Discussion of Beaudry, Cavallino and Willems (2025)
"Monetary Policy along the Yield Curve: Why Can Central Banks Affect Long-Term Real Rates?"

Min Wei
Federal Reserve Board

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The opinions expressed in this presentation are solely mine and do not reflect those of the Federal Reserve Board, the Federal Reserve System, or their staff.

Summary of paper

- Motivating empirical evidence
  - Most of long yield decline occurred around FOMC meetings (Hillenbrand 2023)
  - Log detrended consumption uncorrelated with log detrended wealth but ...
    - highly correlated when wealth scaled by LT real Tsy yield
- Model features: finitely-lived agent NK model (FLANK)
  - Negative duration gap due to retirement duration $>$ duration of assets
  - Lower LT real rate $\Rightarrow$ wealth $\uparrow$ less than retirement liab $\downarrow$ $\Rightarrow$ save more
    - Offset $+$ve intertemporal substitution and asset valuation effects

Summary of paper – cont'd

- Model implications

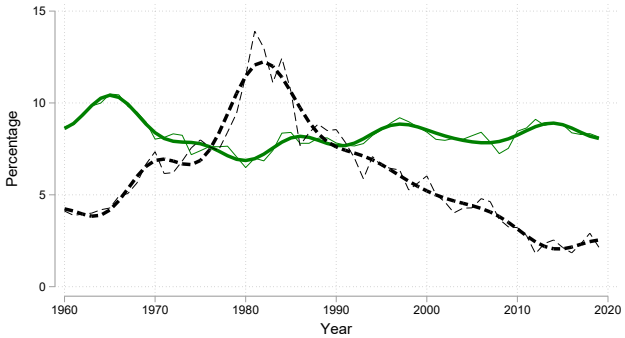
$$\hat{c}_t^w = (1-\delta_1)\,\mathbb{E}_t\hat{c}_{t+1}^w - \frac{1}{\sigma}\mathbb{E}_t r_{t+1} + \delta_1 \sum_{j=1}^{\infty} \beta^j \left[\frac{\sigma-1}{\sigma}(1-\delta_2)^{\frac{j}{\sigma}} - (1-\mu)^j \right] \mathbb{E}_t r_{t+1+j} \quad (21)$$

  - When $\delta_1 > 0$ and $EIS = 1/\sigma < 1$, higher real rate at long horizons could *boost* consumption
  - CB persistently lowering real rate not as stimulative ⇒ CB can affect LT real rates
  - MP and demand shocks work differently ⇒ CB cannot perfectly offset persistent demand shocks
  - HLW-type r* estimates could be contaminated by CB's perceived r* and even transitory demand shocks that CB responds to.
  - CB misperception about r* might be self fulfilling
- Empirical evidence supporting model mechanism
  - GSS FG shock less effective or wrong sign based on local proj.
- Innovative and rich paper. Really enjoyed reading!

Comment on motivating empirical evidence

- Decline in LT gov bond yields, but return to capital remained high (Farhi & Gourio 2018; Marx, Mojon & Velde 2021, Reis 2022)
- Decline in LT gov bond yields driven by rising safety/convenience premiums (DelNegro, Giannone, Giannoni & Tambalotti 2017)

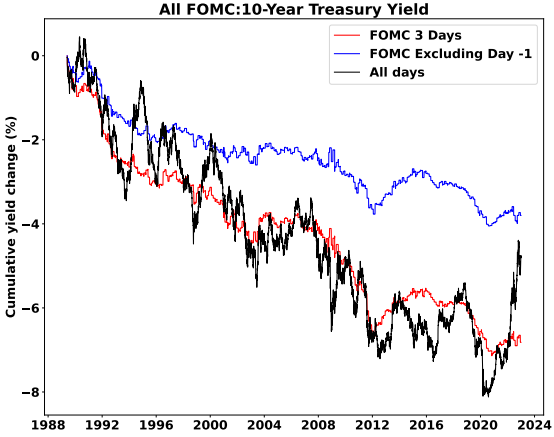
Figure 2: US returns on private capital versus government bonds



Source: Reis, 2022, "Which r-star, public bonds or private investment? Measurement and policy implications."

Comment on motivating empirical evidence – cont'd

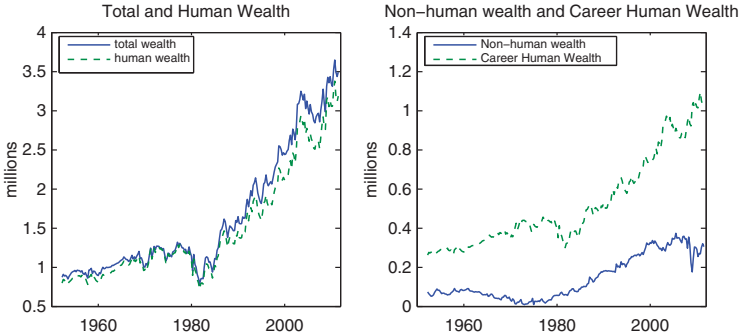
- Hillenbrand (2023): Decline in long bond yields concentrated in three days around FOMC meeting
- Pan & Peng (2024): Large portion occurred prior to FOMC, pointing to risk premiums & non-MP factors



Source: Pan and Peng, 2024, "The Pre-FOMC Drift and the Secular Decline in Long-Term Interest Rates."

Comment on motivating empirical evidence – cont'd

- Correlation between (detrended log) consumption and wealth (w/ or w/o real rate adjustment)
  - Need to include labor income (Lettau & Ludvigson 2001; Lustig, Nieuwerburgh & Verdelhan 2013)
  - Detrending using pre-GFC trends might be overly simplistic
  - Correlation not causality: Non-MP factors (eg productivity, population aging) could drive declines in both consumption and yields



Source: Lustig, Nieuwerburgh & Verdelhan, 2013, "The Wealth-Consumption Ratio," *Review of Asset Pricing Studies*.

Comment on model features and assumptions

- Constant retirement prob: retirement or health shocks?
  - Older households: Duration gap more problematic but also more wealth.
- Missing channels?
  - Households reaching for yield using leverage in low rate environment:
    - Households themselves (Gomes, Peng, Smirnova & Zhu 2025)
    - Through pension funds (Lu, Pritsker, Zlate, Anadu & Bohn 2019)
  - Production using labor only; no investment: no cost of capital channel

Comment on empirical support for model mechanism

- Weak effect of forward guidance shock
  - May need to control for central bank information or fed response to news effect (Swanson 2024)
- Micro-level evidence
  - Evidence of household interest rate expectations on consumption choices (Coibion, Georgarakos, Gorodnichenko & Weber 2023, Dong, Liu, Wang & Wei 2025)
  - Would be interesting to look at effects across household age cohorts

Additional thoughts

- Back to motivation
  - To explain the long yield decline around FOMC, requires investors to perceive the shocks as persistent.
  - Seems in conflict with:
    - Frequent revisions of policy expectations
    - most long rate responses to policy shocks are due to term premiums (Hanson & Stein 2015; Hansen, McMahon & Tong 2019)
- Interpretation
  - r* in this paper defined as the intercept in the policy rule equation
  - r persistently below r* or short-run r* is lower?
- How would incorporating term and risk premiums change the results?

Conclusion

- Thought-provoking paper
- Fascinating new channel + rich implications
- Highly recommended reading!

- Suggestions mainly for follow-up work
- Assess empirical importance of this channel, both motivating evidence and model mechanism
- Consider allowing for additional channels and risk premiums