

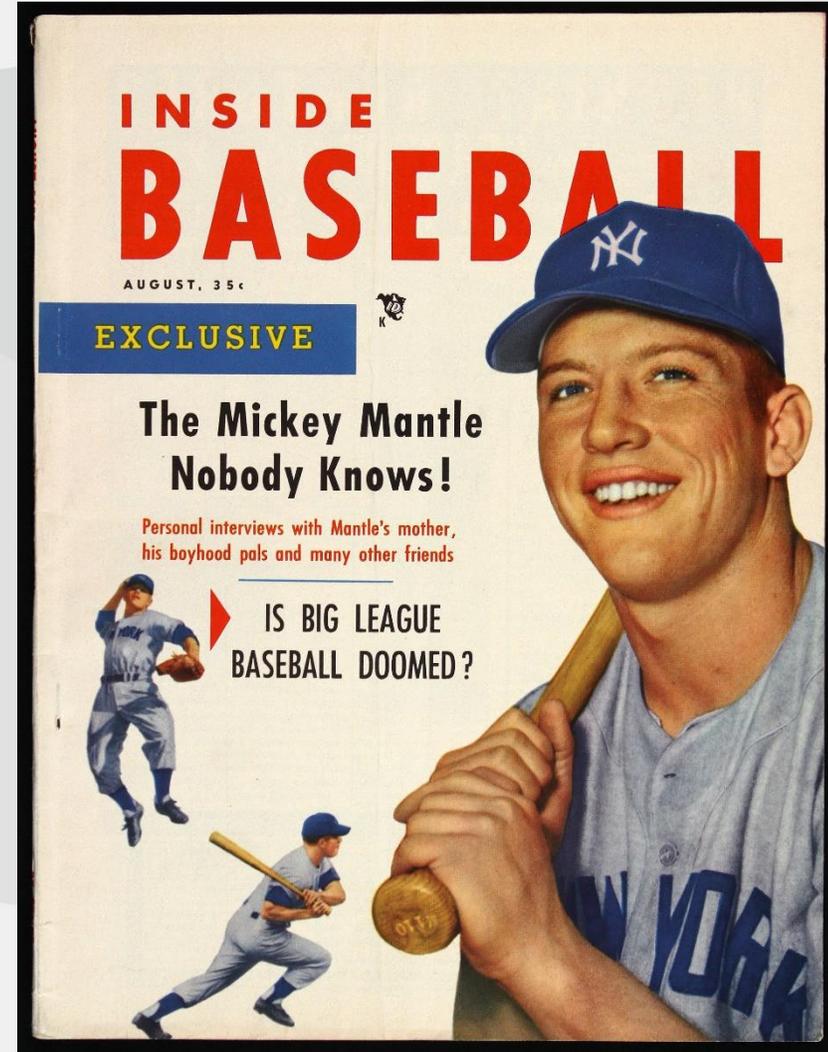
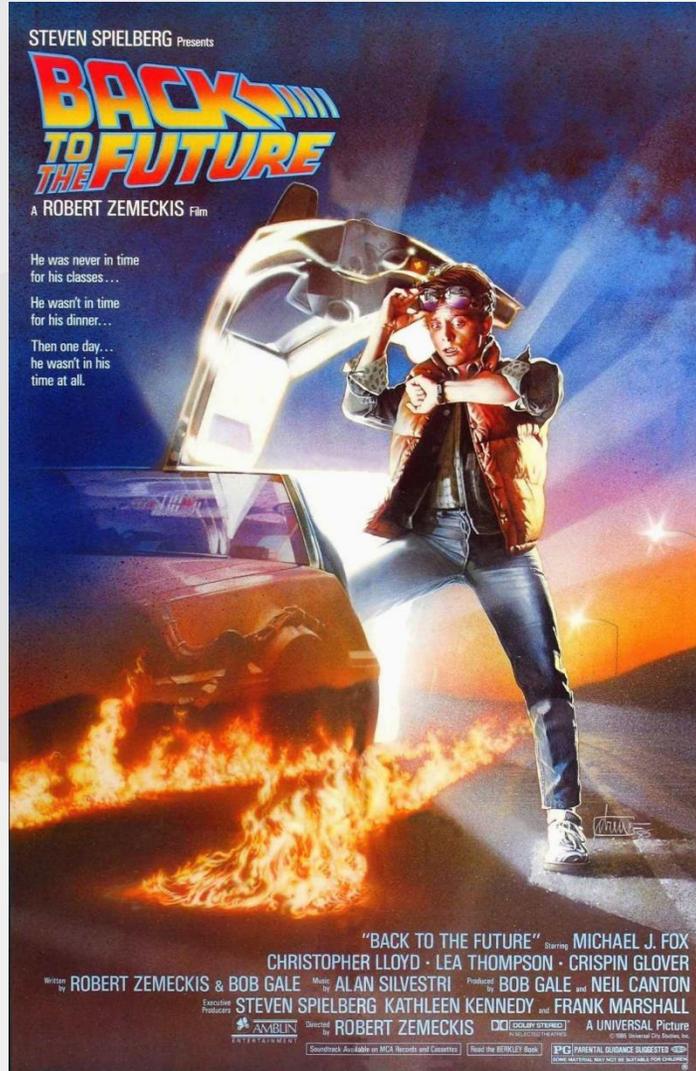
Discussion of “Unexpected supply effects of QE and T”

Morten L. Bech

2022 FMC: “A New Era of Financial Innovation and Disruption: Challenges and Opportunities”

The presentation almost surely does not reflect the views of BIS and its innovation hub.

Two things came to mind when I started to read the paper





INSIDE

CENTRAL BANKING



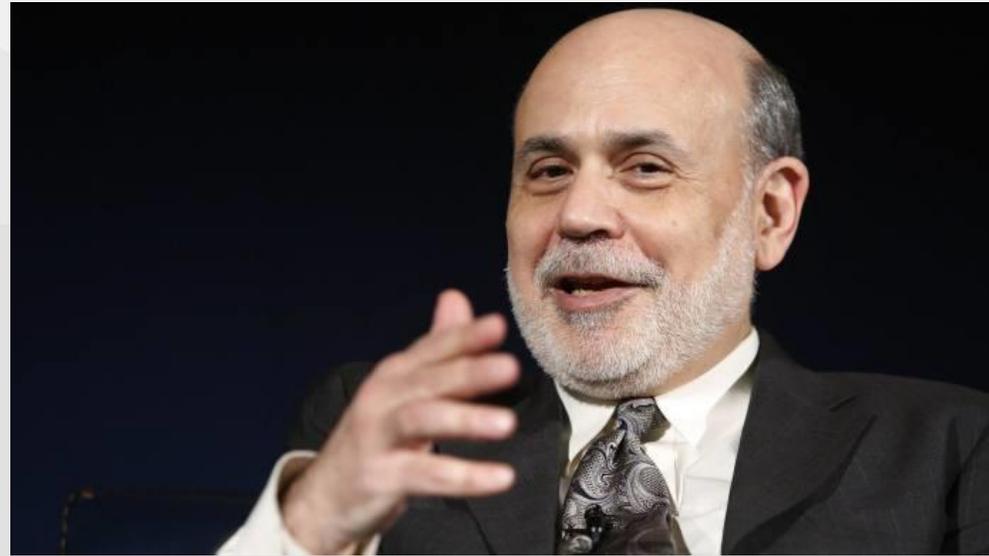
**“Goodbye, QE. Hello, QT”
says the Fed’s D’Amico**

Special issue on monetary policy tool kit

Great paper!

- Well written and clear
- The data is impressive – individual Treasury Securities
- The Event Study is very nicely done
 - Using the Survey of Primary Dealer to get at market expectations is interesting
 - The identification strategy of using sharp kinks in the yield curve is innovative
- The results are convincing and challenge parts of the existing wisdom on QE.
- => Focus on monetary policy implementation in a bit broader context

“The problem with QE is it works in practice, but it doesn’t work in theory.”



What about Quantitative Tightening?

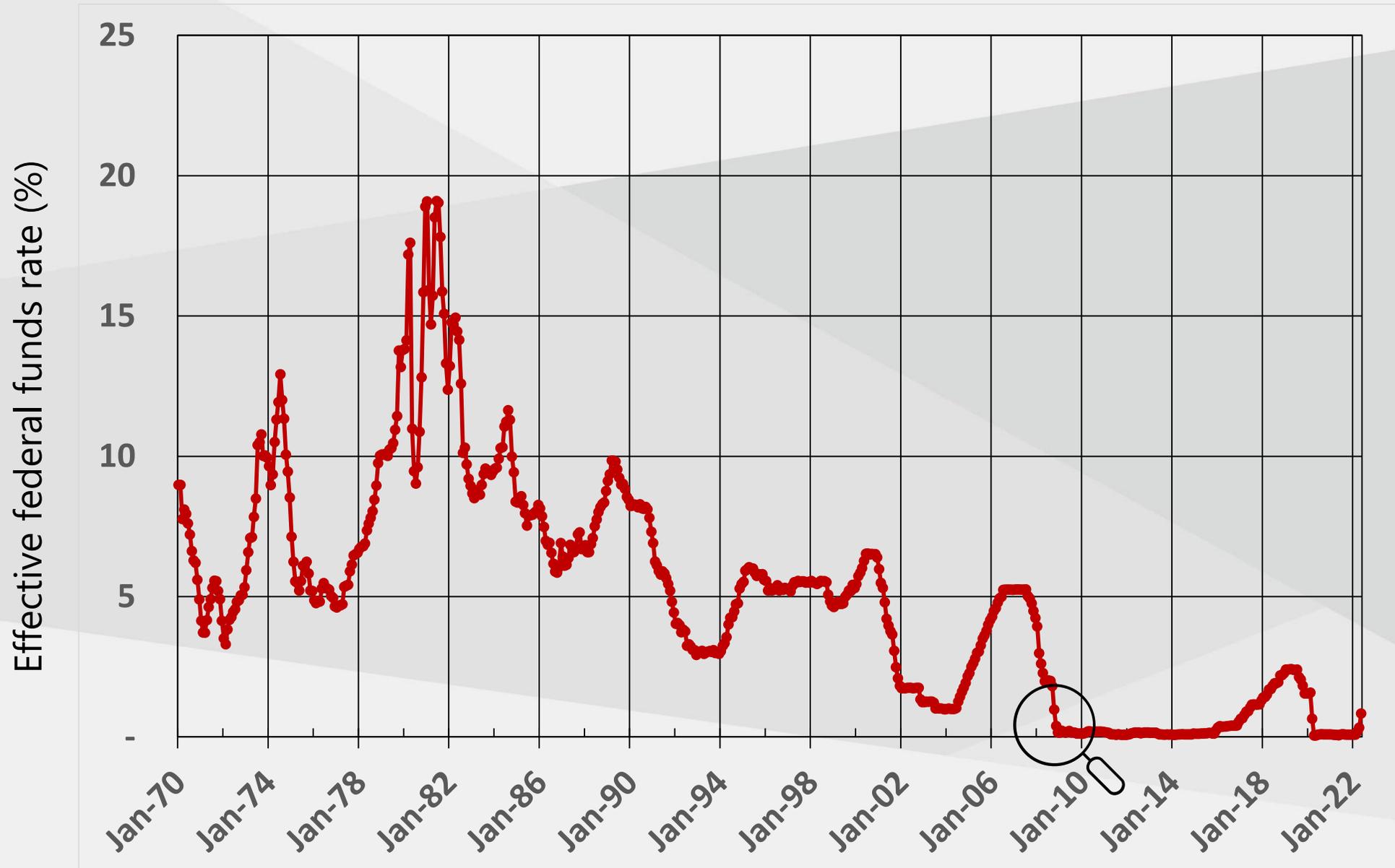
- Does it work? **Yes**
- Does it work like QE? **About the same – opposite sign**
- Does it get weaker over time? **Not really**
- Does it work away from the Zero lower bound? **Yes**

How to think about monetary policy implementation going forward?

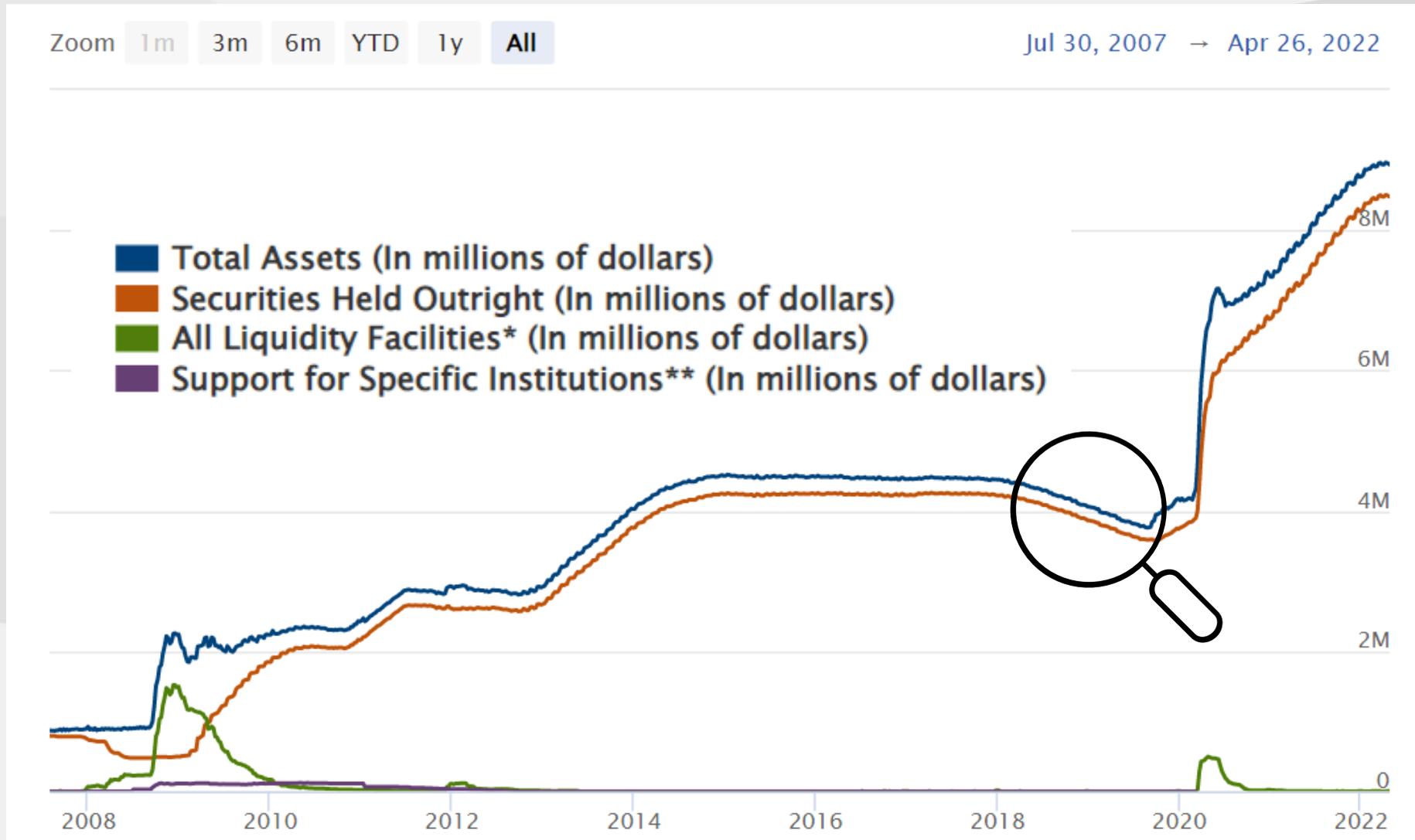
FOMC statement, 4 May 2022

- [T]he Committee decided to raise the **target range for the federal funds rate to 3/4 to 1 percent** and anticipates that **ongoing increases in the target range will be appropriate**.
 - Previous target rate to 1/4 to 1/2 percent
- In addition, the Committee decided to **begin reducing its holdings of Treasury securities and agency debt and agency mortgage-backed securities on June 1**
 - Treasuries \$30B from June and \$60B from September
 - Agencies and Agency MBS \$17,5 from June and \$30B from September
- There are **now two dimensions to monetary policy implementation: (1) Interest rate hikes and (2) quantitative tightening (QT)**

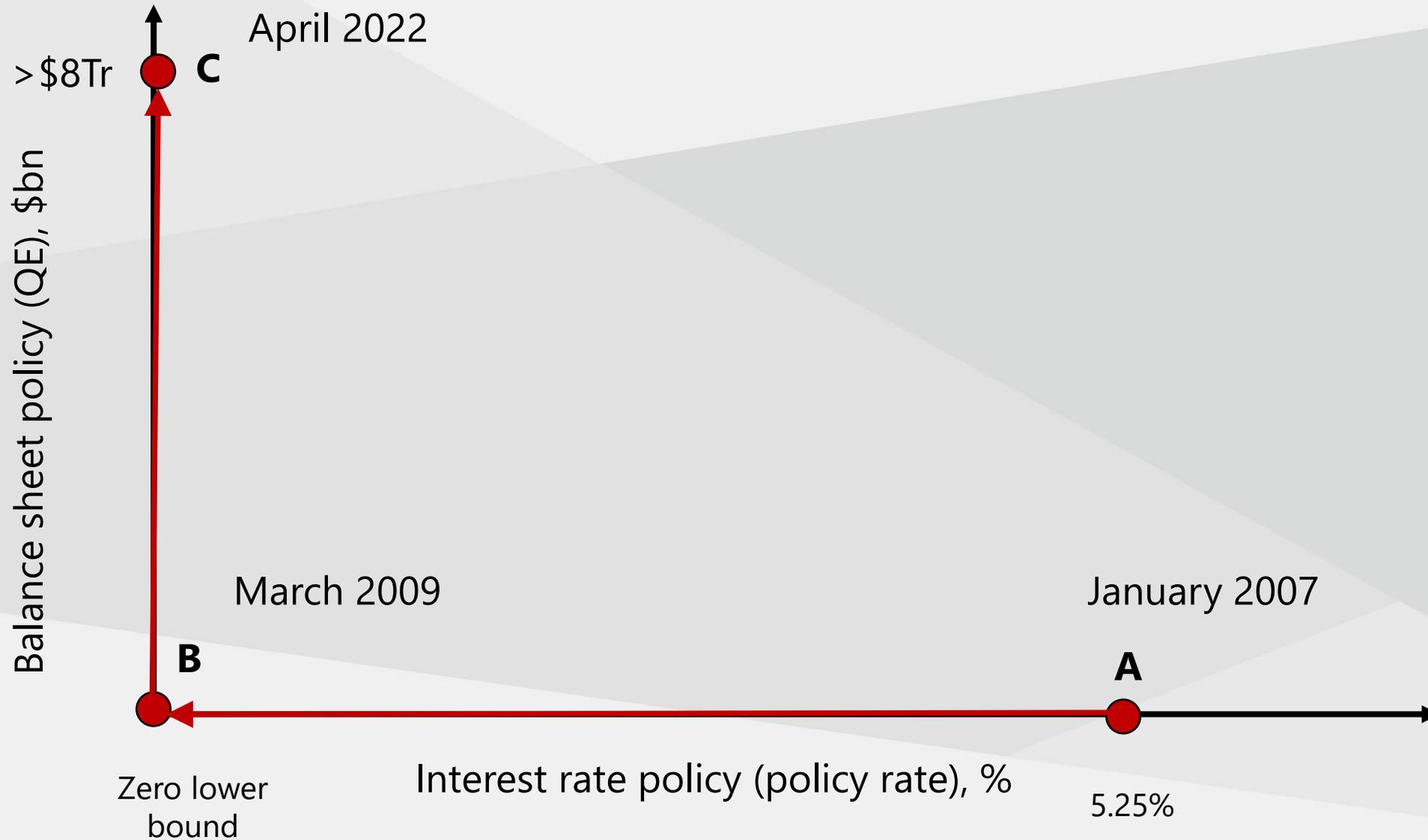
Monetary policy used to be one-dimensional



Once the fed funds rate hit the zero lower bound QE took over

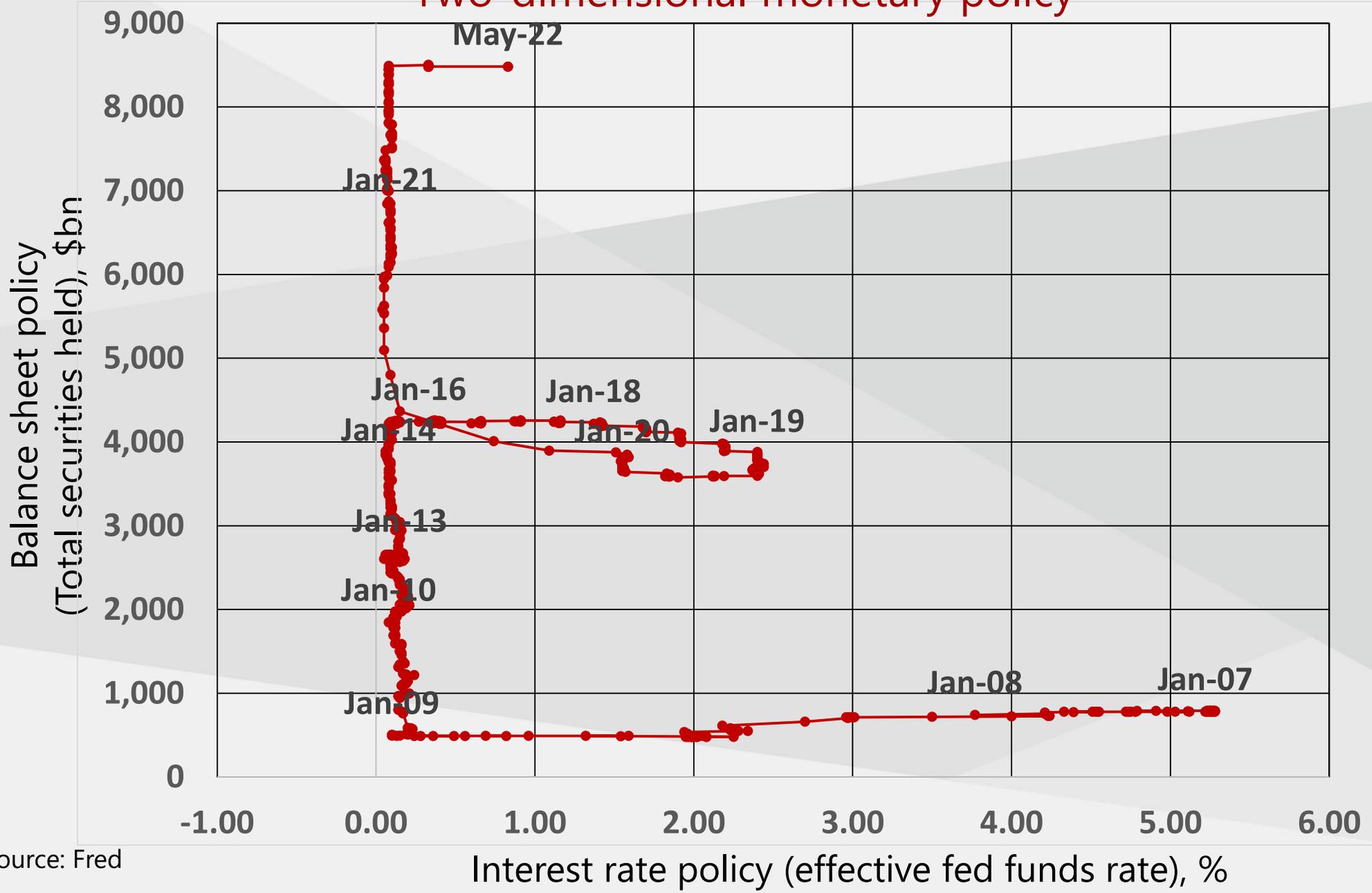


Monetary policy in two dimensions



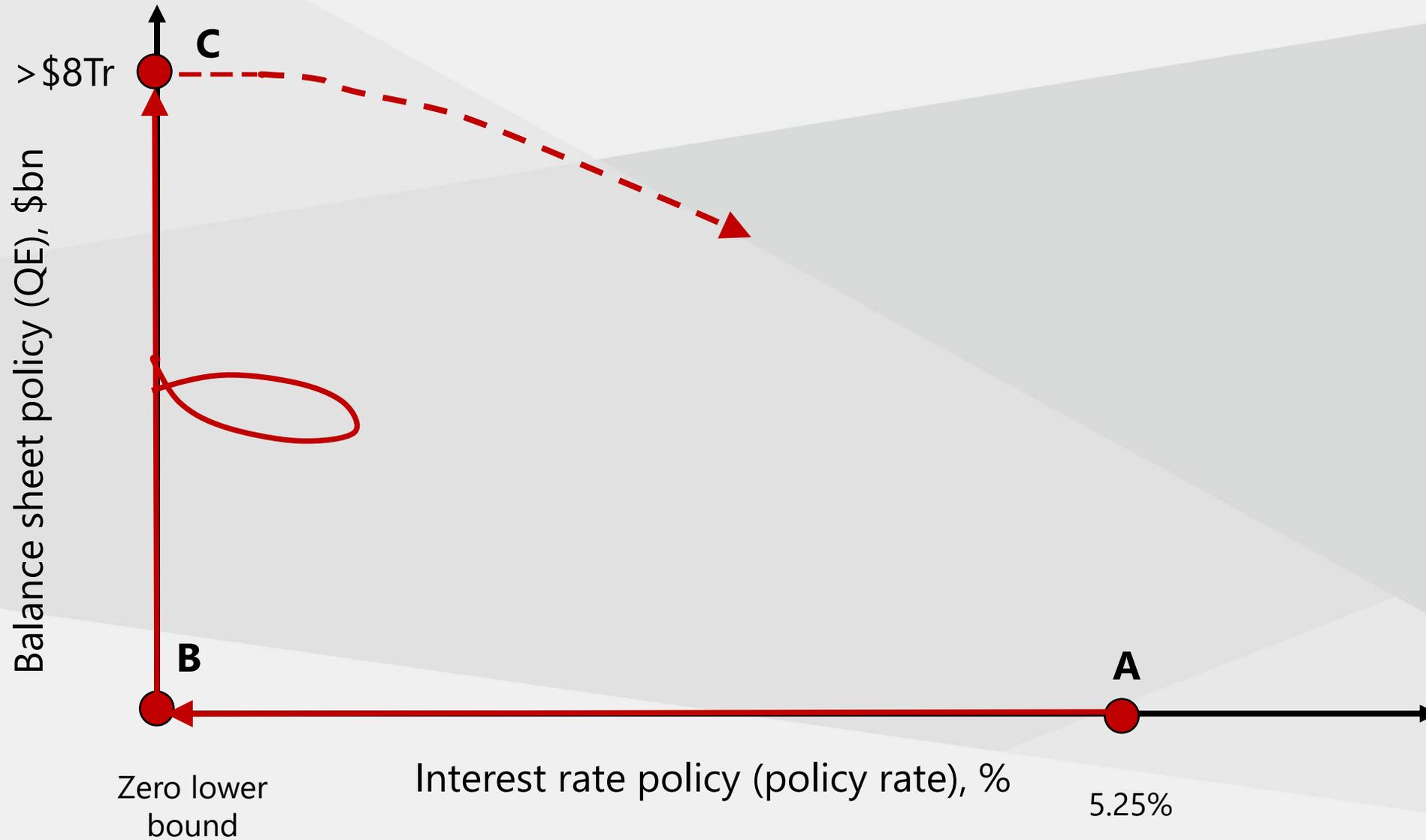
Source: Paul Gruenwald: A Future For QE: Monetary Policy In Two Dimensions (2019)

Two-dimensional monetary policy

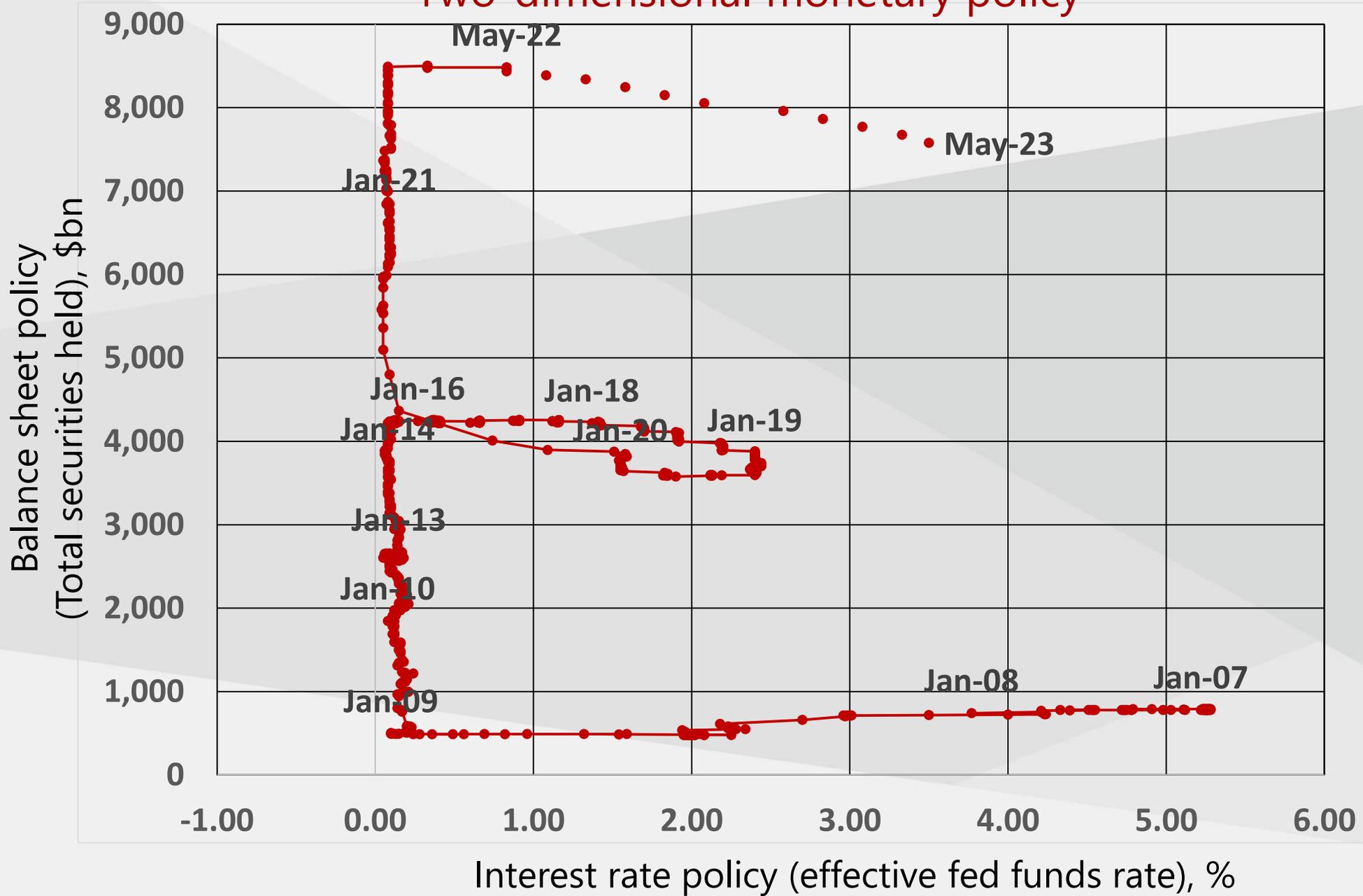


Source: Fred

What happens next?

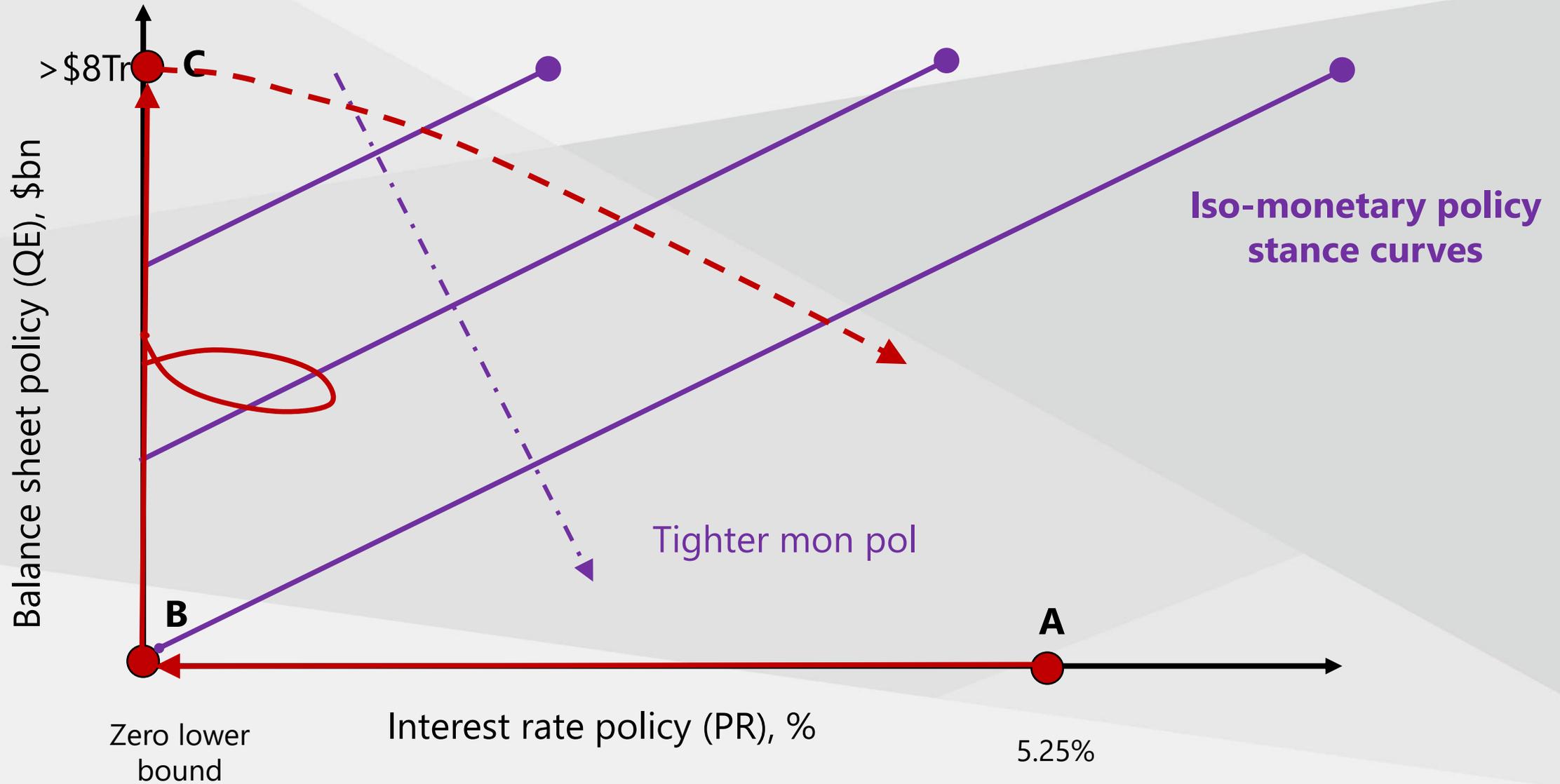


Two-dimensional monetary policy



Monetary policy stance

$$MPS(t) = PR(t) - \gamma QE(t)$$



What is gamma? How big is gamma?

$$\Delta\text{MPS}(t) = \Delta\text{PR}(t) - \gamma \cdot \Delta\text{QE}(t)$$

- Chair Powell's Press Conference on 4 May 2022c
 - "In terms of the effect, I mean, I would just stress how uncertain the effect is of shrinking the balance sheet? ... You know, people estimate that broadly on the path we're on, and this is -- **this will be taken, probably too seriously. But sort of one quarter percent, one rate increase over the course of a year at this pace.** But I would just say with very wide **uncertainty bands, very wide.**"
- The reduction June 22 – June 23 ~ - \$1 trillion
- $\gamma = 25$ bps/trillion

Fedwatchers

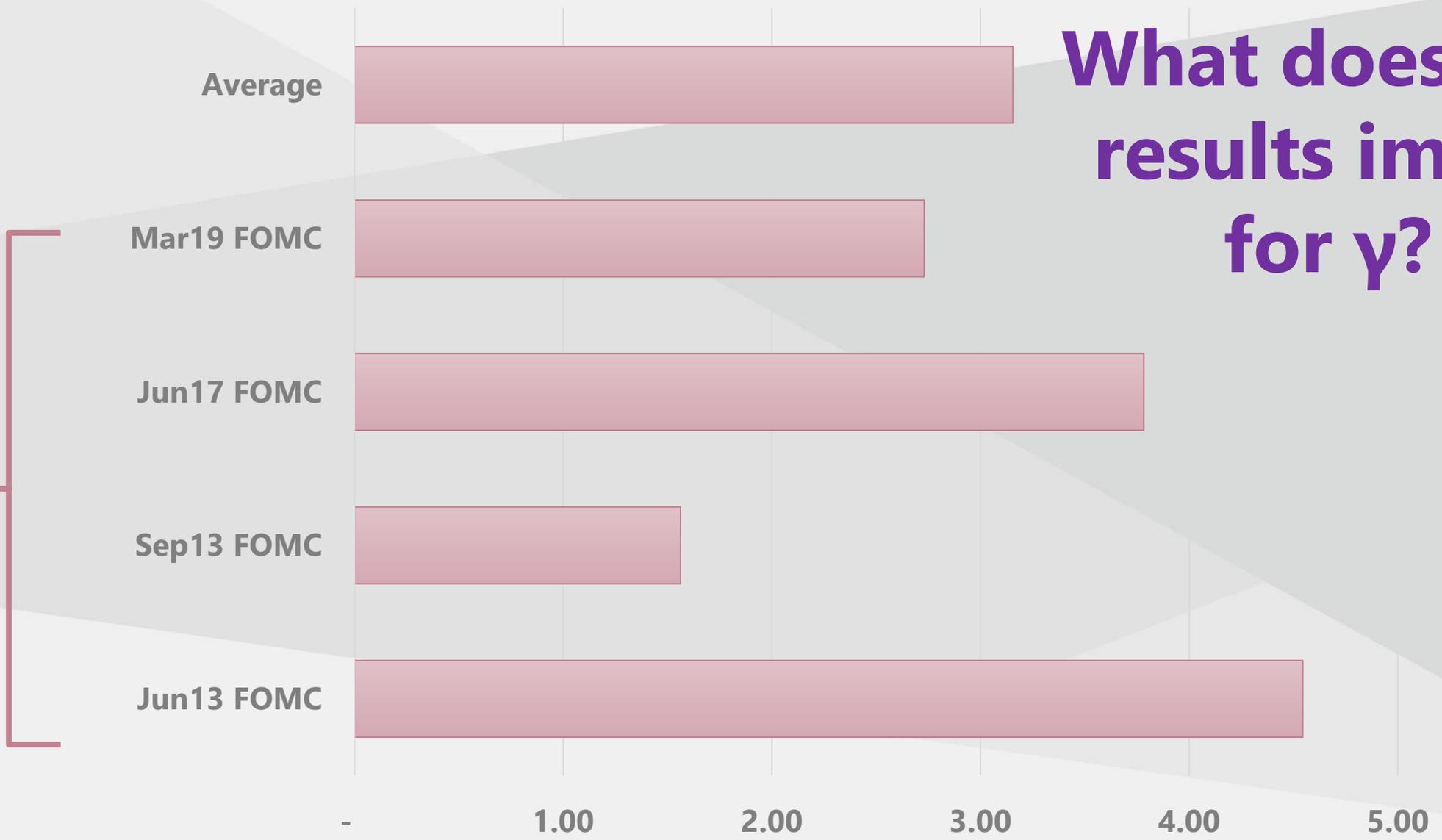
... QT's direct impact on yields—involves **heroic guesstimates**. Some analysts think the Fed will shrink its balance-sheet by **\$3trn over the next three years** (taking it to about 20% of gdp, down from 36% now). **Mark Cabana** of Bank of America reckons this could equate to anywhere between a **quarter point and 1.25 percentage points of rate increases** —a remarkably wide range. Mr Powell has also noted the uncertainty about QT: “We have a much better sense, frankly, of how rate increases affect financial conditions.”

The Economist, Apr 9th 2022

Treasury yield sensitivity to \$100 bn QT (in basis points)

What does the results imply for γ ?

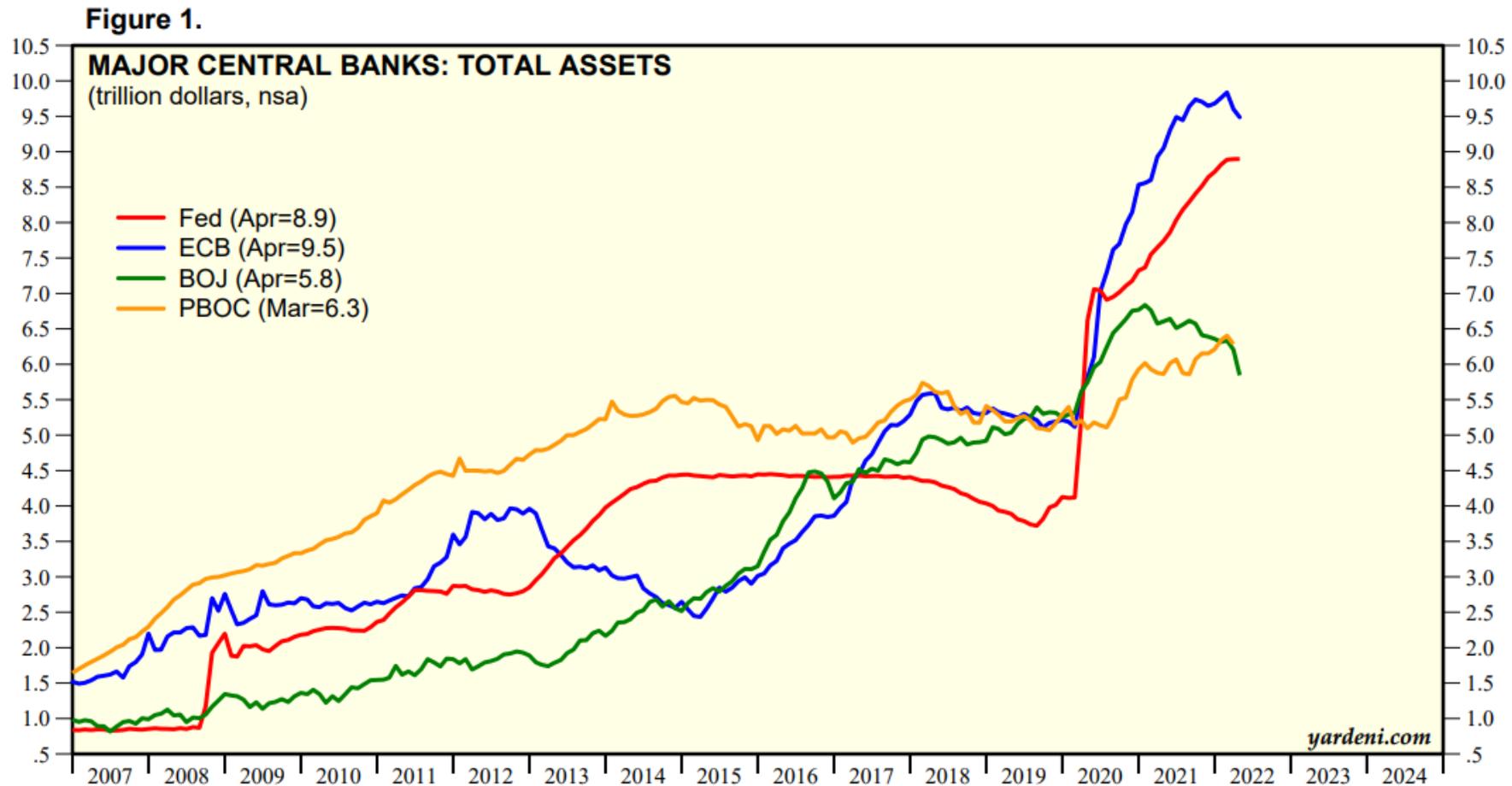
QT1



The rest of the world

Unlike baseball QE is not just a US phenomenon

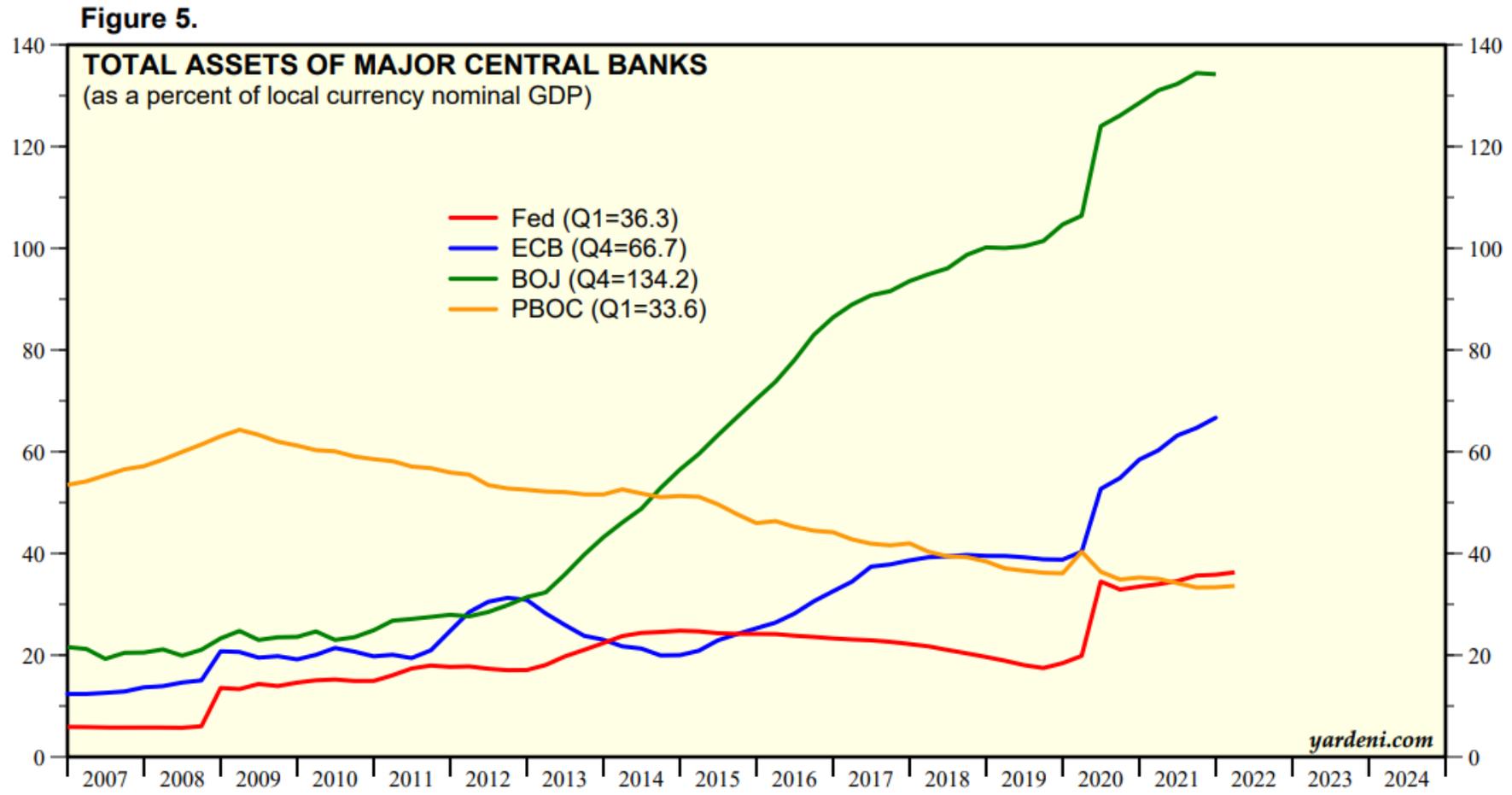
Total Assets of Major Central Banks



Source: Haver Analytics.

Unlike baseball QE is not just a US phenomnon

Total Assets of Major Central Banks



Source: Haver Analytics.

yardeni.com

Monetary policy implementation in the future



PROJECT JURA

Cross-border settlement using wholesale CBDC

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BANQUE NATIONALE SUISSE
BANCA NAZIONALE SVIZZERA
BANCA NAZIONALE SVIZRA
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EUROSYSTEME