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Understanding the World Economy and the Politics of Central Banks

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Abstract

In this paper we are dealing with a very important and sensitive aspect of our days, which influences the life and businesses, that is the monetary policies emerged from central banks.

We are living challenging times and the circulatory system of the economy, that is monetary one, is needed to be carefully followed, stage by stage, in order to react promptly to the possible disruptions in business activities.

Our knowledge in the field of Economics and the experience as a bank customer, we've tried to highlight the importance of the information provided and the feedback from the market, on short or medium term, and the necessity of being cautious in monetary-financial affairs, in order to mitigate the influences of negative factors/challenges as much as possible, both for people and firms. Given this desired situation, it is needed, and we support this, to understand what is communicate through diverse media channels, press releases, other declarations, in order to ensure the quick adjustments of actions and the well functioning of all parts of the economic system.

The data presented can say more, or they can say nothing, consequently people/firms are needed to prevent possible future negative actions and effects, by understanding these information and press releases.

Keywords: *Central Banks, Monetary Policy, Inflation, Interest Rate, Sustainability.*

THE SPECIFIC ISSUE IN DISCUSSION

As an introduction to the present issue, we may say that the *monetary policy* is the macroeconomic policy laid down by the central bank. It involves management of money supply and interest rate and is the demand side economic policy used by the government of a country to achieve macroeconomic objectives like *inflation, consumption* (our emphasize), growth and liquidity (www.economictimes.indiatimes.com/definition/ 2023).

Monetary policy uses tools issued by central banks to keep a country's economy stable while limiting inflation and unemployment. Expansionary monetary policy stimulates a contracting economy, and a monetary policy that contracts slows an inflationary economy. A national monetary policy is often coordinated with its fiscal policy.

A central bank can revise the interest rates it charges to lend money to the nation's banks. As rates rise or fall, financial institutions adjust rates for their customers, such as businesses or home buyers. We care about the goals of monetary policy because they influence our lives and economic activities.

a. Inflation where monetary policy contracts and is used to temper inflation and reduce the level of money circulating in the economy. Expansionary monetary policy favors inflationary pressure and increases the amount of money in circulation;

b. Unemployment where we have an expansionary monetary policy that must lead to the reduction of unemployment, because a larger money supply and attractive interest rates stimulate business activities and the expansion of the labor market;

c. The exchange rate, that is, the exchange rates between domestic and foreign currencies can be affected by monetary policy. With an increase in the money supply, the domestic currency becomes cheaper than its foreign currency. Important in the present analysis is that a tool consists in the fact that the central bank can change the interest rates and the necessary guarantees that it requires (emphasis added) (Brock, 2023).

Next, we developed these aspects on the most important central banks of the world, or financial institutions of the world, entities that play a special role especially now when the economic challenges are multiple and await rational and firm measures.

A very significant aspect for the present issue is that revealed by Frankel and Kartik (2018) that is the public/customers, people, attributes to the Central bank policy choices more to the information provided and less to the technical aspect regarding the operational shock information. Furthermore, the specialists forecast a strategic benefit of *greater competence about Central bank policy objectives* (our emphasis).

What it is highlighted by specialists in the field (see Jia, 2023) is the fact that when a central bank changes its target of increasing the interest rate (the level of it), it means an exogenous action on firms and households, which have imperfect information about the state of economy and the monetary policy really affects the economy and all its actors.

How the information provided affect the consumers and the confidence?

METHODOLOGY

We used in this paper secondary data, extracting the information from banking meetings, from press releases, declarations, opinions. All these sources, as systematic review, are used in order to comprehensively understand how the central banks communicate nowadays with the economic/business environment and with people.

Adding our knowledge in the field of Economics, we've tried to highlight the importance of information provided by the Central Banks and the feedback to the information received, on short or medium term, and the necessity of being cautious in monetary-financial affairs, in order to mitigate the influences of negative factors/challenges as much as possible, both for people and firms.

Furthermore, we try to synthesize all information and forecasts, in order to understand what could be the course of the world economy in the immediate period.

THE WORLD ECONOMY AND THE POLICIES OF CENTRAL BANKS

We want to present, in the first part, other views of other central banks, outside the ECB, of some representative countries in the current world economy.

Let's talk about the Fed (Federal Reserve), the central bank of the United States of America. According to the views expressed by some Fed officials, such as Jerome Powell, the current inflation crisis stems from several temporary supply chain problems related to the pandemic, as well as the rapid reopening of the global economy after a brief recession. As painful as this current inflation crisis is for Americans (and more, we say), it's nothing compared to what people experienced in the early 1980s, before then-Fed Chairman Paul Volcker affected inflation through a series of massive rate hikes (LaMonica, Paul, 2022).

However, the Fed is not done raising the inflation rate. Investors appreciate the likelihood that the interest rate will rise further, precisely to counteract the general negative effects of inflation. And the chances of a fifth consecutive increase of this magnitude at the Fed meeting on December 14 are, also growing. Powell has repeatedly called inflation "transitory" for much of the past year. Yes, that's right, inflation is transitory, but it depends on the timing of it. So, the Fed will continue to raise rates to show that it is serious about inflation, And, it must be taken into account that the Fed, like other central banks (not only of developed countries), has in its monetary-financial policy two clear mandates, two targets, the above material):

a. Price stability;

b. Employment of the labor force as fully as possible.

Let's see the second economy of the world, China, how it presents itself in the current conditions (www.hotnews.ro 2023).

This analysis is carried out after the visit of the Chinese Prime Minister Li Qiang to Europe, France, Germany in the first place and after the discussions with the President of the European Commission, Ursula von der Leyen. The aspect that must give thought and can influence the financial markets and, subsequently, the other markets, is the European Union's position that Europe must reduce the risks on the diplomatic and economic relationship with China (emphasis added). Subjective, invisible or visible barriers must be raised so that the economic fragmentation of the world (which is one of the ways seen at the moment) is avoided and the economic and financial globalization of the world continues. An open world economy, with finding a middle line of communication and understanding to the advantage of all states involved, is the viable solution for humanity, is our credo.

Chinese economy slowed down in Q2 amid housing crash and deflation expectation, and the analysts expect the economy could bottom out in the rest of year with the help of policy support.

We expand the economic vision of China, as the economic contribution of Hong Kong, still considered one of the "Asian tigers", must also be taken into account. Tourists and even businessmen returning from Hong Kong and other recovery sectors will boost the local economy and boost confidence, while the city's unique role in China's financial system will support the recovery of both China and Hong Kong throughout 2023 and beyond (Kang, 2023).

Very important to Hong Kong is the role as a financial center for the nation is the internationalization of the RMB. Hong Kong is the largest offshore RMB business center in the world, accounting for 73% of international RMB payment transactions. As the RMB is expected to play a greater role in China's trade and finance in the future, this will provide new opportunities for the development and growth of Hong Kong's financial sector.

A clarification, the China Central Bank has announced that it will implement the monetary policy in a "precise and forceful" manner to support the national economy commitments. The Bank will maintain a stable credit expansion and keep liquidity reasonable ample, within a more complex and severe external environment, exactly as we said regarding the reports, figures and even the realities in moving (see www.timesofindia.indiatimes.com/business/ 2023).

GDP is losing momentum, mainly in China, but there signs to recover, especially based on the household consumption. The announced measures to be taken will be exactly in the spirit of monetary policy “precise and forceful” (Dong et al., 2023).

The measures that are taken, or will be taken, must lead to economic stabilization - as we have seen it is one of the major goals of the big central banks - even if they face many difficulties, especially taking into account the global geo-economic situation currently very sensitive. Inflation and, as a result, energy and food prices, will be intensively monitored, precisely because it is susceptible to negative economic effects, which an economy like China’s cannot afford (www.bursa.ro 2023)..

An outstanding situation is that *all economic indicators in July 2023 are below market expectations and previous readings* and a reality that comes to strengthen these so-called “unexpected” unforeseen movements.

In UK, it is something coming from the recent part, so-called *Trussonomics*, based on the name of a previous PM, Elizabeth Truss. The real cost of this policy was, to some extent, the austerity and spending cuts to cover fiscal holes in the budget (Pratley, 2022). The Bank of England has appeared with an increased fiscal and monetary accountability. Therefore, for fear of the inherent movements of free markets, the true cost of this financial-economic policy is that of the reduction of public spending, but also with the increase of fiscal restraint measures. When he came into office, Truss promised to make the recession shorter and shallower - in all likelihood he made it deeper and longer (the cited source).

And, in this case, we highlight the fact that the markets have somewhat managed to erase these chaotic measures taken, but the bill for the doomed experiment is yet to arrive for the rest of us.

Because we are talking about the sacrosanct Bank of England, founded in 1694 by a Scotsman, William Patterson, who has to manage the UK situation after Brexit process, is based on a program to relax money printing (perhaps a reminiscence of what I was saying about his activity John Law at the beginning of the 18th century), so the quantitative increase in the money supply, an aspect that naturally led to the galloping increase in inflation, as well as to the deepening of the gap between the rich and the poor (Macpherson, 2023). To better understand, the Bank of England’s program of quantitative easing of money issuance favored high-rate inflation “to take root”. We want to emphasize here, perhaps, the essence of the error of those who thought the monetary policies of this period: central banks around the world deluded themselves into believing that inflation, through the play of the free economy and the appropriate instruments, would return to normal after decades of growth low and stable prices in the economies of developed countries. In the UK, for example, the end of last year recorded an inflation rate of over 10%, an aspect that involved the corroboration of the three great challenges of the period we are going through: the exit from the COVID 19 lockdown period, the war in Ukraine, but also the economic situation, not favorable, after Brexit process. What happened since then? The inflation rate fell at a slower pace than expected to 8.7%, the highest in the G7, forcing the sale of government bonds and yet, in line with the policy of other major central banks, to raise interest rates to further try to dampen inflationary pressure (material above). In the UK, the Bank of England forecasts that the economy will continue to contract until mid-2024.

Where is the global economy headed in 2023? After all the challenges of the past year, it’s a question we’re all dreading. As the economy grapples with the ongoing effects of the Covid-19 pandemic, Russia’s invasion of Ukraine in February 2022 increased inflation. Professor Steve Schifferes asks what’s next for inflation, interest rates and economic growth, i.e. the defining elements of responsible monetary policy (www.city.ac.uk 2023).

It is appreciated that throughout this period of one year, that is, since the central banks of the most developed countries of the world, but also the others that had to follow their example, the countries that had to gain from the record levels of two numbers, some even starting with the number 2 (and two figures), were the over-indebted ones (Cojocaru, 2023). The assessment is aimed at Europe, the European Union. In order for the forecasts to continue to come true, even for 2024, vigorous economic growth and strict budgetary discipline are needed. An example of what we are supporting here and now is Spain, a country that managed, through adjustment, to bring this hitherto ruthless indicator to a value of 2.9%, close to the ECB’s inflation target of 2%. Rating agency Fitch has given Spain an A- long-term Spanish debt rating with a stable outlook. I was saying that high inflation helped the over-indebted states simply that inflation erodes debt, among other things. Also, the more a product becomes more expensive, the more the related VAT increases, and therefore, without effort, more money is brought to the budget. But as inflation subsides, states will feel the pressure of debt that follows, as low interest rates encouraged them to spend money they didn’t have. The negative forecasts target, first of all, the main economy of Europe, with a strong economic contraction, which has been clearly observed in recent weeks, considering, rightly, that Germany has already entered recession. So, this country ranks at the top of the states with a projected negative growth.

High inflation is probably the biggest challenge facing the world economy this year as well. The aspect we need to emphasize is that this rapid increase in the inflation rate, which reached almost 25% in some countries, took the central banks by surprise, which did not expect this, after quite long periods with a low rate and a normal trajectory of national economies.

The last forecasts for 2023, even 2024, are referring to European Union, especially Euro Zone, because we are dealing with the monetary policy of European Central Bank (ECB) (Dong et al., 2023):

Global growth in Euro Zone 0,4 % in 2023 and 1 % in 2024;

Inflation rate in Euro Zone 4,1% in 2023 and 1,5% in 2024;

Unemployment rate above 6 % in 2023 and below 6% in 2024.

We see that the rates are reserved for 2024 and even for the end of this year.

Speking about European Central Bank, after the key-meeting from the mid-september 2023, inflation continues to decline but is still expected to remain too high for too long. The Governing Council is determined to ensure that inflation returns to its 2% medium-term target in a timely manner. In order to reinforce progress towards its target, the Governing Council today decided to raise the three key ECB interest rates by 25 basis points (www.ecb.europa.eu/press 2023).

With the increasing impact of tightening on domestic demand and the weakening international trade environment, ECB staff have lowered their economic growth projections significantly.

Forecasts are also made per country, because the interest of the management of the European Union, especially monetary-financial, is to make all the Member States functional, as the whole mechanism to be able to function without major syncopated.

We want to specify one more thing, that it is important in everyday life. We are referring to astral predictions, which are much closer to people, what everyone is looking for, especially in this troubled time. That's right, even though we're in the last quarter of 2023, the predictions for 2024 are out, especially on what most people care about: who will make more money. This study has now appeared at the end of June, in Astrotalk, made by British specialists and in which it is presented which would be the lucky signs. But, we believe that, no matter how well these forecasts are made, they still have greater error margins than the statistical or empirical ones of economic phenomena and processes. If central banks do pivot from hike to hold, then they will need to give clear and credible communication if they want to anchor rate expectations on an extended hold. Above all, central banks need a coherent narrative that links the old plan with the new plan. It is hard to explain how you are in risk management mode.

And this is the main finding of this paper: we are in the presence of a combined cyclical movement with short or medium-term movements of the nature of

Hike (**until now, by increasing the interest rates**) → hold (stagnation) on a plateau→ go upward/increase or downward/decrease (depending on the activities from the free markets)

CONCLUSIONS

Central banks use monetary policy to manage economic fluctuations and achieve price stability, which means that inflation is low and stable. Central banks in many advanced economies set explicit inflation targets as part of their watchdog, at least over the medium term. International experts have welcomed the measures taken by the ECB, but also by other important central banks, to combat or mitigate inflation as much as possible. So different central banks around the world work with different macroeconomic environments and will react in a specific way to ensure that their own economy is performing at the level they would like. Many central banks have mandates or objectives – most of which include price stability, which is inflation, and because of those economic reports that they produce, central banks are able to track inflation and price stability to make decisions about interest rates.

The permanent communication with the citizens, with the business environment, made by the bodies with attributions in this field, primarily the central banks, is intended to keep consumers and all economic actors informed of what is happening and what may happen in the next forecast interval.

The banks' policies and objectives interfering with public/customers needs are on the first plan of the information received. More said, a so called optimal monetary policy involves the situation in which the interest rate (the main target of our days) has an informational effect and the central banks adjust this rate in order to ensure the well-functioning of the economy.

And, we want to highlight the self-regulating mechanisms of the markets, which allowed and ensured the refutation of some forecasts related to the evolution of inflation (as we already presented), leading to what appeared in media as declarations of "unexpected" movements in the evolution of inflation.

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