COMMENTS on

Income and wealth of Euro Area Households in Times of Ultra-Loose Monetary Policy

(Manuel Rupprecht)

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European Central Bank

"Expropriation of savers"?

DIE ● WELT KOMPAKT

Der größte Albtraum der Sparer wird wahr

DER SPIEGEL
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Ohne Zins und Verstand

Warum die Deutschen ihr Geld falsch anlegen – und wie sie es vermehren könnten

SPARBUCH

Pegida, AfD & Co.
Was ist mit den Sachsen los?

Vor der Euro-Sondersitzung
Kofi Annan fordert:
Legalisiert die Drogen!

Kinder
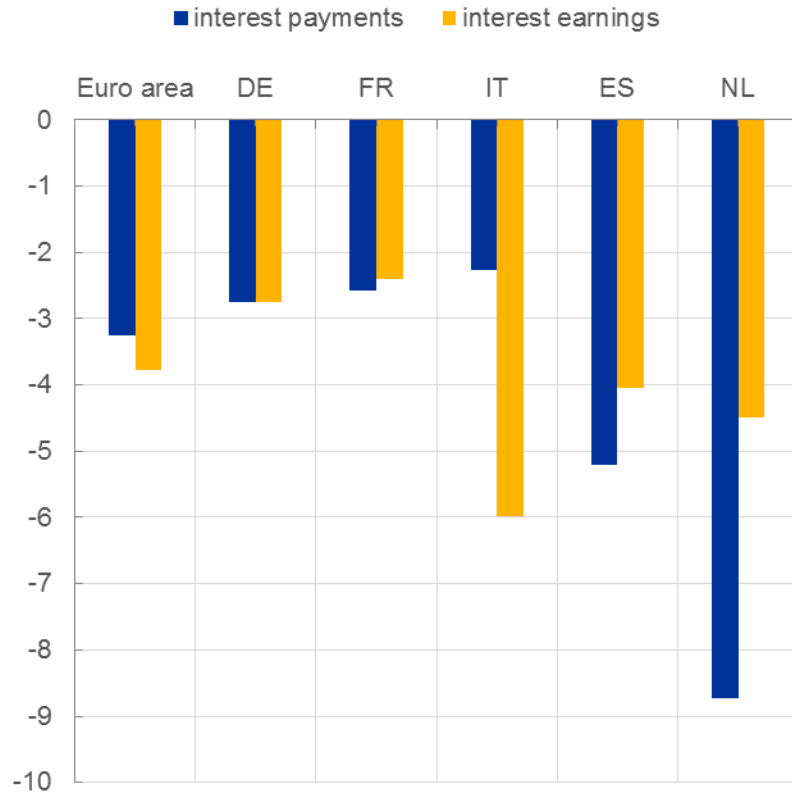Weshalb zu viel Erziehung unglücklich macht

MR: German "Angst" meets stylized <u>facts</u>

- **Effects of "ultra-loose" monetary policy on HH sector**

    – **Using national account and financial account data: stocks and flows**
    – **Limited impact on HH net interest receipts (greater for IT than DE)**
    – **Little evidence for HH portfolio adjustments (notional stocks)**

- **Suggests ECB less of a "villain", but also less of a "hero" ?**

    – **No major "negative side effects" (income, risk-taking)**
    – **Limited transmission via rates and portfolio rebalancing**
    – **Implications for macro-modelling (intertemporal substitution vs. income vs. wealth channels) ?**
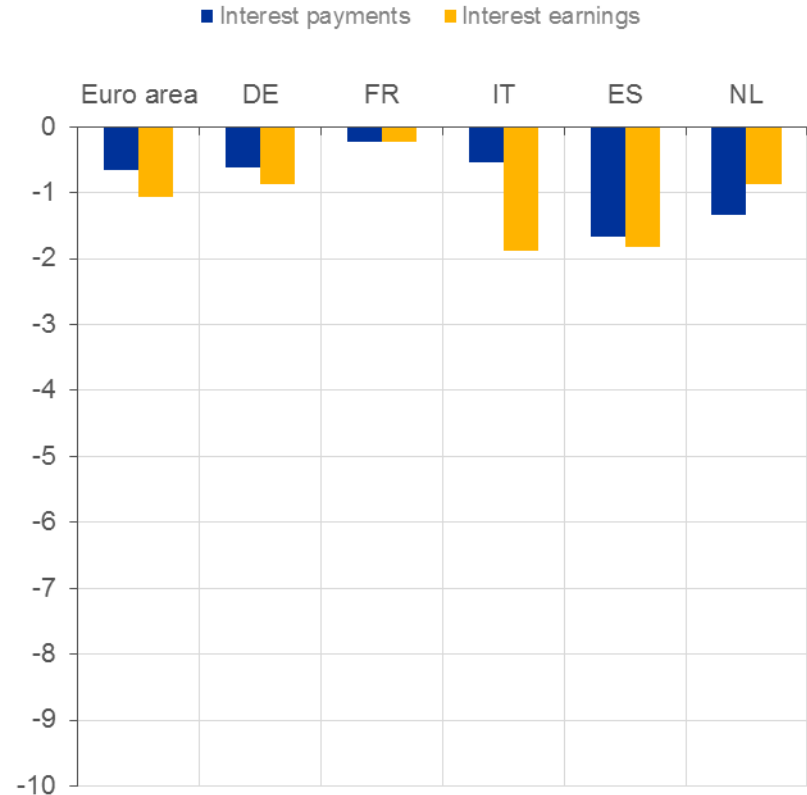
Role of other assets & sectors & inequality

- **MR may <u>overstate</u> (adverse) impact**

  – HH may benefit from rising non-financial assets (housing)
  – HH may benefit from lower rates as taxpayers and company owners
  – HH may be hurt as holders of insurance and pension claims
  – … with main income effect via employment and wages

- **MR may <u>understate</u> (beneficial) effects**

  – Different MPCs for savers and debtors (rich and poor) ?
  – "inconvenient truth": monetary policy always has distributive impact
  – … but broadly neutral over the cycle
  – Implications for macro-modelling: HANK vs. neo-Wicksellian NKM

Households' interest flows 2008Q3 - 2017Q2
(percentage points of gross disposable income)

■ interest payments   ■ interest earnings

Households' interest flows 2014Q2 - 2017Q2
(percentage points of gross disposable income)

■ Interest payments   ■ Interest earnings

EONIA, long-term government bond yield and an estimate of the implicit interest rate for the total economy (ECB Economic Bulletin, Issue 5 / 2017, August)
*(percentages per annum)*
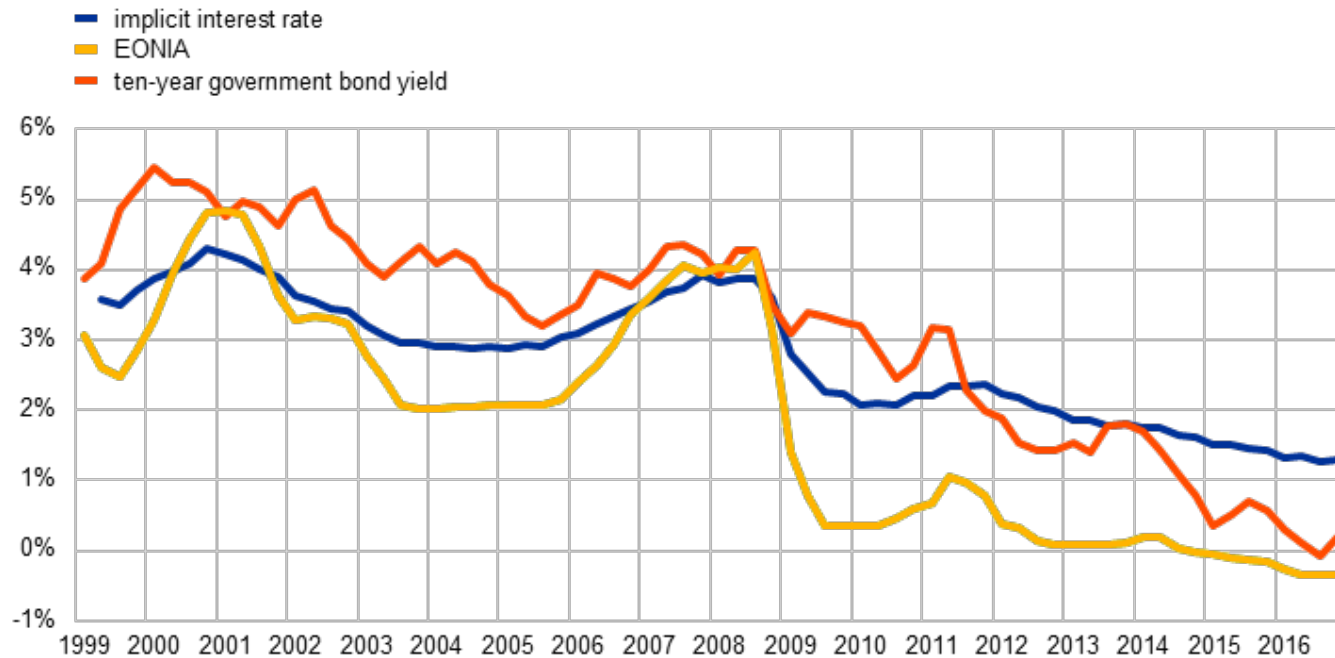
Sources: Thomson Reuters, ECB and ECB calculations.
Notes: The latest observations are for the fourth quarter of 2016. The implicit interest rate shown is on the euro area total economy's assets. The implicit interest rate on the euro area total economy's liabilities coincides with the one on its assets. The ten-year government bond yield refers to the synthetic euro area rate from Thomson Reuters.

Impact of lower interest rates on net interest income
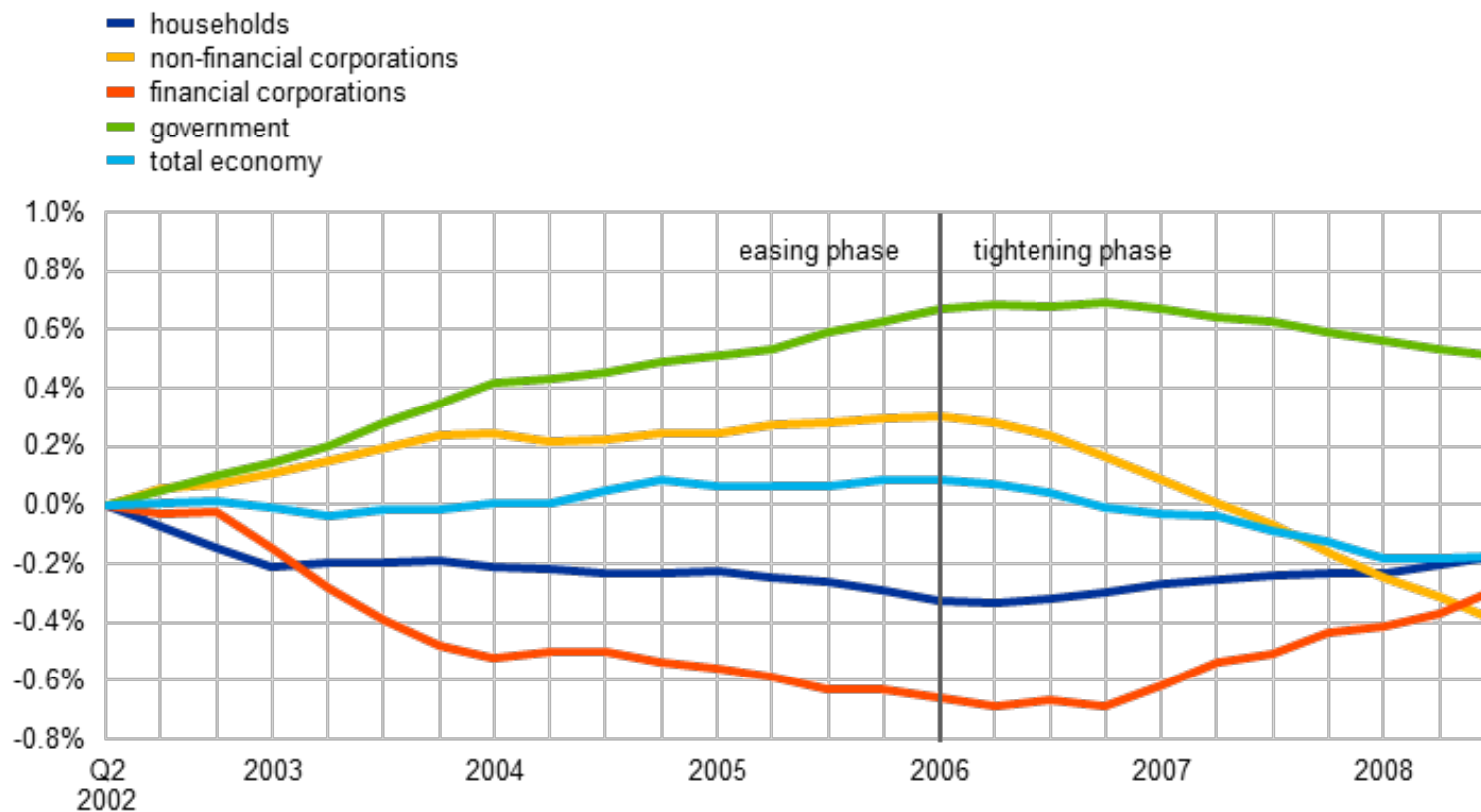*(percentages of GDP; Q3 2008 to Q4 2016)*
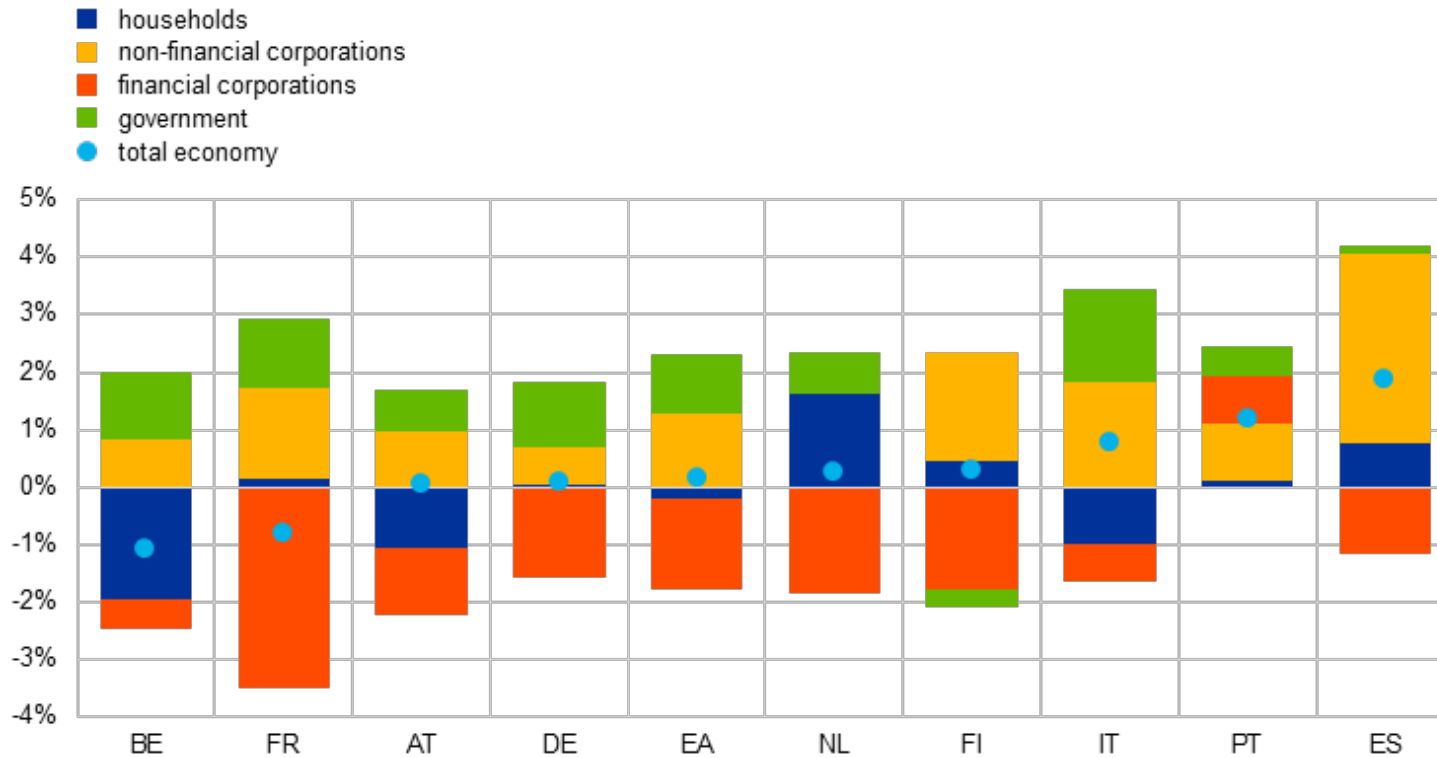
Sources: Eurostat and ECB calculations.
Notes: Countries selected on the basis of availability of quarterly sectoral accounts. The total economy refers to the changes in net interest income with respect to the rest of the world. Owing to different levels of aggregation, the sum of the sectoral changes in net interest income does not add up exactly to the change in net interest income with respect to the rest of the world. Calculations based on four-quarter moving averages.

Cumulative interest income changes over the business cycle – 2002-2008
(percentages of GDP))

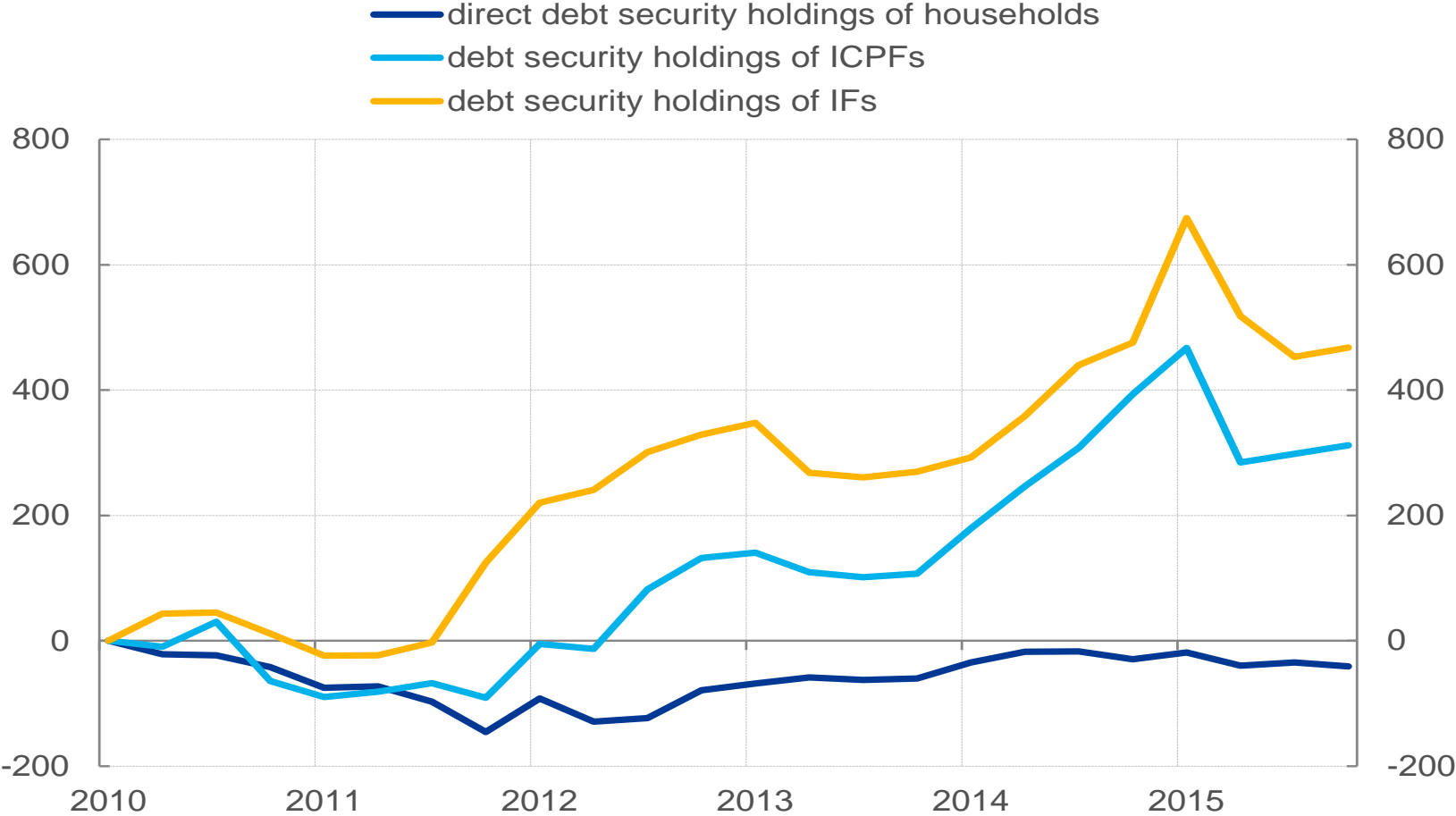# Valuation gains in debt security holdings of selected institutional sectors in the euro area

Legend:
- direct debt security holdings of households
- debt security holdings of ICPFs
- debt security holdings of IFs

Sources: Eurostat, ECB. Latest observation: 2015 Q4.

Household net worth and contribution to private consumption

(lhs: as percent of gross disposable income, annual flows; rhs: percentage point contributions)

Legend:
- other flows in non-financial assets*
- other flows in financial assets and liabilities**
- change in net worth due to net saving***
- change in net worth
- net worth - shock

10

HFCS evidence on household main asset holdings (euro area)

Asset Participation Rates by Income Quintile
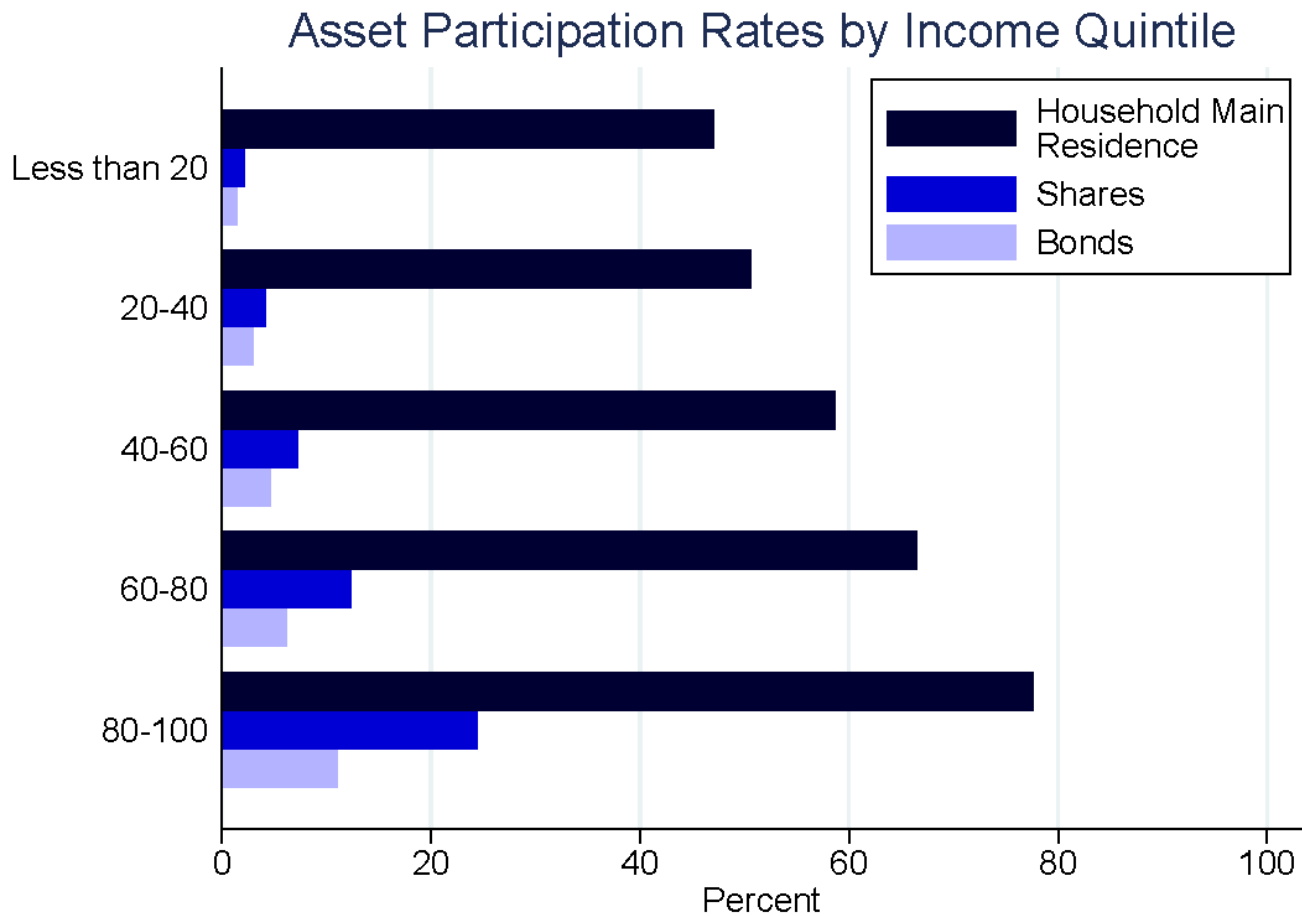
Differences in propensities to consume (for Spain)
(differences from baseline, percentage points)
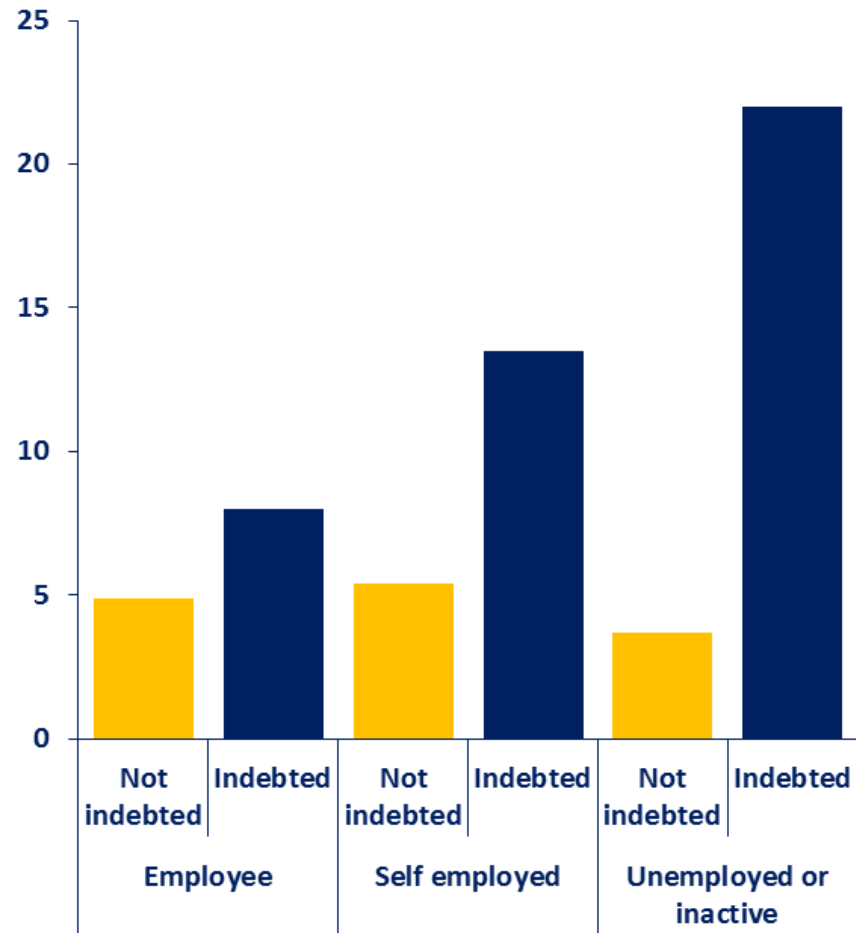
Source: Casado J.-M. and M. Folch (2016), The role of leverage for consumption: Evidence from Spanish panel data (HFCS), Banco de España, mimeo.

Macroeconomic effects of APP

- **Estimate VAR impulse responses to nonstandard monetary policy identified à la Baumeister and Benati (2013) & Altavilla et al. (2016)**

- **IRFs rescaled to initial EA drop in term-spread of 34 bps – to match impact of December 2016 APP announcement on 10-year bond rates**

Average impulse response of variables to MP at quarter 4

Legend: House Prices, Stock Prices, Unemployment, Wages

Note: The chart shows estimated VAR impulse responses 4 quarters after the impact of the Asset Purchase Programme (APP) shock. The bars show average responses across the 4 big euro area countries (DE, ES, FR, IT). Responses are shown in percent for house prices, stock prices and wages; in percentage points for unemployment.

Effects of APP on wealth inequality very small

- **Extrapolate impulse responses to household wealth components – housing, stock prices – in the HFCS data**

- **Wealth goes up by around 1% across the distribution**

- **Gini coefficient ticks down from 68.09 to 68.07**

Growth of Median Net Wealth by Wealth Quintile

	1	2	3	4	5
	(€ 1,200)	(€ 25,400)	(€ 112,800)	(€ 228,200)	(€ 517,900)
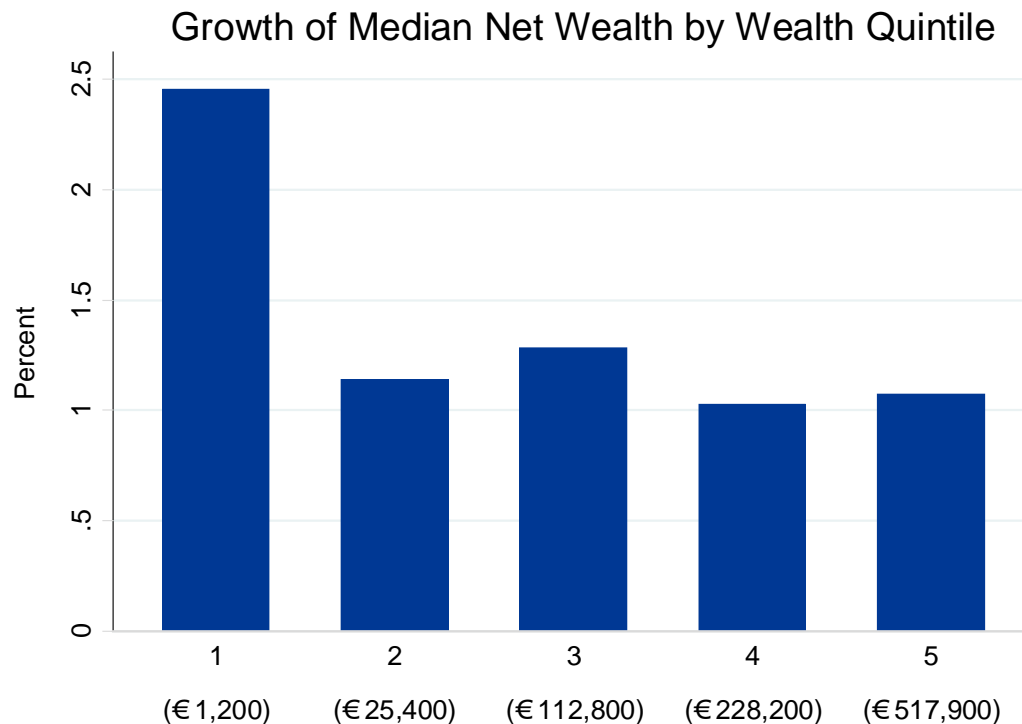
Source: ECB calculations based on Lenza and Slacalek (2017), Eurosystem Household Finance and Consumption Survey.

Note: The numbers in brackets show initial net wealth levels. Euro area aggregates are calculated as the total for the four large countries: Germany, Spain, France and Italy.

Summary and conclusions

- **Very reasonable paper: factual & (unduly) modest**
  - **Limited relevance of net interest in HH disposable income … but role of indirect holdings (ICPF, IF)?**
  - **Little "active" HH portfolio rebalancing … but "passive" via valuations?**
  - **Role of distribution impact across sectors and households?**

- **Implications for monetary policy and macro-modelling**
  - **Heterogenous sectors & agents (HANK), Adam et al, Schneider & Doepke, … matching FA with micro data**
  - **Rates vs. quantities: re-visiting Tobin & Brunner/Meltzer (money, wealth & asset prices, portfolio balance model)**
  - **Stock and flow effects: balance sheets matter (cycle vs secular crisis)**
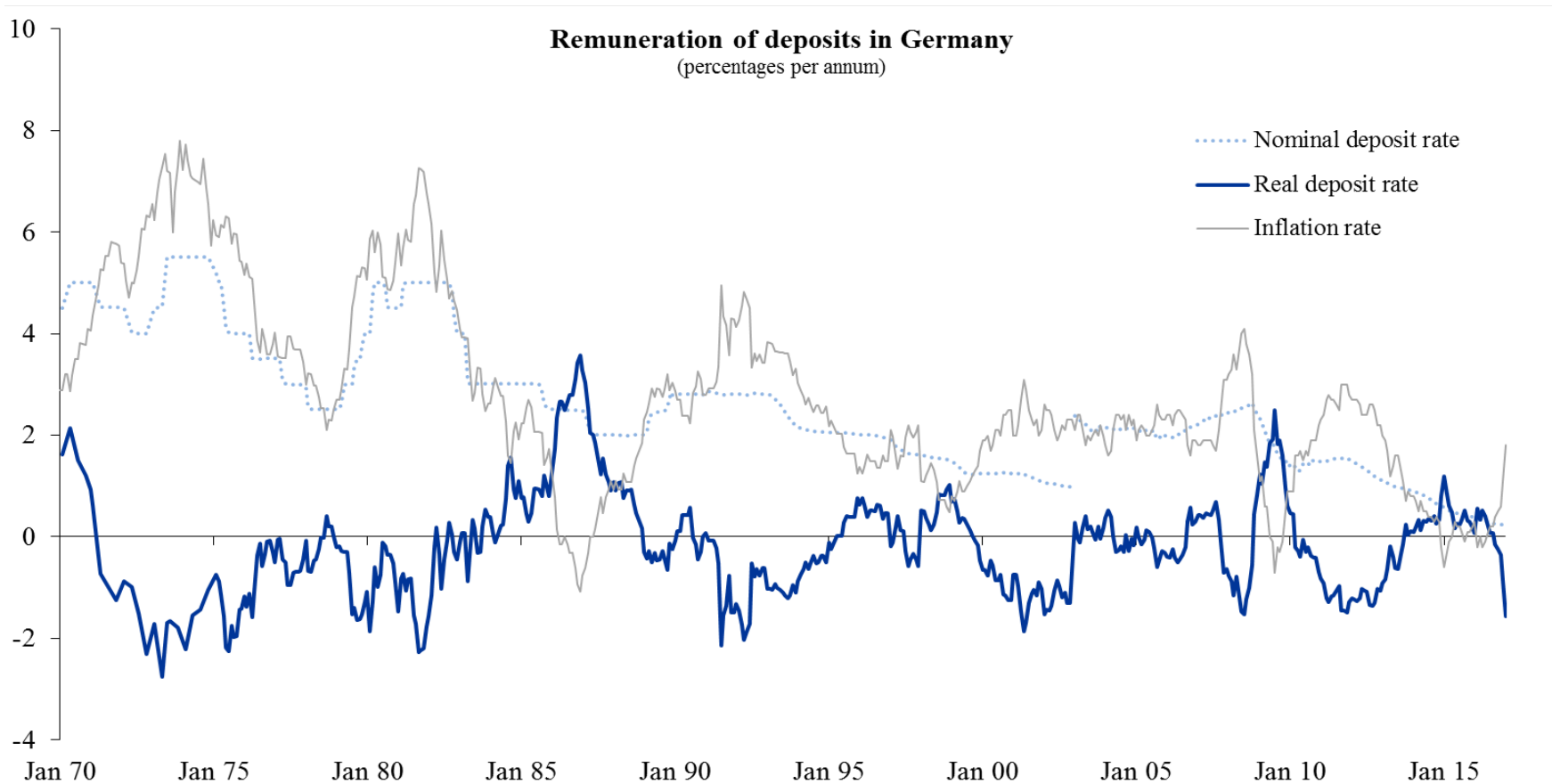
Quantitative Easing

Related work

- **October 2011 ECB Monthly Bulletin** article on flow-of-funds perspective on the financial crisis

- **February 2012 MB Box 3** & April **2012 and 2013 ECB Financial Integration Reports**: Special Features on sectoral balances

- **ECB Working Paper No. 1402** (2011) by Riccardo Bonci on transmission of monetary policy via FoF

- **Chapter 7 on cross-checking and the flow-of-funds, in Papademos and Stark (eds.): Enhancing Monetary Analysis**, ECB October 2010

- **"Flow-of-funds perspective on unconventional monetary policy"**, **The Journal for Money and Banking**, Vol. 63, No. 11, Nov. 2014, B. Winkler

- **Cour-Thimann and Winkler, "Central banks as balance sheets of last resort: ECB's monetary policy in a flow of funds perspective" (2016) in David Cobham (ed.): Monetary Analysis at Central Banks.**

- **ECB Working Paper No. 1528** (April 2013) by Cour-Thimann and Winkler, "The ECB's non-standard monetary policy measures: the role of institutional factors and financial structure" (cf. OxREP 2012)

- **Giron and Rodriguez-Vives (2017), "Leverage interactions: a national accounts approach", ECB Statistical Working Paper Series, No. 19**

Background slides

"Expropriating savers"? Real vs nominal returns

Remuneration of deposits in Germany
(percentages per annum)

Legend:
- Nominal deposit rate
- Real deposit rate
- Inflation rate

*Sources: Deutsche Bundesbank and ECB staff calculations.*
Notes: Deposit rates of banks for savings deposits with minimum rates of return, with agreed notice of 3 months (average interest rate) up to 2003, thereafter effective interest rates of German banks (new business) on households' deposits redeemable at notice of up to 3 months. Deflated with CPI inflation for Germany until January 1999, thereafter euro area (changing composition) overall HICP.

See also: **Bindseil *et al*, Critique of Accommodating Central Bank Policies and the 'Expropriation of the Saver', ECB Occasional Paper 161** www.ecb.europa.eu/pub/pdf/scpops/ecbop161.en.pdf
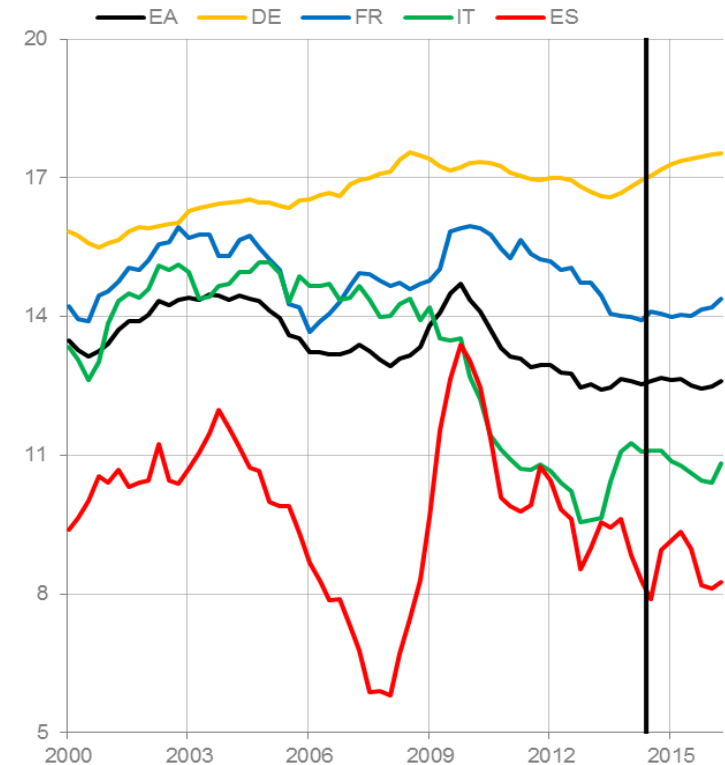
Disincentives for saving?
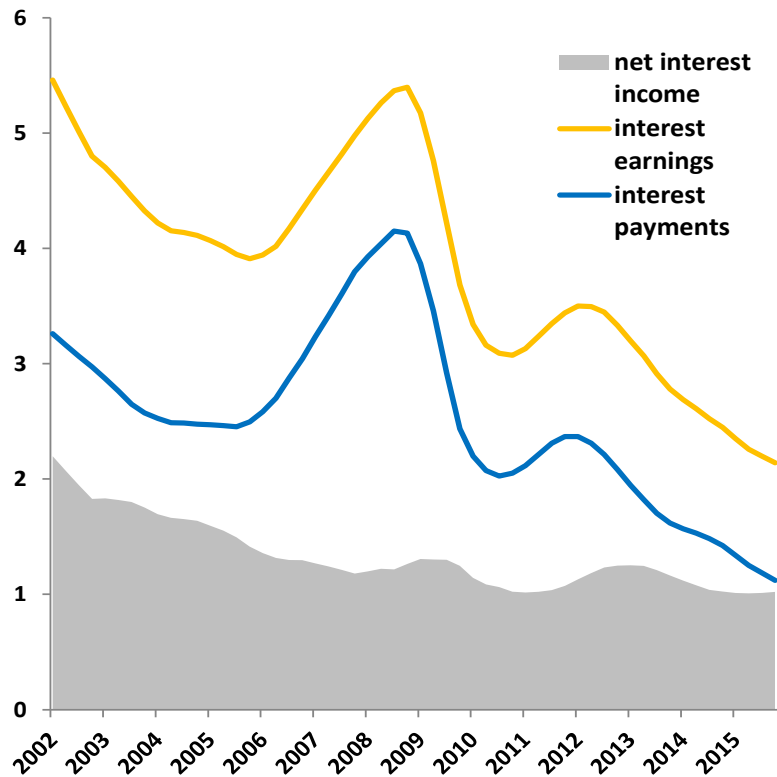
Sources: Eurostat and ECB calculations.
Note: The change has been computed for the period 2008Q3-2015Q4. Interest payments/earnings after FISIM allocation (Financial Intermediation Services Indirectly Measured).
*Latest observation: 2015Q4.*

Sources: Eurostat and ECB.
Note: Calculations are based on 4-quarter moving sums. 2014Q3 was the first quarter where Eonia became negative, after the rate on the ECB deposit facility was lowered to -10 bps and -20 bps in June and September 2014, respectively.
Latest observation: 2016Q2.

… global phenomenon of decreasing "natural" rates

Equilibrium real interest rate
yield p.a.
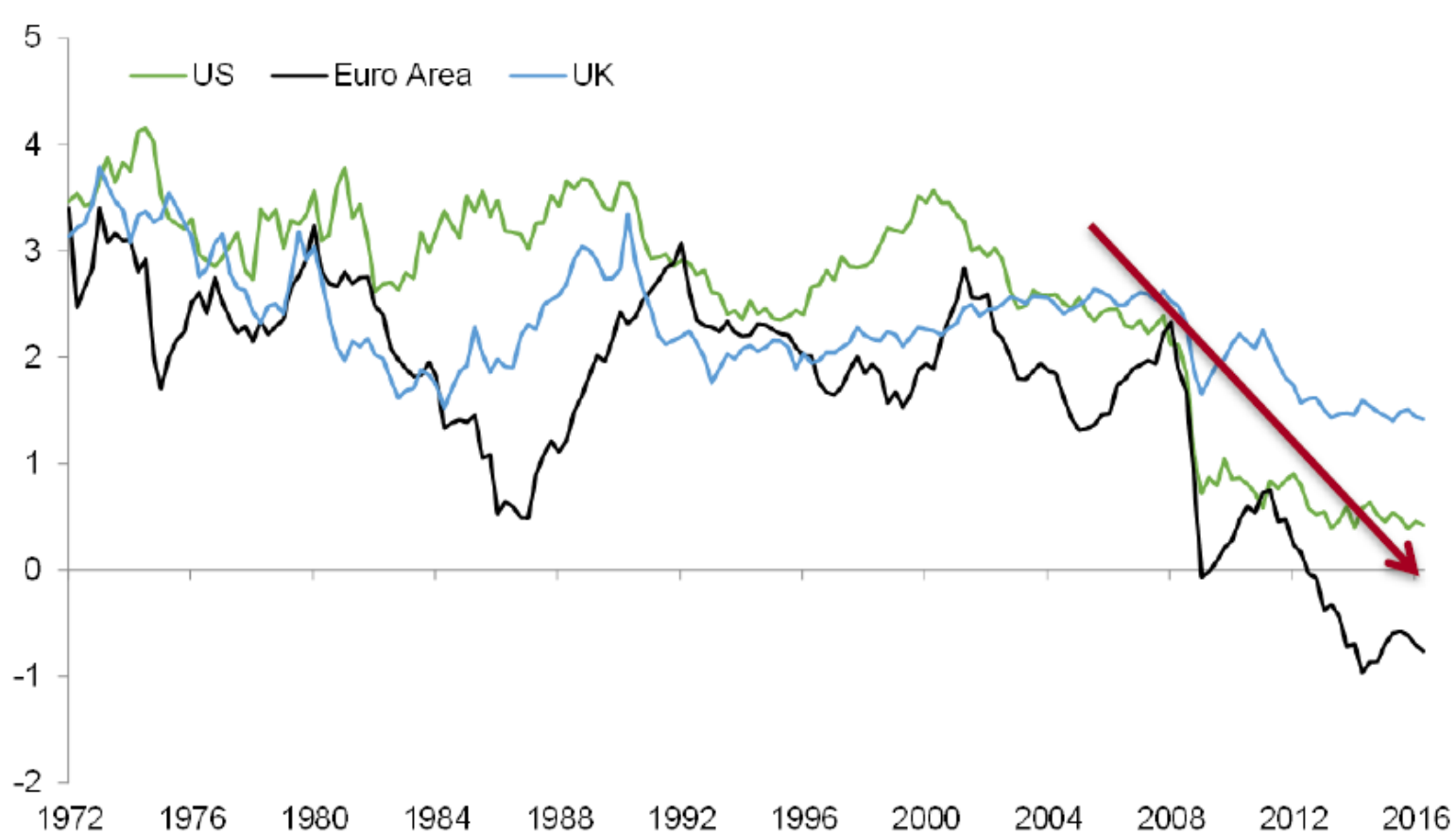
Note: Estimates from "Measuring the Natural Rate of Interest: International Trends and Determinants" Holston, Laubach and Williams, August 2016.

Structural factors determine "natural" rate

Higher trend growth

Higher "natural"/"neutral" rate of interest

Innovation

Productivity

Demography
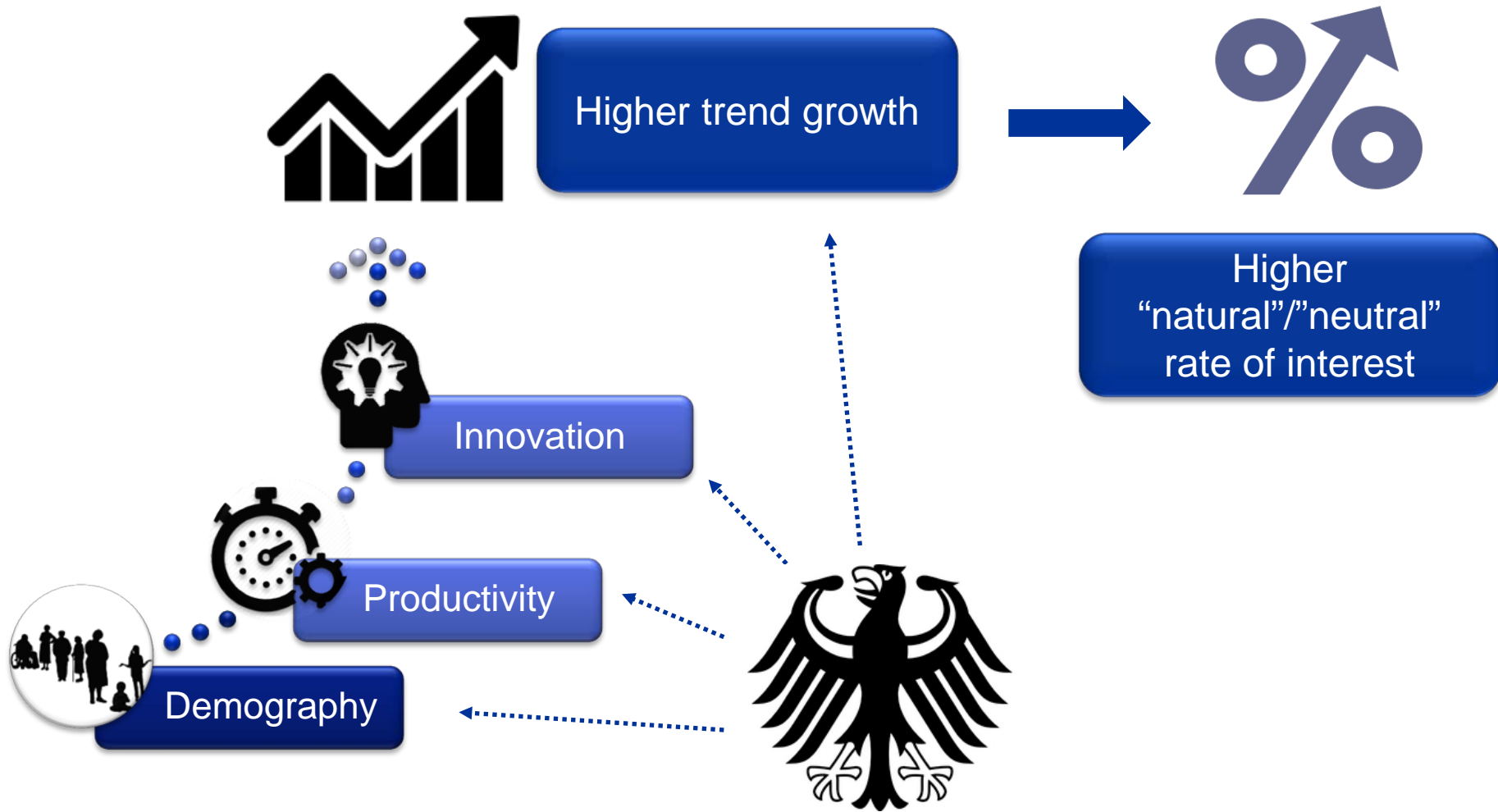
Siehe: U. Bindseil et al.: **"Critique of accommodating central bank policies and the 'expropriation of the saver': A review"**; ECB Occasional Paper No. 161, Mai 2015

Redistributive effects (I) – micro effects

- Beneficial effects on owners of equity/bonds – who tend to be richer

- Negative effects of low rates on savers – mainly hits the wealthy

- Significant effects on **house prices** – spreads positive effects across population, especially in countries with high rates of home ownership;

- Better access to finance – reversing negative effects of previous financial fragmentation; more consumption (brought forward)

See: M. Draghi, "Stability, equity and monetary policy" 2nd DIW Europe Lecture, German Institute for Economic Research (DIW), Berlin, 25 October 2016

Redistributive effects (II) – Macro perspective

- More balanced recovery; more investment, more consumption

- Higher employment: having a job ➡ biggest impact on reducing inequality

Contributions to GDP growth

Cumulated percentage points
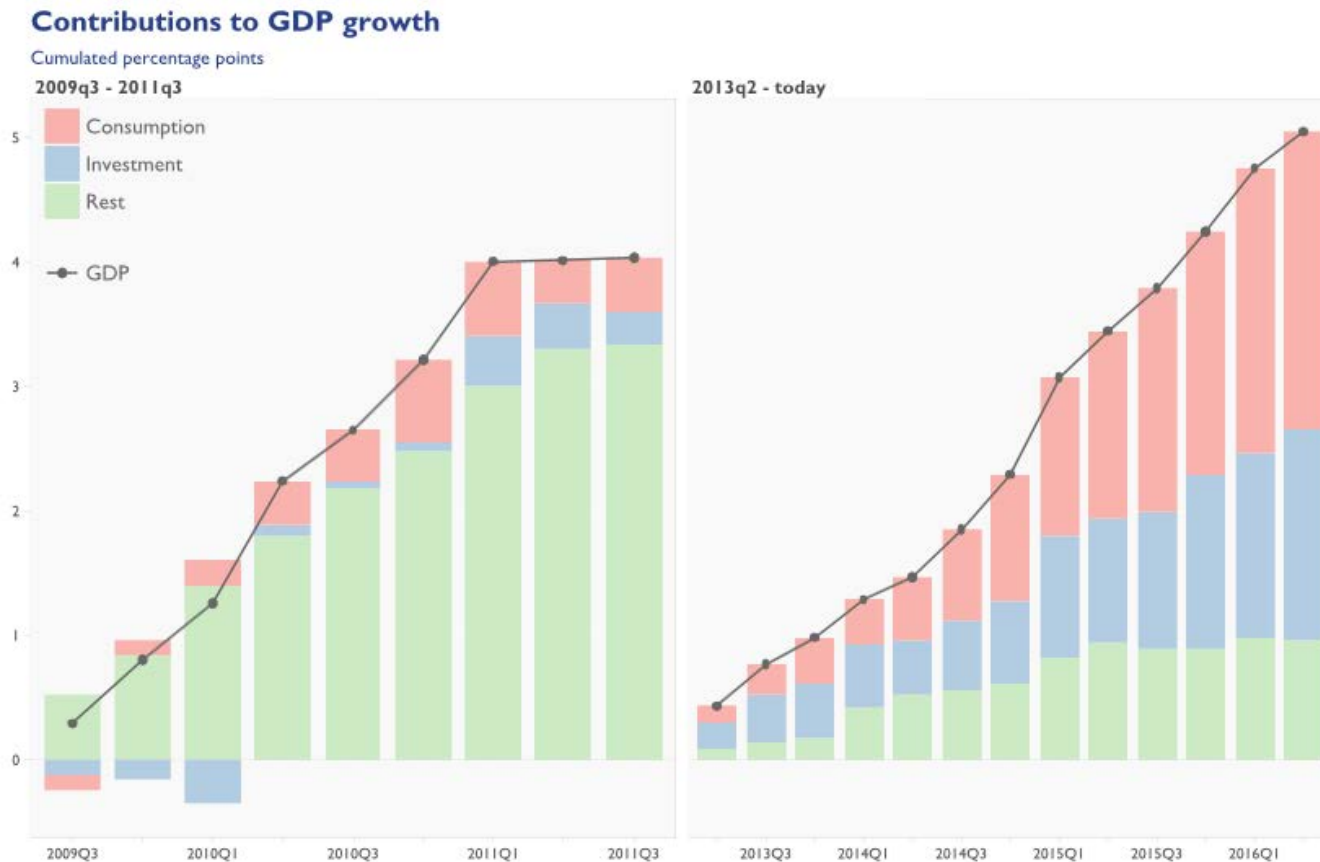
Source: Eurostat and ECB
Note: "Rest" component comprises net exports, government consumption and changes in inventories