The Macroeconomic Impact of Money Market Freezes

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Abstract:
We build a general equilibrium model featuring unsecured and secured interbank markets, and collateralized central bank funding. The model is calibrated and used to analyse the macroeconomic impact of three key developments observed in the European money markets since 2008: i) the reduced ability of banks to access the unsecured market since the onset of the global financial crisis and the shift to secured market funding; ii) the impaired functioning of the secured market during the sovereign crisis; iii) the increased reliance of banks on central bank funding. We find that disruptions in interbank markets, as observed during the financial and sovereign debt crises, generate a sizeable impact on real activity.