On 30-31 May, EBO hosted the Working Group on Econometric Modelling (WGEM) of the ECB for its quarterly meeting, held once a year outside Frankfurt. This working group brings together head modellers from central banks of the Eurosystem and acts as a forum to present and discuss the latest research on models relevant for central banks and to exchange views on national modelling practices. The meeting took place at the Radisson Blu Hotel, in the old centre of Amsterdam, and was attended by representatives of 28 central banks of the Eurosystem.

The first day was dedicated to presenting some of the reports of the subgroups of the WGEM which are destined to the Monetary Policy Committee of the ECB. Four of these teams will be finalizing their projects this year, some of which have been running over two years. These include reports on modelling the macro-financial linkages at the heart of the recent crisis, on performing sophisticated empirical analysis on cross-country aspects of the crisis (such as regime-switching panel VAR techniques, for example), on documenting the role of internal competitiveness in the Euro Area as a way out of the current quandary, and on modelling optimal fiscal responses to it. To close the day, Massimiliano Pisani (Bank of Italy) presented his analysis of the effects of alternative expansionary fiscal shocks (spending vs tax-based) on public and private debt in an estimated DSGE model of an open economy, the results of which suggest less-than-unit multipliers and small current account deterioration and leakages, with little effect of the monetary policy stance (including the zero-lower bound).

The second day started with a brief description by five national central banks of their model developments, activities and plans. Talking in alphabetical order, the Belgian, Czech and German representatives detailed a highly impressive modelling apparatus——ranging from sophisticated short-term forecasting models to suites of multiple DSGE models geared to addressing specific policy questions——and very ambitious plans. All have DSGE models in place with a view to producing forecasts. In stark contrast, the Danes and Estonians appear to rest exclusively on a traditional macro-model for most of the forecast and simulation work, and are only now setting down the DSGE path. The main impression of this first iteration of a general tour de table is that much effort is being spent going down that path. The Bundesbank even holds internal training sessions by its researchers to teach policy workers how to use DSGE models for their own purposes…

The tour de table was followed by a presentation by Peter Heemeijer (UvA) on experimental results on expectation formation, in the line of his work with Cars Hommes on heterogeneous agent models. Such models are presented as a viable alternative to the standard DSGE paradigm; the WGEM members were very receptive to it and the presentation generated a lively session of questions and answers. The session was followed by the presentation by Pierre Lafourcade of the DNB’s latest version of a DSGE model for the Netherlands. The major

message of this presentation, namely that a good hard look at trends in the data is crucial for the well-functioning of a DSGE model, was very well received.
After lunch, two presentations focused on macro-financial linkages. In the first, Caterina Mendicino (Bank of Portugal) analyzed the potential gains of monetary and macro-prudential policies that lean against news-driven boom-bust cycles in housing and credit, with a view to evaluating policies that make loan-to-value ratios respond to macro-economic conditions. In the second, Olivier Pierrard (Bank of Luxembourg) focused on modelling the breakdown of interbank lending in a DSGE framework with a more sophisticated representation of this market than is standard. Accordingly, a fall in quality of collateral (an unsecured interbank market demand shock) and a generalized surge in risk aversion (a supply shock) have different effects and require different central bank instruments and responses, a result somewhat reminiscent of Poole's (1970) optimal instrument choice in a standard IS-LM setting.
The WGEM meeting then adjourned, and it was generally agreed, over multiple biertjes under sunny skies along the Kloveniersburgwal, that it was an unqualified success.
Please contact Pierre Lafourcade (ext 3410) for more clarifications.