

Monetary Policy Uncertainty in the Banking Sector

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Motivation

- Monetary policy uncertainty can impact the credibility and trust in the Fed
- Forward guidance: communicate to make decisions predictable
- Monetary policy uncertainty is recessionary [1]
- Disagreement on the channels of transmission: through bank or firm subjective beliefs?

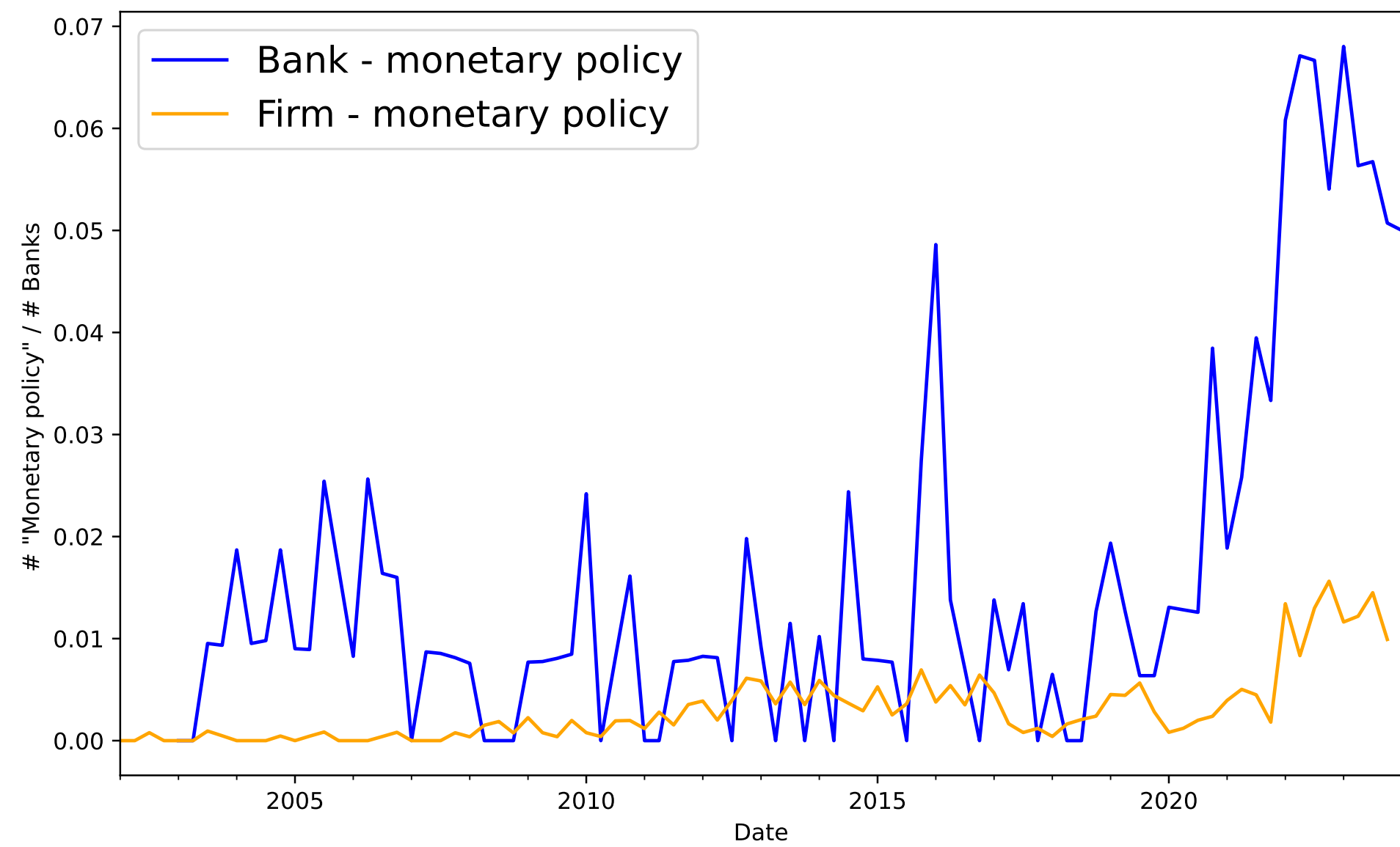


Figure 1: Attention to monetary policy

Research Questions

- 1 What are the macroeconomic implications of perceived aggregate monetary policy uncertainty in the banking sector?
- 2 What role do firm-level subjective beliefs play? Does a direct channel exist at the firm level?
- 3 Is there evidence of a financial friction channel?

Data

The following datasets were used to complete the research:

- 10,957 US bank earnings calls
- 195,732 US firm earnings calls
- Federal Reserve Tealbooks
- Syndicated Loan Transactions from Dealscan

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We need a dictionary of monetary policy words. The Tealbooks are a natural candidate:

- Economic in nature
- Select titles about monetary policy
- Most frequent words in following text are monetary policy bi-grams

I count monetary policy uncertainty following [2]

- Identify a monetary policy bi-gram
- Count risk and uncertainty synonyms within 10 words of the monetary policy bi-gram

Identification Strategy

Sources of endogeneity:

- 1 Economic news affects both bank monetary policy uncertainty (MPU) and monetary policy decisions within quarter
- 2 Monetary policy decisions impact bank MPU within the same quarter

⇒ Focus on monetary policy uncertainty measured on FOMC days

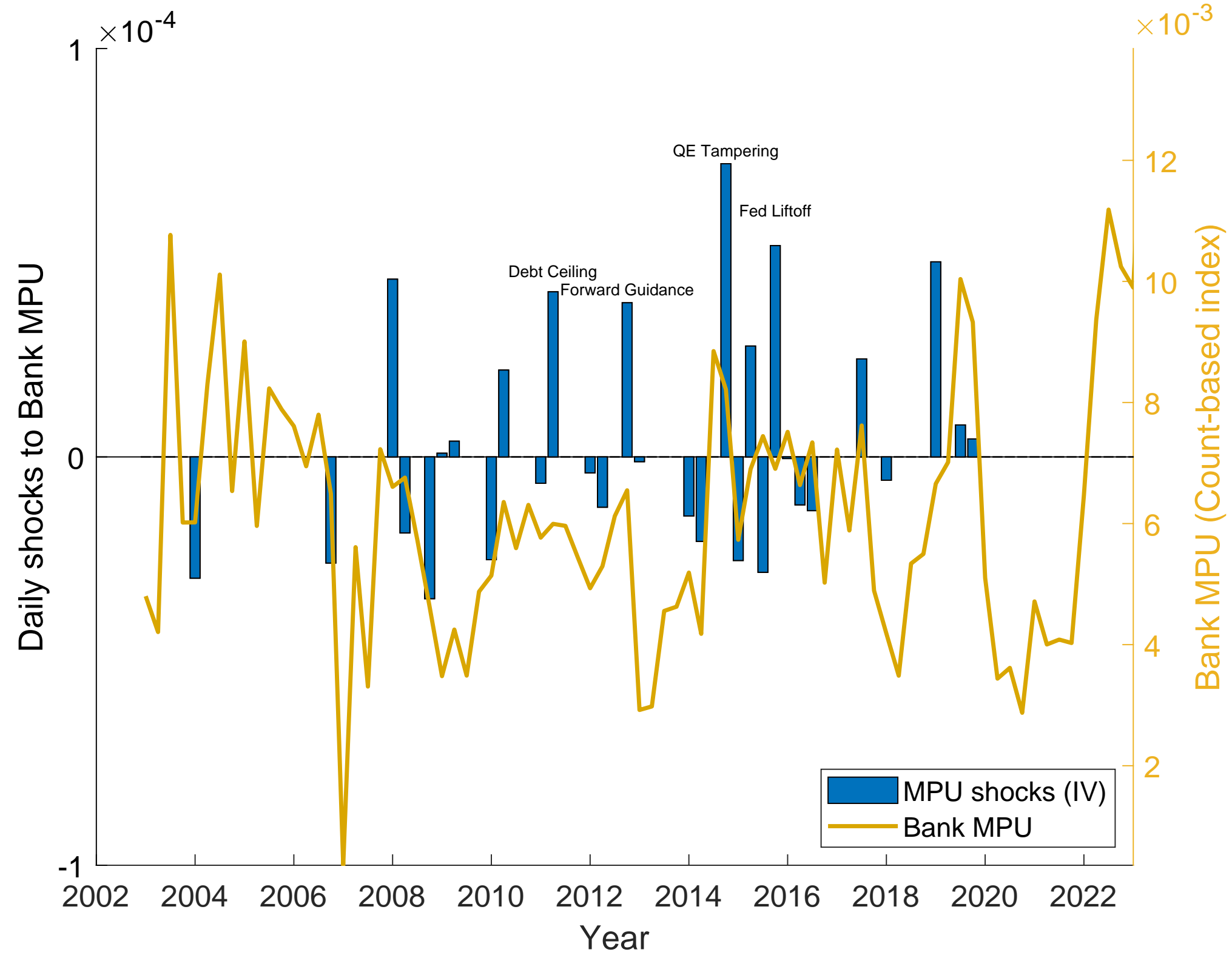


Figure 3: MPU surprises

Macroeconomic Impact

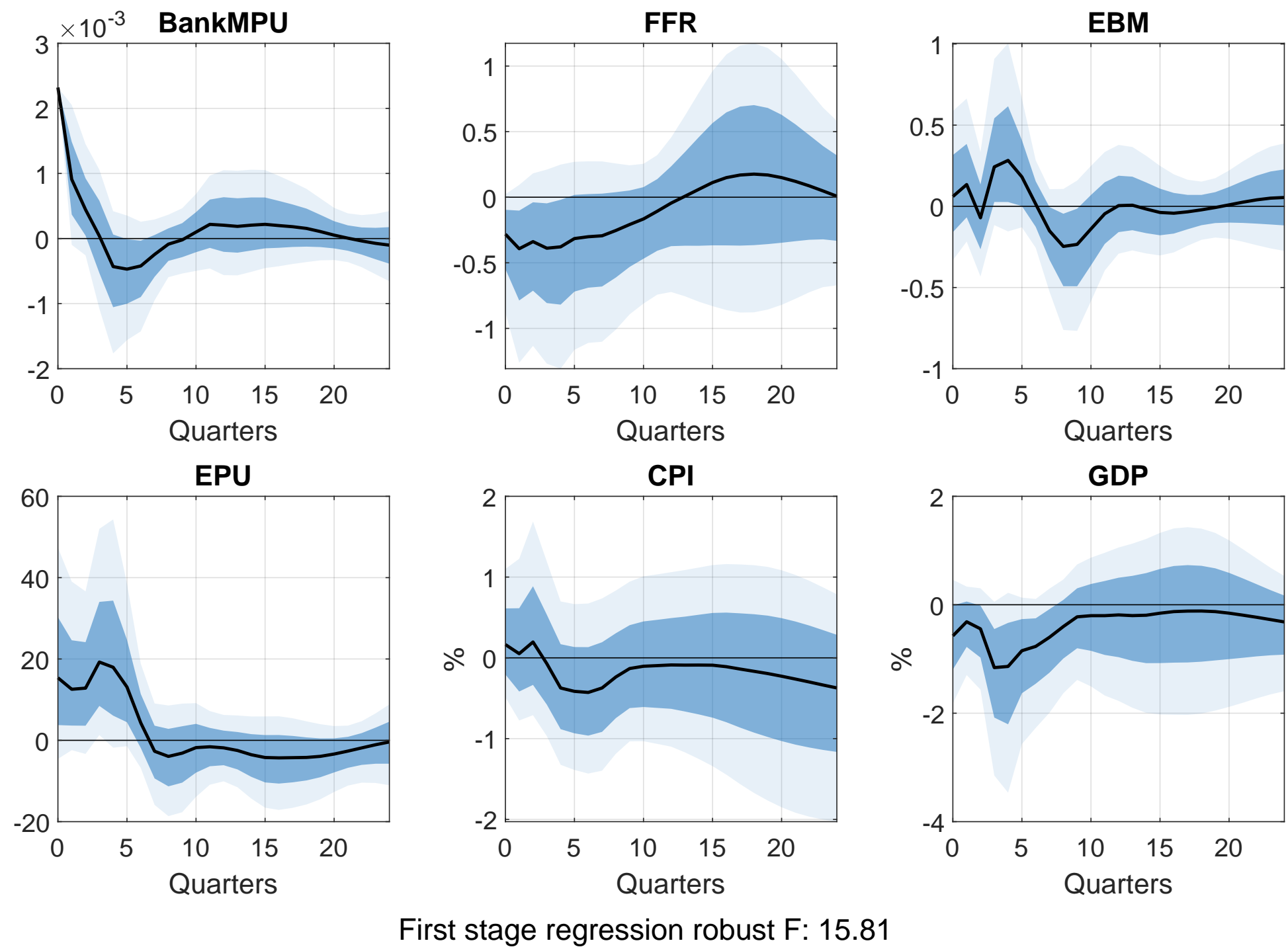


Figure 2: Aggregate Impact

Channels

Table 1: AISD and Bank-level Monetary Policy Uncertainty

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
	AISD	AISD	AISD	AISD	AISD	AISD	AISD
ROA	-0.009 (-0.35)	-0.006 (-0.28)	-0.015 (-0.46)	-0.004 (-0.16)	0.006 (0.17)	-0.014 (-0.76)	0.001 (0.08)
LLP	0.041* (2.03)	0.025* (1.92)	0.029 (0.97)	0.047*** (3.11)	0.029 (0.88)	0.069*** (3.83)	0.011 (1.10)
MPU	0.015*** (5.68)	0.012*** (4.09)	0.007 (1.28)	0.021*** (3.40)	0.050*** (3.59)	0.015** (2.65)	0.008** (2.25)
Bank Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm Controls	No	Yes	No	No	No	No	Yes
Tranche Controls	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Year FE	Yes	Yes	Yes	Yes	Yes	Yes	No
Tranche Type FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Deal Purpose FE	Yes	Yes	No	No	No	Yes	Yes
Ind FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Bank FE	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Firm x Year FE	No	No	No	No	No	No	Yes
Loan Type	Credit Line Term Loan Term Loan B New Borrowers						
N	26,351	24,229	16,927	8,071	3,205	9,555	22,543
R2	0.435	0.461	0.485	0.355	0.317	0.467	0.843

Standardized beta coefficients; t statistics in parentheses
* p < 0.10, ** p < 0.05, *** p < 0.01

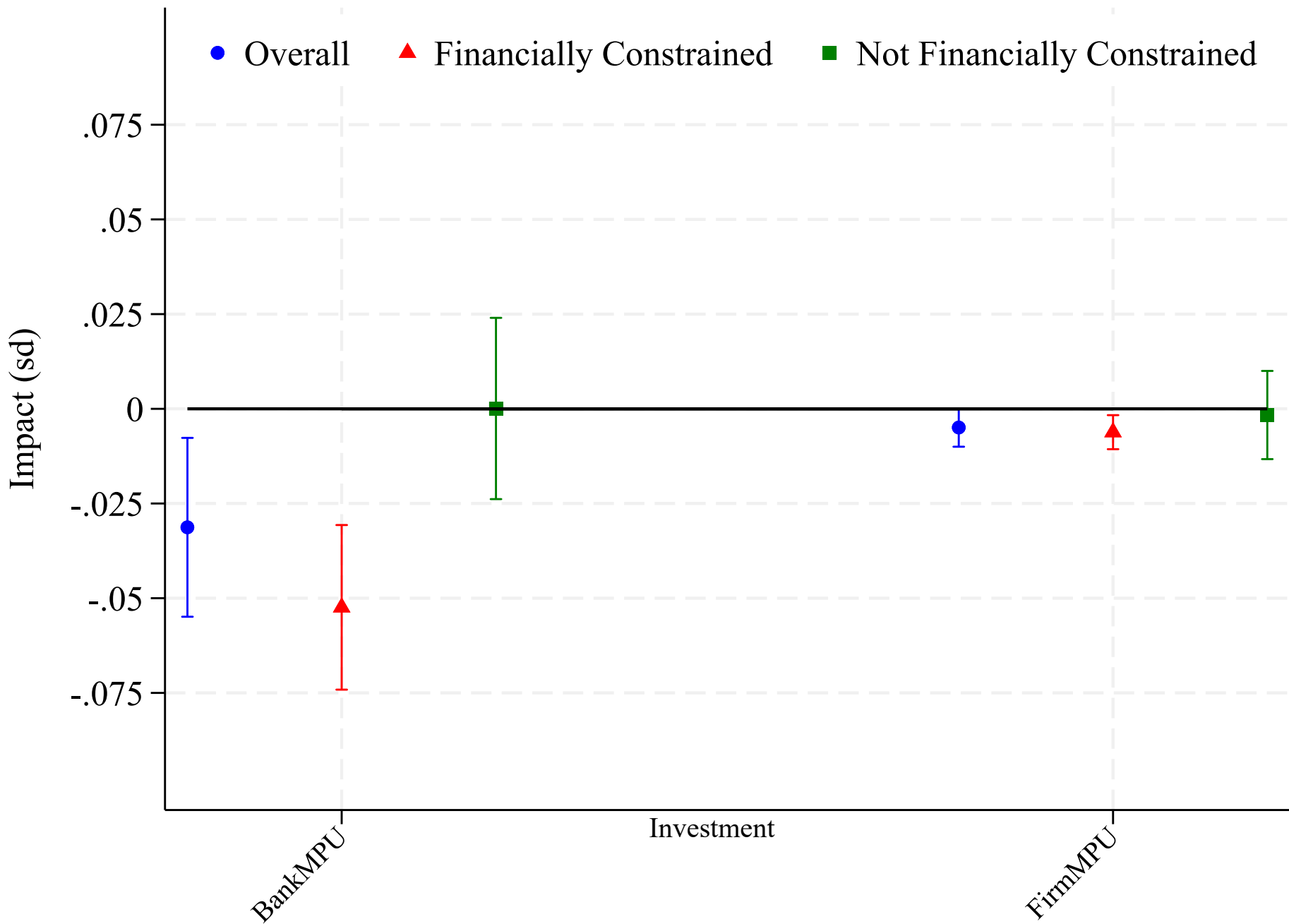


Figure 4: Firm-level regressions

Robustness tests

- SVAR: I do not orthogonalize with bank fundamentals, include News MPU, exploit daily variations in a monthly VAR, introduce the VIX, and change the dictionary construction
- Loan-level regressions: I control for analysts' MPU, apply weighted least squares (WLS) to account for repeating transactions, lag control variables, implement bank-time and bank-firm clustering, and introduce industry-size-location-time fixed effects (ISLT FE)
- Firm-level regressions: I test alternative monetary policy dictionaries, conduct regressions at the industry level (2-digit and 3-digit SIC codes), and use Local Projections with lagged regressor

Conclusion

Aggregate monetary policy uncertainty in the banking sector leads to a decline in GDP. The primary channel operates through the financing costs. Banks perceiving higher monetary policy uncertainty raise their lending rates. This leads to a fall in investment, particularly for financial constrained firms.

References

- [1] Lucas Husted, John Rogers, and Bo Sun. Monetary policy uncertainty. *Journal of Monetary Economics*, 115:20–36, November 2020.
- [2] Tarek A Hassan, Stephan Hollander, Laurence van Lent, and Ahmed Tahoun. Firm-Level Political Risk: Measurement and Effects. *The Quarterly Journal of Economics*, 134(4):2135–2202, November 2019.

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