Discussion of "Negative lower bound as a policy instrument" by Lemke, Rostagno and Vlassopoulos

ECB (2016-12-19)

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Intro

- Preliminary work raises lot's of interesting questions

- Paper covers two main points
  - Risk-premium affected by LB – "recharge" if LB decreased
  - Banking system interacts with LB, due to deposit floor

- I will
  - Provide a few comments
  - Briefly discuss the Swedish experience with negative rates

My comments

- Importance of expectations

- Risk-premium "recharge"

- Degree of competition in banking markets important

- Policy alternatives: removing LB

Importance of expectations

- Model is relatively backward-looking

- Well known "forward-guidance puzzle"

- But perhaps useful to consider more standard model coupled with e.g. Euler equation discounting

- Especially for comparison with forward guidance

Risk-premium recharge

- Idea: If shadow-rate << LB, then i=LB and var(i) small

- Moving LB downward should increase var(i)

- But sequencing?
  - First cut rates all you can
  - Then use communication and forward guidance to lower path
  - Then do QE (cf Brunnermeier and Koby, 2016)
  - Currently: moving LB, first lower rate -> no recharge?

Risk-premium recharge?

$$y_t^n = \frac{1}{n} E_t \sum_1^n i_{t+j} + RP_t^n$$

- Bernanke: QE lowers RP, but might raise $E_t i_{t+j}$

- Hence: can't evaluate QE only by studying Δy_t^n

$$RP_t^n = \lambda_t \sigma_t^2$$

- If λ_t <0 an increase in σ_t^2 will *lower* yields

$$RP_t^n = (\gamma_t - h_t)\sigma_t^2$$
$$RP_t^n = \gamma_t \sigma_t^2 - h_t$$

- Think about more structure for risk-premium

Importance of competition

- If perfect competition in banking sector: marginal cost of loan equals price -> large effect of reducing LB

- If little competition: average pricing…

Policy alternatives

- Remove cash, Rogoff

- Exchangerate between cash/reserves, Kimball, Goodfriend

- Helicopter drops, Buiters

Swedish experience

- Negative reporate since Feb 2015

- Now: reporate -0.50 applies to entire structural surplus

- Overall: Worked roughly as expected

- Some problems (FRN, IT-system)

- But passthrough is incomplete

Passthrough, but incomplete
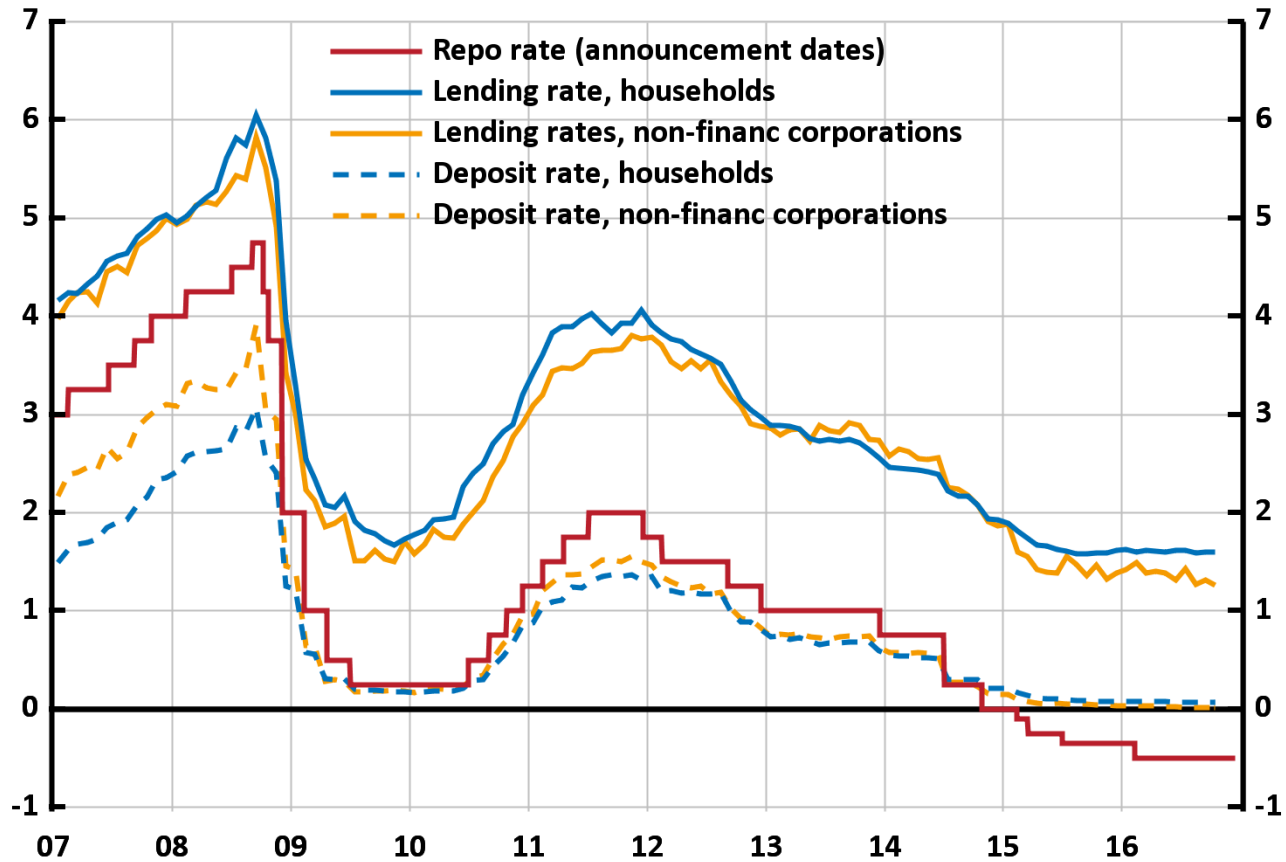
Credits to households and non-financial companies and M3

Yearly percentage change