Hon. Diane Bellemare

And the winner is...

With my title of Senator, one may have thought that I was an intruder in this conference, but I assure you I was in my element considering I studied economics at Western and McGill and taught economics for over 20 years at UQAM. Though, my positions on monetary policy may differ from others as my economic perspective has been shaped by my experience as a labour economist and as a parliamentarian.

More specifically, my work in managing active labour market programs in Quebec in the '90s convinced me that in real life, monetary policy matters and it matters tremendously. Monetary policy affects the everyday life of many people as well as businesses. Its consequences may be long-lasting and may affect the income stream of individuals and businesses for many years after its implementation. It also affects productivity, the future potential of the economy and the distribution of income. Theorists may argue it is neutral in the long-run and this may be the case in some theoretical general equilibrium models. But as Keynes once said: In the long run we are all dead. As a parliamentarian, I would add it is the present that counts most.

That being said, let's focus on the topic of the conference which is the future framework of monetary policy. I entered the conference with a strong preference for the dual mandate. After listening to all participants, I remain convinced that the dual mandate is the option for the 2021 agreement between the Bank of Canada and the Government of Canada. As demonstrated by the daily polls initiated by the organizers, I am not alone in this line of thought.

Let me explain my position.

Firstly, the dual mandate is the only option that takes into consideration the actual economic situation. It recognizes that monetary policy can participate actively in the recovery process of the Canadian economy following the big structural shocks created by the pandemic while keeping an eye on inflation.

Only a few participants addressed the issue of the pandemic and of the increase in uncertainties in Canada and in the world. The renewal of the five-year agreement will happen in a totally different economic environment then the first one which took place in 1991. It has been renewed seven times since then and has respected basically the same objective: Price stability.

Nowadays, inflation is not the problem it used to be in the past. Due to globalization, technological changes and many other factors, price increases have been relatively low on average since the '90s. Apart from the recent years before the pandemic where demographic factors such as aging produced labour shortages in some provinces and sectors, the main problem in Canada has often been unemployment. The crisis of employment is now back in the forefront of public policy debates and monetary policy must acknowledge this reality.

Consequently, if using the economic context as a criterion to choose among the six options presented in the conference, two options can be eliminated at once. Targeting a lower inflation rate does not address the problem of the day. On the contrary, as many agree, the risk of deflation outweighs the risk of inflation. Moreover, including the pursuit of financial stability within the monetary policy framework offers some interest but does not address the concerns of the day either. Besides, financial stability can be achieved through macroprudential policies.

Second, the dual mandate presents itself as the most credible option. The credibility criterion, which was widely discussed in the conference, enables one to pick the best option among the following: The status quo, the nominal GDP targeting, the increase in the target of inflation, and the dual mandate.

Let me elaborate.

Most of the participants agreed that monetary policy efficiency relies in part on its credibility and capacity to shape expectations. Not only should the Bank be credible in its policy, but Canadians need to understand the message as well.

Under the credibility test, the option of nominal GDP targeting should be discarded. Even though it incorporates issues relating to the economic situation including employment, it is somewhat difficult to explain and fails the credibility test.

The option to increase the inflation target also encompasses employment preoccupations, however, it also fails the credibility test. Indeed, how can one explain to the public that the economy needs more inflation while for so many years the Bank argued that the economy needs price stability. It is neither easy to argue nor to communicate.

What about the status quo? I am convinced that the status quo is not an option because it focuses only on inflation targeting while the main problem concerns growth and employment.

On the other hand, one may argue that due to inflation being below target, this option implies the need to stimulate the economy. I believe this argument encounters the same credibility concerns as increasing the inflation target. If the status quo implies stimulating inflation and coincidentally promoting growth and employment, then why not make it explicit through the dual mandate? Undoubtedly, it would make it easier to comprehend.

Having applied those two tests, the choice becomes obvious. It is time for Canada to adopt a new framework for its monetary policy and enlarge it to embrace not only price stability, but full employment or maximum employment as seen in countries such as the USA, Australia and New Zealand. In short, it is time to adopt the so-called dual mandate.

As Professor Pierre Fortin has often argued, the dual mandate adopted in the USA may explain why the American unemployment rate has often been lower than the Canadian one.

The dual mandate is a more credible choice for the coming decades, particularly when facing future challenges such as increased risks associated with climate change, technological changes and many other variables. It is also more credible and more equitable because it considers the concerns of those who have assets as well as those who do not and need a job for their livelihood.

Furthermore, I would argue that the dual mandate is more efficient. By taking employment into account, it could have positive indirect effects on productivity. As everyone knows, increases in productivity help to absorb supply costs increases.

If the dual mandate becomes the new framework, I would argue that the specific target of a two percent average inflation rate may not need to change. The period considered could be enlarged (to 18 or 24 months), especially when considering the Covid-19 factor which creates a lot of uncertainties and unpredictable events.

The full employment target is not as easily defined as the inflation target. However, it should not be understood as the so-called natural unemployment rate. I think that the availability of statistics on vacancies enables the Bank to use a large spectrum of information in order to appreciate the state of full employment. The Bank could utilize the concept once proposed by Beveridge and Keynes: full employment is achieved when the number of vacancies equate the number of unemployed. The Beveridge curve could offer an analytical tool to assess the different labour markets in Canada.

The dual mandate may demand more coordination between monetary and fiscal policies, but that is not an absolute constraint. Indeed, we can already observe that the Bank and the Department of Finance do collaborate.

Finally, let me say a few words on an issue dear to me and other parliamentarians which concerns the democratic deficit surrounding the process of choosing a monetary policy framework.

I agree that the central bank should enjoy independence in its operations, but the monetary policy framework could be defined through a more democratic process. A recent paper from the Bank of Canada[1] compared the practices of different countries in choosing their monetary policy framework. In Canada, the central bank proposes the mandate and the targets, does the research, proceeds to the evaluation of the results and relies on the decisions of the Governor and his team to operate the policy. Is this the best practice? I am not convinced.

Monetary policy is too important to be left to politicians. I agree. However, it is also too important to be left in the hands of the Governor and his team alone no matter how qualified they are. Government and Parliament must have a say in defining the mandate. Policy evaluation could be performed by independent research. The creation of a monetary policy committee, as proposed by Douglas Laxton who convincingly presented the case for the dual mandate, seems like a good idea. If such practices and a dual mandate were adopted, monetary policy would respects the essence of the Bank Act preamble and maximizes the Canadian welfare function.

1 Robert Amano, Thomas J. Carter and Lawrence L.Schembri, (2020), Strengthening Inflation Targeting: Review and Renewal Processes in Canada and Other Advanced Jurisdictions, Bank of Canada.