



# THE MARGINAL BENEFITS AND COSTS OF HIGHLY EXPANSIONARY MONETARY POLICY

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## Background and conclusions

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- **Focus on the marginal benefits and costs of monetary policy easing, in particular additional QE.**
- **Conclusions in a nutshell:**
  - **Marginal benefits have fallen.**
  - **Marginal costs are increasing.**
  - **The net marginal benefits are likely to differ across OECD economies.**



# **Marginal benefits depend on the state of financial markets and the economy**

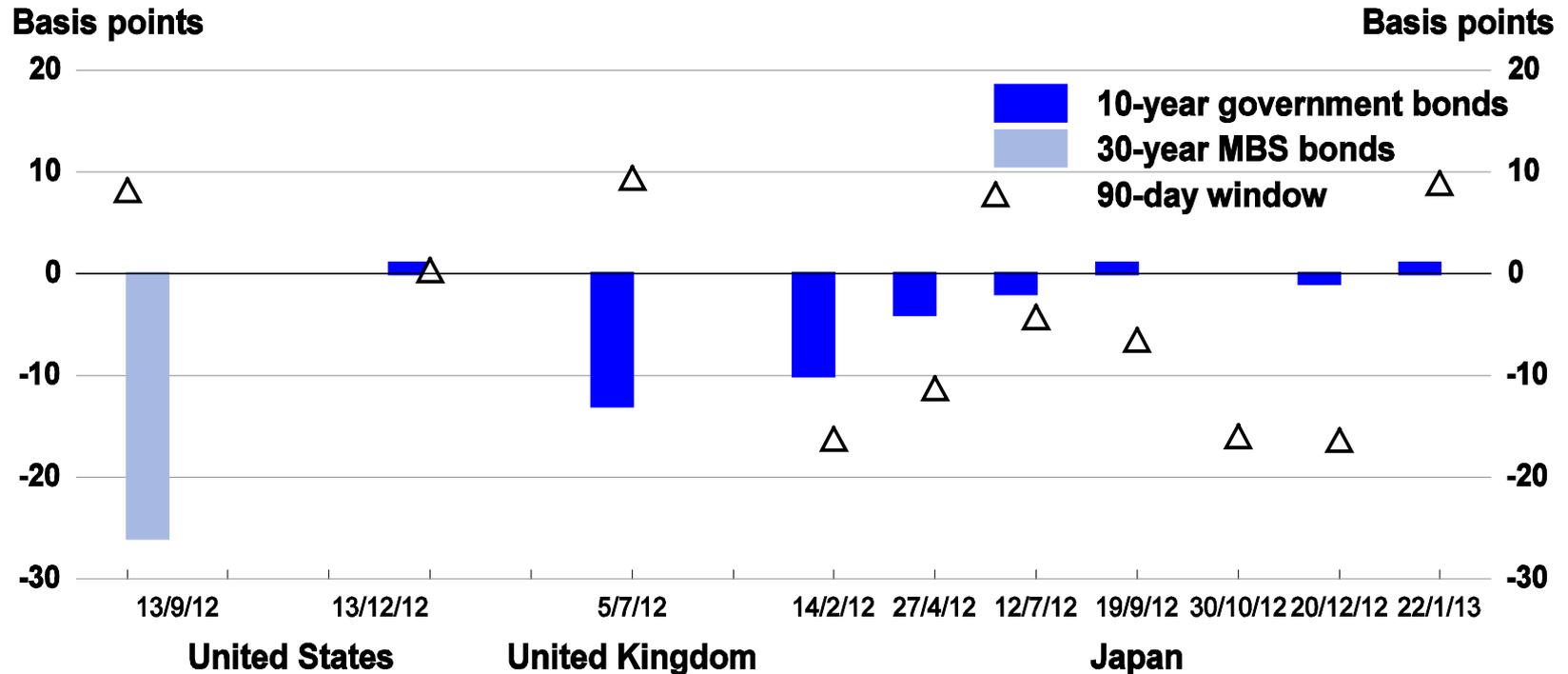
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- **The QE-induced fall in yields and increase in asset prices are likely to be small when asset markets are richly valued.**
- **The benefit of a QE-induced GDP boost is smaller for economies growing at close to potential than for countries in recession and at risk of very low inflation or even deflation.**



# Benefits: Impact of recent QE on bond yields

Changes in bond yields on the announcement of asset purchases and 60 days later



*Notes:* Changes are calculated as a difference in yields between the day of the policy announcement and the day after the announcement.

*Source:* Datastream and OECD calculations.



## Marginal costs may be increasing

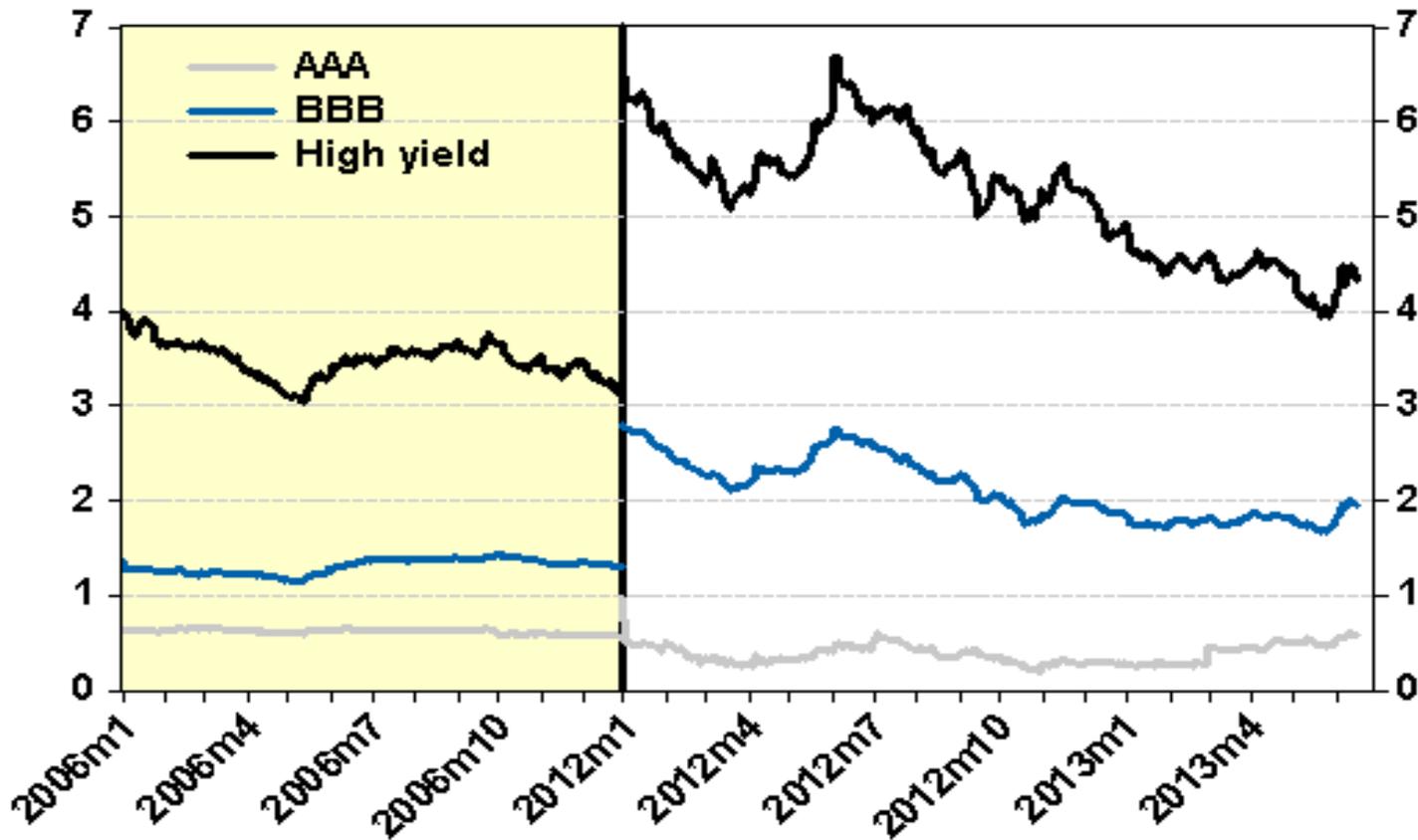
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- **Many different types of costs and most will tend to increase as QE is used more intensively:**
  - **Potential excesses in financial markets as investors search for yields.**
  - **Increased complications of exit as asset holdings of central banks rise from an already high level, notably the risk of bond market instability in the exit phase.**
  - **De-anchoring of inflation expectations as concerns mount about central banks' independence, especially if losses on their purchased assets in the exit phase risk wiping out their capital.**
  - **Ever-greening of non-performing loans.**



# Signs of increased risk-taking

## Corporate bonds: compression of spreads



Source: Datastream.



## **Further signs of increased risk-taking**

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- **Sharply increased issuance of high-yield corporate debt.**
- **Declining underwriting standards: significant increase in covenant-light high-yield loans.**
- **The return of structured products: CLOs (bundles of leveraged buy-out loans and other high leveraged loans).**



# The net marginal benefits of QE at present

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- **Relatively small in the United States.**
  - “... beginning a gradual reduction in the size of additional asset purchases may be warranted in the near future”, OECD Economic Outlook, May 2013
- **Relatively large in Japan ...**
  - “... new quantitative and qualitative monetary easing is appropriate ...” EO, May 2013.
- **... and the euro area.**
  - “Expansion of asset purchases is desirable” EO, May 2013.