The power of dual interest rates

Positive Money Europe roundtable on monetary policy in the Eurozone

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The power of dual interest rates

- The TLTRO is the most powerful monetary innovation since the financial crisis. Far more significant than QE.

- Why dual interest rates are so powerful - always work, in every scenario. Two interest rates matter in EZ: deposit rate, interest rate on TLTROs. Deposit rate should be fixed at zero, and all policy implemented through negative interest rate on TLTRO.

- Comparison of dual interest rates with QE

  A. Impacts demand more directly

  B. Marginal impact increases - in extremis, direct consumption support

  C. Balance sheet ‘risk’ more controllable

The case in favour

A. Legal monetary bazooka in Eurozone - ECB has no excuse for not acting or meeting inflation target.

B. Highest probability of success relative to alternatives - negative interest rates, QE.

C. Does not involve national treasuries. Less controversial than QE, OMT or SMP.

D. Could be ‘targeted’ to support Eurozone Green New Deal, sustainable consumption.

E. Balance sheet effect more predictable than alternatives.

F. Limited asset price distortion.

G. Less likely to increase inequality.

Objections

- ‘Losses’ on central bank balance sheet
  - No different to QE
  - CB ‘losses’ meaningless. Base money can always be controlled
- ‘Subsidy’ to banks
  - All interest rates on reserves are either ‘transfers’ or ‘taxes’ on banks. Negative rates currently are ‘taxes’.
- Direct consumption support is preferable - fairer, more direct, minimal role for banks, no need for credit.
  - True. But more politically controversial than TLTROs.
- Fiscal alternatives are preferable
  - Fiscal policy is always optimal in theory. Never in practice. ‘Optimal’ fiscal policy in Eurozone is illegal for obvious reasons. Emphasis must be on making monetary policy more transparent, democratic and effective. **Key point.**