

Discussion of “Monetary policy and endogenous financial crises” by Cristina Manea

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Should central banks deviate from their objective of price stability to promote financial stability?

- ▶ (Timeless) key question still unresolved in [monetary economics](#)
- ▶ New bold attempt in this paper: incorporate nominal rigidities in an extension of [Boissay, Collard, and Smets \(JPE, 2016\)](#)
 - ▶ [Heterogeneous](#) firms: productive and unproductive
 - ▶ Financial frictions -> [leverage constraint](#)
 - ▶ Crisis due to [credit market stops](#)
- ▶ Main results
 - ▶ [Strict inflation targeting](#) performs surprisingly well
 - ▶ It can be improved by adding [financial variables](#) into the monetary policy rule

What type of crises are analyzed here?

- ▶ These are **not** crises linked to financial intermediaries, instead they are crises related to **inter-firm credit**
 - ▶ As capital grows, the return on capital declines, below a certain threshold credit freezes
 - ▶ Condition for a crisis

$$\Omega \frac{A_t N_t^{1-\alpha}}{\mathcal{M}_t} < K_t^{1+\alpha}.$$

Comments

- ▶ Not all crises are alike
- ▶ On the role of demand shocks
- ▶ Inflation and rate dynamics in the model
- ▶ Trade-off crisis vs. inflation costs
- ▶ Related literature

Not all crises are alike

- ▶ Two types (discussed in the Appendix):
 1. Capital overhang (slow moving credit crises)
 2. Surprise large shock

- ▶ How do dynamics differ depending on the type of crises? Should the central bank respond in the same way?

Inflation and rate dynamics in the model

- ▶ Why don't you show the dynamics of **nominal rates**, **inflation** and **real rates** around crisis?
- ▶ Transmission in NK model with capital (and no adj. costs) is **counter-intuitive**, how relevant is that here?
 - ▶ **Rupert and Sustek (JME, 2019)**

Trade-off crisis vs. inflation costs

- ▶ Welfare analysis critically hinges on the calibration of the costs of inflation versus those of crises
 - ▶ Rotemberg costs calibrated to replicate the slope of the PC equivalent to Calvo with 4-quarters average duration of prices
 - ▶ Cost of financial crises equivalent to a 1.8% decline in output
 - ▶ Frequency of crisis 10%
- ▶ Cheap comment: How robust are results to those parameters?

On the role of demand shocks

- ▶ Why do you consider **two types of shocks**? Why not only TFP shocks?
- ▶ The demand shock Z_t is an (inverse) **risk premium shock**:

$$(1 + i_t) = Z_t (1 + i_t^b),$$

why? (What does it mean that bond yields are below policy rates?)

Related literature

- ▶ How does your model relate to Marbet (2022)?
 - ▶ NK model with crises à la [Boissay, Collard, and Smets \(JPE, 2016\)](#)
- ▶ Other papers analyzing monetary policy with financial crises
 - ▶ [Rottner \(2022\)](#), [Van der Gothe \(2021\)](#)

Conclusions

- ▶ **Great paper**: important question, superb execution
- ▶ My two cents:
 - ▶ If the paper aims at being descriptive (**proof of concept of a mechanism**), I suggest investing more on explaining what is going on
 - ▶ If instead it focuses more on **quantitative results**, I would show the robustness of the results (several moving parts)