Volatility Spillovers of Federal Reserve and ECB Balance Sheet Expansions to Emerging Market Economies

Apostolos Apostolou (https://papers.ssrn.com/sol3/cf_dev/AbsByAuth.cfm?per_id=2124174)
International Monetary Fund (IMF)

John Beirne (https://papers.ssrn.com/sol3/cf_dev/AbsByAuth.cfm?per_id=3488271)
Asian Development Bank

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Abstract

This paper examines volatility spillovers from changes in the size of the balance sheets of the Federal Reserve (FED) and European Central Bank (ECB) to emerging market economies (EMEs) from 2003 to 2014. We find that EME bond markets are most susceptible to positive volatility spillovers from both the FED and ECB in terms of magnitude. Positive volatility spillovers to EME currency markets are higher in the case of FED balance sheet expansions than those of the ECB by a factor of about ten. By contrast, we find that EME stock markets are subject to negative volatility spillovers. Moreover, we find only limited evidence of volatility transmission to the real economy of EMEs following the monetary policy actions of the FED and ECB. Finally, we show that the proportion of the volatility in EMEs that is accounted for by changes in FED and ECB balance sheets shifts over time.

Keywords: unconventional monetary policy, central bank balance sheets, volatility spillovers, financial markets

JEL Classification: F3, F4, F16, G1

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