Discussion of
“The Spillovers, Interactions, and (Un)intended Consequences of Monetary and Regulatory Policies ”
by
K. Forbes, D. Reinhardt and T. Wiedalek

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The views expressed are my own and not necessarily those of the ECB or the Eurosystem.

What is this paper about?

- **Stylized facts:**
  - **Sharp decline in international bank lending, particularly bank-to-bank lending**
  - **…but relative stability in domestic bank lending in the UK**

- **Some explanation in the earlier literature:**
  - **Government intervention (Rose and Wiedalek, 2014)**
  - **Flight home effect (Giannetti and Laeven, 2011)**
  - **Unconventional MPs (Butt, Churm and McMahon 2015)**
    - **No evidence that QE boosted UK bank lending via the bank lending channel**

What is this paper about?

- **Main question here: were regulatory and unconventional monetary policies the driving forces behind financial deglobalisation?**
- **Problem of identification:**
  - **Clustering of different policies: simultaneous launch of unconventional monetary policies and tightening of regulatory policies**
  - **Difficult to distinguish changes in cross-border demand and supply**
  - **Data issues**
- **This paper: unique dataset for the UK**
  - **External bank lending by country (bank-country-time panel)**
  - **Data on regulatory and unconventional monetary policies**

What is this paper about?

- **Policies:**
  - **Regulation: Focus on Pillar 2 policies**
  - **Funding for Lending (FLS; dummy from 2012 Q2) and QE (actual purchases from 2009Q1)**
- **Results:**
  - **Increasing bank's capital requirement (Pillar 2) by 100 bsp leads to a contraction of external lending of about 3.4 %**
  - **Interaction FLS/ regulatory policies significant (for all banks)**
  - **For FLS specialised banks increase is amplified**
  - **Results less significant only for the full FLS programme (including PNFC and <u>household</u> lending).**
  - **Negative impact is only present for international bank-to-bank lending (but not bank-to-nonbank).**
  - **Back of the envelope calculation: <u>*UK external lending 30 percent lower due to suggested policies*</u>**

Comments

- **Relationship with the existing literature on the global impact of UMP and (macro)prudential instruments**
- **Pillar 2 vs. bank restructuring**
- **Some further methodological comments**

International spillovers of UMP

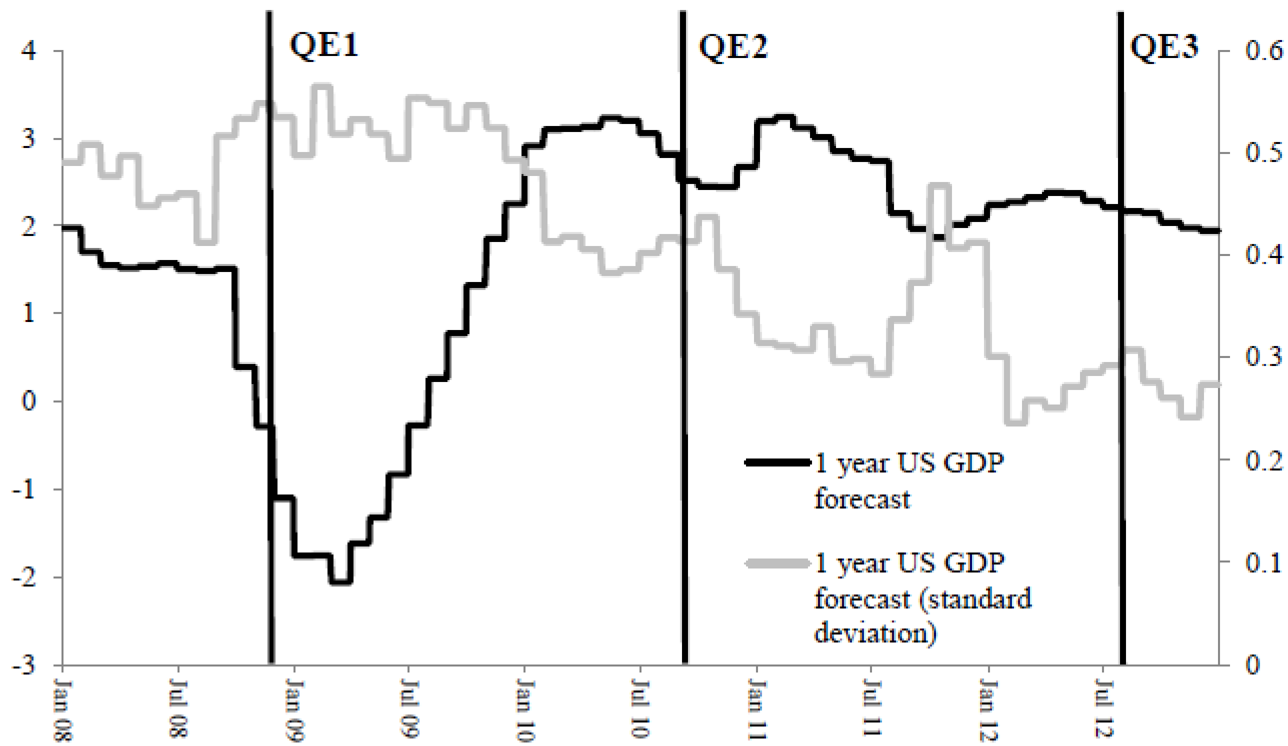
- Literature: mainly on the impact of outright purchases rather than credit operations.
- So far relatively more focus on the domestic effects, only a few studies on the on international spillovers of UMP
  - Neely (2010) – yields in advanced economies (event study)
  - Chen, Filardo, He, Zhu (2012), BIS WP66 – asset prices (event study) and macro (VAR)
  - Leduc (2012), JIMF – commodities (event study)
  - Bauer and Neely (2013), JIMF – channels (event study)

International spillovers: Fed's QE

- US QE policies affected global asset prices, capital flows and exchange rates. (Fratzscher, Lo Duca and Straub, 2015).
- State-dependent impact of QE.
  - QEI: Portfolio rebalancing into the US (out of bonds into equity)
    - In line with Forbes, Reinhardt and Wiedalek (2015)
  - QE2/3: Portfolio rebalancing out of the US (into EME equity and other AEs bond flow)
    - In contrast to Forbes, Reinhardt and Wiedalek (2015)
  - Interaction with macroeconomic risk is significant

The role of risk and the business cycle

US GDP forecast and uncertainty (standard deviation) around the forecast



Source: Fratzscher, Lo Duca and Straub (2015)

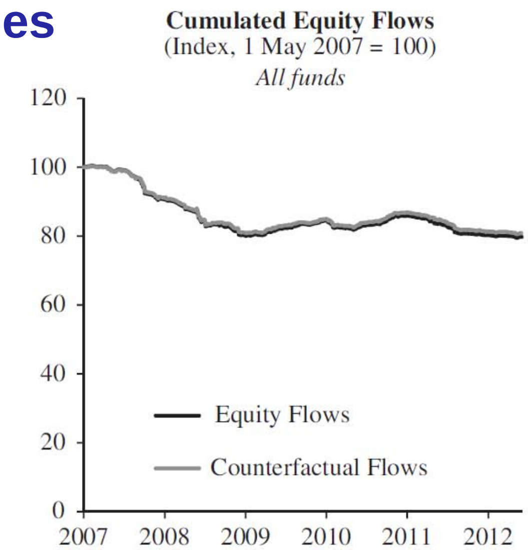
International spillovers: ECB's UMP

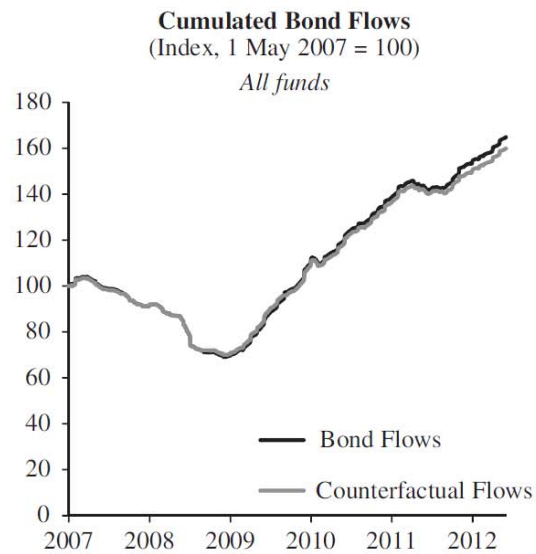
- **Positive impact on market confidence (decrease in implied volatilities) and other risk measures (sovereign and bank CDS spreads) in the euro area (Fratzscher, Lo Duca and Straub, 2015 b).**

- **Little response of international portfolio flows to ECB policies (no global portfolio rebalancing).**

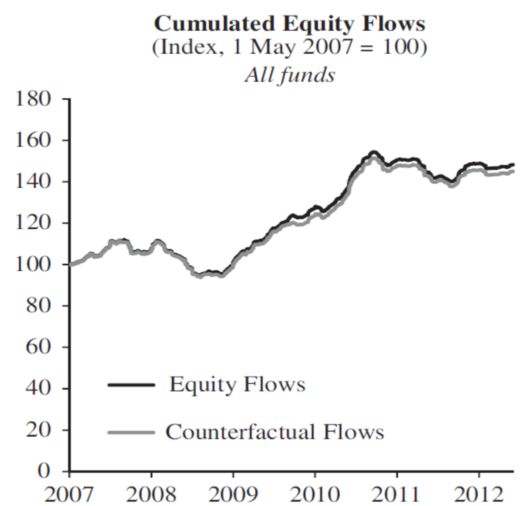
Capital flows and counterfactual flows

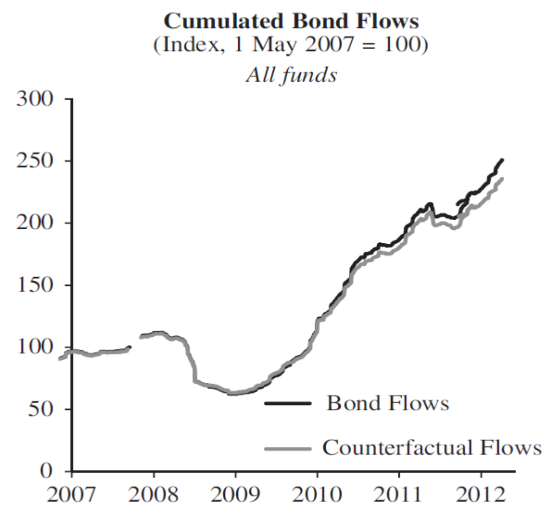
Advanced Economies





Emerging Markets



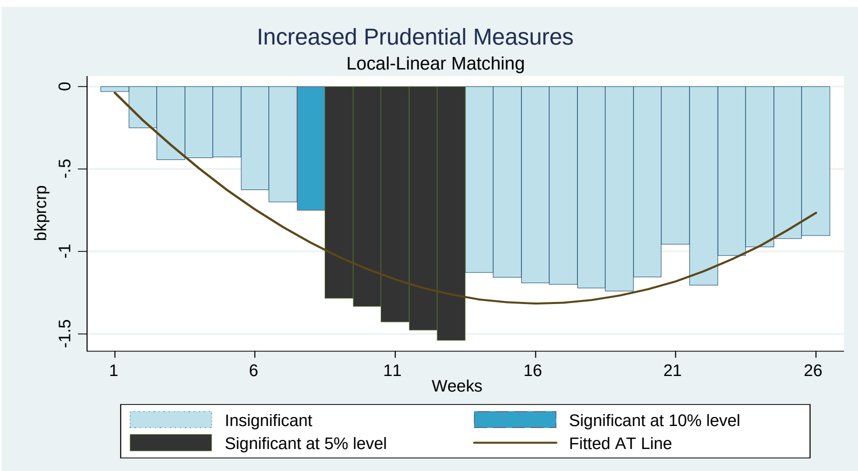


Source: Fratzscher, Lo Duca and Straub (2016)

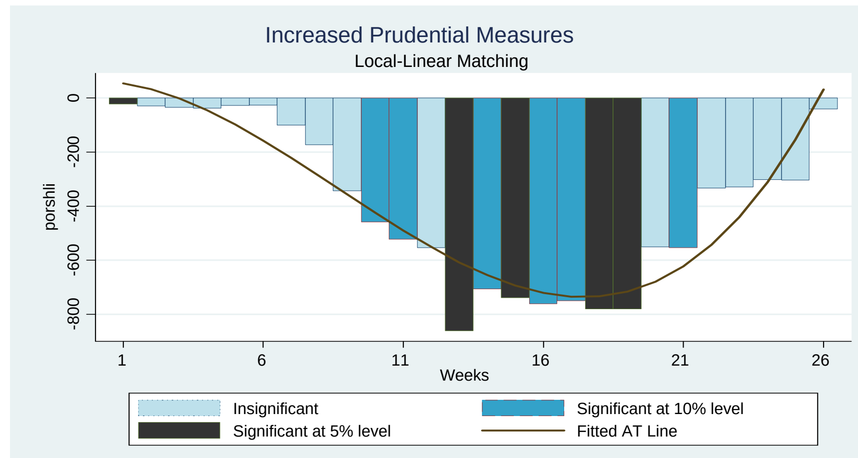
Macroprudential policies can be effective

- **Prudential measure related to international transactions reduce bank leverage, credit growth and portfolio liabilities (Forbes, Fratzscher and Straub, 2015).**

% Change in Bank Credit



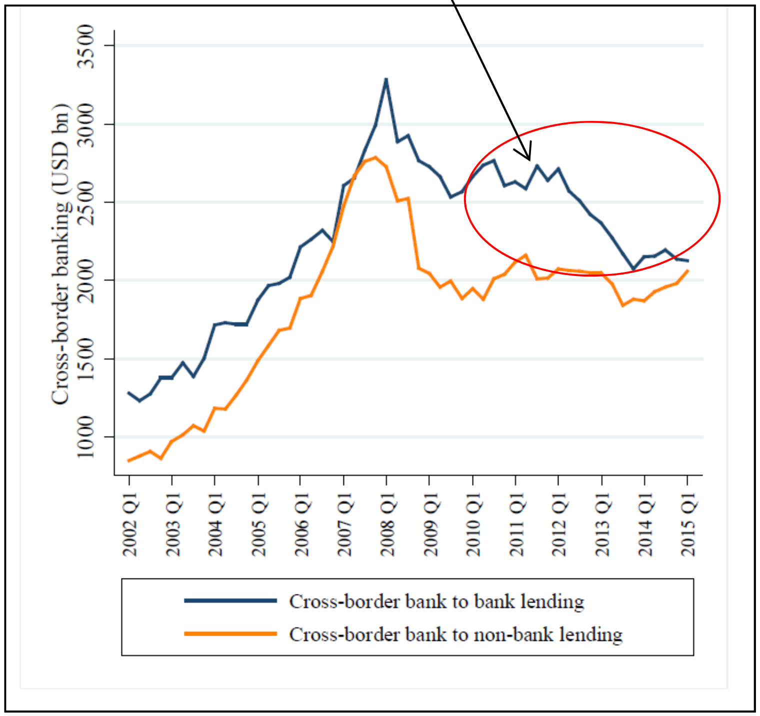
Change in Exposure to Portfolio Liabilities



Source: Forbes, Fratzscher and Straub (2015).

Trends in cross-border banking

- **Change in trend in cross-border bank-to-bank lending**



Source: Forbes, Reinhardt and Wiedalek (2015)

Pillar 2 vs. bank restructuring

- **From 2009 onwards substantial restructuring of business models**
- **Example: RBS state aid case, 12/2009; other banks also affected.** (http://ec.europa.eu/competition/state_aid/cases/233798/233798_1093298_30_2.pdf)
- **A few quotes:**

"RBS will centre on the UK retail and SME corporate banking business while retaining a more focused global operation. It plans to exit retail and commercial banking outside the UK, Ireland and USA".

"According to RBS's restructuring plan, the Global Banking & Markets Division is undergoing the most fundamental change of all RBS business division's".

"RBS's representation in approximately 40 of the 54 countries in which it currently operates will be significantly reduced and sold, including existing completely from retail and commercial businesses in nine Asian and Middle Eastern markets and from wholesale activities in four Asian and four Latin American markets…"

Further comments

- **Exogeneity of Pillar 2: "majority of Pillar 2 requirements are due to non-balance sheet risk."**
  - **Stand in contrast to the original idea of Pillar 2.**
  - **EBA: *"The underlying aim of the Pillar 2 processes is to enhance the link between an institution's risk profile, its risk management and risk mitigation systems, and its capital (EBA, 2006)".***

- **Only Pillar 2 tightening is modelled (justification in footnote 24).**
  - **Problem of censoring.**
  - **Inefficient: throwing away a set of information.**