

How the PBoC's new MLF affects the yield curve

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1. What is the main question(s) raised in the paper (the issue)?

In recent years, People's Bank of China (PBoC) introduced the Medium-term Lending Facility (MLF)¹, this paper is wondering the impact on treasury and corporate bond yield curves.

2. Why should we care about it (the significance)?

Although this policy was proposed as early as 2014, most of the literature in recent years only focuses on traditional monetary policy, e.g., monetary aggregates, the required reserve ratio, the benchmark loan rate or the money market rate. Also the authors seem to agree with Yi (2021), which is MLF plays an important role during the PBoC's transition to a market-based system, particularly in affecting the credit market and yield curve.

3. What is the author's answer (the findings)?

At higher forecast horizons, the yield curve is shifted downward and then slowly returns to its original position. The authors thought that the PBoC seem to encourage portfolio rebalancing from government bonds towards (long term) corporate bonds, increasing supply of the former and demand for the latter, causing government bonds rate to increase. But the authors also said that the presence of other policies can also confound the effect what they expected, because VAR usually identify shocks through their contemporaneous effects.

4. How did the author get there (the strategy, empirical approach)?

The authors used semi-parametric local projection framework because the sample size was not large enough, it can capture the movement of the entire yield curve without imposing a functional form and exploit the data efficiently. First, the authors use simple regression to identify surprise changes in MLF volume (the model setting is similar to recursive SVAR

¹ Medium-term Lending Facility (MLF): the monetary policy of the central bank, commercial banks can mortgage their bonds to the central bank to obtain funds and then increase the money supply.

model). Then they estimated impulse responses to the shocks which is identified in the first step.² Finally, they performed a robustness check (distinguish sterilized and unsterilized shocks).

² About this method, please see Jordà (2005).