

Discussion of:

*Golden Fetters, Paper Fetters
and the Rationale for Eliminating the Effective Lower Bound on
Nominal Interest Rates*

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Overview

- ▶ Interesting paper that covers a lot of ground
 - ▶ I would summarize the arguments in four broad statements:
 1. Physical attributes of the payments instrument can constrain monetary policy
 - ▶ analogies between the gold standard and the effective lower bound
 2. Monetary policy has distributional effects
 - ▶ cost of constraints on policy may fall disproportionately on some groups
 3. Efforts to ease at the ELB may exacerbate these distributional effects
 - ▶ result: the ELB is more costly than you think
 4. A new regime based on CBDC can eliminate the ELB
 - ▶ without eliminating paper currency
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Outline of discussion

- ▶ History
 - ▶ late 19th century
 - ▶ 1930s
 - ▶ today
- ▶ The model
 - ▶ heterogeneity
 - ▶ results and intuition
- ▶ CBDC
 - ▶ fetters of ... what?
 - ▶ is CBDC necessary?
 - ▶ is CBDC equivalent to ~~ELB~~?

Late 19th century

- ▶ Discussion of the distributional effects of the gold standard focuses on the period 1870 – 1900 (the “free silver” movement)
 - ▶ period of deflation and perceived tight credit
 - ▶ benefited creditors, unpopular with borrowers
- ▶ If I were to think of a model that would capture this period:
 - ▶ something in the spirit of Sargent and Wallace (JPE, 1982)
 - ▶ borrowers (farmers) need inputs to produce
 - ▶ lenders have these resources; may want a payments instrument to make purchases
 - ▶ banks lend to borrowers → who use funds to buy inputs from lenders
 - ▶ lenders hold bank deposits; perhaps use them to transact
 - ▶ money in exogenous supply; grows at a given rate (gold?)

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- ▶ Focus on stationary equilibria in which both money and bank deposits have the same real return
 - ▶ If the money growth rate is low:
 - ▶ return on money is high \Rightarrow banks face high cost of funds
 - ▶ “tight credit” \rightarrow good for lenders, bad for borrowers
 - ▶ If the money growth rate is higher:
 - ▶ reverse is true: “loose credit” \rightarrow good for borrowers, bad for lenders
 - ▶ Key point: monetary policy faces a fundamental tension
 - ▶ Should the U.S. have allowed free minting of silver?
 - ▶ doing so may have helped borrowers; hurt lenders
 - ▶ not clear there would have been large macroeconomic gains
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1930s

- ▶ Issue in the great depression period was different (I think)
- ▶ Main story: large macro gains to abandoning the gold standard
 - ▶ would increase inflation, loosen monetary conditions (as before)
 - ▶ which would reverse debt deflation, avoid bank failures, etc.
 - ▶ would seem to call for a different model
- ▶ Presumably there were there also distributional effects ...
 - ▶ moving away from gold would help debtors, hurt creditors (at least initially)
- ▶ ... but these are generally considered to be secondary
 - ▶ the argument for leaving the gold standard was not the need to help debtors at the expense of creditors
 - ▶ but rather: need to promote economic recovery, even if it hurts creditors

Today

Q: Which historical episode better corresponds to the current period?

- ▶ Is the problem with the ELB that it alters interest rates and/or asset prices?
 - ▶ which makes some people worse off and others better off
 - ▶ but may not have much macroeconomic significance (given that unconventional policies are used)
- ▶ Or that it has significant macroeconomic costs?
 - ▶ and also some (secondary?) distributional issues
- ▶ The message of the paper could be clearer on this point
 - ▶ much focus on the free silver era, which I think of emphasizing winners & losers
 - ▶ I understood “golden fetters” to be about the 1930s; macro issues

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Heterogeneity

- ▶ What type of heterogeneity matters in the ELB era?
- ▶ In the 19th century period, I think of borrowers vs. lenders
 - ▶ farmers borrowed to buy land, equipment, seeds, etc.
- ▶ The model has a different focus: savers vs. hand-to-mouth
 - ▶ or, owners of capital vs. workers
- ▶ To what extent is this formulation for technical reasons?
 - ▶ that is, hand-to-mouth consumers have an easy decision problem
- ▶ To what extent is this the relevant type of heterogeneity?
 - ▶ meaning the issue is very different from the free-silver period (I think)
 - ▶ disparate effects come from asset prices rather than interest rates

Results and intuition

- ▶ In the model, presence of an ELB lowers welfare, affects distribution

Q: What are the relative sizes of these effects?

- ▶ Thinking of the discussion above:
 - ▶ to what extent is the effect of removing the ELB largely distributional?
 - ▶ to what extent does it have large macro benefits?
 - ▶ what does the answer tell us about the appropriate historical comparison?
- ▶ The model is very rich; there is a lot going on
 - ▶ I would like to understand the underlying mechanism(s) better

Q: Why does the consumption of hand-to-mouth consumers recover more slowly following a negative shock?

- ▶ is it that savers benefitting from higher asset prices, while hand-to-mouth consumers are not? or are other things going on?
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Fetters of ... what?

- ▶ It is widely understood that the ELB is below zero (-0.5%? more?)
- ▶ But short-term interest rates in the U.S. have remained positive
 - ▶ why?
- ▶ In the aftermath of the financial crisis, a variety of institutional factors were important
 - ▶ MMMFs cannot pay negative interest rates; would shut down
 - ▶ Treasury auctions could not accept negative bids, etc.

*"Why Is There a 'Zero Lower Bound' on Interest Rates?"
Liberty Street Economics Blog, FRBNY, November 2011*

- ⇒ Not clear the ZLB in the U.S. is related to paper currency
- ▶ perhaps the "fetters" are institutional, regulatory
 - ▶ if so, how will the plan proposed here address them?

Is CBDC necessary?

- ▶ Paper proposes removing paper fetters without removing paper money
 - ▶ idea: set interest rate on CBDC < 0 when necessary
 - ▶ and impose fees on large transfers from CBDC to paper money
 - ▶ presumably also will need fees for large transfers from deposits to paper money
- ▶ But ... why do we need CBDC for this?
 - ▶ set IOER negative (\Rightarrow bank deposit rates < 0)
 - ▶ impose fees for large transfers from deposits to paper currency
 - ▶ along the lines of Agarwal & Kimball (2015)
- ▶ Can we remove CBDC from the proposal?
 - ▶ what would we lose in terms of ability to set the desired interest rate?

Is CBDC equivalent to ~~ELB~~?

- ▶ The model is used to evaluate the benefits of removing the ELB
 - ▶ Will introducing CBDC (and fees) will lead to that same outcome?
 - ▶ If people are using CBDC ...
 - ▶ presumably they are holding less of something else. What?
 - ▶ how is the CBDC introduced? How does the CB balance sheet change?
 - ▶ The proposal calls for CBDC to earn the market rate of interest
 - ▶ seems designed to lead to a different outcome than simply ~~ELB~~
 - ▶ how would it affect hand-to-mouth consumers?
 - ▶ For analyzing the effect of introducing a new payment instrument ...
 - ▶ it seems desirable to use a model that includes payment instruments
 - ▶ a literature has developed along these lines; could these effects be combined with your model?
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