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Digest

Carbon pricing, central bank policy and inequality

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Traditionally, the economic literature on climate change has focused more on the long-run growth implications. Only more recently, there has been growing interest in the short-run effects of climate change and climate change mitigation policies in particular. What is the impact of these policies on economic activity and prices? What are the distributional consequences? And how does climate policy interact with other fiscal and monetary policies? Below are some recent contributions on these important topics.

Känzig (2022), in "The unequal economic consequences of carbon pricing," studies the aggregate and distributional impact of carbon pricing using data from the European Emissions Trading System (EU ETS). He finds that carbon pricing is successful at reducing emissions and leads to an uptick in green innovation, but this comes at an economic cost that is not borne equally across society: Poor households lower their consumption significantly while richer households are much less affected.

Konradt and Weder di Mauro (2022), in "Carbon Taxation and Inflation: Evidence from the European and Canadian Experience," study the impact of carbon taxes on consumer prices in Europe and Canada. They find that carbon taxes do not have strong inflationary effects. Their evidence suggests that the increase in energy prices was more than offset by a fall in the prices of services and other non-tradables. The weak inflationary effect may be attributed to a significant contraction in income and expenditure, in particular among the richer households, associated with the tax.

Goulder et al. (2019), in "Impacts of a carbon tax across US household income groups: What are the equity-efficiency trade-offs?," assess the impacts of carbon taxes of various designs across U.S. household income groups in a computable

general equilibrium framework, accounting for both use- and source-side impacts. Their results highlight that the distributional impacts crucially depend on the nature of revenue-recycling and the treatment of transfer income.

Annicchiarico and Di Dio (2015), in "Environmental policy and macroeconomic dynamics in a new Keynesian model," study the dynamic behavior of an economy under different environmental policy regimes in a model with price rigidities and nominal and real uncertainty. They find that price stickiness can alter the performance of the environmental policy regime significantly and that the optimal environmental policy response to shocks is strongly influenced by the degree of price rigidity and by the monetary policy reaction function.

Avtar et al. (2021), in "Understanding the Linkages between Climate Change and Inequality in the United States," review the literature on how physical climate change, adaptation and the low-carbon transition policies affect inequality. They find that measures that individuals and governments take to adapt to climate change and transition to lower emissions risk increasing inequality. Finally, while federal aid and insurance coverage can mitigate the direct impact of physical risks, their structure may— inadvertently—sustain and entrench existing inequalities.

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