Discussion of Signe Krogstrup “Negative Interest Rates”

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Hutchins Center
Brookings Institution

Three questions to frame the discussion

» Krogstrup's presentation covers a broad set of issues.

» Three particular areas seem worthy to help frame the rest of the day's discussion.

- Is the debate about negative rates confounding a debate about monetary policy more generally?
- Do we have enough theoretical understanding of the transmission mechanism to assess the criticism of negative rates?
- Is the U.S. a different case and how important is market structure?

General question about negative rates and monetary policy

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- How much of the debate and criticism surrounding negative rates is a more general debate about the effectiveness of monetary policy?
- The "neutral rate" is likely much lower than historically. Monetary policy may be less effective for a given nominal setting than in the past.
- Are there limits to intertemporal substitution (and therefore monetary policy) independent of negative rates?

- What is "success" for policy? Signe notes that money market rates react to negative rates, just like traditional policy. Can negative rates be successful but monetary policy not be as effective on real outcomes?

We need more theoretical discussion to assess the criticism.

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- Are banks—through their net interest margin—actually harmed beyond the short run?
  - Over time, might banks (and the public) re-think their business models?
  - In the US, until recently, demand deposits paid no interest yet charged fees.
  - Recently , banks have shed “non-operating deposits” because they were costly.
- What explains the differential response of banks to negative rates?
  - Some banks have raised rates/spreads on some loans in response.
  - In a competitive model, would expect banks to compete for loans, pushing down yields. Raising rates would reduce higher-yielding assets at a given bank.
- Are negative rates worse than LSAPs for banks?
  - Historically, a flat curve was seen as bad for bank profits. LSAPs flatten the curve.
  - Cutting rates has historically steepened the curve. Negative rates cut rates.

Is the U.S. different?

- How much does the market structure matter? Is the U.S. different because it is less bank centric than other economies?
- Somewhat ironically, the U.S. did not resort to negative rates, and yet the arguments about the costs to transmission through the banking system may be less applicable.
- The arguments in the U.S. were largely about money market functioning, and yet recent experience has suggested that the transmission to money markets works well.
- The role of money funds, however, is different in the U.S.
- Is it clear how credit easing and negative rates work in tandem?