Comments on Monetary and Macroprudential Policy Mix: An Institutional-Design Approach

Ben Hunt

International Monetary Fund - Research Department

Overview

- Objectives
- Approach
- Results
- Why?

Objective

- Optimal macroprudential policy
- Relevant given financial sector role in the Great Recession
- Relevant given financial stability mandates (Central Banks and Supervisory Agencies)

Approach

- DSGE model with banks
- Grid search approach over parameters in simple monetary policy and macroprudential rules
- Household welfare is optimized rather than minimizing loss function with output and inflation variability
- Complicated and clearly a lot of work – focus on strengthening

Approach - Model

- More useful if model was calibrated more specifically for Mexico – eg credit spread
- Helpful if the reader was provided more comfort that model had sensible macro dynamics
  - inflation under the policy rate shock
  - exchange rate under the bank capital and spread shocks

Approach – The Shocks

- Helpful if there was a clear interpretation of the shocks hitting the financial sector
  - Not clear what the capital shock is (increase in loan losses?) and thus where else it should have implications in the economy
  - What is the spread shock (increase in borrower riskiness?)
- The paper needs to provide more detail about the shocks underlying the optimization
  - relative importance of real and financial
  - plausibility of resulting variability of key macro variables

Results

- Macroprudential policies just don’t matter
- Don’t matter if the economy is open or closed
- Don’t matter even if they are optimized before standard monetary policy is optimized

Why?

- Without more detail on the shocks it is difficult to understand the reasons
- The impulse responses in the paper suggest that shocks emanating from the financial sector don’t have a material impact on consumption which is underlying the welfare metric

Other Questions

- How likely is it that these types of models will find a meaningful role for macroprudential policy
- Specifically:
- Can a loanable-funds framework every generate the types of credit expansions we worry about in practice
- Or can they be generated with a framework that does not incorporate misperceptions about credit risks
- IMF working papers Benes, Kumhof, and Laxton (2014a,b) WP/14/56 WP/14/57

Summary

- Clearly considerable effort has gone in to the paper, but a lot more needs to be done
- On the model's macro properties
- On the shocks that drive macro variability
- On understanding the results
- Extensions to the underlying framework