WHY DO CENTRAL BANKS ‘GO GREEN’?
Alina Azanbayev, Jan-Christoph Rülke
EBS Universität

MOTIVATION
- Physical and transition risks can impede the effective fulfilment of central banks’ mandate of maintaining price stability and also securing stability of the financial system.¹⁻⁻⁶
- 19 out of G20 central banks take climate change into consideration.⁷
- Some of them are taking considerable actions.
- However, it is still unclear when and to which extent green monetary policy is useful.⁸⁻⁻¹⁰
- Primary objective and secondary objective may collide, causing a trade-off between price stability in the medium-term and implementing long-term green monetary policy.

GREEN CENTRAL BANKING
- Passive: Pursuing main goals of price and financial stability could also require considering climate risk and other sustainability-related factors for the design of monetary policy and financial regulation.
- Active: Actively use tools to stir market behavior into desired direction, e.g., encouraging green investments, discouraging brown investments.¹¹

RESULTS
- Low long-term inflation rate seems to be a necessary condition to implement monetary policy.
- Financial market participants should carefully observe whether a central bank is about to go green as this might be associated with higher economic costs and inflation rate.
- Climate change might increase the awareness of central banks to go green particularly in those countries who are not yet fully accommodating towards a green policy.

CONTRIBUTION
- Identifying and quantifying trade-off between greenness of monetary policy and the objective of price stability.
- Estimate how costly the implementation of green central bank policy is.

DATA & METHODS

MULTI-VARIATE REGRESSION MODEL:
Greenness = α + β₁₅ inflation + β₁ independence + β₂ green mandate + β₃ natural resources + β₄ extreme weather + β₅ renewable energy + ε.

IMPLICATIONS
- Price stability is a prerequisite for central banks to go green reflecting the green-inflation trade-off. If the inflation rate increases, more capacities of a central bank’s operations are directed towards their core mandate of maintaining price stability and sustainability topics.
- To be able to implement a green policy, the central bank must operate within its legal framework. Having a sustainability mandate facilitates going green.³
- In countries that are dependent on natural resources with a higher share of their GDP, central banks are less inclined to undertake a green transformation.
- In countries that rely more on renewable energy, central banks are also more likely to adopt green policies.

REFERENCES

CONTACT alina.azanbayev@ebs.edu

CEPR Paris Symposium 2023