

Discussion of: The Financial and Macroeconomic Effects of OMT Announcements

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Capturing the Effects of OMT

Discussion of
Altavilla,
Giannone &
Lenza

Lim

Summary

Comments

- Paper seeks to measure financial market and macro effects of OMT announcements
- **Financial:** Event-study estimate of magnitude of each (of 3) OMT announcements on sovereign bond yields (2s and 10s)
 - Uses both “classical” event study as well as “controlled” study including large matrix of forecast errors in macro variables
- **Macro:** VAR modeling of real/nominal macro variables for OMT and no-OMT counterfactual (unconditional forecast)
 - Recursive identification strategy with Bayesian shrinkage to deal with high dimensionality
 - Impose bond yield paths corresponding to event study results (very clever)

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Broad Comment: Is This Two Papers, or One?

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- The paper tackles an important topic which has thus far not been a focus of the literature
 - Most papers have examined effects of QE
 - OMT is unique in that it had effects *despite never having been used* (a central banker's fantasy come true)
- The paper is still somewhat preliminary, but as it stands, the two parts can credibly stand on their own
 - Extensions to Part 2: (a) expand coverage beyond 2 core-2 periphery; (b) do other financial markets (esp. equity, CDS) respond in a similar way (debt-equity substitution or confidence spillovers?); (c) how does each OMT announcement event differ (diminishing efficacy or no)?
 - Extensions to Part 3: (a) detailed discussion of nominal versus real responses; (b) robustness to incremental perturbations (e.g. DEU yield increase, nonzero EONIA volatility); (c) incremental introduction of small economies?

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Are the Two Parts Answering the Same Question?

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- Most importantly, can we frame the two approaches as tackling OMT *announcement* effects?
 - Event study: Day/intraday pops; more typical of genuine announcement effects
 - VAR: Monthly frequency clouds announcement versus other unobservables (e.g. confidence/sentiment) effects, which are not “announcement” effects *per se*
- BUT possible to sustain one paper (if one must): frame event study as step one of a two-step procedure to “calibrate” the OMT versus non-OMT scenarios
 - Side benefit: Provides more flexibility in use of results from first stage (more on that later)

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Comments for Event Study

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Summary

Comments

- “Controlled” version takes difference in consensus forecasts and actual realization (“forecast error”)
 - But controlling for forecast errors does *not* rule out changes due to: (a) unobservables that are not captured by 151 “fundamentals”; (b) forecast errors react at different speed/timing to OMT (test with lead/lags?); (c) markets anticipate OMT ($\hat{\alpha}$ biased downward)
- Can we distil forecast errors into some simpler signal (after all, most “errors” likely not to differ within each period)? (PCA?)
- Robustness to: (a) forecast window (+1/+3 days?); (b) selected announcements (just 1st and 2nd, esp. relevant since this will pull up average if 3rd is insignificant?)

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Comments for VAR Analysis

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- ITA-ESP bond rates held constant over entire 3-year projection
 - But this assumption is *not* innocuous: (a) assumes that OMT effects do not fade out over time (even QE, which requires actual flow purchases, diminishes in efficacy); (b) OMT effects on yields are essentially exogenous to model
- Leaves open the very interesting question of how what amounts to cheap talk can essentially engender such strong and persistent real effects (I'm greedy)
- More porridge: Discussion of main results remains cursory
 - Can we: (a) Summarize all nominal versus real variable IRFs, and compare implications; (b) Introduce alternative yield paths (allow effects to fade, introduce nonzero path for DEU, impose actual yield path and compare to hypothetical)
- Can we compare model evaluations of effects to actual effects?

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