you are tackling a short crisis, deep as it is. We've got to start thinking about the shape of fiscal policy, and how you move toward thinking about incentives–incentives for firms, incentives for workers, incentives for collaboration. It is a different orientation in fiscal policy.

We have lost sight of public goods for a long time now, in a range of economies. It used to be the fundamental focus of government budgets. But we've lost sight of public goods. And they're greatly underinvested–in both the advanced and emerging world–in public education, basic health care, infrastructure, and now we have to think about the future green economy, it's going to require tremendous infrastructural investments. We won't be able to, and we can't afford it on the public balance sheet alone, but we have to think of incentives. We have to think of incentives for the private sector to be able to come in and serve the public good.

We have to make major changes in our subsidy structures, both in social policy and in fossil fuel subsidies. Fossil fuel subsidies are a chunk of many government budgets all over the world. But even social policy, we have to think hard about what it is to be fair and progressive. What is it really about, being fair and progressive in fiscal terms. It requires a fair bit of thinking.

Finally, health care financing–there is scope for tremendous savings, while improving outcomes. Tremendous savings on the public budget while improving outcomes. So, that's an opportunity for reform. It's not about austerity.

It's about reform. So that we get back to basics, and focus on investing in public goods, focus on incentivizing productivity, focus on technological innovations that can help enhance human capital, focus on incentivizing individual behavior, so that people can get back into a job, get into better jobs and earn success in a way that gives them pride.

Ms. Collins: We have heard three very thoughtful, insightful perspectives on crisis management. I'll close by highlighting the many ties with key themes that we touched on throughout the earlier sessions today. In particular, our sessions have emphasized issues related to trust, public engagement and communication, as well as the importance of recognizing structural and other longer-term trends, and the need for monetary policy to partner with fiscal and other types of policies in order to achieve desired outcomes.