1. Populism, Economic Policies and Central Banking: an Overview

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There seems to be general agreement that "populism" has been on the rise over the past decade, and that it has implications for election outcomes and economic policies. Against this background, SUERF and the BAFFI CAREFIN Centre at Bocconi University brought together a group of experts for a one-day conference in Milano on 8 November 2019. The starting point for the project were ***three groups of questions:***

- *First,* ***what is "economic populism"?*** *Is it actually a new phenomenon? Is it confined to specific political camps? How would it be classified in more conventional economic categories?*
- *Second, what are the* ***sources of the rise in populism****?* ***Can economic policies contribute to a rise or decline of the current rise of populism****?*
- *Third,* ***how could the rise of populism affect central banks****? Conversely, can independent central banks make a difference in helping prevent or moderate economic populism?*

This article synthesizes major insights from the conference, embedding them in a broader overview of populism's interactions with economic policies and central banking. Section 1.1 discusses what "economic populism" might mean, and proposes a comprehensive definition. Section 1.2 offers some economic lines of reasoning for the rise of populism. Section 1.3 summarizes some ways how economic policies may counter populism. Section 1.4 explores how populism and central banking may affect each other. Section 1.5 summarizes and concludes.

1.1. What is economic populism?

There seems to be general agreement that the last decade in Europe and the US was characterized by the spreading of "**populism**". The broader phenomenon of populism has been analysed in detail in social sciences, political sciences, sociology, history and even psychology. The definitions and the historical overview provided e.g. in the German and English versions of Wikipedia already illustrate the diversity of approaches to analysis and connotations associated with the term

[1] OeNB and SUERF, Bocconi University and SUERF, respectively. The contributions in this book were all prepared prior to the COVID-19 crisis. If anything, it would appear that the challenges created by this crisis will exacerbate populist pressures and their impact on economic policies and central banks.

"populism". For the sake of space, we do not develop the broader aspects of populism here. We just note that populism is by no means a new phenomenon and has many faces. What are takeaways with regard to a definition of "**economic populism**"?

Let us start with a somewhat vague and cynical description of the term populism as a "generalised, pejorative term of abuse applied to **any political party of the (extreme) right, or left, that does not share the main economic tenets of the liberal, central establishment**" (see Goodhart and Lastra, 2018). In this reading, economic populism would be more or less equated with "**heterodox**" economic thinking, as long as it were meant by the extreme right or left to appeal to the masses. As this definition obviously lacks precision, the authors then narrow the definition down to "involving a major disagreement with the central liberal tenet that allowing the free movement of labour, capital and goods and services between nations would be both generally beneficial and desirable in almost all circumstances… [Thus,] a **populist want[s] to restrict the movements of people, capital, and goods and services between states**." We will come back to this aspect further down, when discussing populism's attitude towards globalisation.

A second defining element of populism which also extends into the economic sphere and is also mentioned by the above authors is **populists' aversion to checks and balances** (Spilimbergo, 2019) and **to institutional constraints on the political executive's power** (Rodrik, 2018), notably from autonomous institutions (Rovira Kaltwasser, 2018):

- A well-known example of such a constraint is **central bank independence**: by taking away from politicians decision power over discretionary monetary policy, the short-term gains from "printing money" in excessive quantities at the cost of future, socially detrimental higher inflation are no longer available as a policy option. In this sense, central bank independence and the focus of the central bank's mandate on the (primary) pursuit of price stability can be regarded as an "anti-populist economic institution" by a "monetary veto player" (Masciandaro and Passarelli, 2019). In other words, "populists dislike monetary dominance" (Edwards, 2019a). We will deal with this issue in more detail in Section 1.4.
- A second widely studied field of economic populism are **unsustainable expansionary fiscal policies**, notably in **Latin America.** As early as 1991, Dornbusch and Edwards studied "The Macroeconomics of Populism in Latin America" in an NBER volume. The unsustainable fiscal expansions of Latin American economic populism were often financed by the respective central bank. For this reason, Edwards (2019b) finds direct parallels of Latin American economic populist economic policies and **Modern Monetary Theory.**

- A third big area of constraints on economic policies is **economic and financial globalisation**, and the institutions created to pursue and protect it. Trade liberalisation erodes national policy makers' and pressure groups' leeway to preserve rents in goods and labor markets. Financial globalisation does the same for financial services and capital markets. The free movement of labor exposes national workers, and national social security systems and social policies, to competition from foreign workers and other countries' social systems. Against this background, it is not surprising that economic populism often involves protectionist policies (for a recent overview of **protectionism** see e.g. Gnan and Kronberger (2018). An area which drew particular attention in Europe in recent years is foreign investor protection. For instance, the independent arbitration courts, meant to protect foreign investors from protectionist national host-country actions, were among the buzzwords which caused fierce opposition in Europe against, and led to the failure of, TTIP (Transatlantic Trade and Investment Partnership – for an overview of the arguments prior to the abandonment of TTIP by the EU see Gnan and Kronberger (2016). The global retreat of multilateral trade liberalisation and the US administration's retreat of support for e.g. the WTO (World Trade Organisation) can be viewed as expressions of **anti-gobalist economic populism**.
- Finally, many populists' anti-EU stance can be explained with the fact that **EU membership** indeed – and intentionally – constrains national policy makers' leeway in many fields. The **EU Single Market** is a far-reaching form of regional liberalisation of trade, services, capital and workers' movement and is thus associated by populists with all the effects and constraints from globalisation more broadly. The EU's **fiscal sustainability rules** and **competition policy** are further elements of supranational constraints limiting national policy makers' leeway. For an overview of the debates associated with Brexit see e.g. Gnan and Kronberger (2019).

Because of the attacks on institutions they regard as constraining, one major **source of long-term damage from populism** can be damage **to the institutions governing democratic market economies**. This can apply to the rule of law in general, the protection of property rights, state institutions standing for trust, expertise and stability such as central banks, stable state money, institutions that safeguard international cooperation and coordination (e.g. UN, IMF, World Bank) as well as open economic exchange (such as the WTO – World Trade Organisation), or rules that were created to safeguard the long-term sustainability of public finances (e.g. the EU's fiscal rules).

The general literature on populism points out that **populism cannot be pinned down to specific ideologies or political camps**. Populist methods and approaches can be attached to both left and right-wing politics. The same is true in the economic field.

- To illustrate the ideological flexibility of populism, let's first look at Latin American "**left-wing populism**". In broader economic terms, its elements can be associated with a specific approach to **Keynesianism**, in the sense that short-term gains in terms of growth, employment, and social well-being are given preference over the sustainability of public finances or monetary stability. Similarly, recent populist movements in Mediterranean European countries such as Syriza ("Coalitation of the Radical Left") in Greece, Podemos ("We Can") in Spain, the "Gilets Jaunes" in France, or the Five Star Movement in Italy, but also more established parties at the far-out left end of the political spectrum, such as "Die Linke" in Germany, can be associated with left-wing economic populist narratives. Mascandaro's and Passarelli's (2019) definition of populism as comprising two key elements, namely (1) the claim to protect the people from the elite (promise of redistribution) and (2) populism's emphasis on expanding aggregate demand at the cost of future outcomes (short-termism) seems to correspond to left-wing populism.
- **Right-wing populism**, on the other hand, is harder to grasp. Often, it combines elements of (domestic) **economic liberalism** with some measures of social policy, to the extent this is considered to enhance electoral support, as long as it fits the respective parties' other political objectives and narratives, such as anti-immigration policies. But there is no clear general pattern. Lubin (2019) argues that right-wing populist leaders are not necessarily given to irresponsible macroeconomic policies; to substantiate this view, he quotes Poland and Hungary as examples of economically successful populist governments. What distinguishes them from Latin American economic populism is that they seek national self-reliance. This encourages them to avoid dependence on foreign capital, which in turn requires fiscal discipline. On the other hand, the US Trump Administration's economic policy mix combines late-cycle fiscal stimulus with protectionist trade policies. These are combined with an anti-reformist approach to structural change, notably in the energy sector. Thus, overall, these policies can be summed up to focus on short-term domestic advantages at the cost of long-term global benefits.

It is interesting in this context to come back to populism's aversion against globalisation. In fact, both left and right-wing populism **share anti-globalist economic narratives**, but for different reasons. Some authors (see e.g. Morelli, 2019 and the references quoted there) are even arguing that the cleavage between nationalism versus globalism is coming to dominate the political discussion, instead of the traditional left-right discourse of the past.

- **Left-wing populists** resent the power of multinational firms, regard globalisation and free trade as facilitating social dumping and the exploitation of legal arbitrage in the fields of workers' and environmental protection. For them, globalisation serves as a pretence to cut wages, social standards, corporate and wealth taxes also domestically. Global financial flows and globally operating financial firms are viewed as the oil lubricating the global neo-liberal system. "Market discipline" curtails national governments' capacity to pursue expansionary fiscal, notably social policies. Foreign capital inflows are in principle welcomed to the extent that they facilitate growth and the build-up of social welfare; however, left-wing anti-globalism is highly critical of foreign capital withdrawal once investor confidence erodes, and capital controls are regarded as an appropriate tool to stop outflows.
- **Right-wing, nationalist populists resent globalisation** because of immigration, with economic arguments just as an add-on to deeper cultural motivations. In the area of FDI, they resent foreign ownership and influence, notably but not only in strategically important industries (harbors and other infrastructure, IT and communications, banking). There is no hesitance to discriminate against foreign firms through various forms of regulatory discrimination or outright bans. Foreign ownership of real estate is regarded with suspicion and may be strictly limited or discriminated against. In terms of communication, nationalism, by emphasizing external threats, can also serve to distract workers and the poor from calling for more distribution and to attract voters who would otherwise turn to left-wing parties (Morelli, 2019).

While being aware of the many nuances involved and sketched above, in what follows we take as a **working definition for economic populism** "an economic doctrine, **distrustful of liberal mainstream economics and its institutions**, which is oriented towards **short-term (domestic) gains at the cost of long-term (global) benefits**, which **favours pressure groups** at the cost of minorities and other groups less relevant for **electoral outcomes**, and which generally does **not attach great importance to economic facts and analysis**". This definition implies an implicit value judgement, in the sense that populist economic policies are not desirable.

1.2. Sources of populism: economic lines of reasoning

The rise of populism has many causes. If one focuses on **economic** aspects, the **causes** are generally argued to include **technological change** which leaves behind **less educated** groups unable to adjust. Technology and education may also partly explain the increasing rift between old and young as well as urban cosmopolitan and more remote and rural areas. **Economic liberalisation and structural goods and labor market reforms** attack incumbents' rents and increase pressures on workers. **Globalisation** raises fears of competition from low-wage countries with low social and environmental standards. **Migration** raises fears of competition in the labour market and a squeeze on the social welfare state due to migration-induced increased burdens on the social system. The rise of **income and wealth inequality** diminishes the credibility of established political parties and their conventional policy measures of being willing and/or able to establish a promising economic perspective for important parts of the population. **Fiscal austerity**, forced upon many countries, notably in Europe, after the high costs to save ailing banking systems and to avoid the Great Recession, has reduced national governments' leeway to avoid social hardship. The **reform of the social welfare state**, including pension schemes and healthcare, while on the one hand imperative to secure its long-term sustainability in the face of ageing, at the same time leads to the perception of falling standards of living for low and even middle-income groups. At a psychological level, many of these causes may contribute to a heightened sense of **anxiety and insecurity**. The **financial crisis, the Great Recession and in Europe the sovereign debt crisis** exacerbated these developments.

One attempt to put several of these factors into a coherent theoretical framework is Morelli's (2019) "**fiscal theory of populism and paradox of endogenous nationalism**". According to this line of arguing, shrinking fiscal policy space prompts politicians to look for alternatives to cope with domestic needs. The combination of ageing societies, globalisation and technological progress depresses wages and increases demands on the social welfare state (pensions, unemployment benefits, etc.). At the same time, the same factors lead to the erosion of the domestic tax base, since capital largely evades taxation for lack of global tax coordination. Anti-globalists thus try to use protectionism to put a lid on a migration-induced increase in labor supply and cushion downward pressure on wages arising from global competition in goods and labor markets.

To understand populism, it seems crucial to understand **voters' emotions**. Altomonte, Gennaro and Passarelli (2019) explore how emotions may influence voting behaviour and how frustration and anger lead voters to express their emotions and to punish established politicians at the ballot, a phenomenon generally associated with the emergence of protest vote and populism. Individuals develop a **subjective sense of injustice by comparing themselves with others**. Identification with a relatively deprived group reinforces perceived injustice and furthers development of **group-based anger** and the **perception of a common threat**. As the group's bad relative position is associated with past policies, **group anger** turns **against the political system. Populists** manage better to **address voters at the emotional and moral levels** (community, loyalty, tradition) and **emphasise**

cultural differences with non-members of the group **over economic differences.** This approach helps to understand **why recent economic shocks, such as globalisation, technological progress and austerity, entail protest vote rather than calls for more distribution.** Disadvantaged voters derive emotional utility by expressing anger at the ballot, and trade this utility in against material utility from rational voting (see Altomonte, Gennaro and Passarelli, 2019).

While "populism" is hard to measure, **empirical studies** seem to **confirm a relationship between economic developments and the rise of populist parties.** Based on 184 elections in 29 European countries between 1986 and 2014, De Haan (2019) shows that higher economic growth reduces the share of populist parties, on both ends of the political spectrum. This relationship is non-linear, particularly for left-wing parties. Rising unemployment raises support particularly for left-wing populist parties. An increase in the number of asylums seekers reduces support for left and increases support for right-wing populists. An increase in the index of globalisation slightly raises support for populists.

1.3. How can economic policies counter populism?

Our working definition of economic populism given in Section 1 implicitly implies that economic populism defined that way is not desirable. Thinking about the causes of populism, as was done in Section 2, naturally leads to the question **how to resist or counter populism.** Eichengreen (2018) quotes several historical examples, including Bismarck's social policies and Roosevelt's New Deal, of how the rise of **populism could be countered successfully through expansionary demand side and social policies.**

One obvious recipe to counter populism is to **reverse the forces that led to the rise of populism** in the first place. Many authors therefore call for a reduction in inequality through taxing the rich and a reinforcement of the social welfare state, a relaxation of fiscal austerity and the abandonment of "neo-liberalism". It is clear from Section 2 above that others might perceive these recipes as populist themselves. Furthermore, **several of the above potential sources of public anxiety and insecurity are irreversible and beyond the control of policy.** This is certainly true of **technological change.** What is more, technological change and global communication also entails that many aspects of globalisation including migration pressure become more urgent and might, if anything, intensify rather than be reversed.

Morelli (2019) proposes a different approach: He argues that reduced fiscal space combined with the lack of individual monetary policies in euro area countries has led to an economic **policy "straight jacket" perception,** which, combined with globalisation threats, has been the main driver of populism. This has led to the paradox that while policy challenges are increasingly global and national policy space is shrinking, the populist response is national, which in turn reduces the likelihood of effectiveness and success. An alternative to populism, which blocks labor inflow and tries to bolster domestic wages through protectionism, is thus to **regain fiscal space by implementing a global taxation of capital**. It is ironical, though, that Morelli's suggestion to achieve such a global capital tax by means of making countries' WTO (World Trade Organization) membership conditional on agreement to such a capital tax coincides with the WTO itself being seriously challenged and put into question by populists.

The above drivers of populism are often said to have led to "**reform fatigue**" and diminishing "**reform policy scope**", reducing politicians' leeway to secure public support for accepting short-term costs in favour of long-term gains and thus encouraging "populist" economic policies. It is, however, open for discussion to what extent policy scope is actually reduced or whether this argument is just **part of the rhetoric of economic populism**. The argument also neglects the **role of communication** of economic reform programs and the potential useful role of "**package deals**" through which losers from certain reforms are **compensated** in one form or another to buy into the reforms.

Finally, it should also be borne in mind that **(right-wing) populism can be economically quite successful**. As pointed out by Gerlach (2019), the populist governments in Poland and Hungary in the post-2012 era economically performed way better than the EU average.

1.4. How may populism and central banking interact?

Central banking has undergone major changes due to the financial, economic and sovereign debt crisis. Central banks were in many countries the major or even the only game in town to fight the financial crisis. Central banks employed powerful tools to save ailing financial institutions, promote a recovery of growth and inflation, and to ease fiscal policy's debt servicing burden through ultra-low interest rates, large-scale outright asset purchase programmes and commitment about the future policy course ("forward guidance"). In addition, many central banks were transferred additional tasks and functions, notably in the areas of micro and macroprudential surveillance. This should on the one hand have **supported their reputation** as useful and responsible institutions acting in the interest of citizens and in support of general economic and societal goals. Indeed, the transfer of additional responsibilities may reflect trust in central banks' expertise and integrity in assuming such tasks reliably and responsibly.

On the other hand, central banks are also coming under **increasing criticism.**

- *First*, they are seen by some as having **contributed to pre-crisis financial exuberance**, through excessively easy monetary policy, which ignored financial stability concerns.
- *Second,* while some criticize central banks, notably the Eurosystem, for having **acted rather late and timidly** to combat the crisis, others more recently criticize them for **keeping monetary policy too expansionary for too long.**
- *Third*, being in close interaction with the financial sector may lead to negative connotations, given the **loss of trust in finance** after the crisis. By some, central banks are criticized as **favouring the interests of the financial sector.** This assertion is particularly critical as central banks have after the global financial crisis been more heavily involved in banking supervision. To reduce risks of "**regulatory capture**" (besides other motivations such as breaking the sovereign-bank nexus), in the euro area the supervision of large, systemically important banks was centralized at the SSM (Single Supervisory Mechanism) within the ECB. But **banking and financial supervision is also "risky"** in the sense that bank failures are inherently hard to detect far in advance and always politically delicate to resolve, and the supervisor is always at risk of becoming a **political scapegoat**.
- *Fourth*, central banks' unconventional policies come along with larger **distributive effects** than pre-crisis standard tools.
- *Finally*, central banks' scientific approach to policy may turn into the perception of being **technocratic and remote from reality** amidst the **post-crisis scepticism against mainstream economics and the economics profession at large**. Such criticism may be invigorated by **failure to meet (self-imposed) inflation targets**, while **side effects** from an escalation of monetary easing become more wide-spread and visible: it may raise questions about the central bank's willingness to stick to its announced target; or it may raise doubts about the central bank's intellectual capacity to understand changes in the inflation process, and its flexibility to adjust its economic models and tools to a changing economic reality; or it may raise the perception that the central bank is **chasing the wrong target**, if the public and the body politic do not appreciate the costs of below target but positive consumer price inflation, while asset prices, in particular real estate prices, which are highly relevant for people and very present in the public discussion, surge.

Empirically, indeed central bank independence seems to have plateaued globally since the Global Financial Crisis (see Masciandoaro and Romelli, 2018), and central bank independence has increasingly come under discussion, as evidenced by a marked rise of press article on the topic since the onset of the global financial crisis and since 2018 (see Borio, 2019). Many of the above **challenges for central**

banks are in principle independent from "populism". However, some of them **may become more relevant and acute in populist political environments**. Drawing on our definition of economic populism above, there are several potential **channels**:

- *First*, central banks were created as **independent institutions** to pursue the medium to long term goal of price stability. Given **populisms' short-term focus**, interests are likely to clash. More notably, if populist policies entail unsustainable fiscal policies, this may also endanger price stability. The call for monetary financing and fiscal dominance is just a step away. The experience of Latin American populism is a case in point. But also the recent calls for **helicopter money**, the proposals of **Modern Monetary Theory** (see e.g. Weber, 2019) and its variations (see e.g. Bartsch, Boivin, Fischer and Hildebrand, 2019) imply an erosion of central bank independence, likely fiscal dominance, and the neglect of long-term considerations for short-term pressures (see e.g. Borio, 2019). In this sense, they could be qualified as economically populist in nature.

  How legally **independent central banks can actually threaten and shorten the survival of populist regimes** is investigated by Bodea, Garriga and Higashijima (2019). Based on a sample of 94 autocratic countries observed for the time-span between 1970 and 2012, they show empirically that dominant-party autocratic regimes are significantly more likely to callapse when they face constraints on fiscal spending due to formally independent central banks. The combination of collective decision-making within the dominant party imposes checks and balances on the autocratic leader, which make it more difficult for her to override central bank independence, and thus limits her fiscal spending to buy political support. The obvious question then why such regimes create or keep independent central banks in the first place is, first, in order to signal economic policy competence and reliability in order to gain foreign investors' competence, and to divert the blame for economic hardship. So, it is a combination of institutional mechanisms and incentives that yield this result.

- *Second*, central banks are mandated to act in the **interest of the economy as a whole**. While monetary policy always has **distributive implications** (impact on savers versus creditors, growth and employment etc.), these effects have become larger and attracted more attention with unconventional monetary policy. Masciandaro and Passarelli (2019) provide a theoretical framework to show how, with heterogeneous citizens (e.g. bond holders versus deposit holders), a macroeconomic shock can produce monetary policy preferences among the electorate and populist politicians, which are different from a socially optimal long-term orientation of monetary policy. Obviously, similar considerations would apply in the current economic environment of soaring stock and house prices in response to ultra-easy monetary policies, and the resulting widening wealth gap between stock and house owners and non-owners. While central banks do not tire to argue that overall – taking into account effects on growth, employment and income – ultra-easy monetary policies do not affect distribution negatively (see e.g. Lenza and Slacalek, 2018), the public perception may be different and unconventional and ultra-easy monetary policies may invite populist attacks on central banks.

In the **euro area**, this issue may be exacerbated. The ECB is committed to pursuing the mandate for the euro area as a whole, which implies that **monetary policy alone may not entirely fit national cyclical needs**. To take the aftermath of the GFC and sovereign debt crisis, while for some countries, the ECB's policy may be regarded as insufficiently expansionary and too slow, in other countries it may be seen as far too easy. Given populisms' national focus, this may create conflicts. Furthermore, the Eurosystem's large asset purchases may raise **fears of distributive effects between euro area countries** (be it through relative yield effects on sovereign and other bonds, be it through actual or perceived risks of financial loss or potential bailout costs). This was the main reason for the ECB Governing Council's decision to conduct the bulk of the Public Sector Purchase Programme through NCB balance sheets, with no sharing of income and risk for these assets.

- *Third*, **central banks' "scientific" approach to policy** is at odds to populisms' tendency to neglect facts and analysis. As Borio (2019) puts it: independent central banks "raise the bar" for politicians who wish to pursue unsound policies. Most central banks prepare and publish research and analyses clearly beyond the narrow realm of money and finance. They may even go one step further in encouraging policies oriented towards long-term goals such as sustainable growth and employment. Traditionally, such activity beyond central banks' narrow mandate has been termed "**moral suasion**". Central banks' **financial and economic education** activities may be seen from the angle of educating the electorate to becoming less likely the prey of promises which are economically unrealistic.
- *Fourth*, **central banks' inherently "globalist", "cosmopolitan" institutional nature and "elitist" scientific approach** may make them seem suspicious to nationalist politicians (see Rajan, 2018). The intellectual foundations that supported globalisation and open markets with limited government interference also favored the idea that governments should not interfere with money and that monetary policy should therefore be delegated to technocrats with a focused mandate of keeping the value of money stable. As the

value of an open multilateral global order is being questioned and attacked, the same may happen, with a lag, to central bank independence (see Borio, 2019). Similar to anti-globalisation movements, also the criticism of central bank independence and of the separation between monetary and fiscal policies may come both from the left and right-wing populism.

It is important, however, to recognize that the argument can also be used in the other direction: Being internationally closely integrated institutions, central banks can contribute to keeping countries governed by populist leaders involved in the international policy community (e.g. in various BIS fora, in the IMF, through the ESCB/Eurosystem) and, through moral suasion and fact-based analysis, resist forces working against an open multilateral global order. As pointed out above in the work of Bodea, Garriga and Higashijima (2019), whether an independent central bank can actually use its influence and voice successfully without losing independence altogether hinges on other accompanying institutional features and incentives prevailing in a given political and economic setting.

- *Finally*, populism often goes hand in hand with **less transparency and weaker checks and balances**; this makes transgressions into central banks' competences less likely to be detected by political opposition and the protection (notably by the judiciary) of legal central bank independence less reliable (Goodhart and Lastra, 2018).

Empirical studies confirm that pressure on central bank independence has increased worldwide over the past decade and that this is related to the rise of populism. A first approach is to study the **development of statutory central bank independence**. Agur (2019) combines the World Bank's Database on Political Institutions and the Garriga (2016) index of central bank independence to study the relationship between one important aspect of populism, namely nationalism, and central bank independence. He finds, first, that central bank independence has generally strongly increased during the 1990s; however, from there on, it stagnated on average in countries with a nationalist chief executive, while it increased further on average up until up until 2010 in other countries. A panel regression of 113 developing countries, covering the period 1975 to 2012, confirms, second, that nationalism is indeed associated with lower central bank independence at the individual country level. This result holds true when controlling for other institutional variables. Third, the authors also confirm that institutional quality in general matters for central bank independence, implying that broader institutional developments often associated with populism, such a weakening of the rule of law, lower government efficiency etc. are also associated with weaker central bank independence.

Another approach is to consider measures of **actual** (as distinct from legal, statutory) **central bank independence**. Given the importance of credibility, reputation and communication in central banking, already pressure without actual legislative changes may impair the effectiveness of central banks' policies. Such pressure may take the form of calls to ease (in most cases) or to tighten (rare), threats to replace a central banker, as well as actual or potential changes to central bank legislation. Constructing a panel dataset on political pressure of 118 central banks worldwide since 2010, based on country reports from the Economist Intelligence Unit and Business Monitor International, Binder (2019) finds that political pressure on central banks has been widespread since 2010 and increased sharply in 2012 and most notably since 2018. Mostly, pressure was to ease; in 15% of cases it involved actual or threatened replacement of central bankers. Importantly, the study finds that pressure was more prevalent in less democratic countries and when there was less electoral competition, in countries with weaker checks and balances and in countries with nationalist or populist leaders. A possible qualification against the approach of interpreting pressures on central banks as being signs of loss of independence is that tensions between governments and central banks can also be seen as a sign that central bank independence is actually fulfilling its intended role of erecting obstacles against unsound policies (Borio, 2019).

In recent years in developed economies, **actual legislative changes to central bank laws remain the exception**. Binder (2019) found that only in 4% of cases studied by her, pressure on central banks involved actual or potential changes to central bank legislation. However, in 2018, the Reserve Bank of New Zealand's mandate was changed to a dual mandate. In addition, the newly installed central bank committee in charge of monetary policy decisions includes a Treasury representative. As populism remains strong and pressures on central banks increase, Binder (2019) speculates that "legal changes to central banks could also become more prevalent".

1.5. SUMMARY AND CONCLUSIONS

Populism is not just a recent phenomenon but has **long history**; while populist governments share certain common features, there are also large differences in the details. Likewise, **economic populism can take many forms**. Our brief survey of relevant recent literature has yielded a comprehensive **definition** comprising five features: (1) short-termism, (2) a distrust of liberal mainstream economics and its institutions, (3) nationalism and distrust of openness and globalisation; (4) an extreme form of electoral focus, with a resulting neglect for minorities, and (5) a neglect of facts and analysis. There is the general notion that economic populism is undesirable. The **causes of populism** are manifold and are generally thought to include factors which create a sense of being disadvantaged, left behind and living under uncertainty for a sizable part of the population; highly competitive economies, technological progress, globalisation, immigration, fiscal austerity, an erosion of social safety nets and inequality are seen as such factors, the global financial crisis and its consequences seems to have contributed to the recent rise in populism in Europe and the US. **Perceptions** of these factors are at least as important as actual developments; actual or perceived **relative deprivation** plays a key role; **individual and group emotions** are crucial to understand **protest voting** and the mechanisms which lead to support for populist parties and leaders.

Populism cannot be pinned down to specific ideologies; some argue that the traditional cleavage between left and right is being replaced by globalism versus nationalism. But it is noteworthy that both left and right wing populists share **anti-globalism**, though for different reasons and with different narratives. Advice against populism usually suggests to counteract or reverse some of these factors thought to cause populism. Depending on the political origin of the advice and the emphasised supposed causes, advice focuses either on overcoming "neo-liberalism", ending fiscal austerity, reducing inequality and bolstering social safety nets; or on restrictions openness in the quest to achieve "protection" of the domestic electorate. Obviously, both sets of **policy recommendations may be categorized as populist by advocates of the opposing political camp**. A separation between "political" and "economic" populism, as is e.g. done by Rodrik, 2018 ignores that **politics and economics are inextricably linked**. Rejecting political populism while approving economic populism misses the point. Regarding **economic effects of populism**, the economic literature generally finds that left-wing Latin-American populism in the long run led to economic failure. The assessment of recent right-wing nationalist economic populism in Europe and the US is less straightforward; some CESEE countries have fared well with it so far; but the effects from dis-integrationist and protectionist policies (US trade war, Brexit) are already entailing clear negative consequences, which are expected to unfold further as time passes.

Populisms' aversion against checks and balances and institutions not under the government's direct control creates an inherent **tension with independent central banks'** mainstream, liberal, globalist, fact and science-based economic tenet, with their primary focus on a long-term goal price stability. The populism-induced tension hits central banks at a time of post-crisis fundamental challenges they already need to cope with. It remains to be seen whether the **increasing incidence of attempts to interfere with central banks' policies and leaders** will, with a lag, also be reflected in more wide-spread changes in central bank laws. Indeed, it is the **damage inflicted upon institutions** which have been at the heart of democratic open market economies over past decades which may have the most damaging impact on economic development in the long run.

The **appropriate response to populism** is **not** to **turn the wheel backwards**. Instead, it must actively address current challenges such as climate change, global population increase and embrace technological progress and innovation to allow a transformation of the European and global economic and financial system in a way which is sustainable and allows large parts of the population to participate in and benefit from it in a fair manner. In doing so, political leaders should take **voters' perceptions and emotions seriously and address them**.

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