Discussion of "Money and Capital in a Persistent Liquidity Trap" by Bachetta, Benhima and Kalantzis

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Summary of the paper

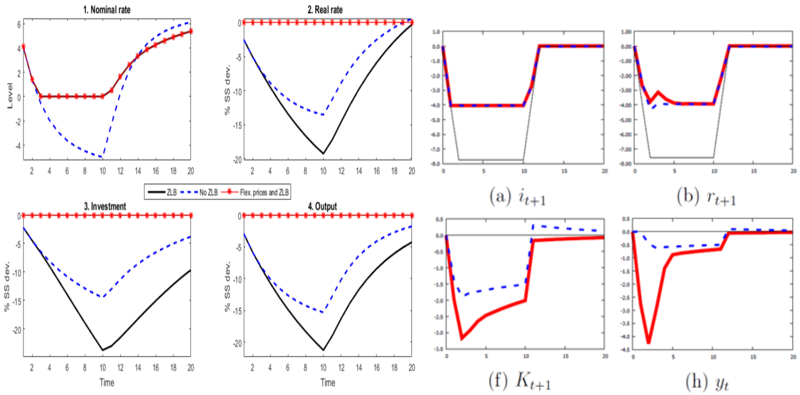
The paper takes a '"long-run"' approach to show the negative relationship between money and physical capital in a persistent liquidity trap.

- Monetary model with flexible prices and asset scarcity
- Leveraged investors finance investment
- Deleveraging shock makes assets scarce pushing down the interest rate
- at the ZLB savers may stop lending and switch to cash (*crowding-out effect of money*)
- This leads to lower capital accumulation and output

$\Longrightarrow$ **money is not neutral in the long-run**

Two worlds compared

Figure: NK model vs Monetary model



Policy implications

Some unpleasant monetarist implications for central bankers in the long run...

1. QE: aggravates asset scarcity and deepens liquidity trap
2. NIRP: effective in contrasting the effects of deleveraging shock, but does not solve asset scarcity problem
3. Helicopter money: it works (in a non-Ricardian setting)
4. Credit easing and increase in gvt bonds: effective as they reduce asset scarcity issue

My two cents...

Three challenges to the validity of the claims:

1. results hold in a non-Ricardian framework but not in a Ricardian one (Wallace neutrality)
2. what about additional transmission channels of unconventional policy measures?
   → portfolio rebalancing works the opposite way (from gvt bonds to risky assets)
3. empirical evidence on money demand during ZLB episodes is inconclusive (at best)
   → stable money demand during long ZLB episodes (Dreger, Gerdesmeier and Roffia, 2016 and Barigozzi and Conti, 2018)

General appraisal of the paper

- Thought-provoking paper about long term effects of unconventional policies
- New mechanism leading to the paradox of thrift
- Interesting path for future empirical research
- Definitely a recommended reading for policymakers!

THANK YOU!