Abstract

A long-standing macroeconomic issue is how monetary policy affects the real economy. Previous VAR research has found that bank loans typically contracted following a monetary tightening. This is consistent with the credit view: a monetary tightening decreases aggregate demand by shifting the loan supply curve left. However, the finding is consistent with another interpretation: a monetary tightening operates through the conventional money channel and decreases the demand for loans. This observational equivalence is called the “supply-versus-demand puzzle.” This paper shows that embedding the loan price in a macroeconomic VAR model reduces the puzzle to the simultaneous equation bias. As a proxy for the loan price, the survey-based data is utilised. The main finding is that the loan supply curve shifts left after a monetary tightening. The effectiveness of monetary policy is also confirmed. From these results, this paper concludes that monetary policy operates through the credit channel in Japan.