Comments of “Global Impact of US and Euro Area Unconventional Monetary Policies: A Comparison”

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Discussion on Global Impact of US and Euro Area Unconventional Monetary Policies: A Comparison

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Paper tackles very relevant issue, spillovers from US and Euro Area Unconventional Monetary Policies (UMP)

Need for coordination? Authors argue there are different views:

- UMP address domestic issues, spillovers are unintended consequences. Not much room for improvement if individual players implement policies to achieve domestic macro stability (Obstfeld-Rogoff, 2002)

- Spillovers changed cost-benefit analysis, especially if there are deviations from rules-based policies (Taylor 2013). Spillovers may trigger macro instability in recipient economies, depending on their cyclical position

GVECM to analyze domestic and international impact of UMP
Focus on impact of monetary policy shocks (MPS)

Ok, but keep in mind that spillovers from MPS are mostly unintended consequences of unintended shocks.

Are the views in the previous slide so different?

Even if obvious to state, identification is critical!

A significant part of UMP is an endogenous response to real shocks.

IMF (2014 and 2015 Spillover Reports): underlying drivers matter, positive real shocks in AEs have positive spillovers despite ensuing tighter monetary conditions.

Conversely, easing UMP dampens the impact of spillovers from negative real shocks in advanced economies.
Overview of Main Comments

✓ Large estimation uncertainty, statistical significance

✓ Some results need more discussion, contrast with results in the literature

Shock Identification

✓ Shadow short term interest: unobservable variable to capture MPS
✓ Identification strategy assumes US dominance
✓ Are these sensible choices?

Some results → Shadow rate → Identification assumptions → Alternative Approach → Conclusions
In contrast with these results, some papers point to interdependence between the US and the euro area; especially after EMU.

Ehrmann and Fratzscher 2002, 2003 and 2005; Ehrmann, Fratzscher and Rigobon 2011; Scotti 2011; and Osorio-Buitron and Vesperoni 2015
Why ECB (easing) MPS reduce stock prices and trigger depreciations pressures in other countries?

Cumulative impulse responses to US and Euro area (loosening) monetary policy shock

Equity price inflation

Foreign exchange pressure

Is this intuitive? Previous literature suggests that euro area easing UMP boosted equity prices and triggered euro depreciation

- Fratzscher and others 2014; Georgiadis and Grab 2015
Is the shadow short term rate a good variable to identify MPS?

- UMP operate through central banks’ balance sheets, whole yield curve gives information about monetary stance
- Does shadow rate capture adjustments in the term premium well?

A critical asymmetry is assumed—the US is not affected by foreign financial variables, while the euro area is affected by them, in the same way that Emerging Markets are affected.

- Other work suggest it may not be a safe to assume no spillovers EA → US
- Is the US shock overestimated?
- If this is the case, assumption is likely driving results on spillovers, notably the relative mild spillovers from euro area shocks

- It is critical to identify the source country of the shock
Shadow Short Term Interest Rate

- Have Fed UMP given place to such a volatile monetary policy stance?
- Has the MEP triggered such a tightening of the monetary policy stance?
  Maybe not, shadow rate captures impact of treasury bills sales, but not of long term debt purchases—see term premium?
- Sample is missing the most active ECB policies

Out of sample: Mid-2009 to Mid-2014
In the 2015 Spillover Report, we jointly identify country-specific real and money shocks in the US and the euro area, and associated spillovers.

- Use information on stock prices and long term bond yields
- Two-country VAR with sign restrictions

**US: 10 Year Yield decomposition**
(cumulative change; percent)

**EA: 10 Year Yield decomposition**
(cumulative change; percent)

EA spillovers to US
Monetary Shocks: Spillovers to EEs and Non-systemic AEs

**Bond Yields**
(basis points)

- **US**
- **US 90% confidence interval**

**USD-EUR EER**
(percent; + = depreciation)

- **EA**
- **EA 90% confidence interval**

**Industrial Production**
(percent)

**Net Capital Inflows**
(percent of GDP)

Source: IMF staff calculations.
Conclusions

- Paper looks into a very relevant issue, a great effort, but be mindful of how contrasting are different views on UMP

- Large estimation uncertainty (statistical significance)—need to address this
- Some results do not look intuitive and contrast with previous work—more discussion needed

- Would be useful to revisit identification:
  - Think about the variable to capture monetary policy stance
  - Identification approach:
    - Lower bound: check correlation between shocks
    - More ambitious: ‘symmetric’ approach for identification, no US dominance
    - First best: estimate shocks jointly to identify source