
Selected quotations of central bankers' views on monetary policy's contribution to broader economic goals

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Introduction

On many occasions, the Reserve Bank of New Zealand has sought to explain how monetary policy contributes to broader economic objectives, particularly economic growth. We have noted that the most effective goal for monetary policy is price stability and that monetary policy cannot directly promote economic growth or employment. The most effective contribution that monetary policy can make to these broader economic and social objectives is through the achievement and maintenance of price stability. This reflects, among other matters, the important part that low and stable inflation plays in assisting investors, consumers and producers to make economic decisions on the basis of relative prices that are not distorted by high or unstable inflation.

The Bank's views on the role of monetary policy and its contribution to broader economic goals are consistent with the views espoused by many other central bankers around the world. In order to place the Bank's views on these issues in the context of the views espoused in the international central banking community, this paper presents a selection of quotations from central bankers from a number of countries, including the United States, United Kingdom, Canada and Australia. Some quotations from the Reserve Bank of New Zealand are included by way of comparison.

In compiling these quotations, we have tried to capture a broadly representative sample of central banks and have sought to ensure that the quotations are not contradicted by other material in the speech or article from which they have been sourced. However, as with any selection of quotations, the reader needs to remember that the quotations are out of context. Therefore, if the reader wishes to glean a fuller understanding of the selected bankers' views on monetary policy and related issues, it is suggested that they read the speeches or articles from which the quotations have been taken. For that purpose, the source of each quotation is provided in this paper.

Selected Quotations

"While monetary policy can achieve a long-run inflation target, economic theory suggests that it cannot affect the level of output or its growth rate in the long run, other than by maintaining low and stable inflation. Therefore, the objective of price stability should be assigned to monetary policymakers, but the objective of high and rising living standards should not be... Whether central banks should accept responsibility for stabilizing output relative to potential is more controversial."

Speech by Governor Laurence H. Meyer (2001)

U.S. Federal Reserve

Inflation targets and inflation targeting

University of California at San Diego Economics Roundtable, San Diego, California, July 17, 2001

<http://www.federalreserve.gov/boarddocs/speeches/2001/20010717/default.htm>

"Since we have such an open economy, it would be unrealistic to expect that monetary policy could shelter it from external turbulence... Once this fact has been grasped, there is one natural and inevitable conclusion: in this country, monetary policy must aim to create favourable conditions for long-term economic development. Price stability, which is the key to effective spending and investment decisions, makes a positive contribution to the potential growth of the economy."

Speech by Mr Jean-Pierre Roth

Chair of the Governing Board, Swiss National Bank

The challenges of Swiss monetary policy

Swiss Bankers Day, September 14, 2001

http://www.snb.ch/d/download/publikationen/ref_010914_jpr_e.pdf

"The best contribution the Bank of Canada can make to this process is by continuing to provide a stable, low-inflation environment. With an eye to the medium term, this will require setting a course for monetary policy that will ensure that the Canadian economy reaches full capacity smoothly and then continues to grow over time at a non-inflationary and therefore sustainable pace. The longer economic growth is sustained, the more benefits we will see in terms of improved incomes and employment."

Speech by Mr Gordon Thiessen

Former Governor Bank of Canada

The future performance of the Canadian economy

Canadian Club of Winnipeg, Winnipeg, Manitoba, March 25, 1998

<http://www.bankofcanada.ca/en/speeches/sp98-2.htm>

"Our goal has never been to contain inflation as an end in itself. Prices are only signals of how the economy is functioning. If inflation had no effect on economic growth, we would be much less concerned about inflationary pressures. But the evidence is compelling that low inflation is necessary to the most favorable performance of the economy. Inflation, as is generally recognized throughout the world, destroys jobs and undermines productivity gains, the foundation for increases in real wages. Low inflation is being increasingly viewed as a necessary condition for sustained growth."

"Too often in the past, policymakers responded late to unfolding economic developments and found they were far behind the curve, so to speak; as a result, their policy actions were creating or accentuating business cycles, rather than sustaining expansion. Those who wish for us, in the current environment, to await clearly visible signs of emerging inflation before acting are recommending we return to a failed regime of monetary policy that cost jobs and living standards."

"If we consider the current rate of true, sustainable growth unsatisfactory, are there policies which could augment it? In my view, improving productivity and standards of living necessitates increasing incentives to risk taking. To encourage

people to take prudent risks, the potential rewards must be perceived to exceed the possible losses. Maintaining low inflation rates reduces the levels of future uncertainties and, hence, increases the scope of investment opportunities. It is here that the Federal Reserve can most contribute to long-term growth."

Speech by Chairman Alan Greenspan

Board of Governors of the Federal Reserve System

Current monetary policy Haskins Partners Dinner of the Stern School of Business, New York University, New York, May 8, 1997

<http://www.federalreserve.gov/boarddocs/speeches/1997/19970508.htm>

"As a result, monetary policy, in my view, needs to focus on achieving balance between aggregate supply and aggregate demand. In pursuing this course, monetary policy is confronted by two competing challenges. The first is to allow the economy to realize the benefits of any decline in the NAIRU and any increase in trend growth. Supporting maximum sustainable growth is very much the business of monetary policy. But achieving maximum sustainable growth also is about ensuring the sustainability of an expansion and hence avoiding overheating. This is the second challenge today."

Speech by Governor Laurence H. Meyer

U.S. Federal Reserve

Sustainability and monetary policy

National Economists Club and the Society of Government Economists, Washington, D.C. January 20, 2000

<http://www.federalreserve.gov/boarddocs/speeches/2000/20000120.htm>

"In the implementation of monetary policy the first objective of the Central Bank at all times is price stability... Price stability is the best foundation for a growing economy and for continuing improvements in employment. This has been demonstrated consistently, not just in the Irish situation but worldwide."

Speech by Mr. Maurice O'Connell

Governor of the Central Bank of Ireland

Joint Committee of the Oireachtas (Parliament) on Finance and the Public Service in Dublin, February 18, 1997

<http://www.bis.org/review/r980309a.pdf>

"...we learned from our earlier experience that consistently low inflation is a necessary (though not in itself a sufficient) condition for the sustained growth of output of the economy as a whole, for high levels of employment, and for rising living standards, which are more fundamentally the things that we are all seeking to achieve. 'Stability is a necessary condition for sustainable growth' has become the universal central-banking credo."

Speech by The Rt Hon Sir Edward George

Governor of the Bank of England

The Bank of England's monetary policy objective and recent challenges

Royal Society for the Encouragement of Arts, Manufactures and Commerce (RSA) Birmingham, April 11, 2002.

<http://www.bis.org/review/r020412a.pdf>

"One of the key factors in setting monetary policy is estimating the economy's capacity to grow sustainably. We then compare that with the economy's actual growth, as a guide to whether inflationary pressures are likely to increase or decrease. If the Bank, for example, under-estimated the economy's sustainable growth capacity, then it would interpret any particular growth rate as potentially a greater inflation risk than actually it was and would run monetary policy too tightly as a result. The converse would happen if we over-estimated the economy's sustainable capacity to grow."

Reserve Bank of New Zealand

The impact of monetary on growth

Published June 2001

<http://www.rbnz.govt.nz/monpol/about/0107088.html>

"...price stability is best thought of as an environment in which inflation is so low and stable over time that it does not materially enter into the decisions of households and firms. Nonetheless, I cannot help but conclude that the progress that the Federal Reserve has achieved over the years in moving toward this old definition of price stability has contributed to the improvement in our nation's longer-term growth prospects that became evident in the latter part of the 1990s."

Speech by Chairman Alan Greenspan

Board of Governors of the Federal Reserve System

Transparency in Monetary Policy

Federal Reserve Bank of St. Louis, Economic Policy Conference, St. Louis, Missouri (via videoconference), October 11, 2001

<http://www.federalreserve.gov/boarddocs/speeches/2001/20011011/default.htm>

"History suggests, however, that higher price inflation tends to surface rather late in the business cycle and, hence, is not a good leading indicator of emerging troubles. By the time inflation pressures are evident, many imbalances that are costly to rectify have already developed, and only harsh monetary therapy can restore the financial stability necessary to sustain growth. This situation regrettably has arisen too often in the past. The challenge of monetary policy is to detect such latent instabilities in time to contain them. Unfortunately, they are rarely visible until relatively far advanced. Moreover, once they are identified, policy actions to counter them take time to have their effects. Thus, the need of monetary policymakers for early indicators of developing problems is evident."

Testimony of Chairman Alan Greenspan

Before the Joint Economic Committee of the US congress, 31 January, 1994

"The path of trend productivity growth has many underlying determinants—the vibrancy of technology, the strength of entrepreneurial motives, the flexibility of labor and capital markets, and the effectiveness of regulatory policies, to name

a few. But there are also two vital macroeconomic policy determinants. One, involving monetary policy, is a credible commitment to stable prices in the long run. The second, involving fiscal policy, concerns the share of total output devoted to national saving."

Speech by Governor Edward M. Gramlich

U.S. Federal Reserve

Macroeconomic policy in recessions- and other times

Conference on Combating Recessions, Ford School of Public Policy, University of Michigan, Ann Arbor, Michigan, March 7, 2002

<http://www.federalreserve.gov/boarddocs/speeches/2002/20020307/default.htm>

"The main test of what is sustainable on the growth front is the inflation test: is the rate of growth compatible with achieving the 2–3 per cent average for inflation, looking forward as best we can over a year or two? If the answer is yes, then that growth is sustainable, at least at that point in time...While monetary policy's major long-term influence will be on the rate of inflation, over shorter periods it can have a significant influence on economic activity and employment. If it is too tight, it will unnecessarily constrain them, and if it is too loose, it could set up the conditions for an inflationary boom. The relationship between monetary policy and economic growth is thus essentially a short-term or cyclical one."

Speech by Mr Ian Macfarlane

Governor of the Reserve Bank of Australia

Monetary policy and economic growth

Australian Institute of Company Directors (Western Australian Division), Perth, August 12, 1997

http://www.rba.gov.au/PublicationsAndResearch/Bulletin/bu_aug97/bu_0897_2.pdf

*"Theory and empirical evidence suggest that there is no long-run trade-off between inflation and production levels. Indeed, there is evidence that a low-inflation regime supports **higher** productivity. Moreover, monetary policy has essentially only*

one instrument. Therefore, the best that monetary policy actions can do to promote the welfare of Canadians is to aim for low, stable, and predictable inflation with a medium-term target horizon, which will maximize sustainable production levels. This will have the important benefit of tending to mitigate fluctuations in production and employment."

Speech by Governor David Dodge

Bank of Canada

Inflation targeting in Canada: Experience and lessons

Central Bank Governor's Panel on Inflation Targeting at a joint session of The American Economic Association and the North American Economics and Finance Association, Atlanta, Georgia, January 5, 2002

<http://www.bankofcanada.ca/en/speeches/sp02-1.htm>

"... we must conduct monetary policy so as to promote sustained economic growth, create conditions conducive to rising investment, employment, and incomes, and encourage a more stable macroeconomic environment... The best contribution that the Bank can make to good economic performance is to preserve confidence in the future value of money. In practical terms, this means that Canadians should not have to worry about the effects of inflation when they make everyday decisions as consumers, business people, savers, and investors. It means that they should be able to go about their affairs confidently, knowing that they can count on their central bank to do whatever is necessary to keep future inflation low, stable, and predictable. In this way, they will be able to make sounder economic decisions, which will lead to better overall economic performance and rising incomes."

Speech by Governor David Dodge

Bank of Canada

The Bank of Canada and monetary policy: Future directions
Toronto Board of Trade Toronto, Ontario, February 20, 2001

<http://www.bankofcanada.ca/en/speeches/sp01-3.htm>

"Price stability isn't the most important objective a society can aspire to - far from it. The real objectives lie elsewhere - growth, employment, equity, justice and so forth. But monetary policy is targeted on price stability for two reasons: first, because inflation is damaging, even at quite low levels, and secondly, because over time monetary policy cannot durably affect anything other than inflation. By maintaining long-term price stability - and in particular by building public confidence that price stability will be a permanent feature of our economy - we ensure that monetary policy doesn't act as a drag on our growth prospects."

Speech by Dr Donald T. Brash

Former Governor of the Reserve Bank of New Zealand

The building blocks of economic growth

Canterbury Employers' Chamber of Commerce, Christchurch, January 28, 2000 <http://www.rbnz.govt.nz/speeches/0086423.html>

"As we have learned over the past 25 years, a sustained expansion is not possible unless we can avoid a resurgence of inflation and the painful cycles of boom and bust that go with it. Thus, the challenge for monetary policy will be to set monetary conditions at levels that allow the economy to expand at a pace that makes full use of its production capacity and at the same time preserves low inflation."

Speech by Mr Gordon Thiessen

Former Governor of the Bank of Canada

What can monetary policy do to help the economy reach its full potential?

Canadian Club of Toronto, Toronto, Ontario, 1 December 1997

<http://www.bankofcanada.ca/en/speeches/spde01.htm>

"What is particularly notable about this impressive growth in output and employment is that it has been sustained over a period of years and, importantly, there is every prospect that we can continue to sustain it looking ahead. This element of sustainability is, above all, what translates periods of strong output and rising employment into permanent improvements

in living standards. Sustainability means having in place a framework to provide a basis of stability on which the economy can continue to grow. Alongside the stable framework the government has put in place for fiscal policy, the Bank of England's contribution to stability is to deliver price stability... Perhaps the most encouraging feature of the strong economic performance I have described is that it has been achieved consistently with low inflation, and it is through maintaining that commitment to low inflation that we can best ensure that the economy continues to grow over time in line with its potential."

Speech by Mr Ian Plenderleith

Executive Director of the Bank of England

Current issues in monetary policy

Aberdeen Chamber of Commerce, July 26, 2000

<http://www.bankofengland.co.uk/speeches/speech93.htm>

"In seeking to keep inflation low and stable, central banks may also have a tendency to smooth the economic cycle. It is now well understood that one of the more important determinants of changes in the inflation rate is the extent to which actual output diverges from potential output. When actual output falls short of what the economy could produce without difficulty - where, in other words, resources of capital and labour are under-utilised - there is a tendency for inflation to fall. Conversely, when the economy is straining to produce more than it can on a sustainable basis, when capital is being used around the clock and the labour market is tight, there is a tendency for inflation to rise. For this reason, all central banks, even those with no formal mandate to be concerned about output or employment, have to watch carefully what is happening to both in their attempt to keep inflation under control. Indeed, once inflation has been brought down to a low level, it is not much of an exaggeration to say that keeping inflation low and stable is mainly about trying to keep actual output tracking close to potential. And, by reducing the economic and social dislocation caused by booms and busts, that is a useful contribution which central banks can make."

Speech by Dr Donald T. Brash

Former Governor of the Reserve Bank of New Zealand

Central banks: what they can and cannot do

Trans-Tasman Business Circle, Sydney, March 30, 2001

<http://www.rbnz.govt.nz/speeches/0102706.html>

"Because the nation's level of investment, to a large extent, determines our prosperity over time, stability in the general level of prices for goods and services is clearly a necessary condition for maximum sustainable growth... For monetary policy to foster maximum sustainable economic growth, it is useful to preempt forces of imbalance before they threaten economic stability. But this may not always be possible—the future at times can be too opaque to penetrate. When we can be preemptive we should be, because modest preemptive actions can obviate the need of more drastic actions at a later date that could destabilize the economy."

Testimony of Chairman Alan Greenspan

Board of Governors of the Federal Reserve System

Monetary policy and the economic outlook

Joint Economic committee, U.S. Congress, June 17, 1999

<http://www.federalreserve.gov/boarddocs/testimony/1999/19990617.htm>

"Economic growth depends primarily not on monetary policy but on real factors - on how fast the labour force is growing, on how skilled the labour force is, on how much capital that labour force has to work with, on the technology embodied in the capital, on the efficiency of the price system in signalling where capital can be most productively invested, on the nature of regulations and restrictions which inhibit the effective working of the price system, and a host of other factors. Prices which are, on average, stable assist the pricing system to work effectively, and thereby help to ensure that investment takes place in the most economically sensible places. Prices which are, on average, stable tend to encourage saving, and thereby help to finance additional investment. But stable prices won't make the labour force grow more quickly, or make the labour force more skilled, or improve the technology embodied in the capital equipment which the labour force uses, let alone make public sector enterprises more efficient; or improve the quality of the education

system; or move resources out of highly protected sectors into those which can be competitive on international markets; or improve the marketing of commodity exports."

Speech by Dr Donald T. Brash

Former Governor of the Reserve Bank of New Zealand

The new inflation target and New Zealanders' expectations about inflation and growth

Canterbury Employers' Chamber of Commerce, Christchurch, January 23, 1997

<http://www.rbnz.govt.nz/speeches/0041771.html>

"Having expectations of low inflation, ie monetary stability, firmly in place is really irreplaceable in providing the conditions for pursuing all those other policies immediately concerned with the real economy and human welfare. This is in my view no minor point."

Speech by Matti Vanhala

Governor of the Bank of Finland

Old age, new economy and central banking

CEPR/ESI Conference, Helsinki, September 14, 2001

http://www.bof.fi/eng/1_suomen_pankki/1.8_puheet/1.8.1_SPpuheet/010914masapuhe.pdf

"As I noted at the outset, it is widely agreed that low and stable inflation is desirable. Several costs of high and variable inflation have been identified. These costs typically arise from distortions in economic decisionmaking arising from high or variable inflation rates and result in lower levels of output than would otherwise be the case. I won't elaborate in detail about these costs here, because I take as a starting point the agreement that price stability is an important, if not the singular objective for monetary policy. But the key point is that price stability is not an end in itself; it is important because it contributes to a higher level of output and perhaps faster growth in output."

Speech by Mr Laurence H. Meyer

U.S. Federal Reserve

Inflation Targets and Inflation Targeting

University of California at San Diego Economics
Roundtable, San Diego, California, July 17, 2001

<http://www.federalreserve.gov/boarddocs/speeches/2001/20010717/default.htm>

"Typically the only time that monetary policy has an impact on the non-inflationary trend growth rate is when monetary policy allows substantial and variable inflation to emerge. In such cases monetary policy harms growth potential, by confusing and distorting decision-making."

Response by Dr Rod Carr

Acting Governor of the Reserve Bank of New Zealand

The Reserve Bank's response to questions from the Finance and Expenditure Committee on May MPS 2002, May 27, 2002

<http://www.rbnz.govt.nz/monpol/statements/0119876.html>

"... although monetary policy cannot lift the euro area's growth potential, the benefits of price stability for growth are evident, as stable prices provide the proper environment for structural reforms to work."

Speech by Dr Willem F. Duisenberg

President of the European Central Bank
What exactly is the responsibility of central banks of large economic areas in the current slowdown of the world economy?

Central Bankers' Panel at the International Monetary Conference, Singapore, June 4, 2001

<http://www.ecb.int/key/01/sp010604.htm>

*"It is the **sustainability** of the expansion which is the key to maximising economic growth and employment. Thus, another way of expressing the aims of a monetary policy based on inflation-targeting is to say that its aim is to maximise the length of the economic expansion... In short, it is clear that the best thing that monetary policy can do to reduce unemployment is to prolong the expansion and delay and reduce the size of any subsequent recession. On*

occasion, that means tightening monetary policy early to forestall inflationary pressures, as an alternative to more vigorous application of the brakes when inflation has built more momentum... Our tightenings or loosening of monetary policy are determined by the inflation outlook. If the economy wants to grow faster than it currently is, and inflation is not showing any tendency to rise to the point where it could threaten our medium-term objective, then we would not restrict the economy's growth."

Speech by Mr IJ Macfarlane

Governor of the Reserve Bank of Australia

A Medium-term Perspective on Monetary Policy

Queensland University of Technology Business Leaders' Forum, Brisbane, August 10, 2000

<http://www.rba.gov.au/Speeches/2000/index.html>

"Monetary policy will best contribute to the long-term growth prospects for the Euro area if it remains firmly focused on the maintenance of price stability. This will create a stable monetary environment for economic agents to operate in. At the same time, greater flexibility in labour, product and financial markets together with sound fiscal positions and wage moderation will support the objective of maintaining price stability and will create stable conditions to foster employment creation."

Testimony of Dr Willem F. Duisenberg

President of the European Central Bank

Committee on Economic and Monetary Affairs of the European Parliament, Brussels, May 21, 2002

<http://www.ecb.int/key/02/sp020521.htm>

"The Riksbank cannot affect potential growth; our role is to create good conditions for other private and public operators. It is their work on structural reforms, better infrastructure, education, research, entrepreneurship, innovations, etc. that improves the economy's long-term capacity to create growth and thereby welfare in the long term."

Speech by Ms Kristina Persson