Funding the Future

The IMF is suggesting that monopoly power is underminin...

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In a fascinating new blog post that was published yesterday three IMF authors suggested that:

Some central banks are currently debating whether to tighten monetary policy to fight inflationary pressures, after having eased decisively in response to the COVID-19 shock. In making such decisions, central bankers have to consider how much businesses and consumers will respond. The structure of the financial system and the future expectations of consumers and businesses are key drivers of how effective monetary policy actions will be. Yet there's another, overlooked, driver: corporate market power.

New IMF staff research has found ever larger and more powerful companies are making monetary policy a less potent tool for managing the economy in advanced economies, all else equal.

The argument is that, in effect, monetary policy is premised on the idea that all companies are small enough to be subject to market pressures, and that interest rate policies can impose changes on markets that will, because of those market pressures, be transmitted into both corporate and personal behaviour.

However, the assumptions does not hold true, they suggest, when there are companies of exceptional size. As they note:

Our study finds that firms with greater market power respond less to monetary policy actions, possibly because of their bigger profits. Larger profits make these firms less sensitive to changes in external financing conditions, such as those triggered by central banks' decisions. For example, as of March 2021, Apple had over $200 billion in cash and investment in marketable securities, while Alphabet had over $150 billion. Firms with such large cash cushions can decide on investment and other projects without having to worry about how easily they could tap other funding sources.

They added:

Specifically, using data for the United States and a panel of 14 advanced economies, we find that high-markup firms respond a lot less to a monetary policy shock–an unexpected change in the policy rate–than the average firm in the economy. For example, in the US, a 100 basis point increase in the policy rate causes a low-markup firm to cut sales by about 2 percent after four quarters, while a high-markup firm barely reduces its sales. Results for the panel of advanced countries are qualitatively similar.

Note the comment on profits: they suggest that these companies not only control their own supplies of capital, they also note that they appear able to control their own profit margins, which have been rising significantly over time. This is monopoly power in play.

A while ago I suggested to colleagues that when we were looking at large corporations we should drop the idea that they are microeconomic entities and instead assume that they might be macroeconomic entities instead, since they seem to be in charge of their own economic policies. This IMF finding supports that view. These entities are not subject to market constraints. They are not even in the market, as such. They do, instead, run their own economies that co-exist with those of countries but are at least in part removed from them.

And that is why campaigns to tackle monopolist abuse are now of special significance.