



BANK FOR INTERNATIONAL SETTLEMENTS

Discussion of:
**The US dollar Exchange Rate
and the Demand for Oil**
by Selien De Schryder and Gert Peersman

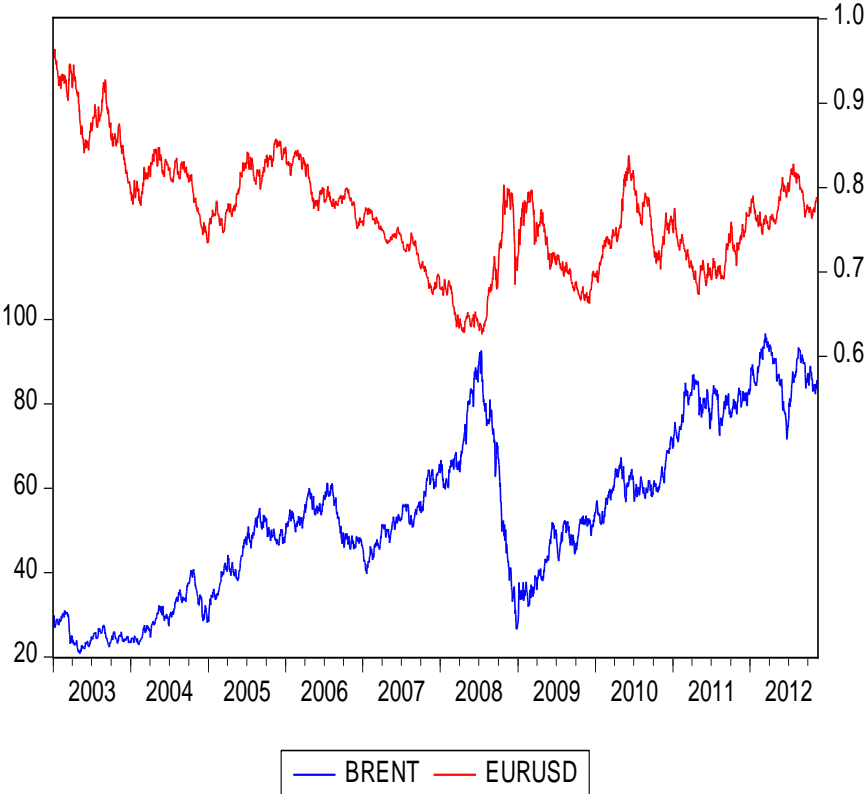
Marco J Lombardi

Frankfurt am Main, 19 November 2012

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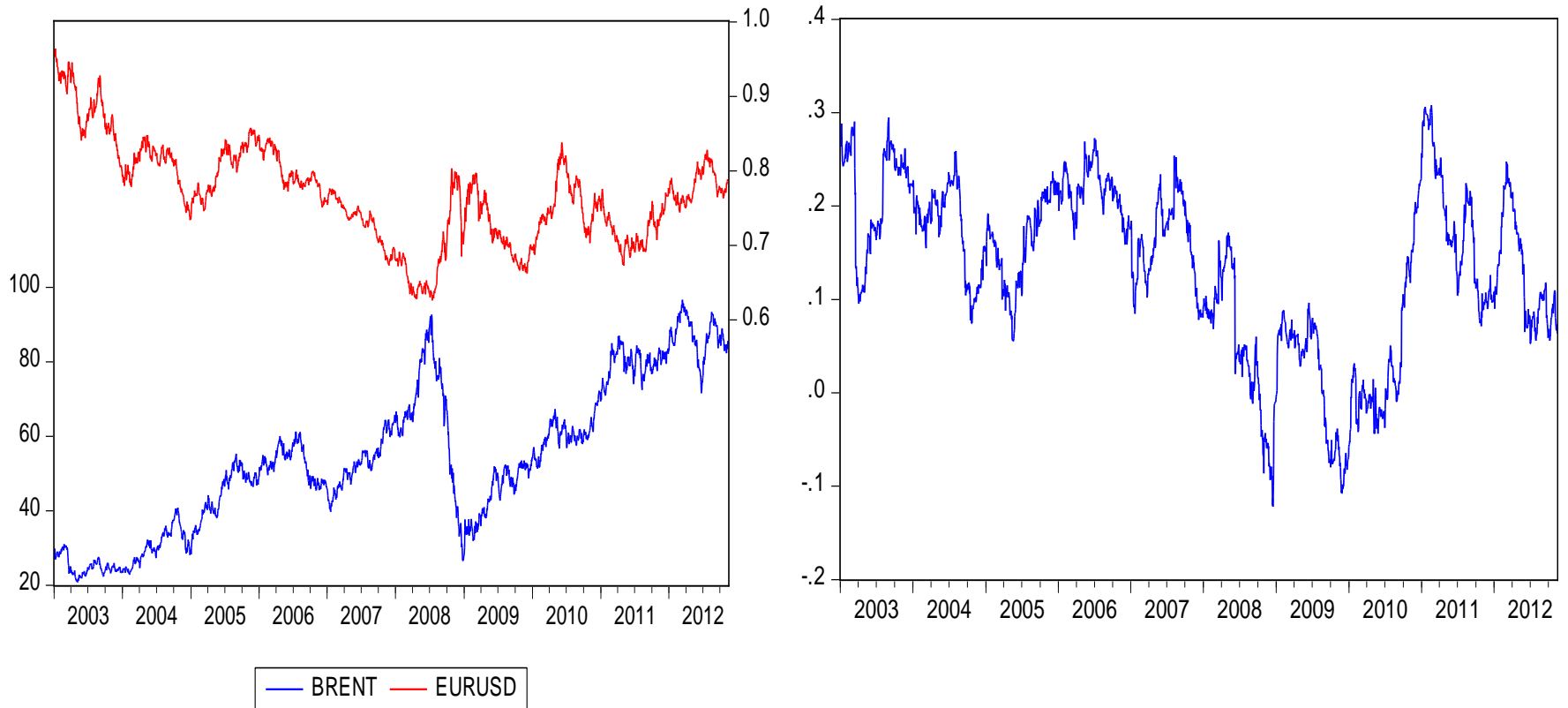
EUR/USD and Brent



Transmission channels (USD depreciation)

- Demand
 - Lower price in USD boosts demand
- Supply
 - Oil exporters may want to stabilize revenues
- Hedging
 - Investors buying real assets to safeguard portfolio value
- Emerging economies
 - USD depreciation linked to stronger growth in commodity-intensive economies

Correlation or common trends?





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Where's monetary policy?



...scattered around in footnotes and robustness checks!

¹To our knowledge, the only empirical study which also considers the US dollar exchange rate as a possible determinant of oil demand is Askari and Krichene (2010). They estimate, however, a time series simultaneous equation model for (aggregate) world oil demand and supply between 1970 and 2008, whereas we estimate the impact of the US dollar exchange rate for a panel of 65 countries. In addition, they examine the effect of the exchange rate as part of a monetary policy channel affecting global oil prices, rather than an independent driver of oil demand.

⁴Frankel (2006) argues that oil and other commodity price developments are influenced by interest rates. Specifically, when the interest rate declines, commodities become more attractive as an asset for investors. In addition, a lower interest rate stimulates overall demand, including the demand for oil. Notice, however, that this is not relevant for our analysis since we consider oil consumption (not inventories) at the LHS of the oil demand function, while real GDP is included at the RHS.

we instrument the first difference of the US dollar real effective exchange rate in equation 2 by the first difference and the level of the US federal funds rate, the lagged level of the



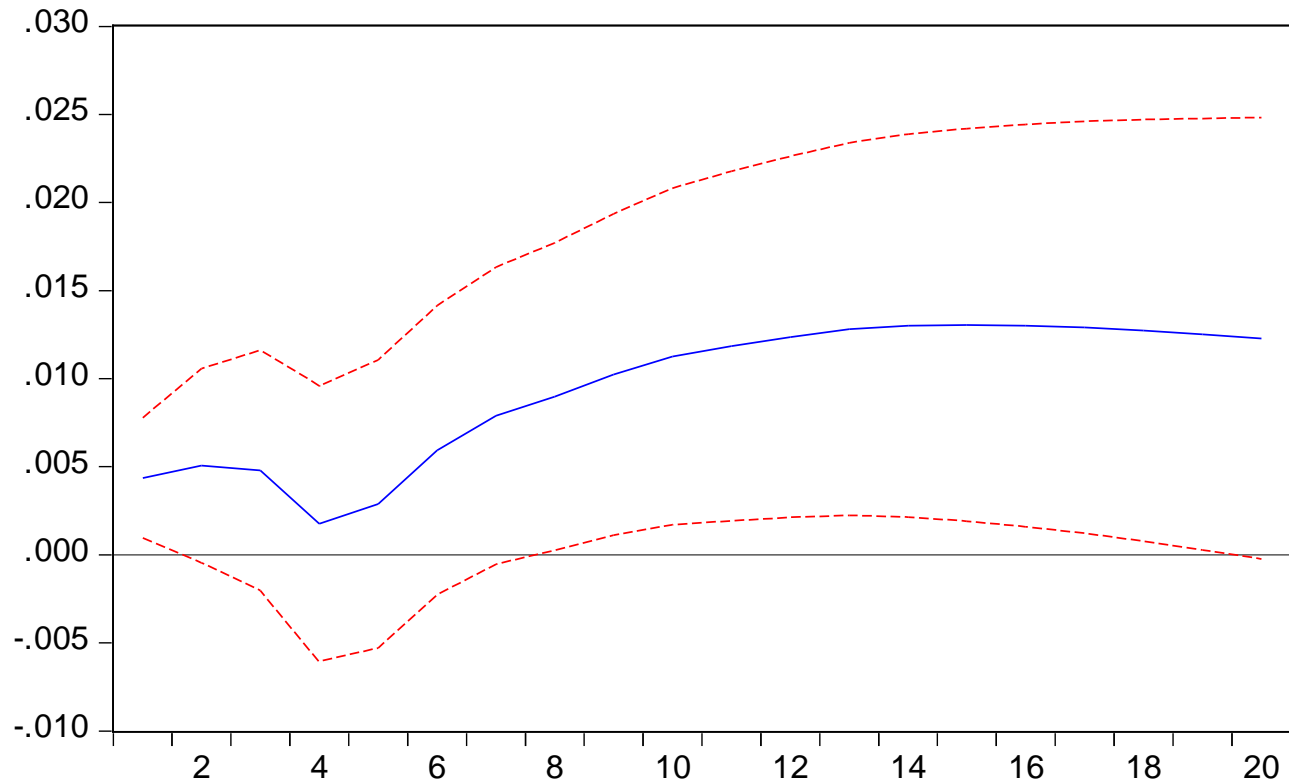
Monetary policy and the REER

- Eichenbaum and Evans (QJE 1995)
 - Impact of MP shocks on nominal and real exchange rates
- Kim (JME 2001, JMCB 2005)
 - Impact on terms-of-trade
- Scholl and Uhlig (JIE 2008)
 - With sign restrictions
- Binder, Chen and Zhang (2010)
 - Multi-country VAR with LR restrictions



A simple CEE identification...

Response of LOG(REER) to Cholesky
One S.D. OR_US Innovation

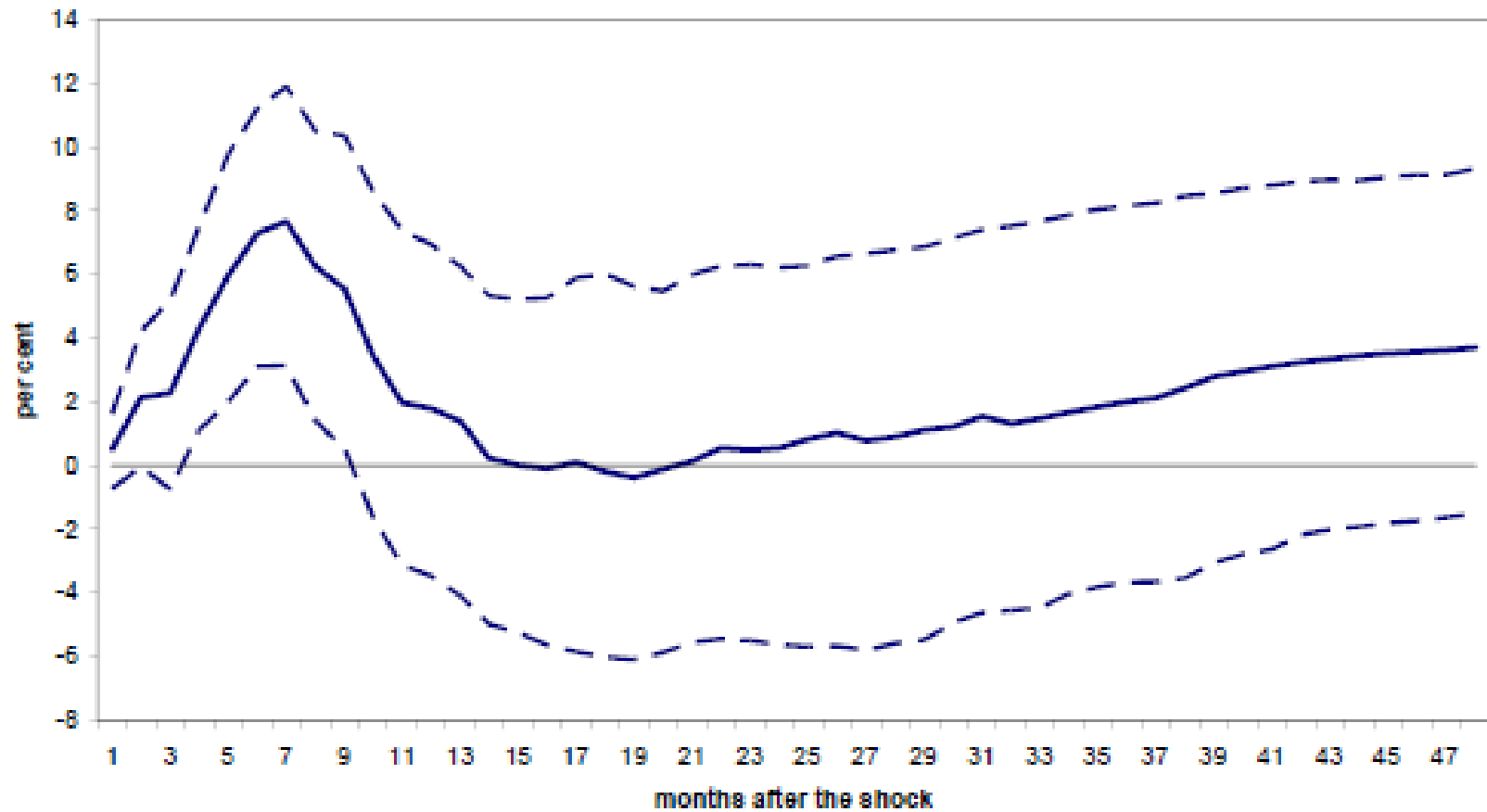


Monetary policy and the price of oil

- Barsky and Kilian (NBER 2002)
 - Monetary policy as alternative explanation of oil price increases in the 70s
- Kilian (AER 2004)
 - Relevance of demand shocks
- Anzuini Lombardi and Pagano (2010)
 - Impact of monetary policy shocks on the price of oil
 - Transmission via 'indirect' channel of higher growth and inflation



Response of oil to a monetary policy shock à la Kim (1999)



Is monetary policy the missing piece?

- High relevance of REER for oil price dynamics
- Smaller impact of REER on demand in non-OECD countries
- Bigger impact on demand of REER than real oil price

