The Heterogeneous Bank Lending Channel of Monetary Policy
DISCUSSION

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Paper in brief

- **Structural (quantitative) HA-GE model**
  - studies the role of bank heterogeneity in the transmission of monetary policy, through the bank lending channel
  - calibrated to the euro area: ideal laboratory (country specific institutional arrangements)
    - Matches many cross-section and time-series moments well …except for the distribution of capital
  - two layers of heterogeneity:
    - ex-ante (exogenous) differences in loan pricing
    - ex-post (endogenous) variation in capital buffers (ratios) driven by idiosyncratic default risks (and banks optimal behaviour)
- **Findings:**
  - The elasticity of new lending to monetary policy is one-third larger in fixed-rate economies (stronger credit channel)
  - Highly leveraged banks drive these differences:
- **Mechanism:**
  - Monetary tightening causes more severe net interest margin compression for fixed-banks, than float-banks
    - as funding costs rise while income from legacy loans remains unchanged,
  - Thus more capital erosion, thus deeper lending contractions (credit channel).
  - The more so the more leveraged the banks, closer to regulatory constraint (interacting with default risk)
- **Policy implications:**
  - Additional tradeoff between monetary policy and financial stability,
  - Support for gradual monetary policy
  - Fundamental limitations of representative-agent banking models.

My comments

- **Main driver: heterogeneity in interest rate exposure.** Two major doubts:
  - is it really there? Banks swap it out on IRS market. Gray scale not black and white.
  - Exogenous Fixed/floating rate is unrealistic. If truly driven by institutional arrangements, such large consequences for credit channel should lead to mend such market failure (eg outlaw fixed rate). Truly driven by consumer demand.
- **Cannot match cross section of capital positions.**
  - I don't buy it is "down the line of calibration":
    - The action of your model comes from the interaction of randomness of defaults with capital constraint
    - in simulations, most banks are close to the capital constraint
    - your large fixed/float differential in credit channel is driven by this bias in the distribution
  - Cannot match because your bank capital has no market
    - Banks are risk neutral
    - Consumers own banks, are risk averse, but ignore bank capital risk as it has no price
    - If there was capital market, it would discipline bank capital well before regulatory requirements
- **You explain the "mechanism" during a monetary tightening.**
  Would it be different during easing? My guess: **YES**.
  - Fixed-Banks would now gain more than Floating-Banks
  - As capital constraint is asymmetric, during easing credit channel stronger for Floating Banks.