Discussion of "Risk Premium Shocks and the Zero Bound on Nominal Interest"

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- Can we make zero bind in a quantitative DSGE model?
  - Literature largely qualitative, liquidity trap "assumed"
- Useful to learn about
  - Model: new shocks, new frictions
  - World: locate source of problems
  - Desirable policy response

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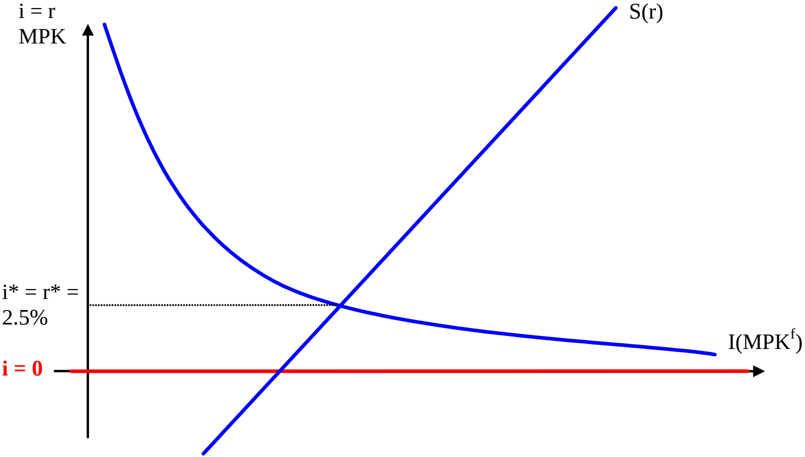
- How about the other variables?
- Unconditional analysis must also account for dynamics at zero

Some Intuition



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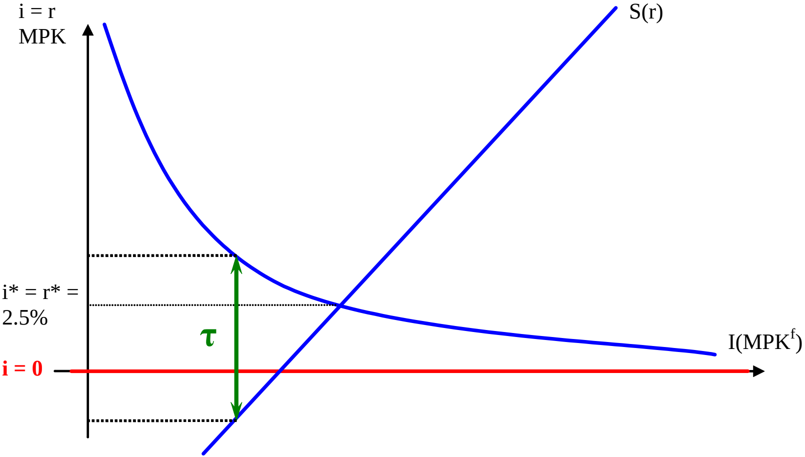

An Alternative Strategy

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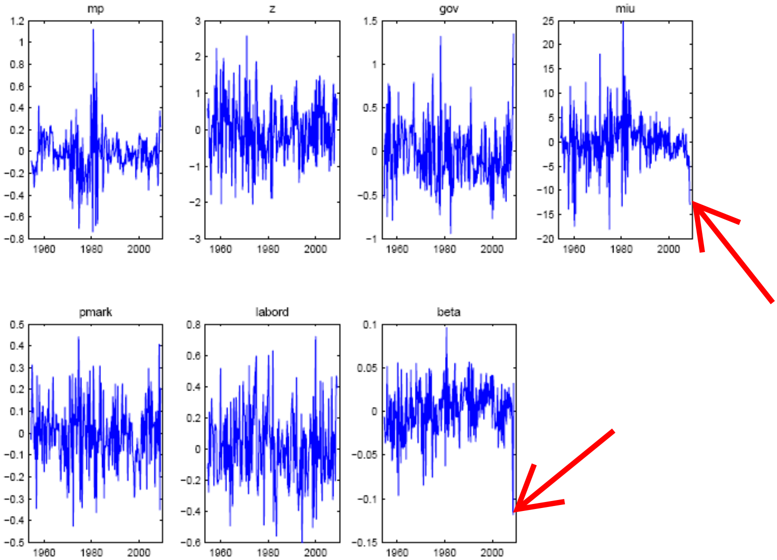
  - Procedure picks shocks to reproduce observables *exactly*
- What shocks are crucial for what variables?
  - -5.5% GDP might be harder than FedFunds at 0.18%
- How large are the shocks? Compared to
  - independent evidence (prior)
  - posterior distribution in "normal" times
- Measures of fit excluding selected shocks

Alternative Strategy: Implementation (JPT)



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  - Is this always feasible with zero bound binding?
- Zero bound a bizarro world, policies matter a lot
- With appropriate policies, zero bound no big deal
  - Ignore the non linearity and use alternative strategy
- Zero bound can become a nightmare with "wrong" policies
  - Policies at least as important as non linearity, need careful modelling

Conclusion

- Positive analysis of the zero bound is hard!
  - Policies are crucial, but little historical evidence
- If question is: how did we get to 2008Q4 (when FedFunds first ≈ 0)?
  - Ignoring non linearity might be OK, follow alternative strategy
- If question is: what happens from here?
  - Non-linearity important, but so are policies
- Two questions better addressed separetly