

Monetary and Macroprudential Policy Research in the Economic Modelling Unit

Economic Modelling Unit, IMF
jbenes@imf.org

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Demand for macroprudential analysis

In the aftermath of the crisis, national policymakers and international regulatory bodies have recently created demand for

- formalising the basic macroprudential policy paradigm
- building simulation tools integrating real and financial sectors
- developing an integrated operational framework for monetary and macroprudential policies

What is macroprudential policy (MacP)?

Halfway between monetary policy (MonP) and microprudential policy (MicP):

- Aims to strengthen the resilience of the domestic financial sector as a whole;
- Not concerned with the health of individual financial institutions;
- Not concerned with the resilience of the real sector.

Sometimes, though, the term MacP is also used in a broader sense (containing the balance sheets of non-financial institutions and households, too).

MacP tools interact with both

- MicP: the design of the tools – regulatory requirements imposed on the balance sheets of financial institutions;
- MonP: the effects of the tools – influencing the banks' marginal lending and borrowing cost.

Pragmatic approach

... needed, at least initially.

Similar to MonP 15 or 20 years ago – no established theoretical paradigm existed at that time, yet a few central banks (BoC, RBNZ) dared to build new policy models (endogenous expectations, endogenous policy). Heaps of ad-hockery, but proved extremely useful and spread out eventually. Economic foundations came gradually.

Modelling balance-sheet effects in a dynamic general equilibrium model is not straightforward. Deeply microfounded approach would be necessarily too restrictive for the design of the rest of the model.

Key bits of the framework we're currently working on...

- Banks as agents with their own net worth bearing macroeconomic risks.
- Dynamic and sectoral capital regulation.
- Maturity transformation, maturity mismatches
- Liquidity requirements.
- Credit growth, credit controls, and asset prices.
- Design of MonP and MacP rules.

Some of the dots still unconnected.

Possible topics for the three days

In a simple SOEMOLI model:

- Review and modify BGG's financial accelerator.
- Simulate credit growth pulled by fundamental and not-so-fundamental factors (productivity, bubbles).
- Introduce a simple extension with banks and bank capital.
- Introduce maturity transformation and maturity mismatches to DSGEs.
- Discuss simple MaP rules.