

A Literature Review of the Impact of Monetary Policy on the Real Economy through Stock Markets

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Abstract. Researchers have found that with the implementation of monetary policy, the stock market undergoes certain changes thereby affecting the movement of the real economy. Through the existing research progress and situation of monetary policy on the transmission mechanism of the stock market is categorized and organized objectively. Firstly, the basic transmission channel of monetary policy is categorized into credit transmission channel and bond transmission channel. Secondly, the transmission mechanism of monetary policy is divided into two steps, the first step of the impact of monetary policy on the stock market is the impact of monetary policy on stock prices through the money supply, interest rates, respectively, from the credit transmission channel and the bond transmission channel two routes; the second step of the stock market on the real economy, respectively, the impact of investment and consumption. Comprehensive comparison found that the existing research on the bond transmission channel on the impact of stock prices there are still large differences and shortcomings. It is recommended that the Government pay attention to and improve the transmission mechanism of monetary policy on the stock market to the real economy, so as to enhance the macro-control ability of monetary policy on the real economy.

1 Introduction

As the global capital market grows, more and more scholars are starting to look at how currency policy is conducted to the capital market. In the financial market, the stock market has a crucial position. According to the Monetary Policy Implementation Report for the Third Quarter of 2024 released by the PBOC, the PBOC has adhered to a supportive monetary policy this year, which has strongly and effectively supported the economy to rebound and improve. Macroeconomic strategy's effects through the credit channel is manifested in the reasonable growth of financial aggregates, with the stock of social financing scale and broad money M2 growing by 8.0% and 6.8% year-on-year at the end of September, and new RMB loans of 16 trillion yuan in the first three quarters. The influence of policy means through the bond transmission thoroughfare is manifested in the steady decline in financing costs, In

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September, the average cumulative interest rate on newly issued commercial loans was 3.51%, 0.31 percentage points lower than the same period last year. This series of monetary policy through the control of currency provision and interest rates from the credit transmission channel and bond transmission channel respectively, the Chinese stock market corporate stock prices have brought about greater fluctuations, the stock market fluctuations further affect the real economy.

Based on this, the research in this paper centers on the theme of currency policy affecting the real economy through the progress of the share market to construct a synthesis framework, and decompose the influence mechanism into “what”, “how” and “what to fear”. That is, what is the basic transmission thoroughfare of currency policy; how does currency policy influence the development of share market and further influence the entity economy by basic transmission mechanism; what should the government pay attention to when enacting monetary policy, and the above aspects are sorted out and summarized. Monetary policy is an important tool for macro-control in China, and in the process of its implementation, no matter what the ultimate purpose is, it will have more or less impact on stock prices, and changes in stock prices will affect enterprise investment and personal consumption and then affect the real economy.

However, most of the current commentary simply summarises the influence of currency policy on the physical economy, ignoring the law of the share exchange in the middle of the process, and lack of a complete logical organization. Therefore, this paper will study the dissemination mechanisms and the level of influence of currency policy on the share market and deeply analyze the influence of stock prices on the real economy through literature review, to make up for the lack of research on the law of the stock market in the study of the law of conduction, and pay attention to the degree of influence of the government on monetary policy in time to further improve the conduction laws of monetary policy, which is of great relevance to the economic expansion of China..

2 Basic transmission channels of monetary policy

2.1 Credit transmission channels of monetary policy

It is argued that shocks to interest rates in the credit transmission channel happen to be important for credit dynamics by analyzing whether external variables (e.g., the commodity price index and U.S. GDP) are correlated with the dynamic interactions between the important domestic variables for Brazilian credit, GDP, inflation, interest rates. important. In the short run, shocks to credit itself have extremely function in explaining this variable. In addition to the interest rate, the prediction error influenced by credit averages 30% in the short run and 25% in the long run [1]. By studying the study of monetary policy transmission mechanism and effects under the perspective of liquidity stratification, Professor Zhang studied the bond market and credit market transmission effects separately and concluded that the credit transmission channel of monetary policy is relatively smooth and concluded that credit transmission is the main delivery channel of currency policy [2]. The credit conduction process of currency policy refers to the improvement by which shift in currency strategy can alter the supply and demand for bank loans, which in turn affects the investment and financing costs and credit supply of the real economy and ultimately affects economic activity.

2.2 Bond Transmission Channel of Monetary Policy

Some scholars have studied the whole process of conveyance system of monetary programme to the real economy through that bond market in China and found that: the adjustment of lending rate and statutory reserve requirement ratio will cause the Treasury bond yield to move in the same direction, but the sensitivity of the short-end Treasury bond yield is higher than that of the long-end; there is a significant long-run positive covariation between the policy bank bill issuance interest rate and the Treasury yield and a negative adjustment will be carried out when it is deviated from the long-run equilibrium [3]. Zhang in the context of liquidity stratification, research that different economic environment background, monetary policy interest rate on the price level of the transmission of pro-cyclical and counter-cyclical, the impact on the output gap shows volatility, time-varying. The transmission effect is enhanced by lower bond credit ratings, but the transmission effect on consumption is weaker at too low a rating [2]. Monetary policy bond transmission mechanism refers to a series of process by which the policy bank influences market interest rates through monetary policy instruments and further influence the bond exchange and ultimately the real economy. The central bank influences the currency provision and interest rate level in the market through disclose market business, deposit reserve ratio adjustment, adapting the rediscount rate and other monetary policy tools.

3 The implication of currency policy on the stock market through basic transmission channels

3.1 Monetary policy affects stock prices through the credit transmission channel

Some scholars studied the transmission mechanism of monetary policy in China and argued that money supply is the cause of changes in the real economy and that interest rates are not significant exogenously [4]. Other scholars have found that through a study of how currency policy affects the financial exchange in areas such as Africa, a higher degree of financial openness in West African location, changes in monetary policy have a very profound influence on the performance of share exchange in West African markets, and positive variations in currency supply have a positive impact on the long-term performance of stock markets[5]. Studies from different perspectives confirms that monetary policy shocks cause changes in bank credit behavior and that bank loan-dependent firms are widespread in China with sticky prices. Further the higher the degree of regional marketization (or financial marketization), the smoother the credit transmission channel [6].

Through the study of domestic and international literature, it is found that the influence of currency policy through the credit channel mainly emphasizes the importance of indirect financing on the transmission of currency policy. Monetary policy indirectly exchanges firms' stock prices by influencing the supply and demand of bank loans and thus subjective conditions such as the cost of corporate financing and the supply of credit.

3.2 Monetary policy affects stock prices through the bond transmission channel

Chinese scholars study the influence of currency policy on the share market by constructing a GARCH-MIDAS model, and the results of the study show that in the short period, changes in interest rates will have a significant influence on stock prices, but the long-term impact is weak [7]. Further studies have concluded that there exists a phenomenon called cross-asset

time-series momentum effect between stock and bond markets around the world, and that there is not only a predictability of their own returns between stocks and bonds, i.e., past stock returns or bond returns are a positive predictor of their own future returns, but also a short-term cross-asset return predictability between stock and bond markets, i.e., short-term bond market historical returns positively predict stock market future returns and stock market historical returns negatively predict bond market future returns [8].

By summarizing the studies of domestic and international literature, most scholars unanimously agree that the bond transmission channel has an important and close influence on stock changes, and the main disagreement is whether the change of interest rate in the bond transmission channel really has an impact on stock prices. However, the main point of view is that the change of interest rates will product a big influence on share prices in a short period of time but will gradually weaken with the passage of time.

4 Impact of the stock market on the real economy

4.1 Impact of stock market on consumption

Some scholars argue that China's consumption is mainly influenced by income and that the wealth effect of the stock market is not significant. However, there is a more pronounced wealth effect on automobile consumption measured using relatively high-frequency monthly data, a finding that is consistent with established foreign findings that the wealth effect is more significant for consumer durables, suggesting that the wealth effect of China's stock market is more significant in the short run for consumer durables than for full-caliber consumption [9]. Maggio, Kermani and Majlesi examines the effect of changes in stock market returns on consumption in Sweden and finds that that when dividends are paid, household consumption expenditures respond more rapidly in all areas of wealth distribution [10]. And the general research suggests that the stock market affects consumption mainly through the wealth effect and liquidity effect, and from two aspects respectively, the enhancement of stock prices has a positive effect on consumption [11]. In summary, it can be seen that the increase of stock price will have a promotion effect on consumption in different degrees.

4.2 The impact of stock market on investment

The latest research shows that there are obvious regional asymmetric effects of monetary policy transmission channels in China. Bank credit and interest rate conduction channel on the regional economic growth and prices of the impact of the direction of the basic consistent, the impact of the magnitude of the large differences; stock market prices and real estate prices in addition to the individual regional economic growth rate and prices have a certain impact on most of the region, the impact of the magnitude of the magnitude of the impact is not large, but the regional asymmetric effect is more obvious [12]. Other studies argue that stock prices affect investment through the Tobin's q effect, balance sheet effect, and resource allocation effect, proving from three aspects that stock price enhancement has a positive impact on investment [11]. In summary, it can be seen that the enhancement of stock price has different effects on investment in different regions, but most of them are promotion utility.

5 Review of Existing Issues

Through the literature review, it is found that most of the scholars' research conclusions are different due to the different backgrounds and theoretical foundations of their studies. In

particular, the difference in research conclusions between Chinese and foreign scholars is due to the difference in the development process of developed capital markets in the West stock exchange, and the study of the conducted mechanism of a country's currency policy should be combined with the specific national conditions, taking into account the economic cycle, policy changes, and other factors to conduct specific empirical research. The conclusions of distinct scholars on the conductance of currency policy to the share market in different periods are different, on the whole, mainly due to the fact that the development of the conductance of currency policy to the stock exchange in China is not perfect enough; the link between the share market and the money bazaar is not close enough; and the impact of the stock price is not taken into account that there may be more complex factors.

It is noteworthy that in the research on this aspect of the roles of currency policy on the share market, most scholars on the stock marketplace stage of the study focused on the difference in the currency demand and interest rates as a measure of the variables of monetary formulation, while ignoring the other influences embedded in it, due to the possible neglect of other important factors, which has led to the lack of most researchers for the study of interest rates on the stock professional work over the long stage Breakthrough. In the link of share market selection, the current domestic research on stock market is not perfect, which is manifested in the lack of research on emerging stock markets such as the Science and Technology Innovation Board, the Growth Enterprise Board and other small and medium-sized enterprises, while the above stock markets represent specialization, specialization and newness, which can be seen in the relative lag of the domestic research. Finally, most of the researches are limited to studying a single link of the stock market, for example, only focusing on the study of the currency policy on the stock market, but lack of a complete review and combination of the share market in the real economy, which makes it difficult to project the changes of the real economy through the changes of the share market.

The research about the impact of the share market on consumption, some scholars believe that the equity security market will have an influence on consumption, but there is no refinement and in-depth study; another part of the scholars believe that the stock market has no bumper impact on the full caliber of consumption, but has a certain impact on some consumer goods, such as durable goods consumption. In the research on the influence of the share market on investment, there is a more unified view that the increase in share prices has a promoting effect on investment. In the research on the final link of monetary policy affecting the entity economy through the share market - how the share market affects the entity economy - there are fewer studies on this link and most of them focus on the theoretical deduction stage, and the few empirical studies are mostly focused on a particular context or the data are relatively lagged while stopping at a past Stocks and the real economy changes in the study, it is difficult to carry out extrapolation and outlook, and therefore lack of forward-looking in time.

6 Policy Recommendations

Through the study, it is found that in the basic conductance of monetary policy, the conduction method of the credit channel is relatively perfect, while missing research on mechanisms for conveying bond channels, therefore, to solve the problem of the validity of the conduction method of currency policy, it is necessary to monitor the role of the bond transmission mechanism in it. At the same time, through the study of stock prices can be located in the short period interest rate changes have a certain influence, but the chronic impact is elusive, so we need to improve the short-term interest rates to the chronic efficiency of the transmission rate of return, so as to strengthen the ability of macro-control. And in the face of the link between the stock market and the entity economy, if we want to play the wealth effect of the share market in consumption and the resource allocation effect in

investment, we need to improve the current stock market instability, a long time in the doldrums, the bull short and the bear long status quo.

Relevant departments need to concern the effectiveness of the performance of currency policy in both credit and bond channels, and improve the efficiency of policy transmission; further strengthen the performance of monetary policy, improve and strengthen the financial regulatory system and the macro-prudential system to give ample play to the function of monetary policy tools, and at the same time play the role of market guidance of the Directorate General of Financial Supervision and always pay attention to the changes in the stock market; use forward-looking monetary policy to Reasonably guide the up and down movements of the stock market to stimulate the vitality of enterprises; and reasonably innovate the use of monetary policy tools to maximize their effectiveness.

7 Conclusion

In order to obtain a deep comprehension of the role of the shares market in the adjustment of monetary policy to the entity economy, and to better control market movements so as to strengthen the manipulation of the market and improve the effectiveness of monetary policy, this study, by summarizing the literature at home and abroad, discusses the process by which monetary policy has an influence on the real economy by the stock market. The central bank, through enacting negative or positive monetary policies, adjusting the money supply, interest rates, etc., affects stock prices through the bond transmission channel and the credit transmission channel, respectively. Changes in stock prices in turn directly or indirectly affect consumption and investment and thus have a certain impact on the real economy. There are some limitations in this study, which focuses on the two major channels of monetary policy transmission, namely bond and credit, and may neglect the other transmission channels. Secondly, this study is limited to the literature review aspect, and there is no relevant empirical research. Therefore, the study can be further explored and deepened by combining relevant data.

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