

Managing climate change: Some lessons from monetary policy

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Blair on climate change (2006)

“The scientific evidence of global warming caused by greenhouse gas emissions is now overwhelming. It is not in doubt that if the science is right, the consequences for our planet are literally disastrous.”

Keynes on inflation (1919)

"There is no subtler or surer means of overturning the existing basis of society than to debauch the currency. The process engages all the hidden forces of economic law on the side of destruction, and does it in a manner which only one man in a million is able to diagnose."

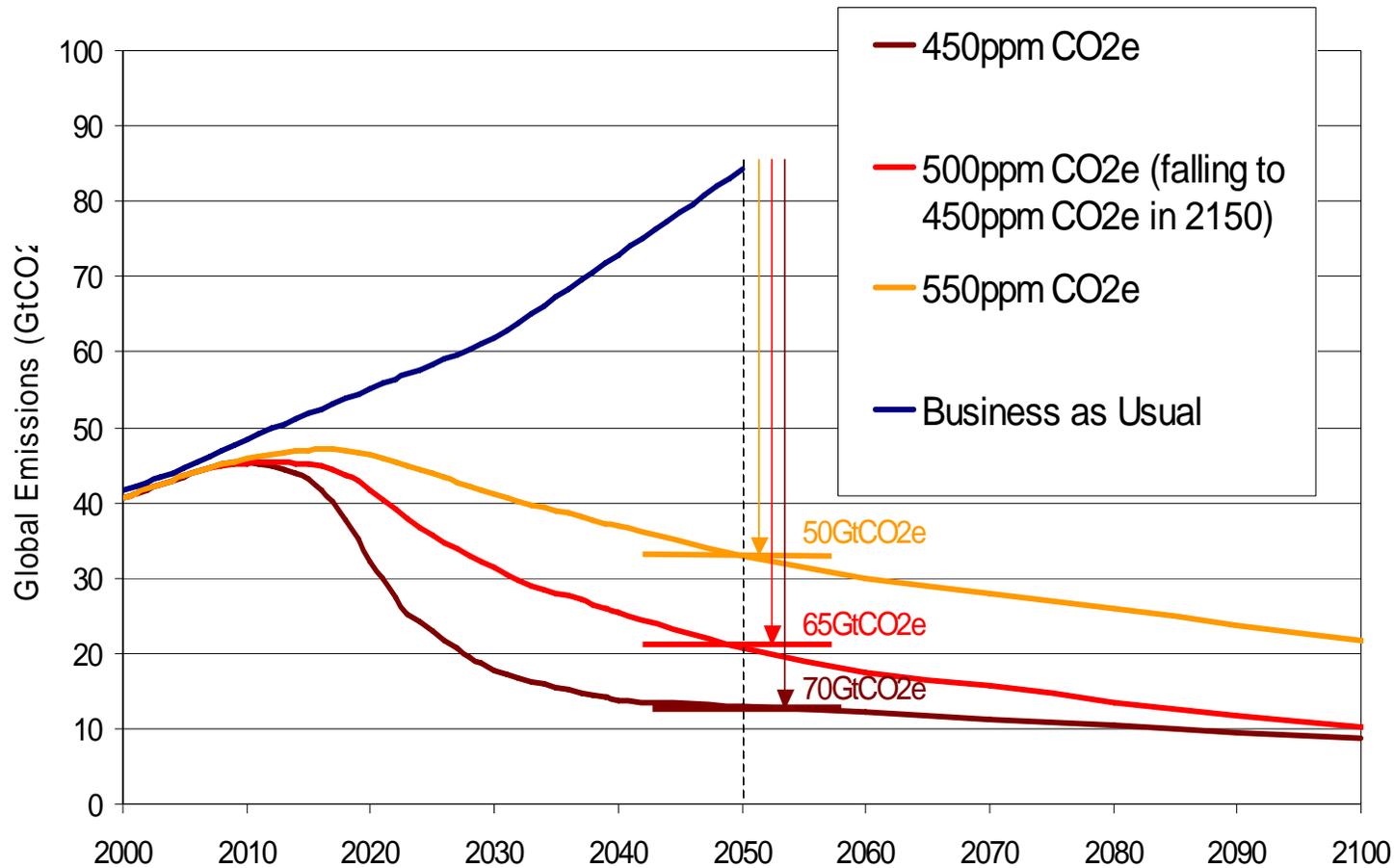
UK and G7 Inflation



Note: UK figures are consumer expenditure deflator prior to 1976

Source: OECD and ONS

Stabilising the global climate



Source: Stern Review

Monetary policy: Key elements

- Objective, framework and target(s)
- Clearly identified policy instrument(s)
- Understanding of transmission mechanism
- Robust, independent and credible process
- Communication, transparency and accountability

Some common challenges

- Stability objective
- High damage potential from policy failure
- Economic instruments needed to change wide range of behaviours
- Establishing robust processes
- Building credibility and consistency

Some important differences

- Natural vs social systems
- International vs national frameworks
- Different time horizons
- Different policy instruments
- Development of policy frameworks

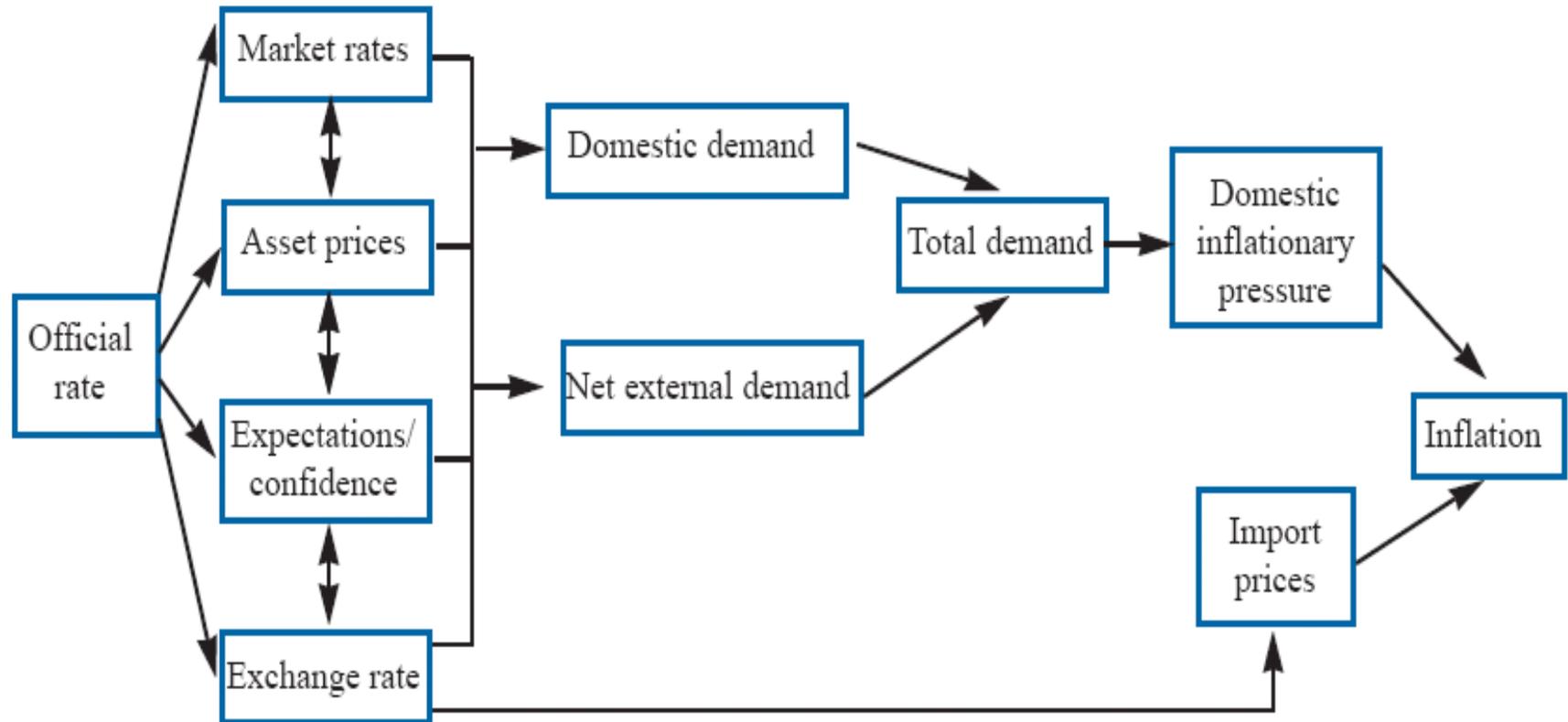
Objective, framework and target(s)

- Political consensus needed to underpin stability and consistency of policy objective
- Ad hoc short-term international co-operation has not worked well
- International policy frameworks require long-term commitment & political/institutional underpinning
- Clarity of target is essential
- Framework and target can be tailored to suit different national requirements

Policy instrument(s)

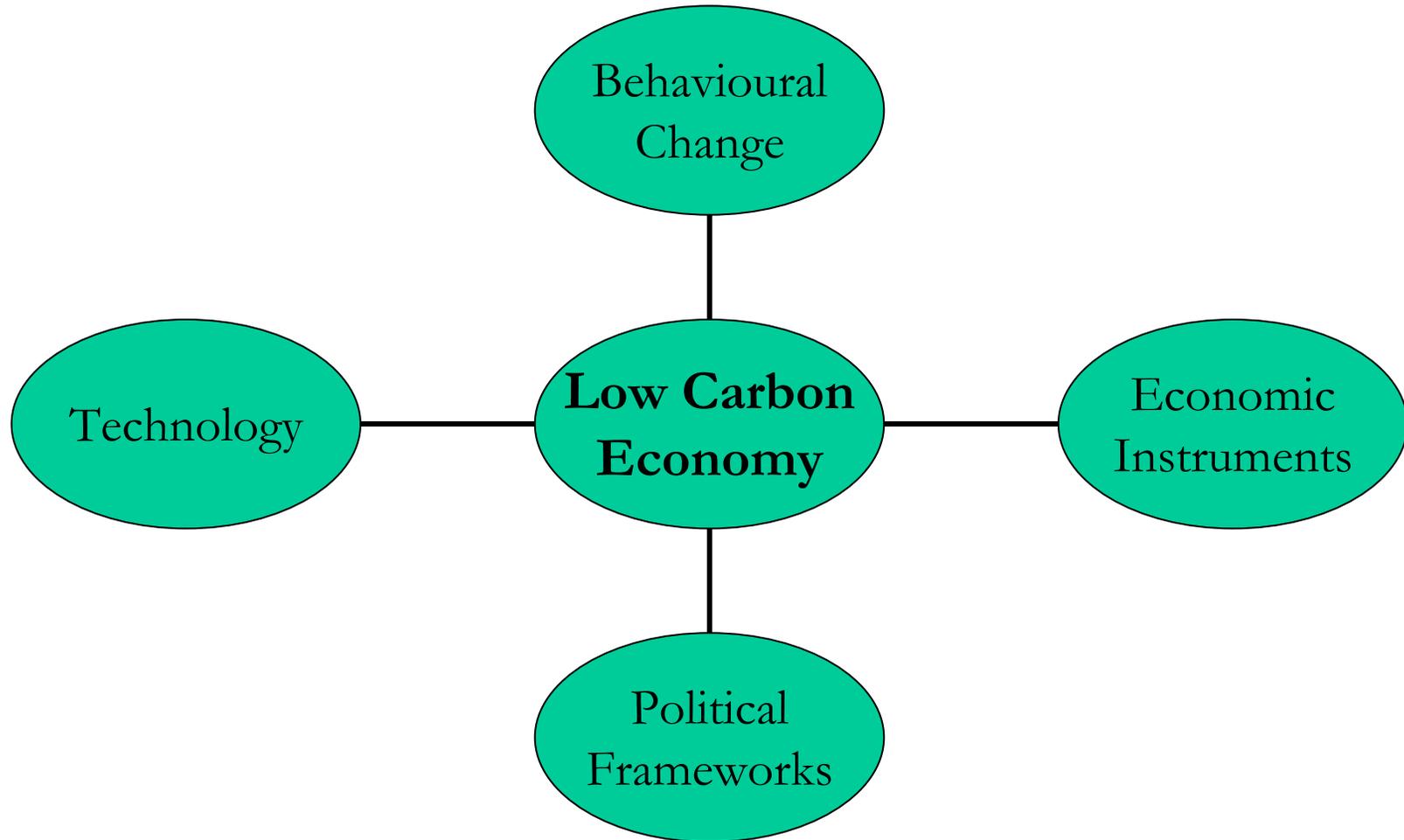
- Use of monetary policy instruments has evolved through time with development of markets
- Single policy instrument approach reflects highly developed and liberalised market structure
- Multi-instrument policy (including regulation and direct intervention) used when policy was less mature
- Independent bodies have assumed greater control over policy instruments as frameworks have evolved and developed credibility

The transmission mechanism of monetary policy



Source: Bank of England

Building the “low carbon economy”



Process and related issues

- Stronger monitoring and sanctions for international agreements
- Importance of evolution in establishing institutions and processes
- Involvement of experienced, expert and independent individuals
- Clear timetables for action and reporting supports credibility and underpins independence
- Communication, transparency and accountability are critically important

Conclusions

- Experience with development of monetary policy can inform development of climate change policy
- Need to recognise differences in policy challenge and less mature/developed markets, institutions and processes
- International institutions and frameworks will need to play a larger role in climate change policy
- Multi-instrument approach may be better suited to current phase of development of climate change policy
- A better model of the transmission mechanism to deliver a “low-carbon” economy needs to be developed
- Robust processes, institutional credibility, accountability and communication mechanisms need to develop over time