

Discussion of 'Assessing Potential Inflation Consequences of QE after Financial Crisis '

Tomasz Wieladek
(Bank of England)

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Introduction

- Following the 'Great Recession', central banks pursued unconventional monetary policies.
- These policies were mainly aimed at stimulating the real economy.



Introduction (II)

- But there may be unintended consequences...
- financial stability
 - Looser monetary policy may lead to more risk-taking
Madaloni and Peydro (2011);
Paligorova and Santos (2012)
- Inflation
 - This paper → QE today may lead to medium-term inflation



This Paper

- Examines the link between money and subsequent inflation based on the quantity theory of money:
 - Once and are accounted for, changes in will be reflected in
 - But in practice, it is difficult to know
 - That is why this fell out of favour in the 1980s
 - ➔ Financial liberalisation may lead to rapid shifts in

This Paper (II)

- Samuel's insight: Proxy with long-term interest rate to calculate equilibrium money level
 - leads (3 years) in Argentina, CH, Japan & US
 - ➔ Predicts that QE will raise US inflation to 4-5%

My main comments

- Why I like this paper very much:
 - Simple, intuitive & creative approach
 - Most papers only look at short-term impact of monetary policy (via VAR or estimated DSGE model)
 - There is clearly not enough work of this kind!
- Pushbacks
 - Lucas Critique → Does the assumption hold at ZLB?
Does unconventional monetary policy work differently?
 - Econometrics?
 - Applicable to more countries (UK, EA)?

Is the impact of QE different...

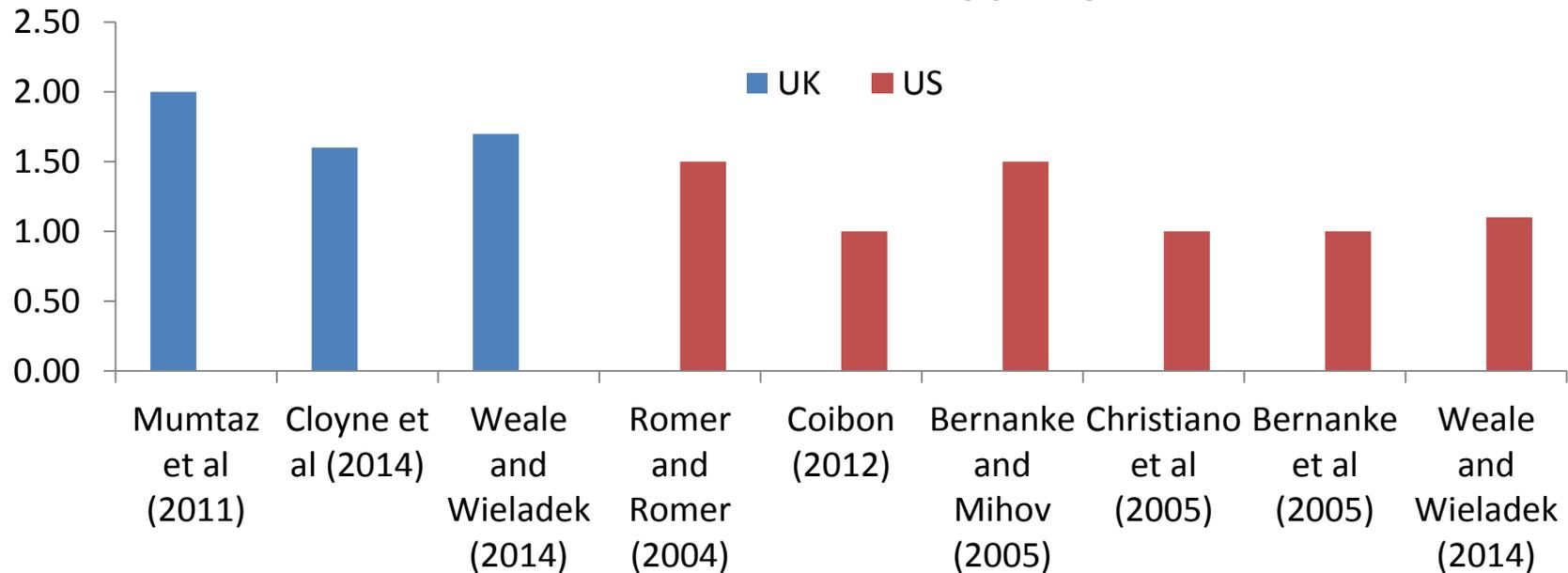
- Weale and Wieladek (2014) estimate Litterman/Panel prior BVARs with 3 different identification schemes to assess impact of QE announcements on output and inflation (always left unrestricted)
 - BVARs estimated on QE time period (2009m3 to 2013m5)
- Real GDP and CPI impulse response to asset purchase announcement is always statistically significant and positive
- Table below shows ratio of CPI to GDP peak impact (Ratio allows easy comparison to conventional monetary policy responses)

Ratio of Peak Impact of CPI to GDP following 1 % asset purchase announcement shock

Model/ Variable	Litterman I	Litterman II	Litterman III	Panel I	Panel II	Panel III	Average
CPI/GDP (US)	1.09	1.20	1.21	0.20	0.92	1.11	1.06
CPI/GDP(UK)	0.17	2.35	2.21	0.75	1.32	1.86	1.67

...from 'normal' monetary policy? Not really.

Comparison of Peak impact CPI/GDP ratio for studies of conventional vs unconventional monetary policy



➔ Ratio of peak impact CPI/GDP seems very similar across studies of conventional monetary vs asset purchase policy

➔ Lucas Critique probably less of a problem than initially thought

Econometrics

- The idea here is that there is a longer-term relationship between and
 - But why not examine predictive properties & test for asymmetric cointegration formally?
- Potential measurement problems?
 - When potential output is not available, HP filter is used to estimate it → But different filters give different answers (Canova, 1998)
 - Long-term interest rate is also obtained via HP filter → But HP filter, when applied to financial variables, can generate spurious trend/cycle (Harvey & Jaeger, 1993)

Conclusion

- I like this paper very much:
 - It provides an intuitive and creative approach of thinking about the medium-term inflationary consequences of an expansion in money
 - More work like this should be done!
- But we need more empirical work:
 - Use filters other than HP for econometrics
 - Do more formal testing
 - if this is a truly universal proposition, it should hold in most OECD countries