Responses to Monetary Policy Shocks in the East and West of Europe: A Comparison[a]

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Monetary policy transmission mechanism

in the euro area in its first 10 years

European Central Bank

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[a]The comments do not necessarily reflect the views of the OeNB

Contribution

Economic contribution: Joint inference on several countries

- Comparison between NMS and euro area region before (joining) EMU
- May be extended to the comparison of NMS region to actual euro area region
  $\longrightarrow$ Actual situation is relevant when joining EMU

Methodological contribution: Bayesian framework

- Regional panel VAR where the parameters are shrunk towards a common mean
- Heterogeneity within the region panel is estimated simultaneously with the parameters

Basic conclusions of the paper

- No evidence for ineffectiveness of monetary policy
- Evidence for steeper Phillips curve in NMS, i.e. a lower sacrifice ratio

Comments/Extensions

- Estimate country-specific or variable-specific heterogeneity
- Provide a quantitative assessment of (dis-)similarities
- Include aggregate indicators about financial market/firm behaviour

Additional dimensions of heterogeneity

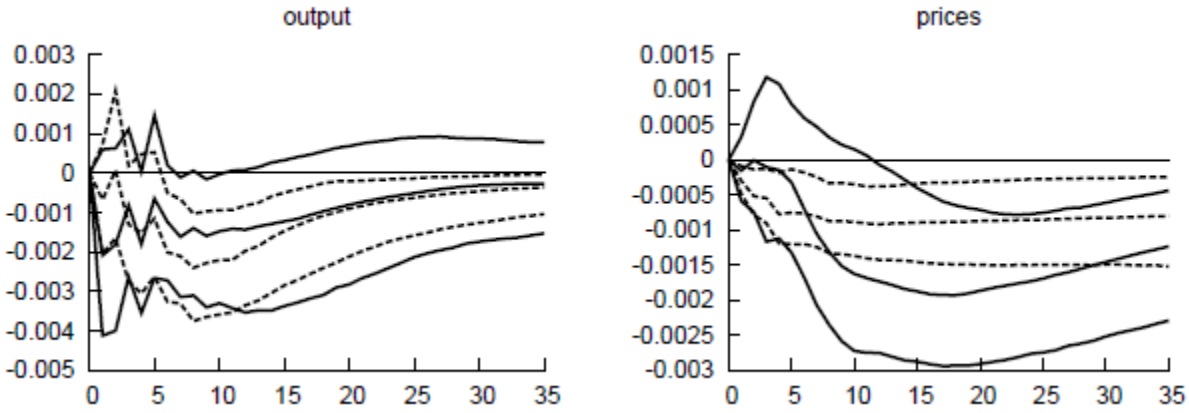
$$
\begin{aligned}
\text{var}\left(\beta_c(k,n)\right) \quad &= \quad \lambda\hat{\sigma}^2_{c,nk} \\
&\text{or} \quad \lambda_c\hat{\sigma}^2_{c,nk}, \quad \lambda_c = \frac{\lambda}{\tau_c},\ \tau_c \sim G(\frac{\nu_0}{2}, \frac{\nu_0}{2}) \\
&\quad \rightarrow \text{country-specific heterogeneity} \\
&\text{or} \quad \lambda_n\hat{\sigma}^2_{c,nk}, \quad \lambda_n = \frac{\lambda}{\tau_n},\ \tau_n \sim G(\frac{\nu_0}{2}, \frac{\nu_0}{2}) \\
&\quad \rightarrow \text{variable-specific heterogeneity} \\
&\text{or} \quad \lambda_t\hat{\sigma}^2_{c,nk}, \quad \lambda_t = \frac{\lambda}{\tau_t},\ \tau_t \sim G(\frac{\nu_0}{2}, \frac{\nu_0}{2}) \\
&\quad \rightarrow \text{time-varying heterogeneity} \\
&\text{or} \quad \lambda_{ct}\hat{\sigma}^2_{c,nk}, \quad \lambda_{ct} = \frac{\lambda}{\tau_{ct}},\ \tau_{ct} \sim G(\frac{\nu_0}{2}, \frac{\nu_0}{2}) \\
&\quad \rightarrow \text{country-specific, time-varying heterogeneity}
\end{aligned}
$$

Quantitative assessment of (dis-)similarities

What you read...

Papers fall into two categories:
those that find significant differences (3 papers) ...
and those that do not (2 papers)

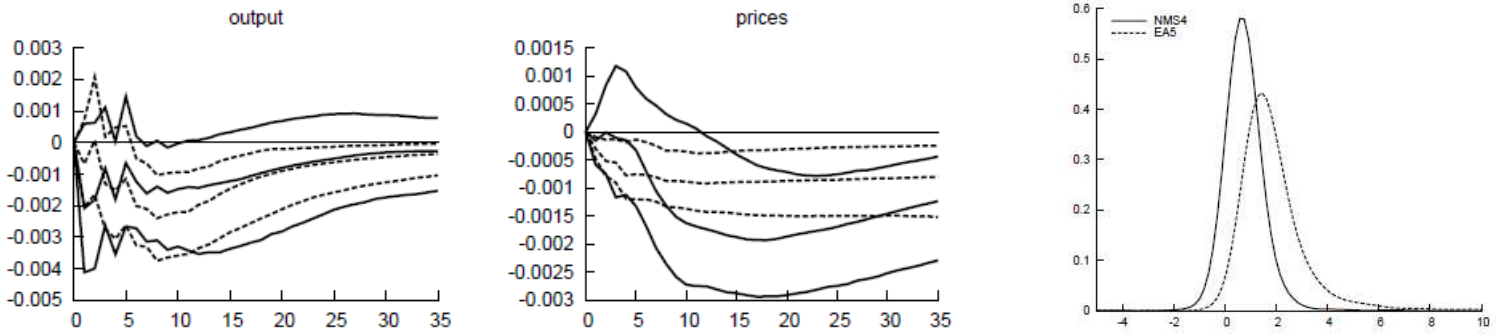
Figure 1



Overall, the impulse responses are similar. *Yes and no*

Output responses to a contractionary monetary policy shock are negative and transitory *for NMS4* (they last about two years *for EA5*), and price level responses are negative and very persistent *Yes.*

Figure 1 and 3



... for the NMS4 ... the possibility of much stronger price responses ... that output responses tend to be similar, while those of prices are stronger in the NMS4, suggests that the output cost of disinflation ... might be lower.

$\longrightarrow$ give a P-value like $Prob\left(\text{resp}^{NMS4}_{\text{horizon}} > \text{med}(\text{resp})^{EA5}_{\text{horizon}}\right)$

$\longrightarrow$ give a P-value like

$Prob\left(\text{sacr.ratio}^{NMS4}_{\text{horizon}} > \text{mean}(\text{sacr.ratio})^{EA5}_{\text{horizon}}\right)$

Note: use highest posterior density interval for skewed distributions

Financial system indicator: e.g. lending standards

Pertains to the cost channel of monetary transmission

$$\hat{\pi}_t = \lambda_0 \hat{\kappa}_t + \lambda_1 \psi \hat{R}_t + \lambda_2 \hat{s}_t + \gamma_f E_t \hat{\pi}_{t+1} + \gamma_b \hat{\pi}_{t-1}$$

To sum up

- The paper contains a valuable economic and methodological contribution which can be applied to obtain answers to various other questions
- (Dis-)similarities should be quantified
- New channels and innovations call for the inclusion of new aggregate indicators of economic agents