

Quantitative Easing (QE) – A Higher Level Narrative

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Introduction

- What is a narrative
- Narrative risk
- The existing QE narrative
- A higher level QE narrative
- Conclusion

What is a Narrative

- What is a narrative
 - A story
- Example
 - A stock market crash
- Why is it important?
 - People cast their own identity in some sort of narrative form
 - The 'narrative' effectively dominates the 'analysis'

Narrative Risk

- Dangers of low level narratives
 - Rhetoric can prevail over reason and logic
- Low level narratives inhibit rather than facilitate progressive outcomes and inhibit resolution of conflicts
- Low level narratives usually result in poor outcomes
- Example
 - Banking Crisis in Ireland

Existing QE Narrative

“QE involves a central bank creating new money electronically and using this to buy assets, normally government bonds.... By buying these bonds from investors or banks the central bank is giving these parties more cash to lend out of invest elsewhere. QE is also designed to drive down interest rates, not only official rates, but also those charged to borrowers. It should also lower the value of the currency, helping exporters and pushing up import prices. QE is also designed to improve confidence in the future by consumers and investors, thus encouraging them to spend more.”

Cliff Taylor (Irish Times)

Existing QE Narrative

The US and the UK economies have outperformed the EU which remains in recession. The US and the UK have pursued QE policies in recent years. Their economies have recovered, albeit in an unequal way. Wage growth has been low, but corporate profits have been buoyant, aided by lower interest rates and wealth effects from rising asset prices.

Despite money printing, inflation rates in the US and the UK are still low and QE does not seem to have increased inflationary expectations to any significant extent.

A Higher Level QE Narrative

The central bank prints money and uses it to buy bonds. This increases bond prices and makes profits for those who own bonds. Those who sold their bonds, typically buy other bonds to replace them. This increases the prices of other bonds, making profits for those who own them.

Those who sold the other bonds, typically buy other assets to replace them. This increases the prices of other assets, such as equities and property, making profits for those who own other assets, such as property and equities.

QE drives up the prices of assets making those with assets better off.

A Higher Level QE Narrative

The more assets that you have the more you will have gained from QE. Those with the most gain the most. However, relatively speaking, everybody becomes poorer than those who were richer than them in the first place. If you have no assets or very little assets, you have gained nothing or only very little - but will have become relatively much poorer.

Banks only lend to those who they consider creditworthy. QE has made the rich proportionately more creditworthy and consequently improved their access to credit. Those who have little or no assets have not seen any significant improvement in their access to credit.

A Higher Level QE Narrative

Overfunded pension schemes (the better-off ones) have more assets than liabilities – so the value of the assets will increase by more than the liabilities – so they'll be better off.

Underfunded pension schemes (the majority – the less well-off) have assets less than their liabilities – so the value of the liabilities will increase by more than the assets – so they'll be worse off. These schemes effectively have negative wealth. They are directly and indirectly worse off from QE.

Has QE helped Japan?

A Higher Level QE Narrative

Money printing creates short term gains from '*money illusion*'.

QE creates short term gains from '*wealth illusion*'.

The higher asset prices result in the expected future returns being lower than otherwise so it's a temporary distortion – asset bubbles are likely.

The wealthy don't typically spend their money on the goods in the CPI so inflation will not increase, the inflation is typically confined to asset prices.

Money has been printed, your money is worth less than it was before QE started! The less well-off are working for relatively less, this stimulates economic growth as the better off take advantage

Conclusion

Since QE started, economic growth and lending have increased but mainly for the relatively better off, with just crumbs from the rich man's table for the poor.

QE has been unfair and unequal, but due to the complicated nature of QE, this unfairness has yet to come to the surface. The unfairness and inequity have been greatest for underfunded pension schemes.

Thank you for your attention

Comments?

Questions?

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