Discussion of:

Mending the link: heterogeneous bank lending and monetary policy pass-through

by Altavilla, Canova and Ciccarelli

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Unconventional monetary policy: effectiveness and risks

Banca d’Italia, October 2016
Very interesting paper
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I like the paper.

Food for thought.
The paper

- How does expansionary monetary policy affect lending rates and lending margins? The pass-through (PT).
- Rich dataset covering 260 banks in Europe
- Focus on the Great Recession and its aftermath
- First part on conventional measures (↓ in the policy rate)
- Second part on unconventional measures (credit easing (CE) + quantitative easing (QE)).
Discussion

- Results

- The empirical model
  - Conventional
  - Unconventional

- Few comments/questions
  - Policy shocks with CE/QE
  - Non-linearities
Effects on the pass-through, PT

Conventional
- Stressed vs non-stressed countries is irrelevant
- Bank balance sheet relevant (low PT for 1. low capital, 2. exposed to domestic sovereign debt)

Unconventional
- ↓ cross-sectional dispersion of lending rates (uncertainty?)
- Larger pass-through than conventional measures
- Lending rates ↓ for banks 1. low capital 2. from stressed countries, 3. high share of non-performing loans, 4. high uptakes in the CE operations.

Unconventional on lending rates to households
- ↓ of lending margins (lending - deposit) for: 1. low capital, 2. exposed to domestic sovereign debt, 3. high share of non-performing loans.
- This made profitability lower. Hampers banks’ profitability.
The model: conventional mon. policy 2007-14

VAR model for $X_{ij}^t =$ \begin{bmatrix} \ y_{i,t} \\ \ x_{j,t} \\ \ z_t \end{bmatrix} \\
bank i \ \ country j \ \ EONIA

$z_t$: EONIA

$x_{j,t}$: 10- yrs sovereign bond, E(default prob. non-fin. corp.), unempl. rate

$y_{i,t}$: lending rate, deposit rate, bond yield

\begin{align*}
  z_t &= \text{lags} + v_t \\
  x_{j,t} &= C_j z_t + \text{lags} + \varepsilon_{j,t} \\
  y_{i,t} &= A_i x_{j,t} + B_i z_t + \text{lags} + u_{i,t}
\end{align*}

$v_t$: conventional monetary policy shock (temporary or persistent shock?)

VAR bank by bank, then slicing the distribution, conditional on few criteria.
The model: unconventional mon. policy 2014-15

Event-study approach:

\[ \Delta Y_t = aD_t + bD_{t-1} + c(\text{macro news})_t + \varepsilon_t \]  \hspace{1cm} (1)

3 lhs variables. EONIA: \( z_t \); sovereign yields: \( x_{1,t} \); bond yields: \( y_{3,t} \).

\( D_t \): dummy variable. \( D_t = 1 \) in the dates of the CE/QE announcements

3 forecasts: path under the assumption that the announcements were the only thing happening.

\[ E(y_{1i,t+h}^1|\Omega_t, z_{t+h}^*, x_{1,t+h}^*, y_{3,t+h}^*) = \alpha z_{t+h}^* + \beta x_{1,t+h}^* + \gamma y_{3,t+h}^* \]  \hspace{1cm} (I think...)

\[ E(y_{1i,t+h}^1|\Omega_t, z_{t+h}, x_{1,t+h}, y_{3,t+h}) \): VAR forecast
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\[ E(y_{1i,t+h}|\Omega_t, z_{t+h}, x_{1,t+h}, y_{3,t+h}): \text{VAR forecast} \]

Impulse responses of lending rates for bank \( i \):

\[ u_{i,t+h} = E(y_{1i,t+h}|\Omega_t, z_{t+h}, x_{1,t+h}, y_{3,t+h}) - E(y_{1i,t+h}|\Omega_t, z_{t+h}, x_{1,t+h}, y_{3,t+h}) \]

Slicing the distribution, conditional on few criteria.
Comments: policy shocks

- Monetary policy shocks are deviations from the policy rule (CEE).

\[ i_t = f(\Omega_{t-1}) + \epsilon_t \]

- This means that displacements of expectations are identifying policy shocks:

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- But what if the policy rule is changing?

- What if markets expected some changes in the policy rule?

- Behavior of yields before the announcements?
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- “News shock/foresight” environment. Agents know about the shock in advance: \( y_t = \epsilon_{t-1} \). Agents receive a signal on the shock: \( s_t = \epsilon_t + v_t \)

- Are \( \Delta \) in expectations really identifying exogenous policy shocks?

- Isn’t there a difference between: 1. the effect of the announcement/variations in expectations; 3. the effect of policy shocks?
Comments: policy shocks

If I wasn’t the discussant, I would do what you did!!
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2) Conditioning on the business cycle/credit conditions.

- Balke, 2000 and Ciccarelli, Maddaloni and Peydro, 2013: monetary shock has larger effect in tight credit conditions.

- If CB wants monetary tightenings to have an effect, it needs bad (small, illiquid and poorly capitalized) banks, that cannot shield increases in i.

- If CB wants monetary expansions to have an effect, it needs good banks, that can easily pass-through.

- US: contractionary shocks have stronger effects than expansionary shocks (see figure).

- As far as I know, no study on this. Interesting to relate this to bank balance sheet/credit channel asymmetries.
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5) Conditioning on uncertainty. Does it generate variations in the PT?

6) A source of non-linearity: downward rigidity of lending and deposit rates. Should them be negative? Strong non-linear effect at the ZLB?

7) What about quantities? Weak demand of loans in Europe? Does this come from banks’ supply or from demand? Are lending rates low enough?