Monetary Policies in Systemic Advanced Economies: Spillovers on Other Countries

Prakash Loungani (IMF)
Esteban Vesperoni (IMF)

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Views expressed are those of the presenters
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Motivation for Analysis in 2015 Spillover Report

1. Increasing divergence in monetary conditions in systemic advanced economies (SAEs)

2. Asynchronicity of monetary conditions in SAEs

1. Different speeds of recovery
2. Fluctuations in SAEs bilateral exchange rates

3. Asynchronicity in future:

1. US liftoff may strengthen the USD AND push interest rates in EA.
2. ECB-QE may weaken the € AND push yields down in the US.

Methodology

1. Spillovers within Systemic Advanced Economies (SAEs)

1. Controls for autonomous risk-appetite shocks
2. Identify country-specific money/real shocks & spillovers among SAEs

2. Spillovers effects of real and money shocks in each SAE

1. PVAR of 4 key variables in EMNS: bond yields, net K flows, USD-EUR EER, activity
2. Changes in risk-appetite caused by real/money shocks in SAEs can affect EMNS variables
3. Sample: 29 EMNS over 2000m1-2014m12

3. Synchronicity in SAEs and Spillovers to Emerging Markets

1. Interact external shocks with shock-specific synchronicity index
2. Differentiate spillover estimates of each shock in (a)synchronous states of the world

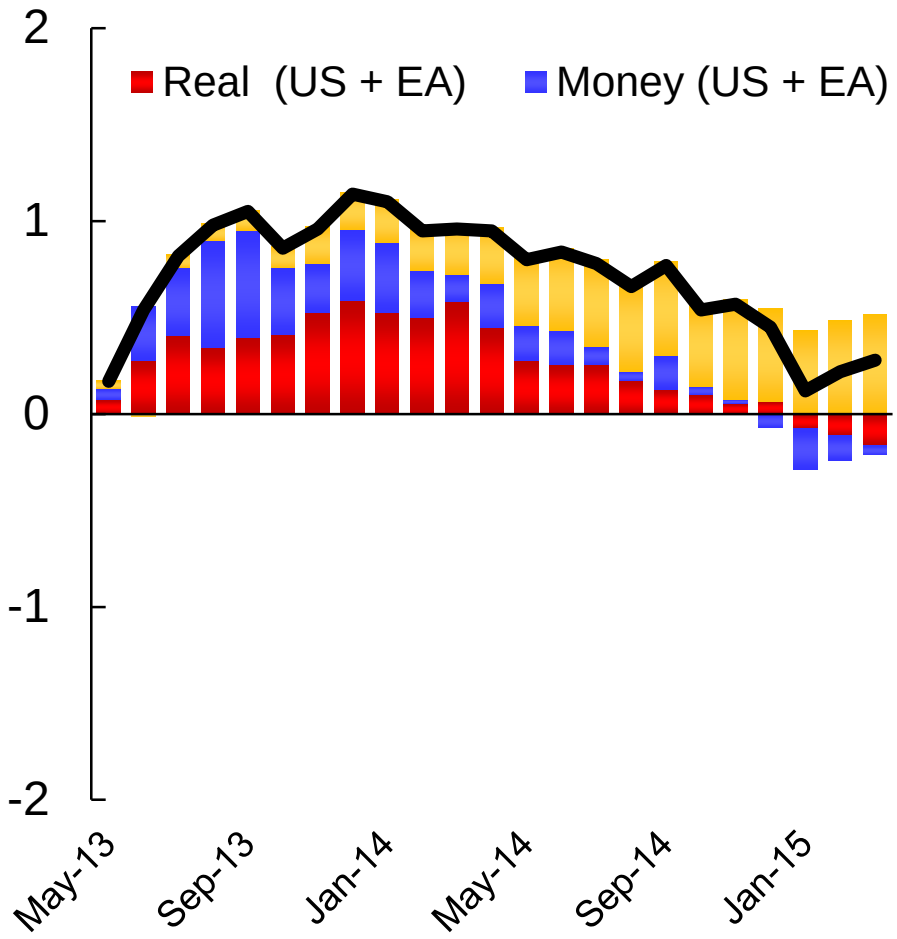
Identification of Country-Specific Real and Money Shocks

Shocks	Variables[1]			
	US Stocks	US 10 year yields	EA Stocks	EA 10 year Yields
Real US	+	+	+	.
Money US	-	+	.	.
Real EA	+[2]	.	+	+
Money EA	.	.	-	+

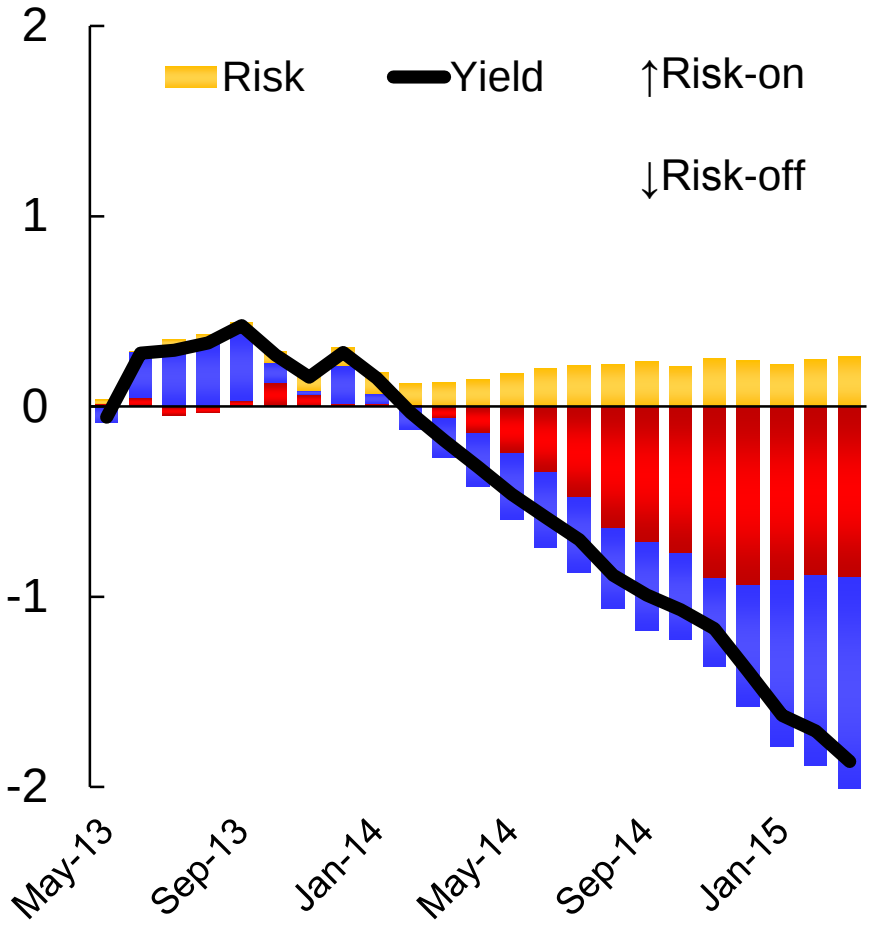
1/ Variables purged from risk-appetite shocks
2/ Restriction on lagged variable

US and EA 10-Year Yield Decomposition Since 2013

US: 10 Year Yield decomposition
(cumulative change; percent)



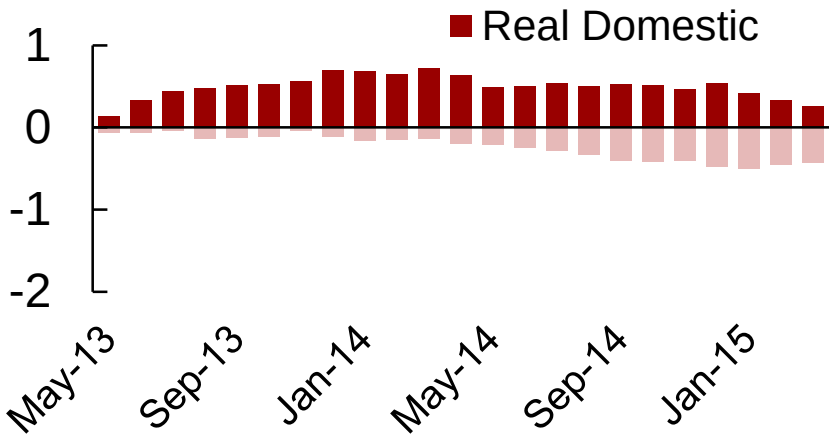
EA: 10 Year Yield decomposition
(cumulative change; percent)



Source: IMF staff calculations.

Asynchronicity and Important EA Spillovers

US 10-Year Yield: Real Components
(cumulative change; percent)



EA 10-Year Yield: Real Components
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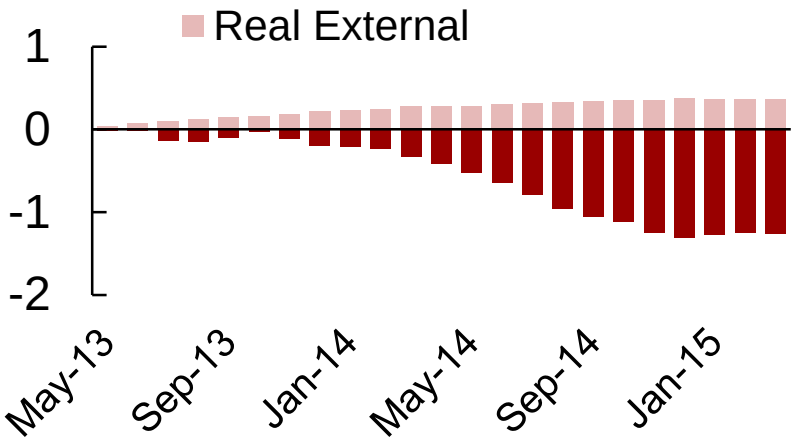
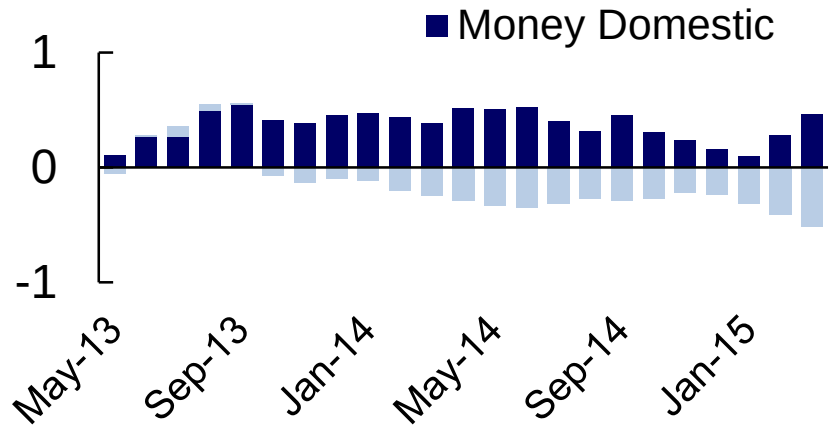
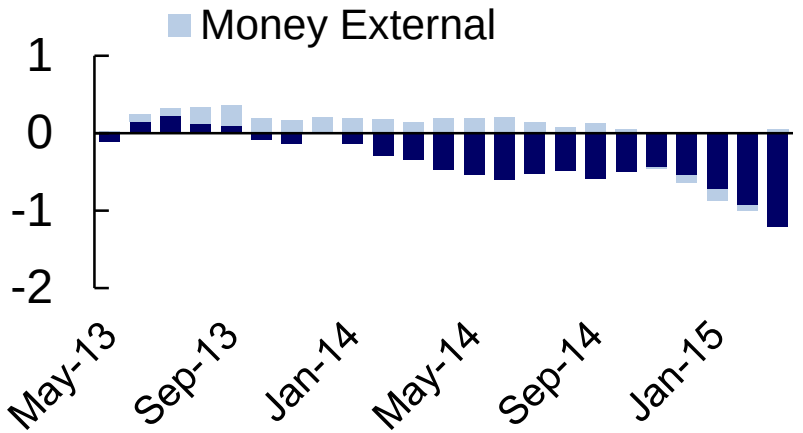


US 10-Year Yield: Money Components
(cumulative change; percent)



EA 10-Year Yield: Money Components
(cumulative change; percent)

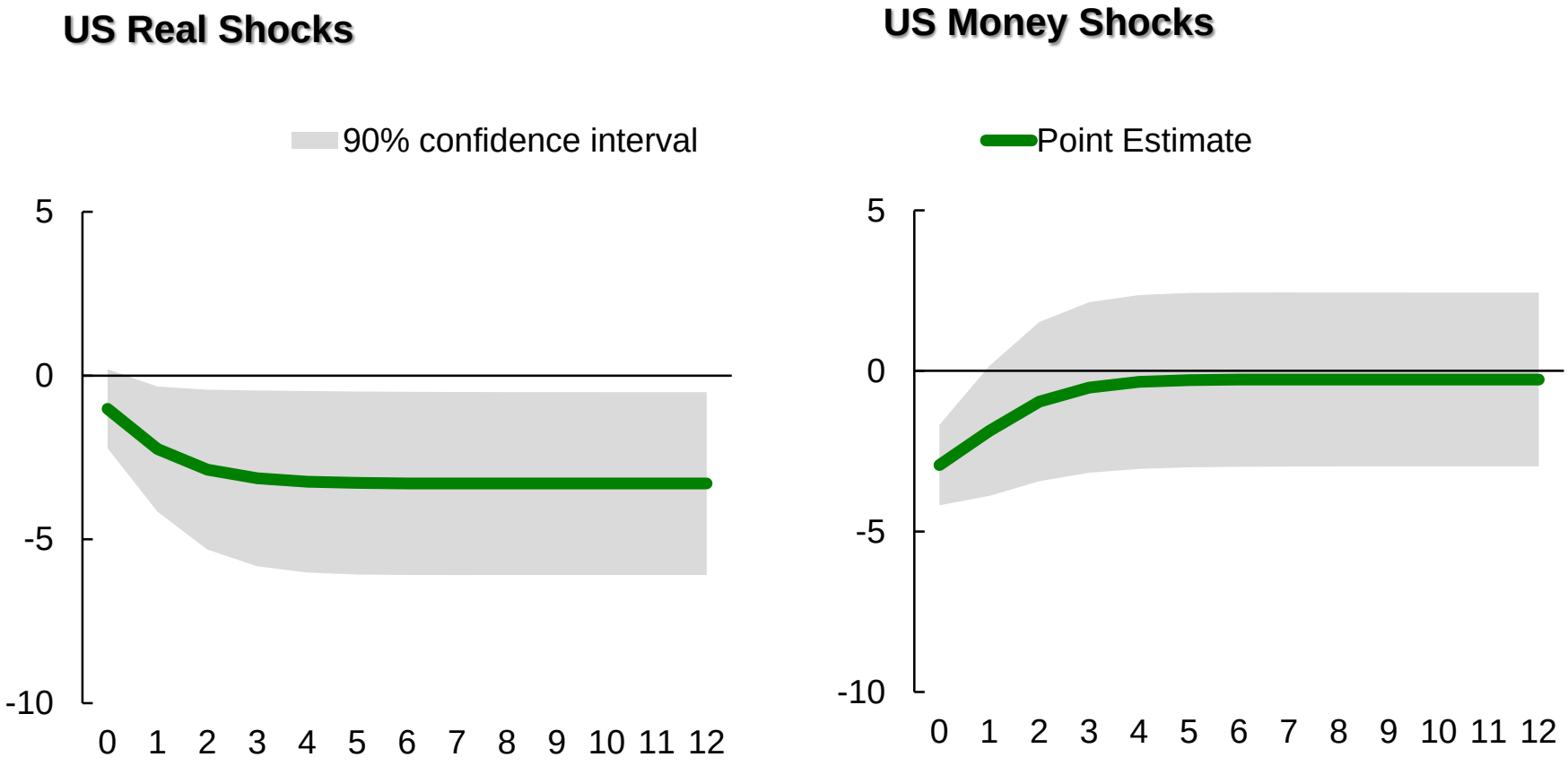


Source: IMF staff calculations.

Asynchronicity and strengthening of the USD

Response of USD-EUR Exchange Rate to Shocks that raise US yields by 100 bps

(cumulative percent change, + = USD depreciation)



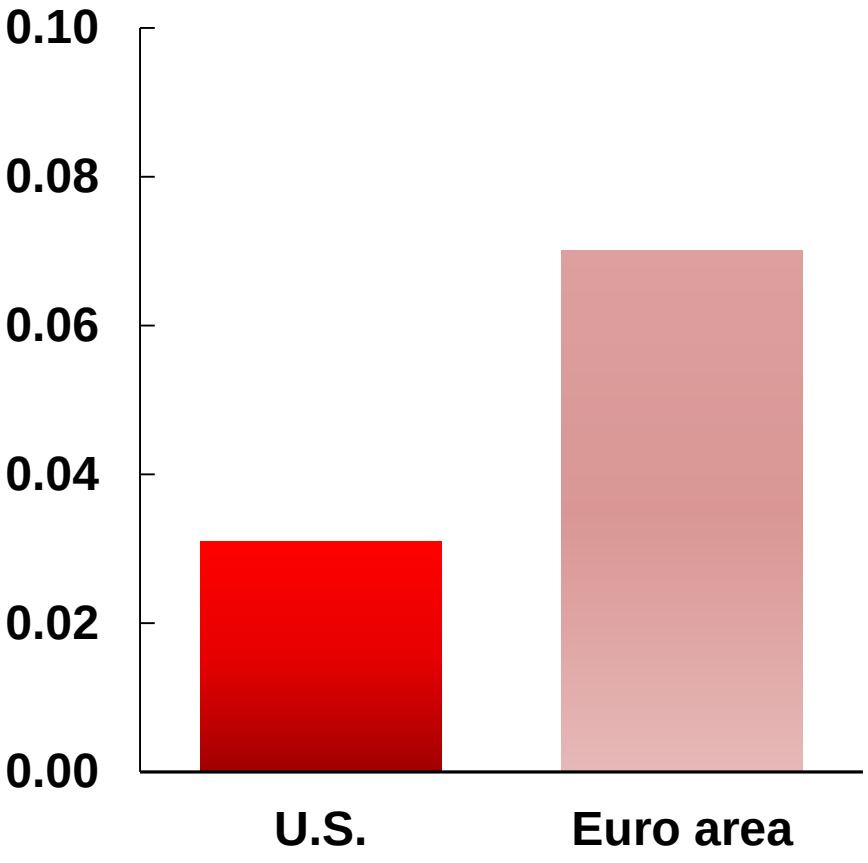
Source: IMF staff calculations.

Spillovers from Monetary Policies in Systemic Advanced Economies:

Impact of 'Good News' about Growth Prospects

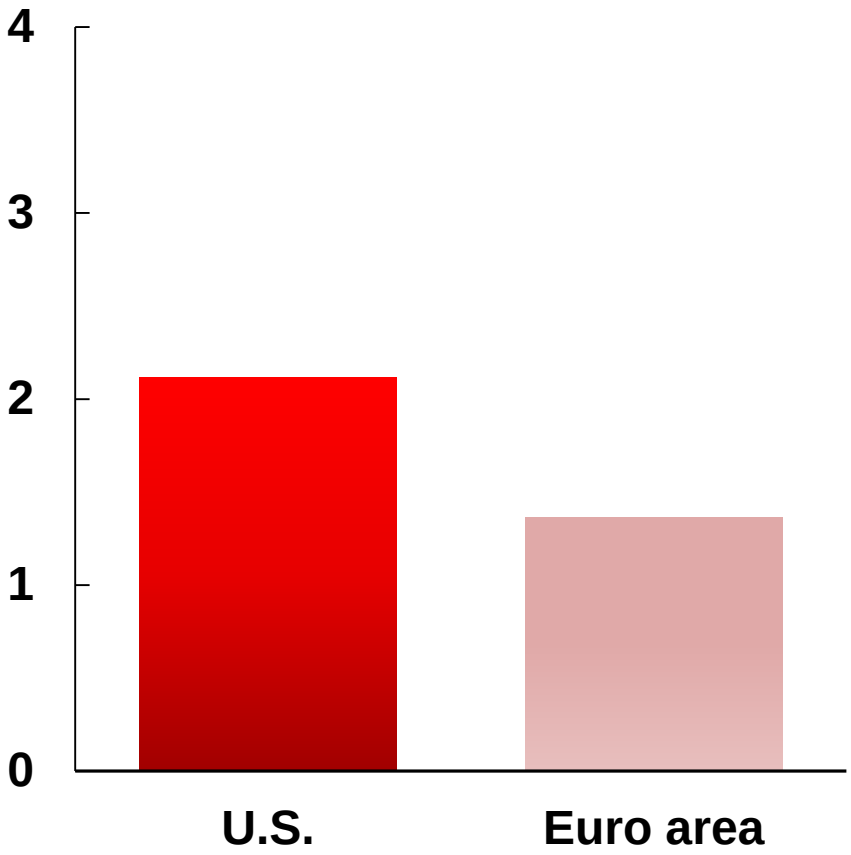
Net Capital Inflows 1/

(percent of GDP)



Industrial Production 2/

(response after 12months; percent)

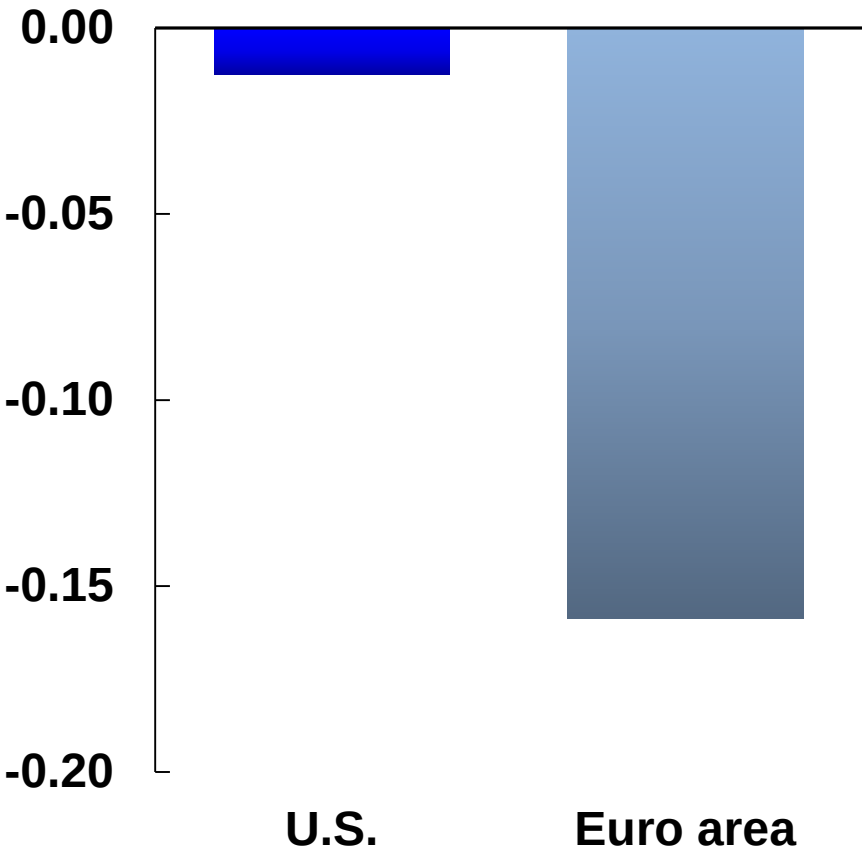


Source: Osorio-Buitron and Vesperoni (2015).
1/ Net debt and equity inflows (in percent of GDP).
2/ Annual change in industrial production.

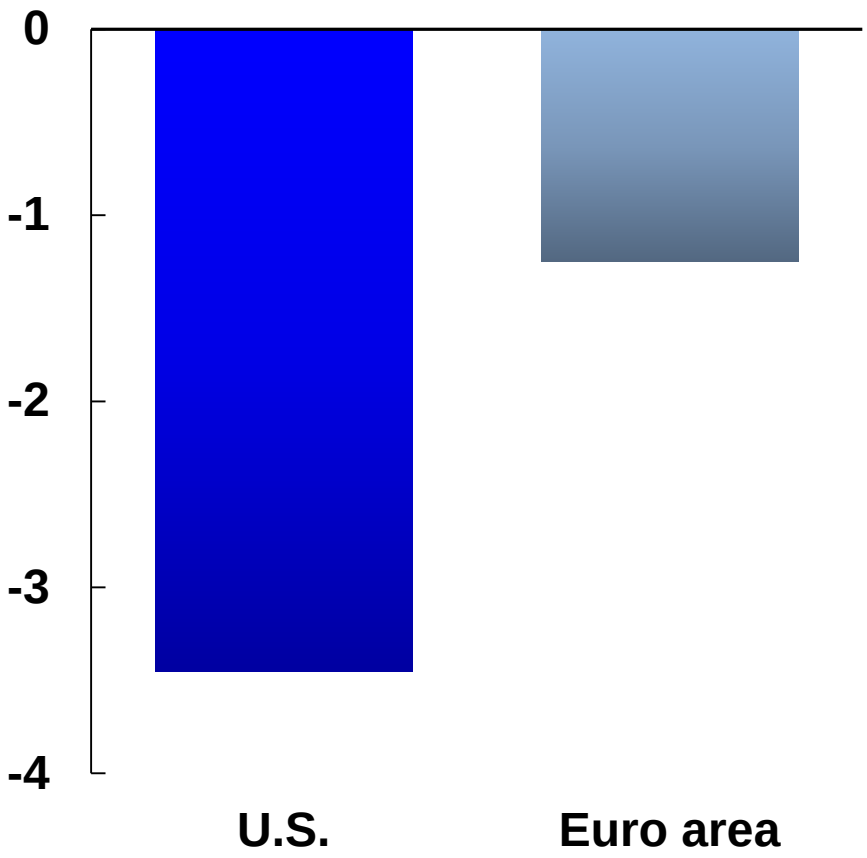
Spillovers from Monetary Policies in Systemic Advanced Economies:

Impact of 'Money Shocks'

Net Capital Inflows 1/
(percent of GDP)



Industrial Production 2/
(response after 12 months; percent)

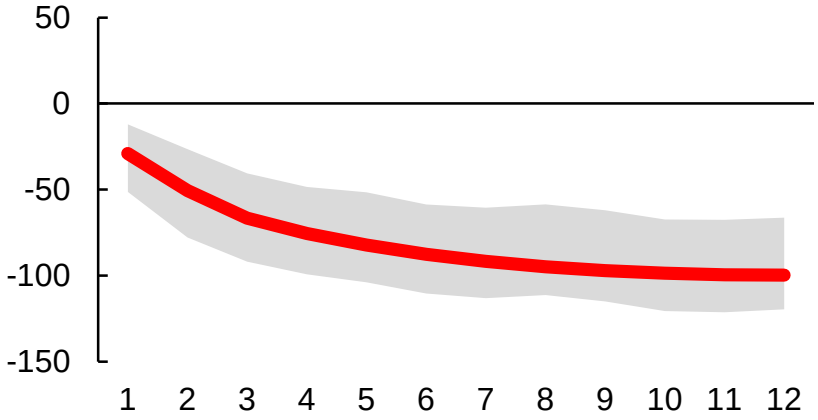


Source: Osorio-Buitron and Vesperoni (2015).
1/ Net debt and equity inflows (in percent of GDP).
2/ Annual change in industrial production.

Effects of Real Asynchronicity (US Shock)

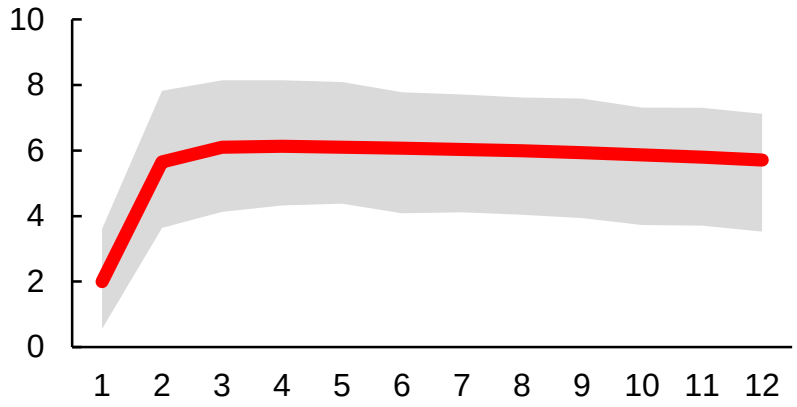
Bond Yields

(basis points; [-] = less tightening)



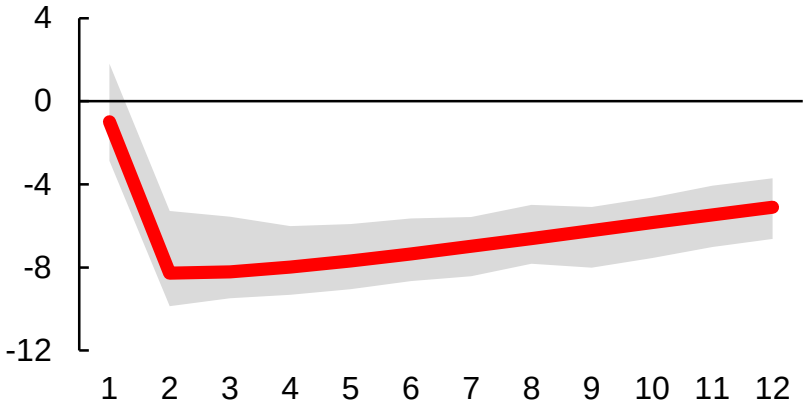
USD-EUR EER

(percent; [+] = less appreciation)



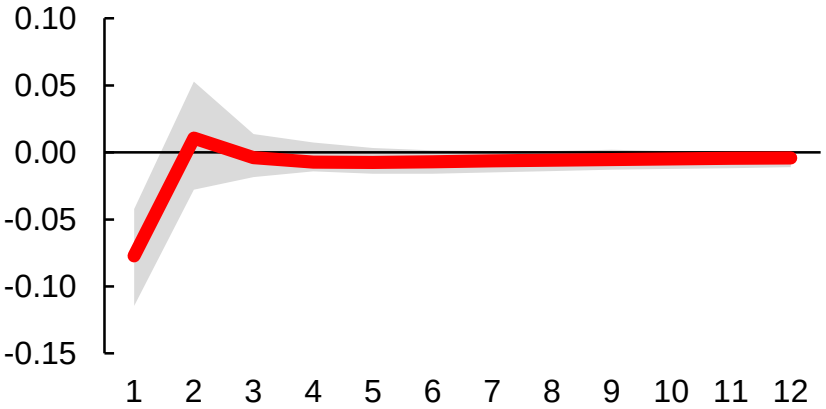
Industrial Production

(percent; [-] smaller positive growth spillovers)



Net Capital Inflows

(percent of GDP; [-] = fewer capital inflows)



Source: IMF staff calculations.

Main Takeaways

- SAEs real and monetary conditions have been asynchronous in the past
- Asynchronicity has given place to spillovers within SAEs, in both directions; e.g. shocks in the EA can have an impact on yields in the US
- Spillovers to EMNS differ in asynchronous scenarios: impact on activity is dampened, as well as impact on financial conditions and capital flows

Implications going forward:

- Diverging monetary conditions in US and EA can have an impact on both the bilateral exchange rate AND interest rates
- Spillovers can affect monetary policy strategies in all SEAs, with potential implications on exchange rates
- Asynchronicity may dampen spillovers to EMNS

Spillovers from U.S. Dollar Appreciation

- In the past, association between emerging markets crises and dollar appreciation

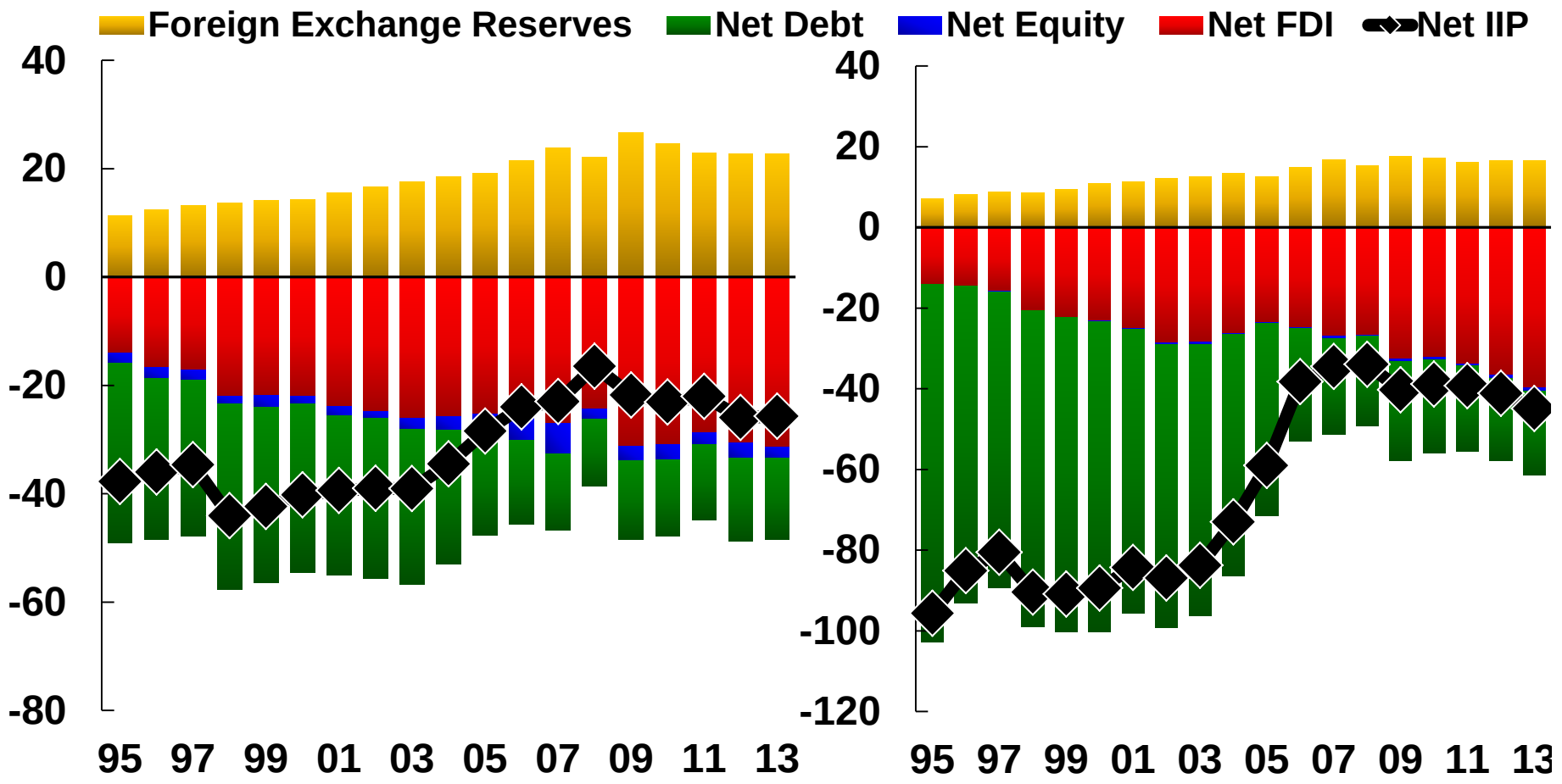
- Greater resilience since the mid-1990s
  - more reliance on domestic-currency, equity-type liabilities, more reserves, and improvements in current accounts.

- But some reasons for caution
  - large gross positions
  - currency composition of debt
  - some balance sheet risks

Improvement in Net International Investment Positions

Emerging Market Countries: Net IIP Decomposition
(percent of GDP; unweighted average)

Low-Income Countries: Net IIP Decomposition
(percent of GDP; unweighted average)



Source: Chow, Jaumotte, Park and Zhang (2015).
Note: FDI = foreign direct investment; IIP = international investment position.

Emerging Markets Corporate Debt

- Share of FX in corporate debt high in many emerging market
- In many cases, leverage ratios are high as well, with variation across sectors (e.g. utilities, real estate & construction more leveraged)
- Composition of FX debt varies across countries
- Maturity structure is generally long-term
- Stress test points to some vulnerabilities

Sorry for going over my allotted time