Discussion of “Forward Guidance Matters: Disentangling Monetary Policy Shocks” by Leonardo N. Ferreira

Alistair Macaulay

August 11, 2020

Overview

What is the aggregate effect of monetary policy? Short run (conventional) rate changes vs forward guidance.

The method:

1. Take ‘target’ and ‘path’ factors from short-term surprises in futures markets (Gürkaynak et al, 2005).
2. Include them in a VAR with macro variables, identify with sign restrictions.

Overview

What is the aggregate effect of monetary policy? Short run (conventional) rate changes vs forward guidance.

The method:

1. Take 'target' and 'path' factors from short-term surprises in futures markets (Gürkaynak et al, 2005).
2. Include them in a VAR with macro variables, identify with sign restrictions.
3. Narrow set of admissible IRFs with **narrative restrictions** - episodes where we think we know what the shock was (Antolín-Díaz and Rubio-Ramírez, 2018).

Overview

What is the aggregate effect of monetary policy? Short run (conventional) rate changes vs forward guidance.

The results:

1. Conventional monetary policy works as expected.
2. Forward guidance is at least as powerful as conventional policy in affecting industrial production.

Comment 1: Why not more narrative restrictions?

With just three, I have to be very convinced that all three are correct - each one does a lot of work.

Restriction 2: in Feb 1994, monetary policy shock contributes more to unexpected movement in FFR than all other structural shocks combined.

Comment 1: Why not more narrative restrictions?

With just three, I have to be very convinced that all three are correct - each one does a lot of work.

Restriction 2: in Feb 1994, monetary policy shock contributes more to unexpected movement in FFR than all other structural shocks combined.

- What do most identifications in the set say was going on in Feb 94 without restriction 2? Are they obviously wrong?
- My prior: conventional monetary policy shock drives less of the FFR variation than other shocks, as in every other period (figures 4 and 6).

Comment 1: Why not more narrative restrictions?

With just three, I have to be very convinced that all three are correct - each one does a lot of work.

Restriction 2: in Feb 1994, monetary policy shock contributes more to unexpected movement in FFR than all other structural shocks combined.

- What do most identifications in the set say was going on in Feb 94 without restriction 2? Are they obviously wrong?
- My prior: conventional monetary policy shock drives less of the FFR variation than other shocks, as in every other period (figures 4 and 6).

Better to use more narrative restrictions, then systematically delete them. Which are necessary for the results?

Including all the Antolín-Díaz and Rubio-Ramírez restrictions, IRF set becomes *larger*. IRFs

Comment 2: Dealing with QE

Footnote 5: you admit that your identification of forward guidance shocks also picks up QE shocks, but then say that's fine because QE mostly works through signalling.

- Not obviously true! Why not try to disentangle conventional policy, forward guidance *and* QE?
- As in Altavilla et al (2019) - QE and FG affect different parts of the yield curve.
- Would also give more narrative episodes to use.

Comments: Other

- It's not obvious that financial market expectations are the only ones that matter (e.g. Haldane, Macaulay, McMahon, 2020).
- The lack of forward guidance effect on impact is a surprising result. Do more to explore what is going on there - and bring it out more.
- For output you use industrial production. Services make up $\approx 75\%$ of US GDP, and might respond differently to policy (e.g. Skaperdas, 2017). Possible mixed-frequency VAR to look at GDP overall (e.g. Schorfheide, Song, Yaron, 2018)?
- Bring out the results more in the introduction - I care about what you found as well as how you did it.

References

Altavilla, C., Brugnolini, L., Gürkaynak, R. S., Motto, R. and Ragusa, G. (2019) Measuring Euro Area Monetary Policy. *Journal of Monetary Economics*

Antolín-Díaz, J. and Rubio-Ramírez, J. F. (2018). Narrative sign restrictions for SVARs. *American Economic Review*

Gürkaynak, R. S., Sack, B., and Swanson, E. T. (2005). Do actions speak louder than words? The response of asset prices to monetary policy actions and statements. *International Journal of Central Banking*

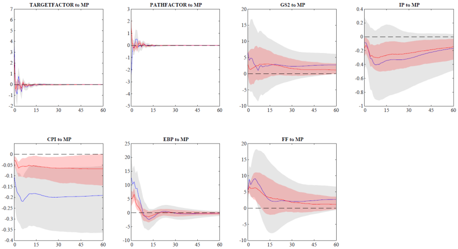
Haldane, A., Macaulay, A., and McMahon, M. (2020) The 3 E's of Central Bank Communication with the Public. *Bank of England Staff Working Paper*

Schorfheide, F., Song, D., and Yaron, A. (2018) Identifying Long-Run Risks: A Bayesian Mixed-Frequency Approach. *Econometrica*

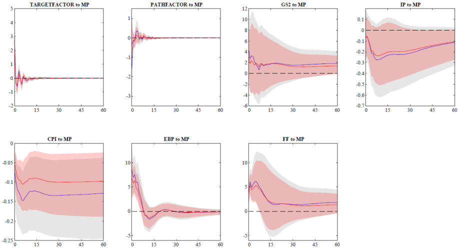
Skaperdas, A. (2017) How Effective is Monetary Policy at the Zero Lower Bound? Identification Through Industry Heterogeneity. *Finance and Economics Discussion Series*, Fed Board.

IRF comparison

(a) Baseline restrictions



(b) all ADRR restrictions + restriction 3



Back