

International Bank Lending Channel of Monetary Policy

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Summary

- **Research Question:**

The effect of monetary policy on cross-border bank lending flows

- **Two potential channels with contrasting effects:**

bank lending channel vs. portfolio channel

- **Existing empirical literature:** mixed findings

Bruno and Shin (2015), Ghosh et al. (2014)

Cerutti et al. (2017), Correa et al. (2017), Avdjiev et al. (2018)

Innovations

- **Use exogenous monetary policy shocks:** Romer and Romer (2004), Coibion (2012), Furceri et al., (2018)
- **Apply the local projection method (Jordà, 2005) to estimate the cross-border banking lending effect**
- **Explore nonlinear effects of monetary shocks**

Main Findings

- Monetary tightening in source economies leads to a significant decline in cross-border bank lending. This holds for the U.S. and for the other advanced economies.
- The effects are larger during periods of low global risks or when lending towards emerging market borrowers.
- The degree of spillovers does not depend on a recipient country's exchange rate regime or capital account openness. But some evidence for the trilemma when the exchange rate regime and capital account openness are jointly considered.

Main Comment: Other Channels

A negative association b/w monetary tightening in the source country and cross-border bank lending can be explained by other channels.

Bank lending volume is an equilibrium outcome affected by both supply and demand. The current analysis (and also many previous ones) focus mainly on the supply side.

But U.S. monetary policy can also affect the demand side. To the extent a U.S. monetary tightening affects domestic monetary policy stance and, in turn, local firms' investment decisions, it will result in a reduced demand for bank loans and thus a lower equilibrium bank lending volume. This channel is also consistent with the paper's finding regarding the trilemma (a stronger effect for host economies with a lower degree of monetary autonomy).

Main Comment: Other Channels

Consider also a balance sheet channel. To the extent a U.S. monetary tightening affects domestic monetary policy stance and local firms' balance sheets, it will result in an increased external finance premium for local firms and, in turn, a reduced bank lending to local firms from both domestic and global banks. Again, this channel is also consistent with the paper's finding regarding the trilemma.

Finally, the bank lending channel does not necessarily predict a negative association b/w monetary tightening in the source country and the volume of cross-border lending. Imagine a U.S. tightening that results in a domestic tight credit environment for a host country with limited monetary autonomy. It may reduce domestic bank lending but can in theory increase lending of global banks as the latter has comparative advantages in obtaining funding. This substitution effect is not considered in the current analysis.

Minor Comments

- Sample period: 1990Q1 – 2012Q4 (for US), 2001Q1 – 2012Q4 for others
 - 1) The monetary shock data of Romer and Romer (2004) dates back to the late 1960s. Why not use a longer period?
 - 2) The inclusion of the global financial crisis period causes complications. Whether the Romer and Romer method can be applied to the shadow federal funds rate is an issue. Also, there was a severe liquidity crunch happened at the same time of monetary easing, making the identification more difficult.

Minor Comments

- A contribution of this study is the use exogenous monetary shocks

But what is the rationale? It would better to provide some discussions on why, in the scenario of cross-border bank lending, the use of exogenous shocks in the source countries is crucial and, especially, why in theory we should expect a different result (compared to previous studies).