Chapter 26

Transmission Mechanisms of Monetary Policy: The Evidence
Monetary Transmission Mechanisms

Traditional Interest-Rate Channels
\[ M \uparrow, i \downarrow, I \uparrow, Y \uparrow \]
\[ M \uparrow, P_e \uparrow, \pi^e \uparrow, i_r \downarrow, I \uparrow, Y \uparrow \]

Other Asset Price Channels

*International Trade*
\[ M \uparrow, i \downarrow, E \downarrow, NX \uparrow, Y \uparrow \]

*Tobin’s q*
\[ M \uparrow, P_e \uparrow, q \uparrow, I \uparrow, Y \uparrow \]

*Wealth Effects*
\[ M \uparrow, P_e \uparrow, W \uparrow, C \uparrow, Y \uparrow \]
Credit View

Bank Lending
\[ M \uparrow, \text{deposits} \uparrow, \text{bank loans} \uparrow, I \uparrow, Y \uparrow \]

Balance-Sheet
\[ M \uparrow, P_e \uparrow, \text{adverse selection} \downarrow, \text{moral hazard} \downarrow, \text{lending} \uparrow, \]
\[ I \uparrow, Y \uparrow \]

Cash Flow
\[ M \uparrow, i \downarrow, \text{cash flow} \uparrow, \text{adverse selection} \downarrow, \text{moral hazard} \downarrow, \]
\[ \text{lending} \uparrow, \]
\[ I \uparrow, Y \uparrow \]

Unanticipated Price Level
\[ M \uparrow, \text{unanticipated} P \uparrow, \text{adverse selection} \downarrow, \text{moral hazard} \downarrow, \]
\[ \text{lending} \uparrow, I \uparrow, Y \uparrow \]

Liquidity Effects
\[ M \uparrow, P_e \uparrow, \text{value of financial assets} \uparrow, \text{likelihood of financial distress} \downarrow, \]
\[ \text{consumer durable and housing expenditure} \uparrow, Y \uparrow \]
Lessons for Monetary Policy

1. Dangerous to associate easing or tightening with fall or rise in nominal interest rates.
2. Other asset prices besides short-term debt have information about stance of monetary policy.
3. Monetary policy effective in reviving economy even if short-term interest rates near zero.
4. Avoiding unanticipated fluctuations in price level important: rationale for price stability objective.