

Discussion of 'Effects of US Quantitative Easing on Emerging Market Economies'

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- The effects on EMEs of QE implemented by some advanced economies have been a focus of debate among academics and policy makers.
- This paper empirically assesses the impact of QE by the Fed on real and financial variables for major EMEs.
- Two-part methodology:
 - 1 Estimate an identified Bayesian VAR using monthly U.S data on macro and financial variables and assess the impact of a QE shock on U.S variables.
 - 2 Use the identified QE shock in a separate Bayesian VAR for each EME, treating the U.S QE shock as an exogenous variable.

- Expansionary U.S QE shock results in:
 - An increase in U.S output and prices;
 - Downward pressure on long-term Treasury yields (and U.S corporate and mortgage yields);
 - Depreciation of the U.S dollar.
- Using the estimated QE shock as an exogenous variable in separate VARs for each EM, results show that an expansionary QE shock leads to:
 - Exchange rate appreciation, reduction in long-term yields, and rise in stock prices for the 'Fragile Five';
 - Increase in equity flows and negative effect on trade flows for the 'Fragile Five', although evidence is weak;
 - Effects on macro variables for EMEs largely insignificant.

- Domestic implications of U.S QE:
 - Mostly event studies focusing on high-frequency financial market variables; a few VAR-based studies looking at macro effects.
 - Current paper's framework allows focusing on effects on both macro and financial variables, as well as examine persistence of the effects.
- Nascent but rapidly growing literature on the effects of U.S QE on EMEs:
 - Event studies focusing on 2013 “taper tantrum”
 - Panel estimation and VAR-based approaches - Ahmed and Zlate (2014), Bowman et al. (2014), Chinn (2013), Fratzscher et al. (2013), Lim et al. (2014), Moore et al. (2013), etc.
 - Authors use different approach to identification and inference. *How do the results compare with above studies?*

Comments and questions

- Identification strategy
- Interpretation of results
- Possible extensions

Identification strategy:

- Neat and complementary approach to identification and inference. But it raises some questions.
 - The more standard approach to identification in the QE literature is to use a mixture of zero and sign restrictions (e.g., Baumeister and Benati, 2013; Gambacorta et al., 2014; Peersman, 2011; etc.).
 - Instead, authors appeal to the conventional monetary policy literature and use a combination of zero restrictions and liquidity priors.

Not clear why this approach is better? Could identification of the QE shock in the paper be sharpened?

Interpretation of results:

How do the results fit in the literature?

- Paper's effects on output and prices seem to be much longer lived compared to other studies on U.S QE (e.g., Gambacorta et al., 2014).
- Some studies have shown that UMP shocks have relatively larger output and smaller price effects than conventional monetary policy shocks.
 - There is also evidence that monetary policy shocks have larger effect on output and a smaller effect on the price level in recessions (e.g., Weisse, 1999, Peersman and Smets, 2002).
 - But current paper finds effects on prices that are much larger than in the conventional monetary policy literature.

Comments and questions

- QE could affect EMEs through various channels: Portfolio balance channel, signalling channel, exchange rate channel, and trade flows channel.
 - The paper's results could shed some light on the relative importance of the different channels of transmission.
- Some have argued that the overall impact of QE on EMEs may not be very different from that of conventional easing since the two work through similar channels.
 - Key question for policymakers is whether the effects of QE on EM capital flows and asset prices are outsized relative to those of conventional policies.
 - Would be nice to conduct a counterfactual exercise to compare the results under two scenarios: (i) with QE, and (ii) without QE policies. For example, Pesaran and Smith (2012) for the U.K.

Possible extensions

- Results show heterogeneity in responses of EM variables to QE shocks.
 - Which country characteristics drive these vulnerabilities? Banking sector vulnerabilities, exchange rate regimes, financial openness, fiscal positions, etc...
- Would be nice to exploit the cross-sectional nature of the data more.
 - Why look at only the 'Fragile Five' vs. others?
- Another nice extension would be to estimate a panel VAR which will allow exploiting the cross-country dimension.

To sum up

- Nice paper addressing a very widely debated topic in recent years.
- Elegant empirical approach which allows the authors to look at impact of U.S QE on both real and financial variables for EMEs.
- Several possible extensions could be explored. In particular, it would be very interesting to link the heterogenous responses of EMEs to respective country characteristics and to compare results with a no-QE counterfactual.