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Is “Inflation First” Synonymous with “Rentiers First” in the Pursuit of Monetary Policy? The Dominance of the Taylor Rule and the Rentier Income Share in Industrialized Countries

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In this paper, we analyze the effect of monetary policy on the functional distribution of income by adopting an alternative Keynesian socioeconomic class analysis that was fashionable historically, and which still remains common, to a significant extent, among post-Keynesian/institutionalist economists (see, for instance, Seccareccia & Lavoie 2016, and Seccareccia & Matamoros Romero 2022). The latter approach differs methodologically from what is currently in vogue, namely the use of the representative agent and/or heterogeneous agent-based modeling, with the latter having proliferated within the mainstream literature since the Great Financial Crisis (GFC) and which has become particularly popular among New-Keynesian economists. Instead, inspired by Keynes’s original class analysis going back almost a century to the Tract (1923) and General Theory (1936), we consider how monetary policy impacts on the income dynamics of three broad social classes not because of their heterogeneity as in the usual binary classification of rich or poor households, for instance, in two-agent New-Keynesian (TANK) models, but because of these groups’ special socio-economic class interests qua wage earners, profit earners and interest-income earners.

Although framing our analysis within this original Keynesian and post-Keynesian tradition, this paper investigates, more precisely, whether monetary policy has favored the income of one group, that of rentiers (or net creditors) relative to the income of the non-rentier groups (or net debtors). This has been especially so since the widespread implementation of “inflation first” monetary policy starting in the late 1970s and, then, of the increasing use, either implicitly or explicitly, of the Taylor-rule policy framework by central banks in major industrial countries in the early-1990s as they espoused inflation targeting (IT).

Moreover, we wish to draw particular attention to the ongoing debate over the Taylor rule, which is usually presented superficially in context of the perennial debate over "rules versus discretion" in pursuit of monetary policy, in this case in prioritizing inflation-fighting over all other possible goals. As is well known, because of possible structural break in monetary policy implementation after the crisis of 2007-2009 (see Seccareccia & Kahn 2019), the Taylor rule has returned as a significant political issue, especially over the last dozen years since that crisis. For instance, in recent times in the US some Republican representatives have argued that the Fed has been given too much discretion in pursuit of its current dual mandate cum its 2 percent IT "add-on" since 2012. In its place, the Fed authorities should be bound by formalized rules, that is, they should be guided strictly by the Taylor equation. While officially objecting to the latter framework, for instance, by former Fed chair, Janet Yellen, in 2016, the whole political economy of how this rule is adopted remains a major flashpoint as the problem of inflation has climbed once again to centerstage within monetary policy circles since early 2022.

The object of our paper is to analyze how widespread use of the Taylor rule (or its variants) by IT regimes had very specific consequences on income distribution. We divide our paper into three broad sections that try to cover history, theory, and evidence on the subject.

In the first section, we study what is the connection between rentier interests and the adoption of the Taylor rule as a general framework to meet specific inflation targets. In other words, what has been the political economy, especially with pressure coming from rentier groups, to introduce and integrate the Taylor rule as framework to conduct monetary policy under inflation targeting regimes? Were there alternative frameworks at the time? What was the role of rentier groups in its adoption and subsequent establishment? This section puts forth the historical and institutional context in which the adoption of the Taylor rule has taken place.

The second section explores the theory behind the Taylor rule in relation to its potential consequences on rentier income share. In doing so, some of the questions that would be addressed are: Are there crucial differences between the Taylor rule and the Wicksell rule with regards to the implications on interest rate policy and on income distribution among socioeconomic groups? What role does the unemployment variable take in the Taylor formula and is it compatible with, say, a dual mandate? To what extent can the Taylor rule be considered a real interest rate rule whose purpose is that of stabilizing rentier income while destabilizing incomes of non-rentier groups?

The third and last section addresses empirically whether monetary policy has benefitted rentiers compared to non-rentier groups during the era of the Taylor rule dominance that began roughly three decades ago in the early-1990s and until the GFC but which, in some ways, still dominates the conduct of monetary policy in major industrial countries. We explore conventional panel data

econometrics with different measures of rentier and non-rentier income shares for several industrial countries covering at least the last three decades. We start by discussing the empirical measures of the rentier income share. Particularly, we compare variants of the Pasinetti index as proxies for the evolution of the rentier share with respect to more conventional measures. We, then, carry out panel data regressions where different measures of rentier income share would act as dependent variable. Another purpose of our proposed research is not only to shed light on what is most certainly a neglected aspect of monetary policy on income distribution but also to point to the current relevance of these older Keynesian and current post-Keynesian ideas to understanding monetary policy.

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