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The Role of Federal Reserve Policy in Creating Wealth Inequality

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Our paper studies the effects of monetary policy on wealth inequality in the United States, estimating its historical contribution since 1980. It contributes to the burgeoning literature in the past decade on whether central bank policy is contributing to income and wealth inequality. Our dependent variable of interest includes several distributional statistics of wealth inequality—Gini coefficient and wealth ratios 99/50 and 90/50—as well as the real value of wealth accumulated to the top 1, 10, and bottom 50 percent of the wealth distribution. These data come from the World Inequality Database. We use the local projections instrumental variable (LP-IV) regression method in which we instrument changes in the policy rate using three different monetary policy shocks series that each attempt to capture the effects of unconventional monetary policy in different ways. This identification method aims to create a quasi-experimental design that will allow us to identify the cause-and-effect relationship between our explanatory variable, changes in the Federal Reserve’s policy rate, and our outcome variables of interest. Our initial findings are promising and run counter to the findings in some of the recent literature that indicates a negligible or even negative effect on wealth inequality due to monetary policy. Our preliminary results indicate that expansionary monetary policy shocks have sustained and significant effects over time by increasing wealth inequality measures as well as the average wealth of the top 1 and 10 percent of the income distribution. Moreover, our analysis of the historical changes in average wealth has also led us to conclude that monetary policy, between 1980 and 2019, has, on net, contributed significantly to the yawning gap between the top and median of the wealth distribution, especially since the advent of unconventional monetary policy after 2008.