

Return on Collateral, Target Deviation, and Interest Rate Corridor

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The previous literature on monetary policy in a channel system suggests that the cost of collateral for obtaining funds from standing facilities affects not only the inter-bank market rate deviation from its target but also the way in which central banks implement monetary policy. Empirical studies regarding these relationships are insufficient. Therefore, I estimate empirical models to test these relationships with data from four countries. The results is indicative of the idea that higher cost of collateral is associated with tighter monetary policy and vice versa although some central banks' monetary policy may not respond to changes in the collateral cost. However, the effect of collateral cost on money market rate deviation from the target rate is negative under some circumstances.