

Managing Monetary Policy Normalization

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The paper in a slide

- The paper introduces a novel transmission mechanism based on a liquidity channel, giving central banks an additional tool via balance sheet (BS) operations.
- ⇒ BS policies affect AD even outside the ZLB.
- ⇒ The size of the BS also reflects fiscal and liquidity-management objectives.
- ⇒ Optimal policy requires an expansion of reserves once the ZLB is reached, with QT beginning before interest-rate liftoff, in response to a liquidity-trap shock.

The liquidity channel

- Banks hold reserves and Treasury bills, which they use to back household deposits.
- The central bank sets the interest rate on reserves, which influences the deposit rate.
- ⇒ Deposits are the main liquid asset for households and embed a liquidity premium.
- ⇒ The liquidity premium creates a disconnect between the policy rate and the return on illiquid assets that drives AD.
- ⇒ Changes in reserves are amplified by banks' deposit creation, generating a liquidity multiplier:

public liquidity → deposits → liquidity premium → return on illiquid assets → AD

Comment 1: Visualizing the mechanism

- The liquidity channel is the key innovation of the paper.
- IRFs would help make the mechanism clearer.
- In particular, it would be useful to trace the responses of:
 - Deposits and liquidity premium;
 - The return on illiquid assets versus the policy rate;
 - Output, inflation, and the natural rate.
- IRFs would also help illustrate how the standard Neo-Wicksellian model is nested as a special case.

Comment 2: Liquidity shocks

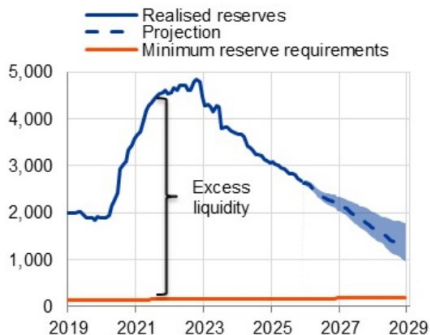
- Liquidity shocks – $\xi_t, \xi_{q,t}, \hat{\rho}_{\gamma,t}$ – are potentially very useful to:
 - Capture disruptions in safe-asset supply;
 - Help interpret episodes of financial stress;
 - Proxy shifts in liquidity demand or uncertainty.
- But the three shocks have isomorphic effects on the appropriately-defined natural real rate.
- Can they be separately identified? Money-market spreads, deposit, reserve, and bank balance-sheet variables could help.

Comment 3: Normative analysis

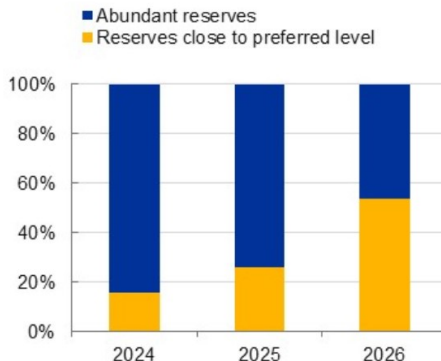
- The paper has sharp implications for optimal policy in a liquidity trap.
 - Normative implications on the role of BS policy outside the liquidity trap would be interesting.
 - A related issue is implementation:
 - Reserves and Treasury bills are perfect substitutes in the model;
 - In practice, they differ in holders, remuneration/yields, and market functioning.
- ⇒ These differences may be relevant for the liquidity multiplier and for the timing of QT.

Reserves management and preferences in practice

(a) Projected path of reserves
(EUR billions)



(b) Share of banks close to their preferred
reserve level
(percentage of banking assets)



Source: Iskaki et al., How banks are adjusting to declining reserves, The ECB Blog, 2 April 2026 and Eurosystem Bank Treasurer Survey.

Conclusion

- Very interesting paper for both central banking and academia, with lots of food for thought.
- Many policy-relevant directions for future research, including macroprudential policy and liquidity management in “normal” times.