“Cross border spillovers of monetary policy / The international transmission of monetary policy through financial centers”

Discussion of Barbosa, Bonfim, Costa and Everett (2017) and of Hills, Ho, Reinhardt, Sowerbutts, Wong and Wu (2017)

IBRN Conference - BdF, Paris, 30 June 2017

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Disclaimer: Opinions expressed are the author’s own and do not necessarily reflect the views of the Banque de France
Context of the two papers

• Important policy debate about international (unconventional) MP spillovers over 2010s
  – Exporting QE? Currency wars in disguise?

• Booming empirical literature on international transmission of shocks through bank networks
  – Mostly based on US bank data (e.g., Cetorelli and Goldberg, JoF 2012) or BIS LBS data (Hale and Obstfeld, JEEA 2016)

• Nice feature of the IBRN endeavour:
  – Each country team has access to both local bank balance sheet and local bank cross-border assets/liabilities
  – Common framework: comparative approach
Overview of the papers: IE/PT vs UK/HK

• Baseline = Bank-level panel regressions (quarterly data, 2000s-2015) akin to Cetorelli and Goldberg (JoF 2012):
  – impact on local bank lending (L) of interacted foreign MP*local banks’ international exposure (IL or IA) or balance sheet strength (B) (+ controls, FE etc.)

• Two mechanisms:
  – “Bank lending channel”: \( \frac{d^2 L}{d \text{MPrate} \cdot d\text{IL}} < 0 \) or \( \frac{d^2 L}{d \text{MPrate} \cdot d\text{B}} > 0 \)
  – “Portfolio rebalancing channel”: \( \frac{d^2 L}{d \text{QE} \cdot d\text{IA}} < 0 \) or \( \frac{d^2 L}{d \text{QE} \cdot d\text{PBHE}} > 0 \)

Foreign MP = US, UK (IE/PT) or Home country MP if EA, US, UK, JP (HK) or EA, JP, US (UK) – MP indicator: MP rate (interacted with ZLB) vs CB’s BS growth vs Shadow rate…

\( IL = \) local bank’s (net) crossborder liabilities to foreign country [IE/PT/UK] – \( B = \) local bank’s liquid assets [IE/PT], parent bank’s liquid assets or deposit ratio [HK] - \( IA= \) local bank’s crossborder assets [E/PT/UK] - PBHE = parent bank’s loan to asset ratio at home [HK] (opposite sign expected then)

Mésonnier - Discussion of BBCE and HHRSWW - BdF/IBRN - 30 June 2017
Summary of (main) findings

Bank lending (funding) channel (loans to non-financial sector)

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Portfolio rebalancing channel (loans to non-financial sector)

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Interesting additional results on currency denomination: strong “dollar funding channel” in UK and HK

Comments (1)

• **Interesting team work**, lots of results (too many?) => some streamlining effort still needed…

• **Comparability**: Striking the right balance between accounting for specifics of local banking systems vs making results comparable
  
  – HK results due to general transmission channel or to focus on bank branches only (cf. Peek and Rosengreen, AER 1997, on JP branches vs subsidiaries in US in 1990s)

• Some **country-specific issues**:
  
  – Very small sample of local banks in IE (9), highly parameterized model…

  – IL/IA of PT banks vis-à-vis US very small: interpretation of results?

  – Possible endogeneity of Parent banks’ controls to foreign MP in HK (parent banks are located in foreign country)
Comments (2)

General identification issue: MPs worldwide are correlated (e.g., respond to global shocks).
Comments (3)

• **General identification issue**: MPs worldwide are correlated (e.g., respond to global shocks). Hence, need to disentangle between two possible stories:

  1. MP foreign => Balance sheet of international banks => lending local
  2. MP foreign => MP local => lending local

  - Some easy improvements still possible: include [Local MP*Local bank] terms
  - Use Foreign MP shock series from external source (e.g.: VAR, narrative)

• Alternative settings could allow for better identification of foreign MP shocks (for further work?):

  - Event-study type
  - FAVAR type
Alternative approach (1): event-study

• Idea close to Cetorelli Goldberg (JIE, 2012) (use subprime panic 2007/08 and Fed’s TAF 2007/12 as instruments)

• Select idiosyncratic, unexpected policy moves:
  – Examples: Bernanke’s 2013 taper tantrum, BoE’s and BoJ’s announcements about higher QE limits, Draghi’s 2012 London speech on “whatever it takes” etc.
  – Must be arguably specific for “foreign” country

• Run Diff-in-Diff style regressions of local lending on event dummy interacted with bank category (highly exposed to crossborder funding or not)
Alternative approach (2): FAVAR

- Idea close to Buch, Eickmeier, Prieto (JEDC 2014)

- Domestic bank-level loan growth follows a simple factor model:
  \[ y_{it} = \Lambda F_t + \varepsilon_t, F_t = [G'_t, H'_t]' \]
  - Observed factors \( G \) (local macro and MP; foreign MP indicator or shocks)
  - Unobserved bank factors \( H \) (simple PCA)

- Factors follow a VAR model:
  \[ F_t = \Phi F_{t-1} + \eta_t \]

- Plot median IRF of domestic bank-level \( y \) for sub-groupings of banks (highly exposed to crossborder funding vs not)

- \textit{NB: could be embedded in hierarchical model (global vs local factors)}