Abstract

The Bank of Japan (BoJ) has been implementing the quantitative monetary easing policy. Namely, the BoJ commits itself to maintaining short-term rates at low levels for several years, and, by doing so, tries to achieve also stabilization at low levels of long-term rates, which we know as so-called “policy duration effect”. Theoretically, the existence of the effect can be shown on the basis of the expectations hypothesis about the term structure of interest rates.

The purpose of this paper is to model the financial market with the banking system in Stiglitz and Greenwald (2003), and to examine in terms of equilibrium analysis how the effect is transmitted into the economy. If we assume long-term rate based on the expectations hypothesis, it can be decomposed into (1) an average of short-term rates from present to future and (2) a risk premium. Then, it is presented that a level of the long rate depends upon the impacts of an exogenous shock on (1) and (2). In other words, it is demonstrated that the efficacy of policy duration effect depends on them.

Keywords: Quantitative Monetary Easing, Policy Duration Effect, Term Structure of Interest Rates, Risk Premium

JEL Classifications: D50, E43, E52