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Innocent Bystanders? Monetary Policy and Income Inequality in the U.S.

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Innocent Bystanders?
Monetary Policy and Income
Inequality in the U.S.

Discussion by Romain Ranciere

Redistributive Effects of Macro Policies

- Macro Policies → Macro Outcomes → Welfare of Representative Agent.
- Real word: **macro policies have redistributive effects.**
- Fiscal Policy: effects on post-tax income distribution is straightforward (at least in partial equilibrium)
- Monetary Policy: much less clear, many channels: ambiguous overall effects.
 - Does it matter? How does it matter?

Monetary Policy and Income Inequality

- Directly: e.g. inflation surprise
 - Redistribute from savers to borrowers.
 - Inflation tax on cash holdings (but Ragot (2012))
- Indirectly
 - Income inequality and business cycle fluctuations.
 - Earning heterogeneity channel.
 - Difference in wage rigidity.
 - Difference in risk of Unemployment.

Main Results

- Contractionary Monetary Policy raises:
 - income inequality
 - labor earnings inequality
 - Expenditures and consumption inequality
- Effects are very sizeable and very persistent.
- Discussion of channels through different sources of income.

Data

- CEX: consumption expenditure / survey.
 - vs. IRS data (Piketty-Saez)
- **Bias 1:** Badly informed on top income shares; key drivers of changes in income inequality.
- **Bias 2:** Limited information on non wage income; no information on wealth.
- **Gains:** Quarterly Data and Data on Consumption.
- **Suggestion:** effects are very persistent so why not trying to use annual data as well and use then all the post 69 data (and use top income share)

Identification: Monetary Policy Shocks

- As in Romer and Romer (2004)
- Big Advantage: as in literature and same shock series to study aggregate outcome and income distribution.
- Issue: the question here is really different.
- R&R make full sense for the effect of monetary policy on output and inflation: exogeneity of shocks / purging from systematic response.

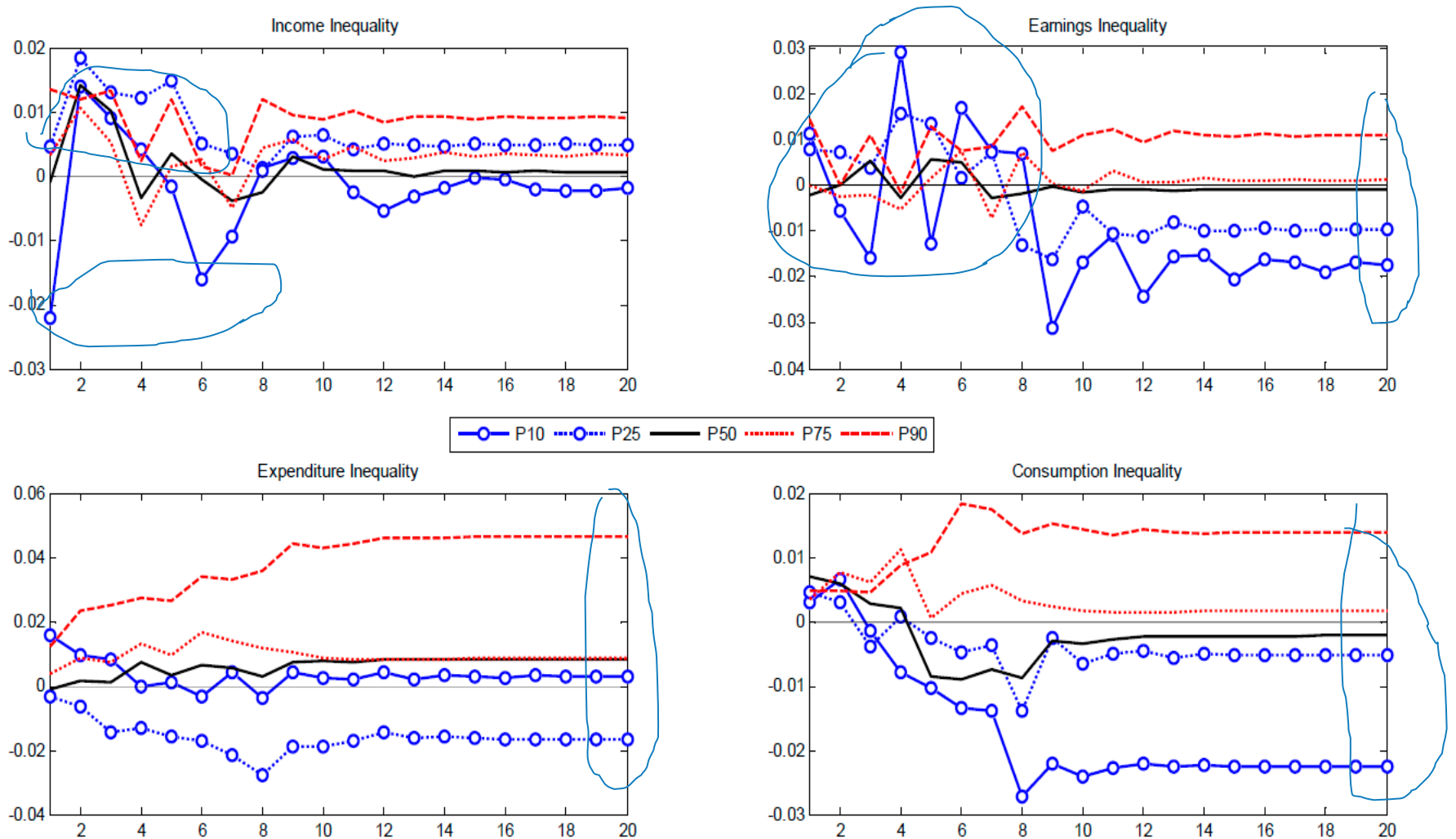
Identification: Issues

- But is R&R the most adapted identification strategy to study the effect of monetary policy on income inequality?
 - Income inequality is not in the objective function of the Fed (so less problem of endogeneity a priori)
 - Systematic response can have important effects on income inequality.
 - But other drivers of inequality can contaminate the shock series.
 - Should'nt we have an identification strategy that is targeted to the question at stake.

Presentation of Results

- Directly in terms of inequality measures.
 - Standard Deviation of logs
 - Gini
 - 90th percentile / 10th Percentile.
- Indirectly in terms of percentiles.
 - P10,P25,P50,P75,P90: much more transparent (and less dependant of specific inequality measures)
 - Inequality under different dimension (choice of this paper)
 - vs. Inequality in one dimension ((income or earning) and and the distribution of other variables across same groups (consumption, expenditures)
 - Consumption / Expenditure response to change in income/earning inequality (more economics).

FIGURE 5: DISTRIBUTIONAL EFFECTS OF CONTRACTIONARY MONETARY POLICY SHOCK BY PERCENTILE S

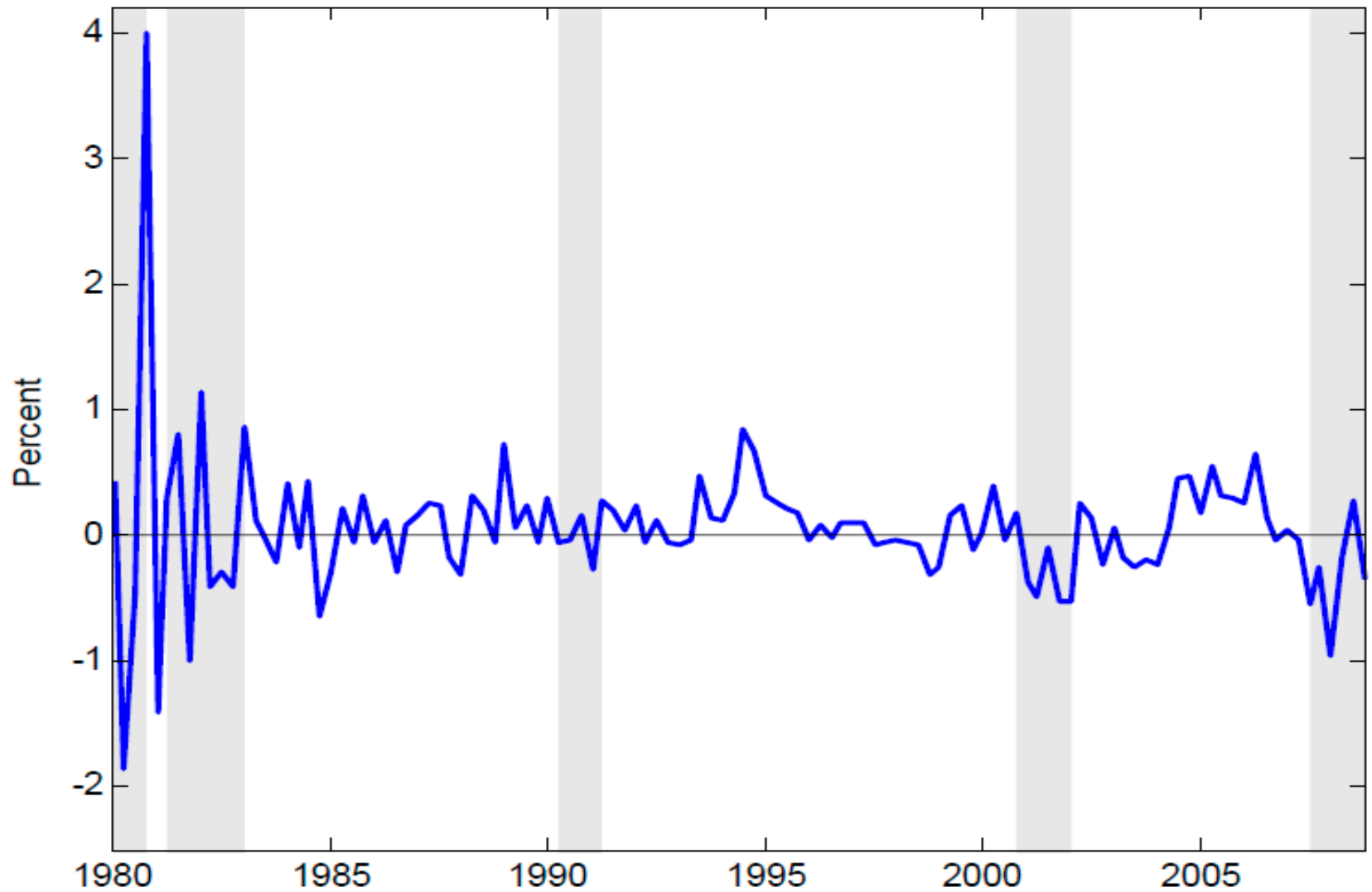


Notes: The figure plots the responses of each percentile of the income, salary, expenditure and consumption distributions of households in the CEX to a 1 percentage point (100 b.p.) contractionary monetary policy shock using data from 1980Q1-2008Q4. P10 corresponds to the 10th (lowest) percentile of each distribution and equivalently for P25, P50, P75 and P90. See section 3.3 for details.

Contribution of Monetary Policy to Historical Variations

- Why only looking at variation in income inequality from 1969? Data availability?
- **Post 1980: Small Monetary Shocks but Strong Power in Explaining Income Inequality.**
- Monetary Policy seem to have a much higher explanatory power than any other explanation for the rise in income inequality!
- MP does not only explaining fluctuation but also the rising trend in income inequality since the 1990s.
- **Super Impressive but Puzzlingly so.**

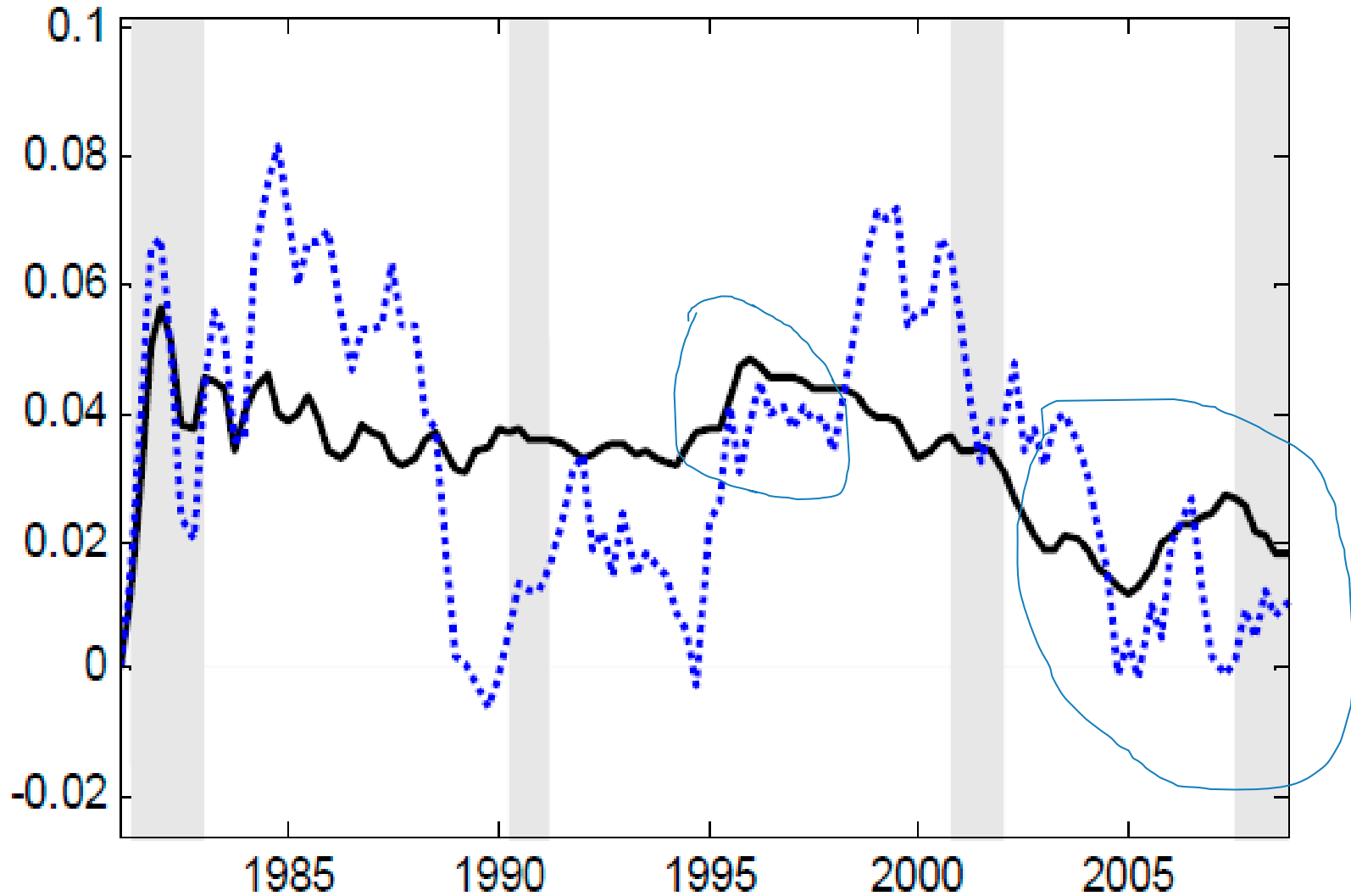
FIGURE 2: MONETARY POLICY SHOCKS



Note: The figure plots the quarterly sum of monetary policy shocks as identified in Romer and Romer (2004). See section 3.1 for details.

Historical Variation and MP Contribution

Income Inequality



Summing up

- I have some issues with identification strategy but their approach is defensible.
- **On the effect of MP on income inequality:** Results are very impressive, specially the historical contribution of monetary shocks (almost too good!)
 - Strong case for distributional effects of monetary policies
- **On How monetary policy affect Income Inequality:** Not really convinced on the channels/explanations but this can be left for further research (there is already significant contribution without)