Monetary Policy Lessons from the Global Crisis

Introduction to a Special Issue of the International Journal of Central Banking

Giancarlo Corsetti, Andrew Levin, Frank Smets, and Carl Walsh

The global crisis of 2007–09 led central banks to employ an array of traditional and non-traditional monetary policy tools. Many central banks cut policy rates to levels close to zero, and a few of them provided explicit forward guidance about the anticipated future path of policy rates. Some followed a quantitative easing strategy, while others took actions aimed specifically at improving conditions in private credit markets. Finally, with signs of economic recovery becoming evident, central banks refined their exit strategies for unwinding these extraordinary policy measures.

These issues are analyzed in this volume of the *International Journal of Central Banking* (IJCB), which includes the papers, discussions, and commentaries that were presented at the second annual IJCB Monetary Policy Conference that was hosted by the Bank of Japan on September 16–17, 2010. In addition to these contributions, the conference included a keynote speech by Governor Masaaki Shirakawa (Bank of Japan) and a policy panel in which Stephen Cecchetti (Bank for International Settlements), Ryuzo Miyao (Bank of Japan), John Murray (Bank of Canada), Francesco Papadia (European Central Bank), Lars Svensson (Sveriges Riksbank), and John Taylor (Stanford University) discussed the implications of the global crisis for macroeconomic and monetary policy research.

The first two papers in this issue consider the characteristics and effects of *unconventional monetary policies*. One of these papers—"The Financial Market Effects of the Federal Reserve's Large-Scale Asset Purchases" by Joseph Gagnon, Matthew Raskin, Julie Remache, and Brian Sack—presents evidence that the Federal Reserve's large-scale securities purchases that were initiated in late 2008 led to substantial reductions in longer-term interest rates; moreover, those reductions primarily reflected lower risk premiums rather than reduced expectations of future short-term interest rates. This paper is discussed by Tsutomu Watanabe (Hitotsubashi University). The second paper—"On the Quantitative Effects of Unconventional Monetary Policies in Small Open Economies" by Javier

García-Cicco—analyzes such policies in a small open-economy model of the Chilean economy in which the central bank has several distinct policy instruments. This paper is discussed by Kosuke Aoki (Bank of Japan). Lawrence Christiano (Northwestern University) provides broader commentary on the rationale for unconventional monetary policies.

Another pair of papers uses empirical analysis to investigate *the determinants of inflation and inflation expectations*. One of these papers—"Did Easy Money in the Dollar Bloc Fuel the Oil Price Run-Up?" by Christopher Erceg, Luca Guerrieri, and Steven Kamin—uses a dynamic general equilibrium model to analyze how various shocks affect global oil prices in a setting where the currencies of many emerging-market economies are pegged to the U.S. dollar. This paper is discussed by Giancarlo Corsetti (Cambridge University, Rome III, and CEPR). The other paper—"Did the Crisis Affect Inflation Expectations?" by Gabriele Galati, Steven Poelhekke, and Chen Zhou—analyzes daily data on break-even inflation for the euro area, the United Kingdom, and the United States and gauges the extent to which long-run inflation expectations in each economy remained well anchored during the crisis. Shigenori Shiratsuka (Bank of Japan) discusses this paper and presents comparable evidence on the evolution of Japanese long-term inflation expectations. Fumio Hayashi (Hitotsubashi University) provides broader commentary on these issues.

The final pair of papers considers the relationship between *monetary policy and housing booms*. One of these papers—"The Effects of Housing Prices and Monetary Policy in a Currency Union" by Oriol Aspachs-Bracons and Pau Rabanal—uses a New Keynesian model of a currency area with durable goods to investigate the roots of soaring house prices in the case of Spain. Robert King (Boston University) discusses this paper. The other paper—"Risky Mortgages in a DSGE Model" by Chiara Forlati and Luisa Lambertini—develops a model with housing and risky mortgages and finds that economies with less idiosyncratic volatility are characterized by higher loan-to-value ratios and lower rates of mortgage default. This paper is discussed by Tomoyuki Nakajima (Kyoto University). John C. Williams (Federal Reserve Bank of San Francisco) provides broader commentary and explores the factors that may contribute to the onset of a housing bubble.