

International Monetary Policy Coordination: Past, Present and Future

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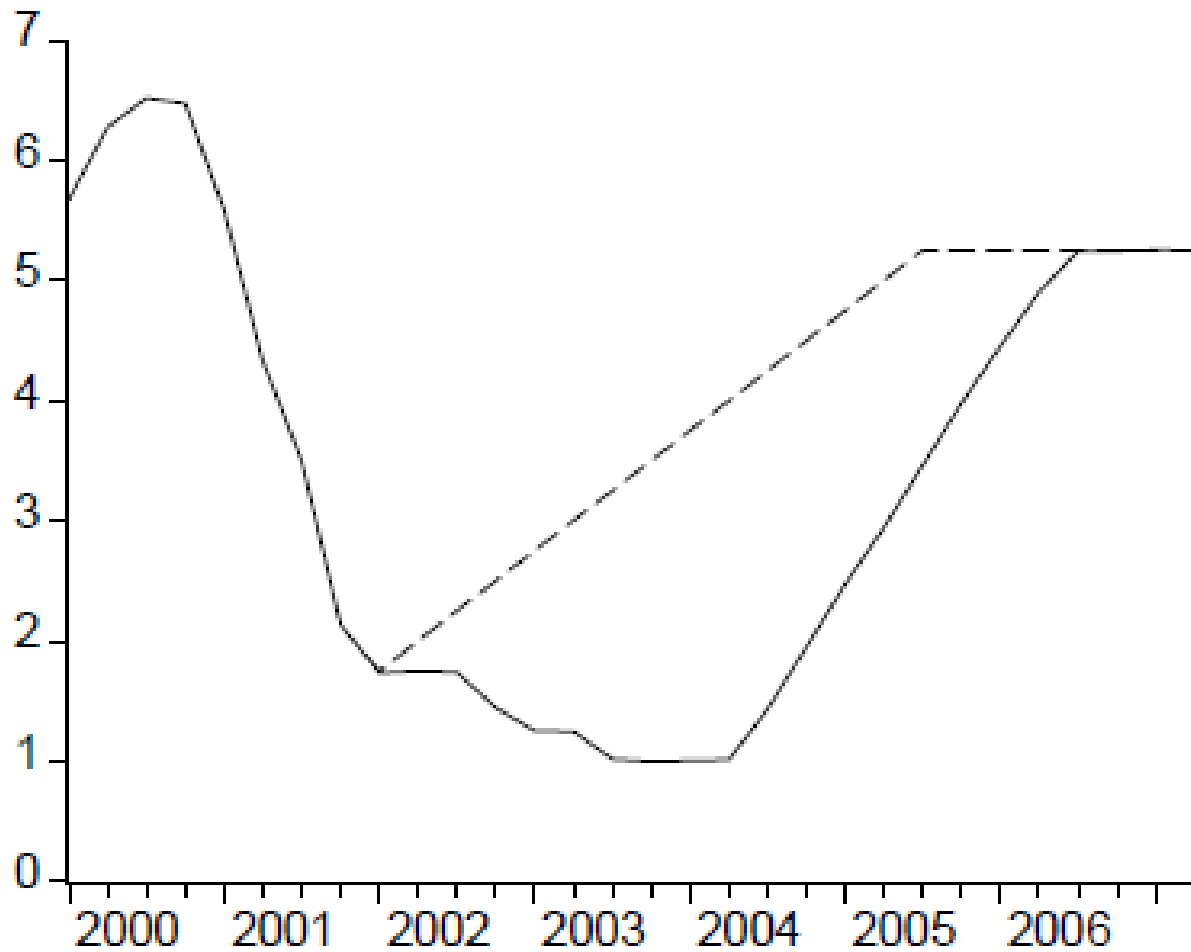
Overview

- Present: Many complaints about cross-border monetary policy spillovers
 - calls for international monetary policy coordination
- Past: Contrasts sharply with 1980s, 1990s and until recently, which was...
 - Near an Internationally Cooperative Equilibrium (NICE)
 - Much as theory predicted
 - Non-Inflationary Consistently Expansionary (NICE)
 - a NICE system for a NICE time
- Future?

Explanation #1

Monetary policy deviations at some central banks led to policy deviations abroad

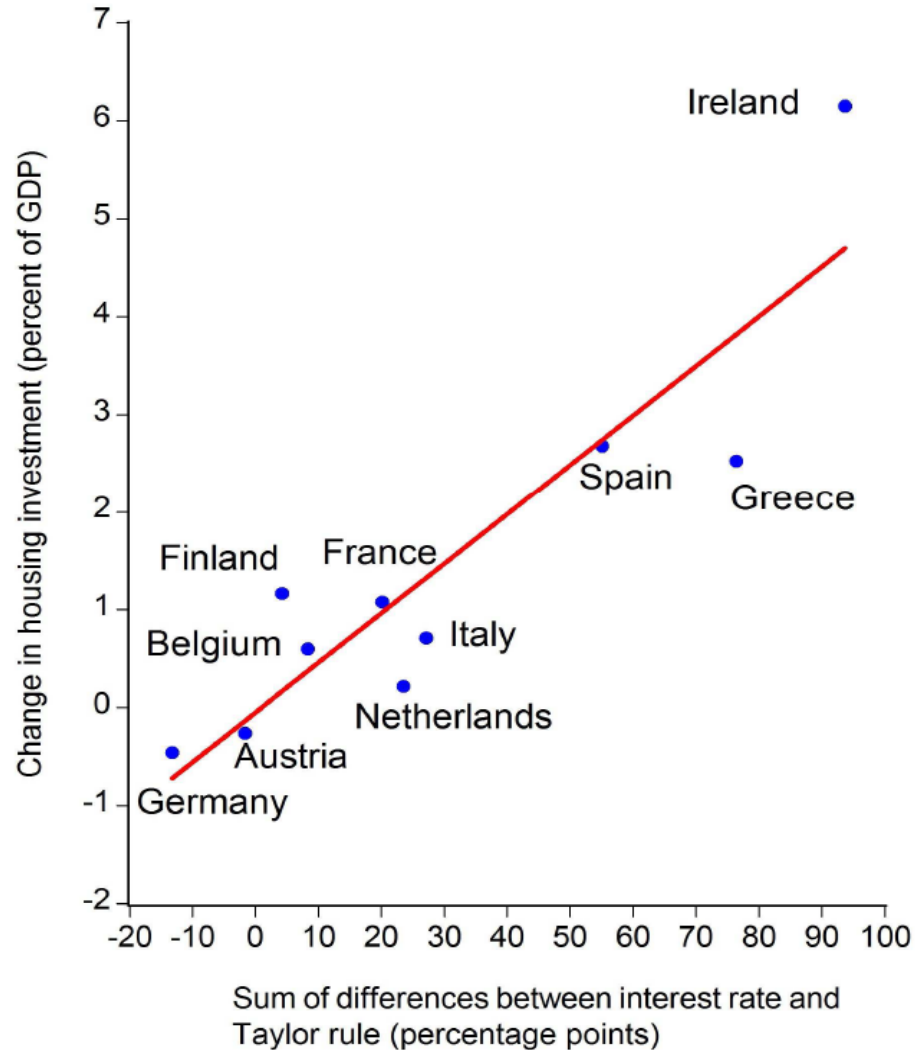
- Examples
- Global Great Deviation
 - Hoffmann & Bogdanova (2012)



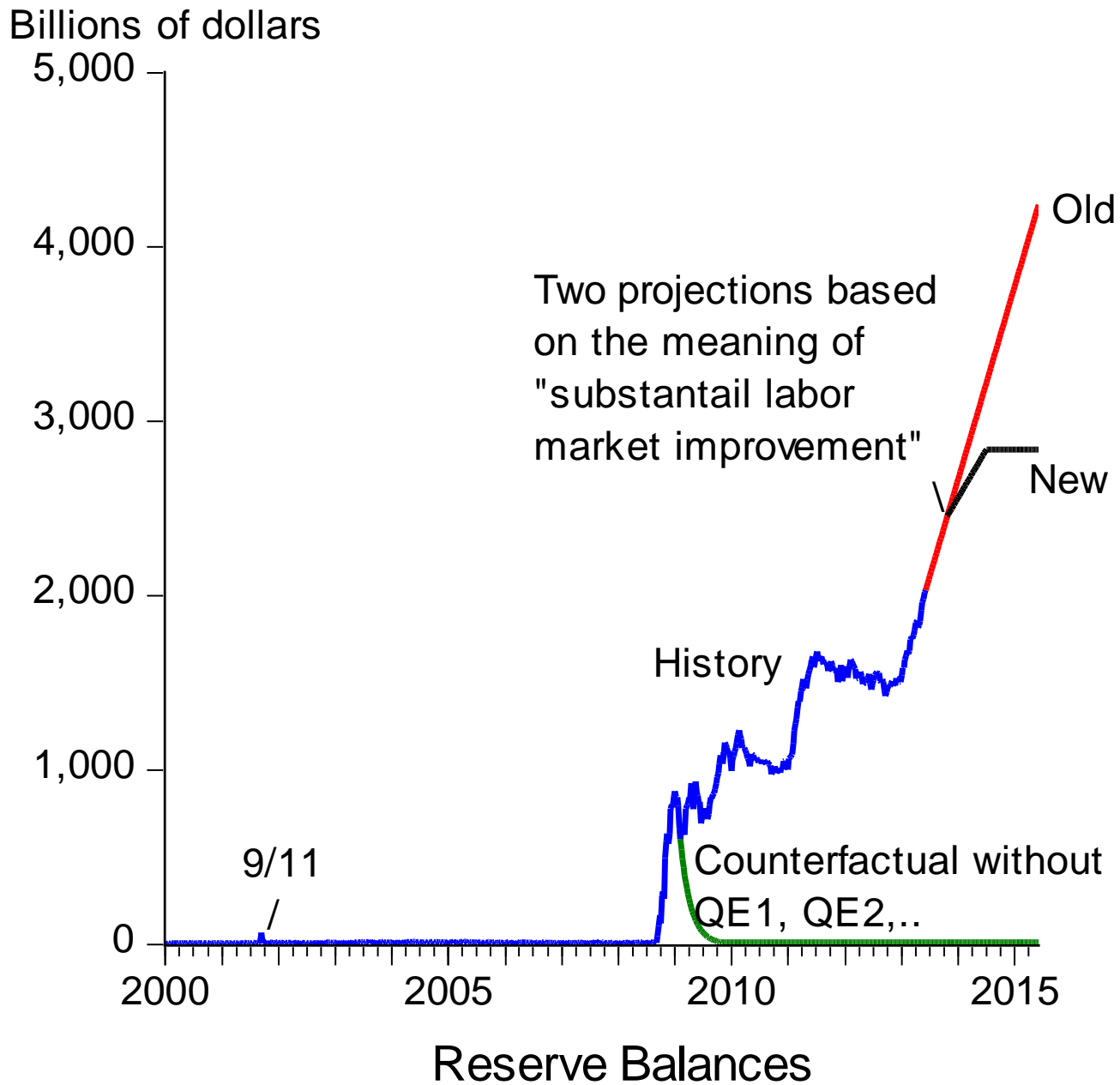
--- Counterfactual Federal Funds Rate
— Actual Federal Funds Rate

Source: Taylor (2007)

Housing Investment versus Deviations from Policy Rule in Europe During 2001-6



Source: OECD



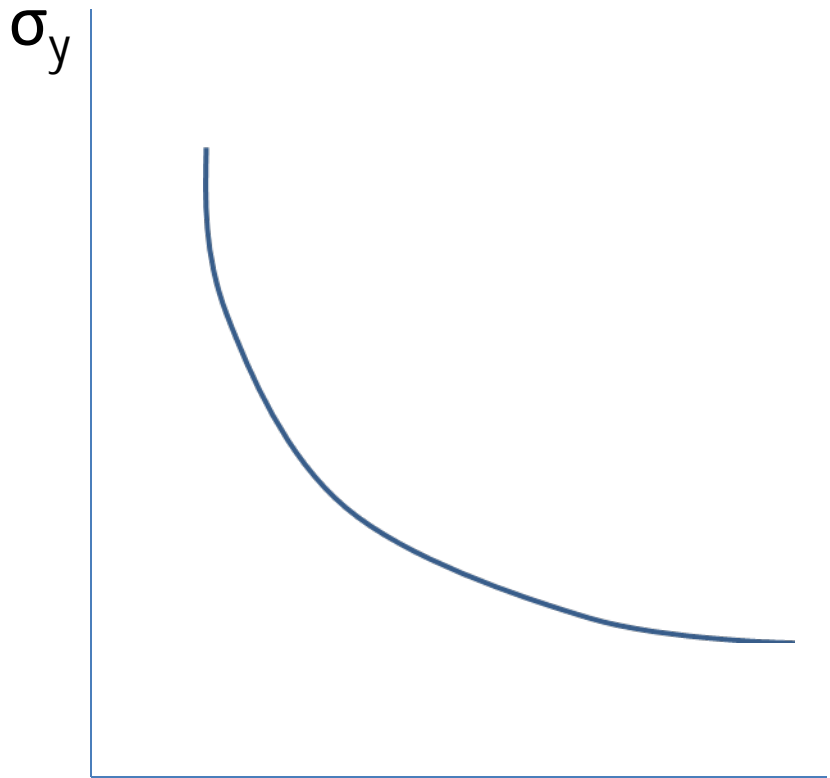
Explanation #2

No policy deviations; policies are good.

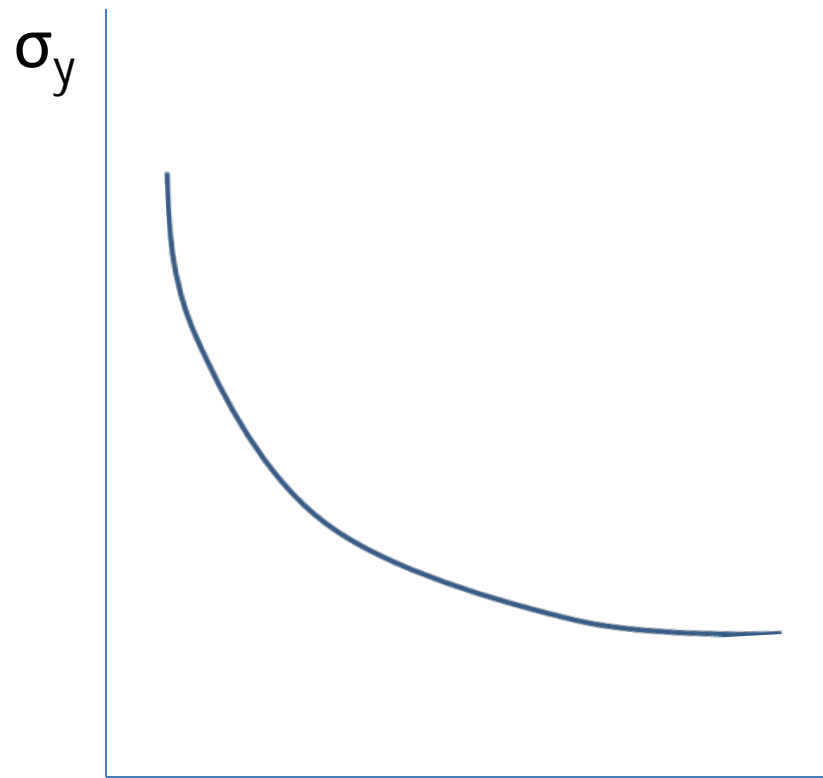
- Not beggar-thy-neighbor
- Complaints are part of a move to easier policies
- Don't worry so much about interest rate differentials or capital flows and controls.

Simple Monetary Theory of NICE

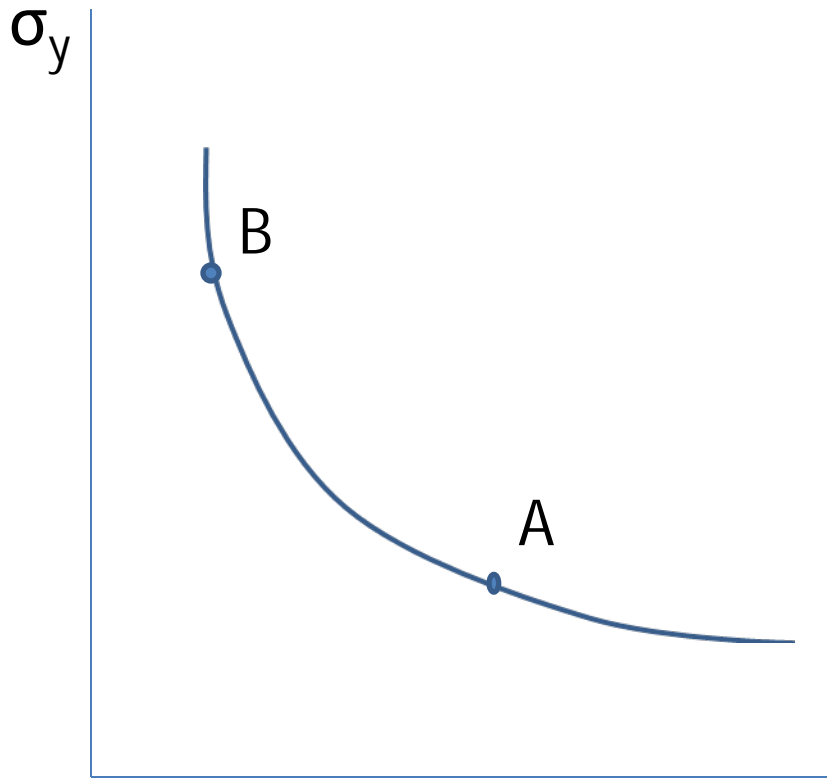
- perfect capital mobility
- a flexible exchange rate
- staggered wage setting
- domestic prices affected by
 - domestic wages
 - price of foreign goods
- output influenced by
 - the real interest rate
 - the real exchange rate
 - foreign demand for exports
- demand for real money balances determined by
 - real income
 - nominal interest rate
- Simple rule for monetary policy in each country:
 - policy rate responds to aggregate prices



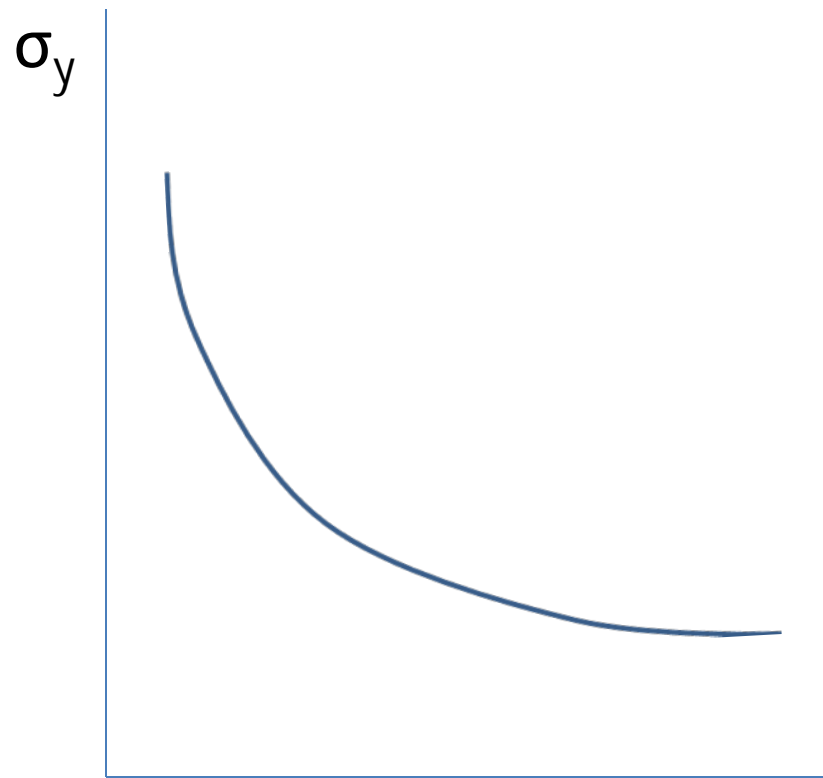
Country 1



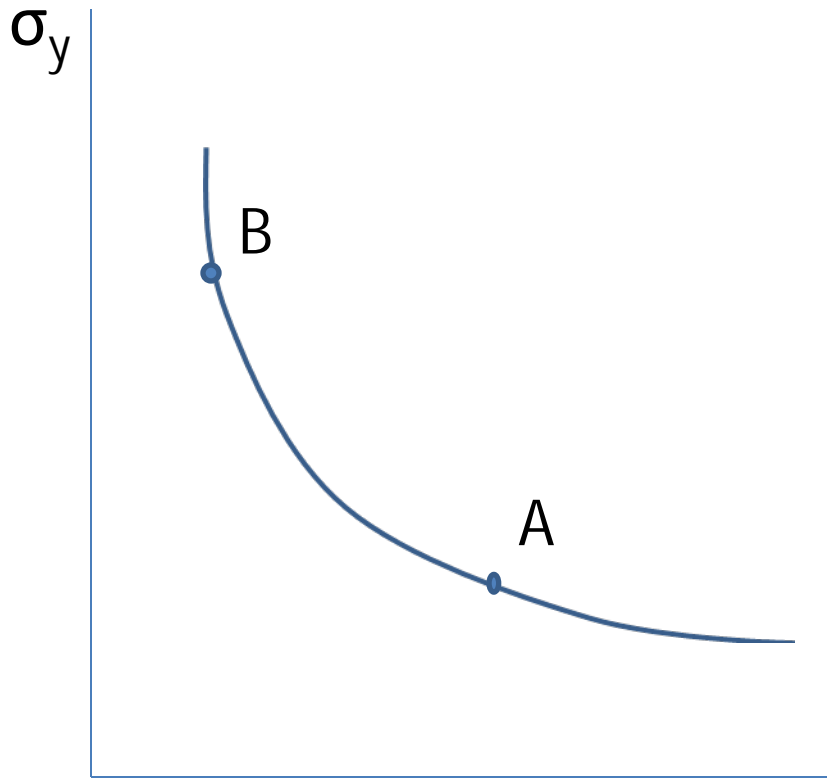
Country 2



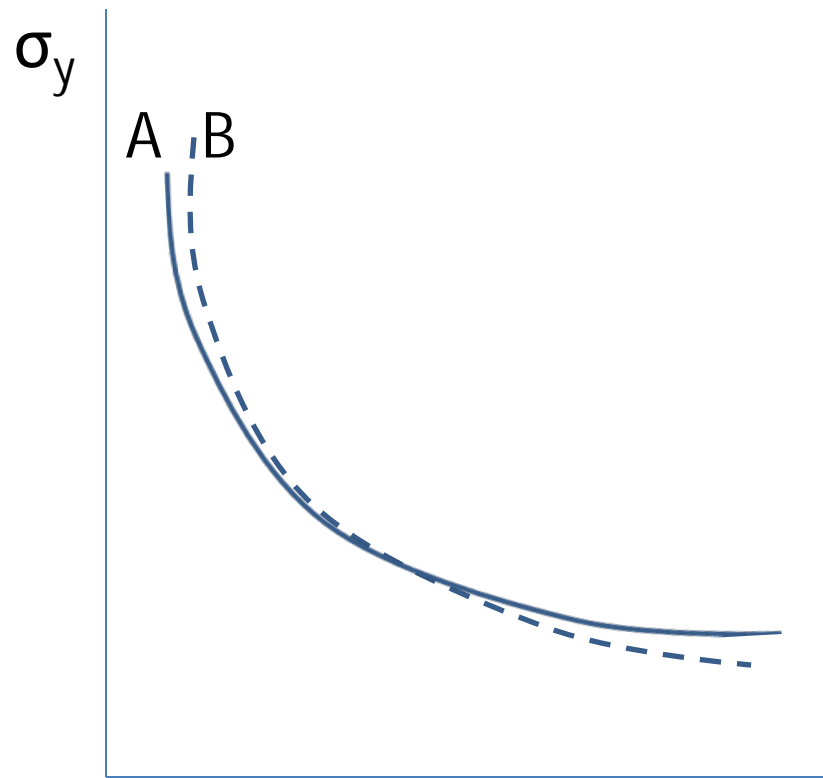
Country 1



Country 2

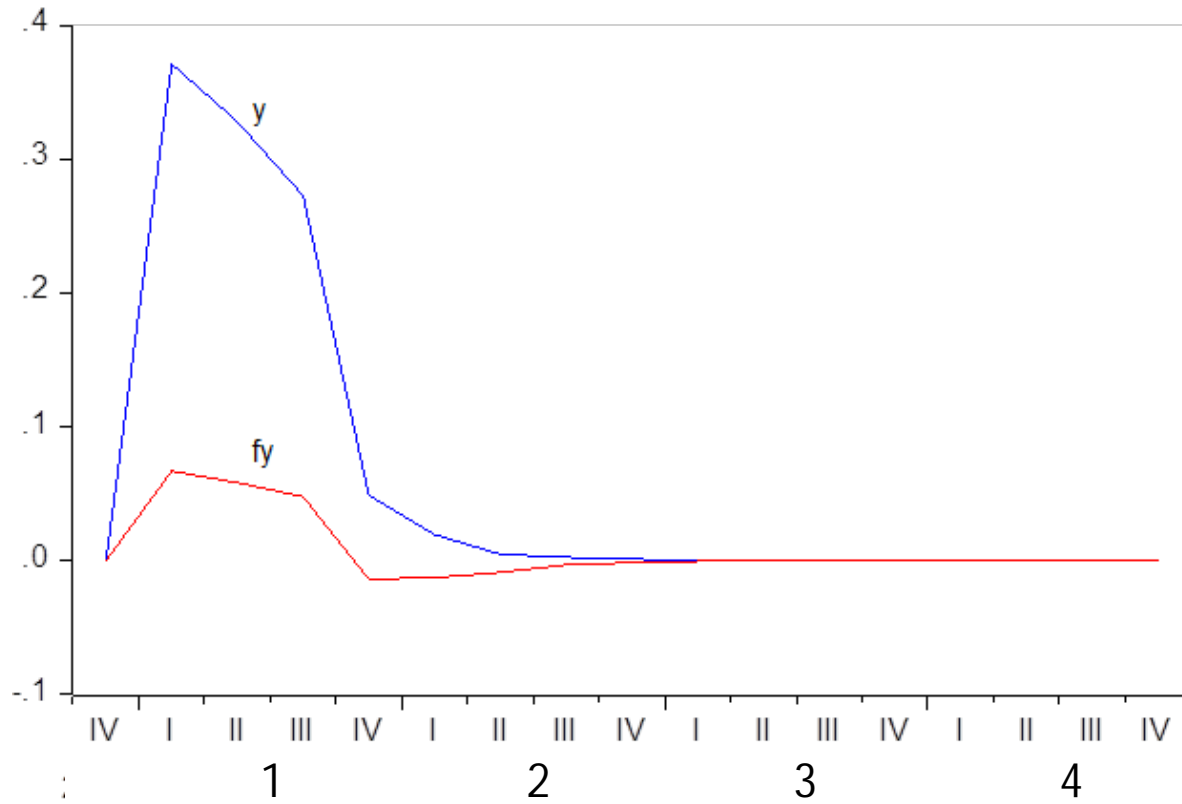


Country 1

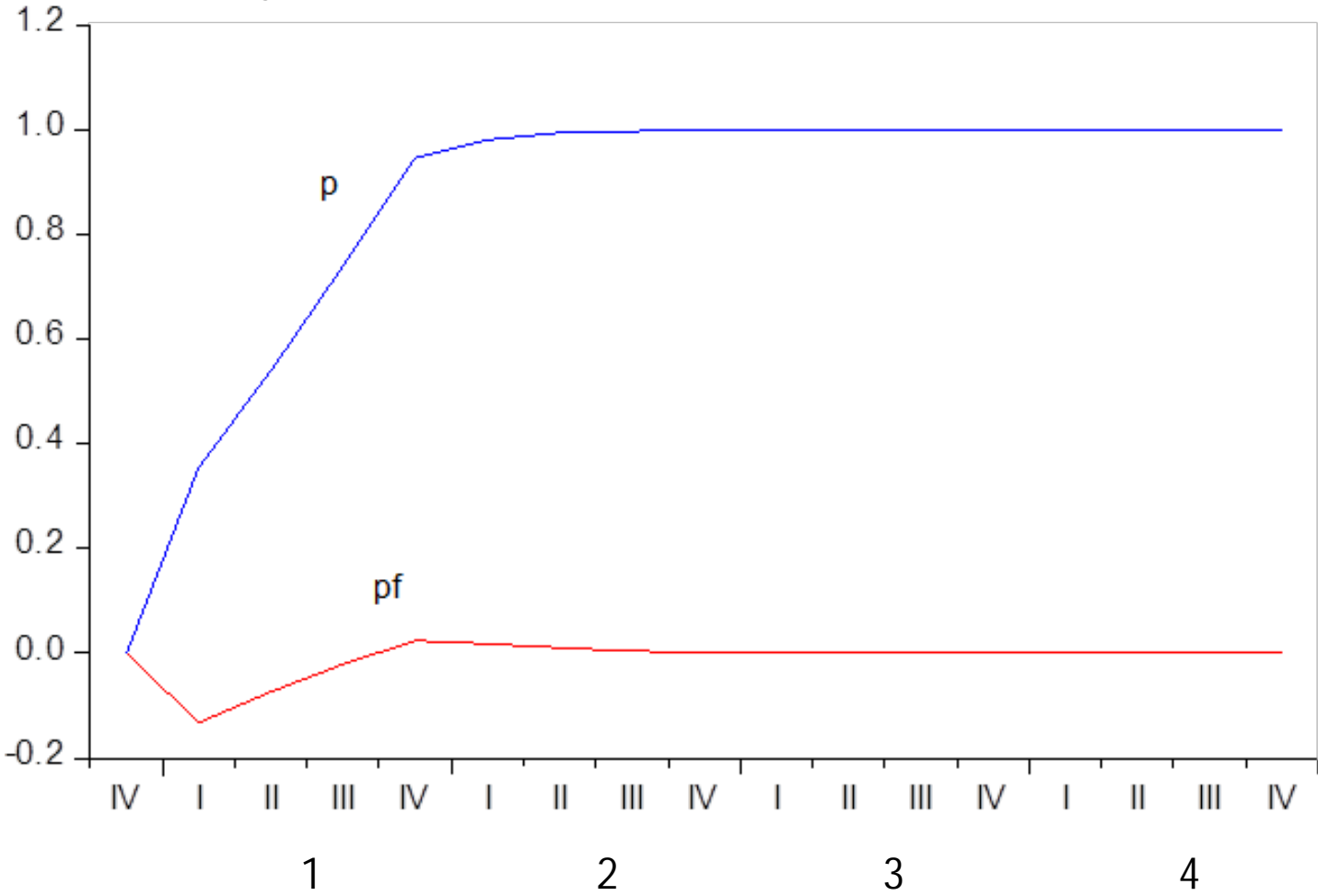


Country 2

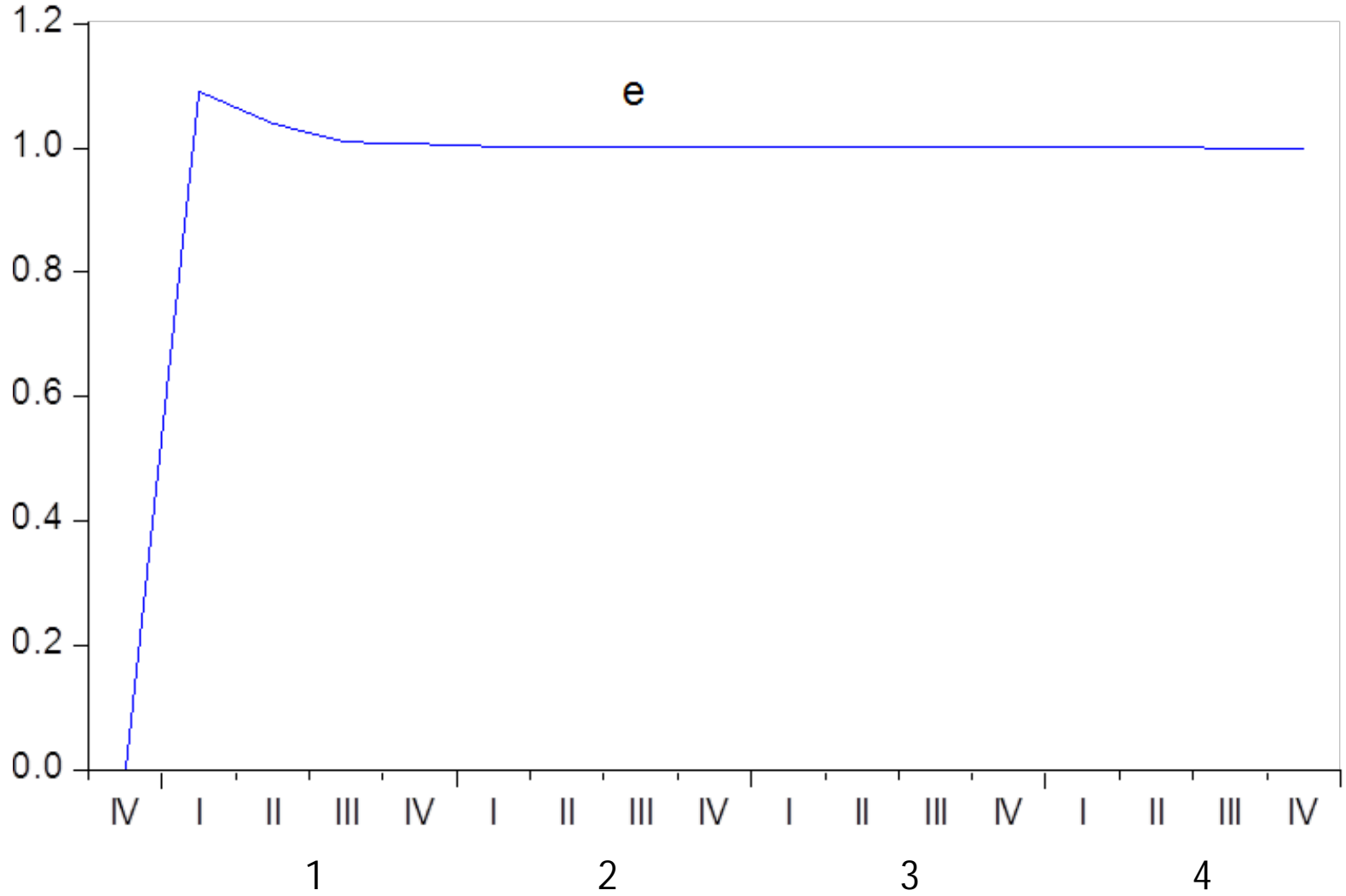
Percent change from baseline



Percent change from baseline

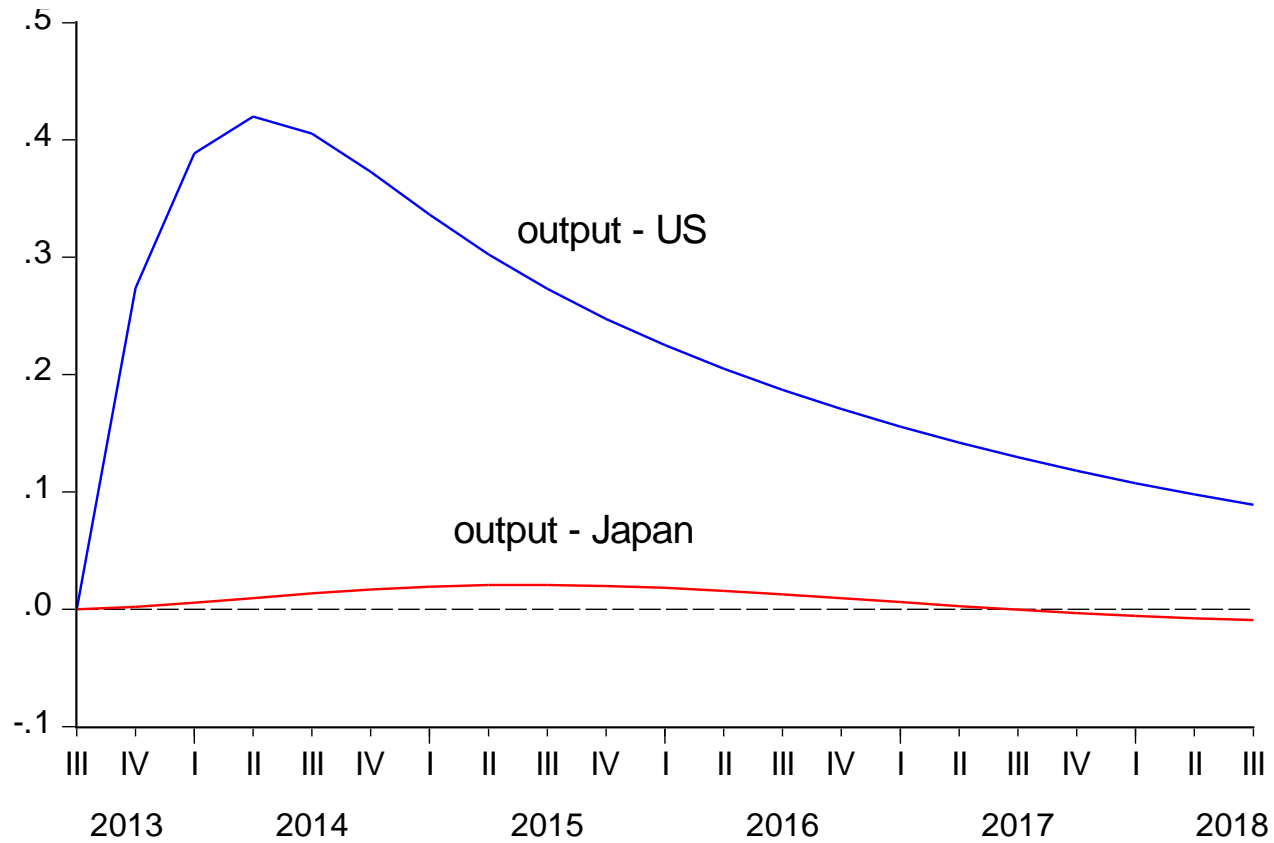


Percent change from baseline



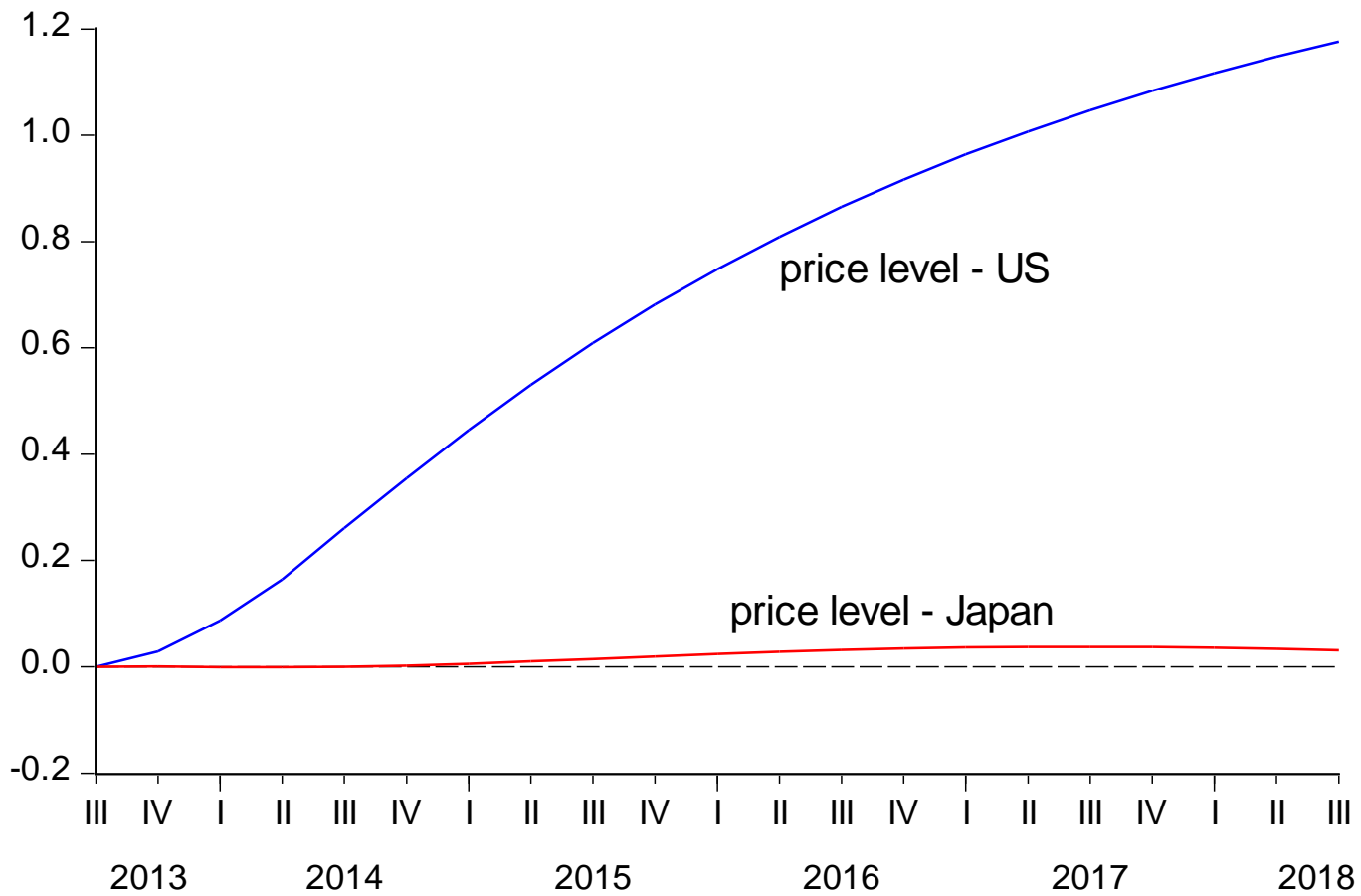
Empirical Support from Estimated Models...

Percent change from baseline



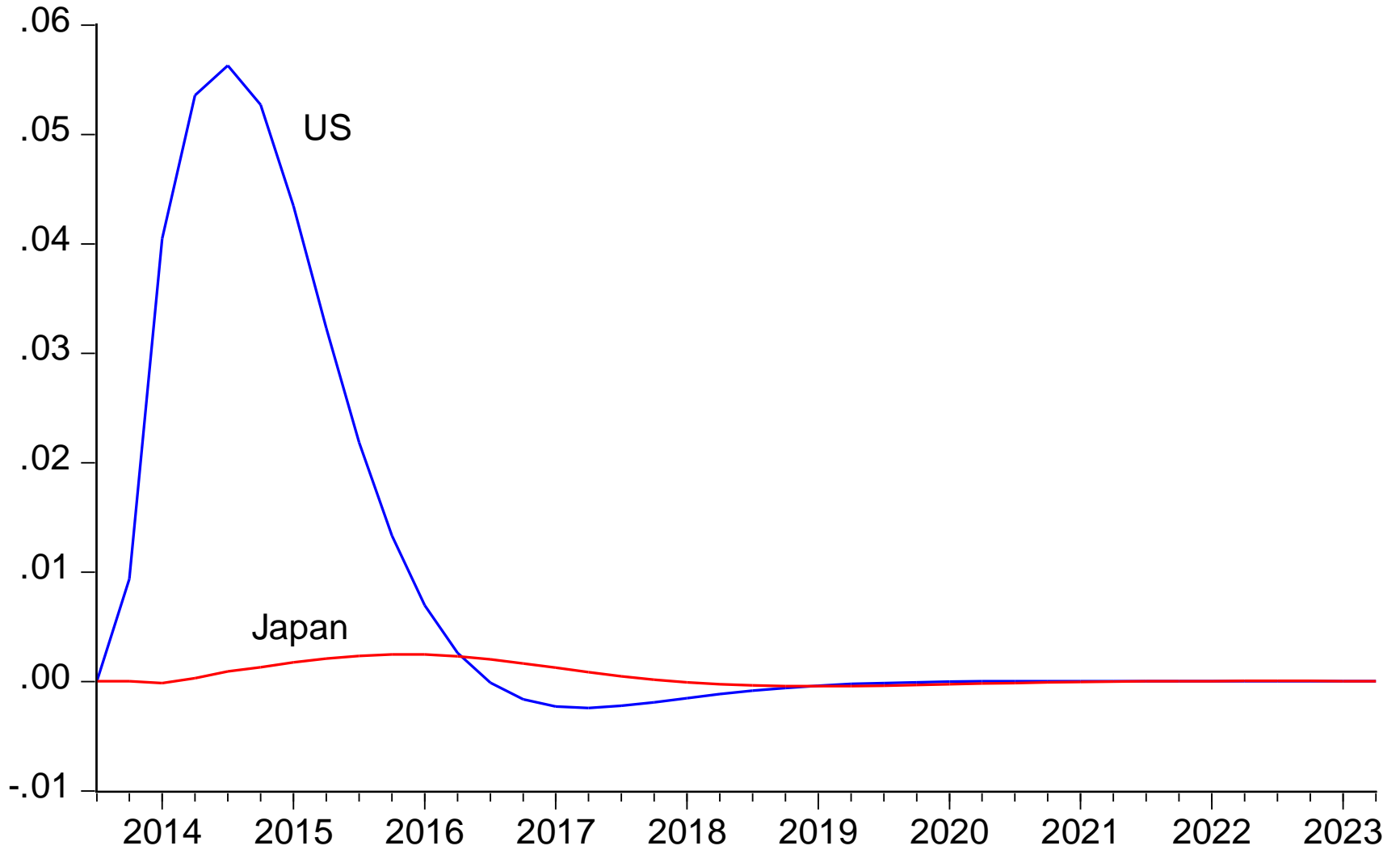
TMCM

Percent change from baseline



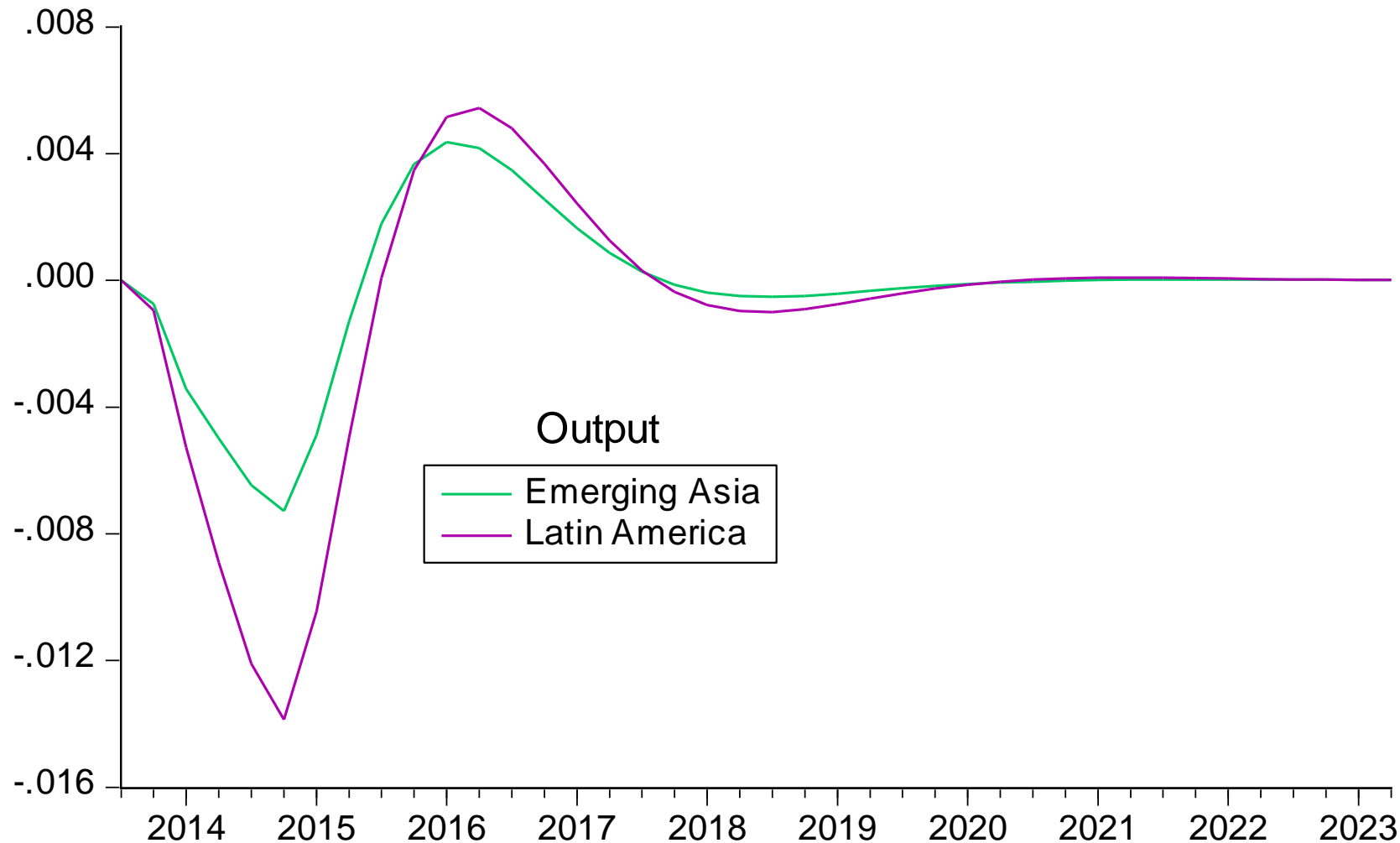
TMCM

Percent deviation
from baseline



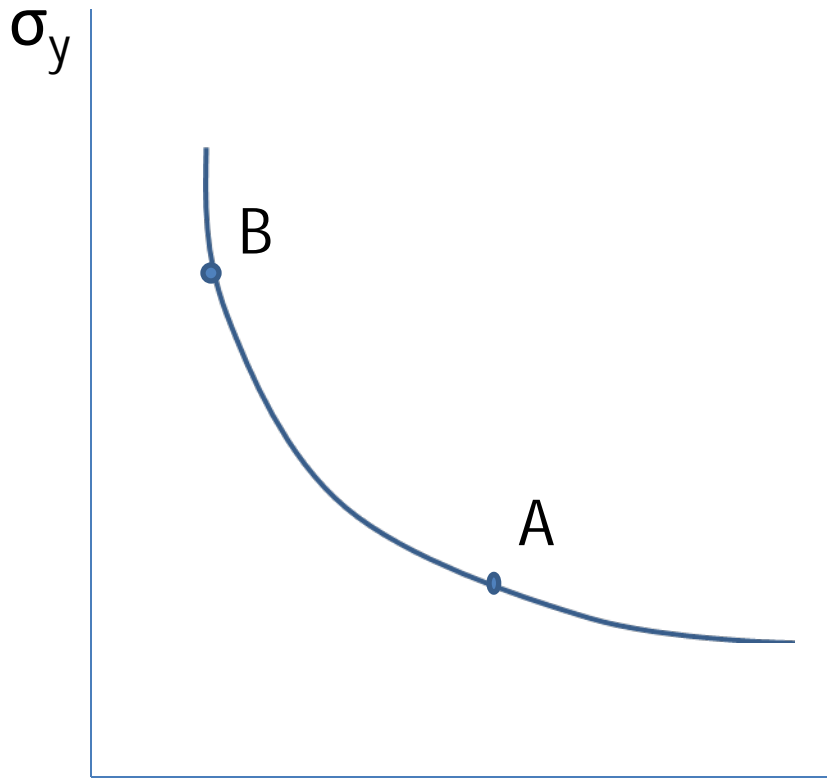
GPM6 - IMF

Percentage deviation
from baseline

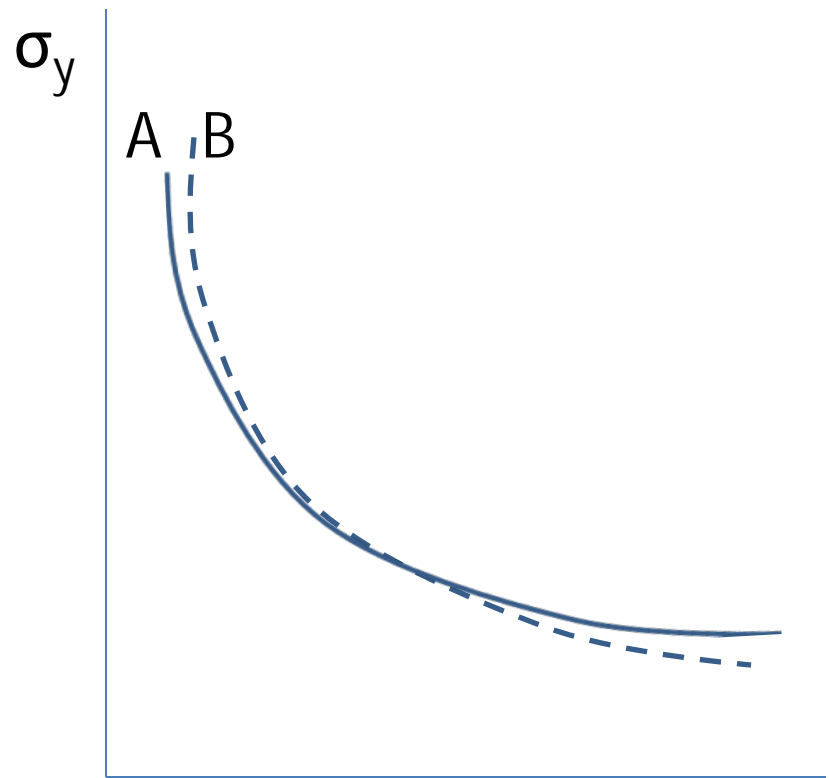


GPM6 - IMF

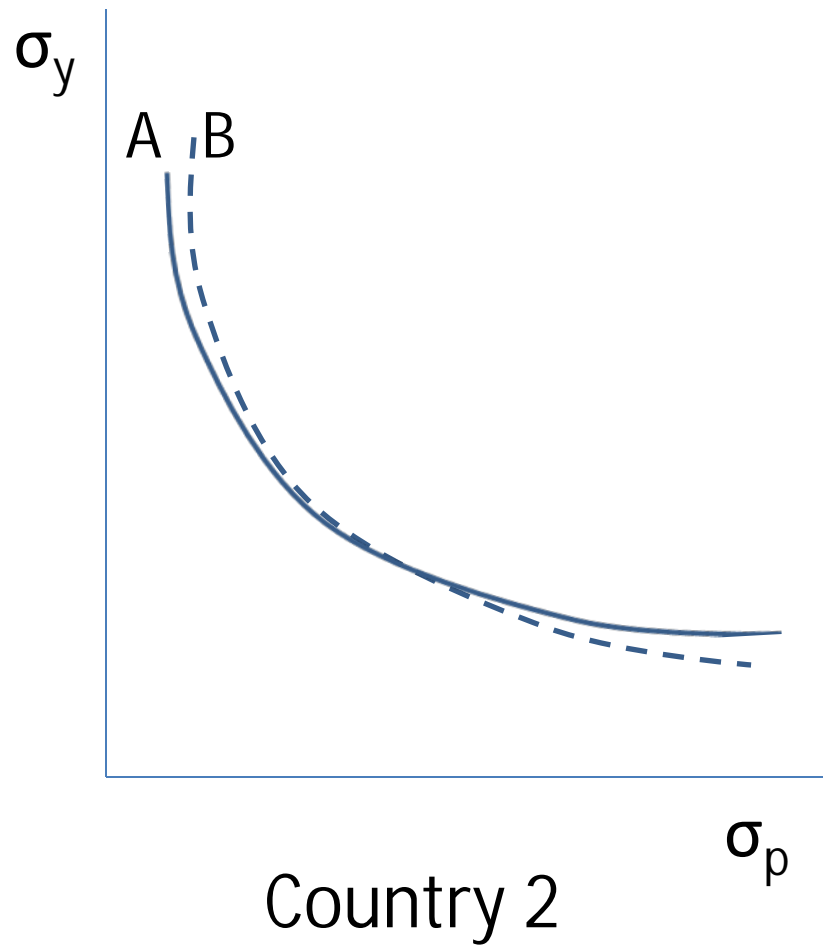
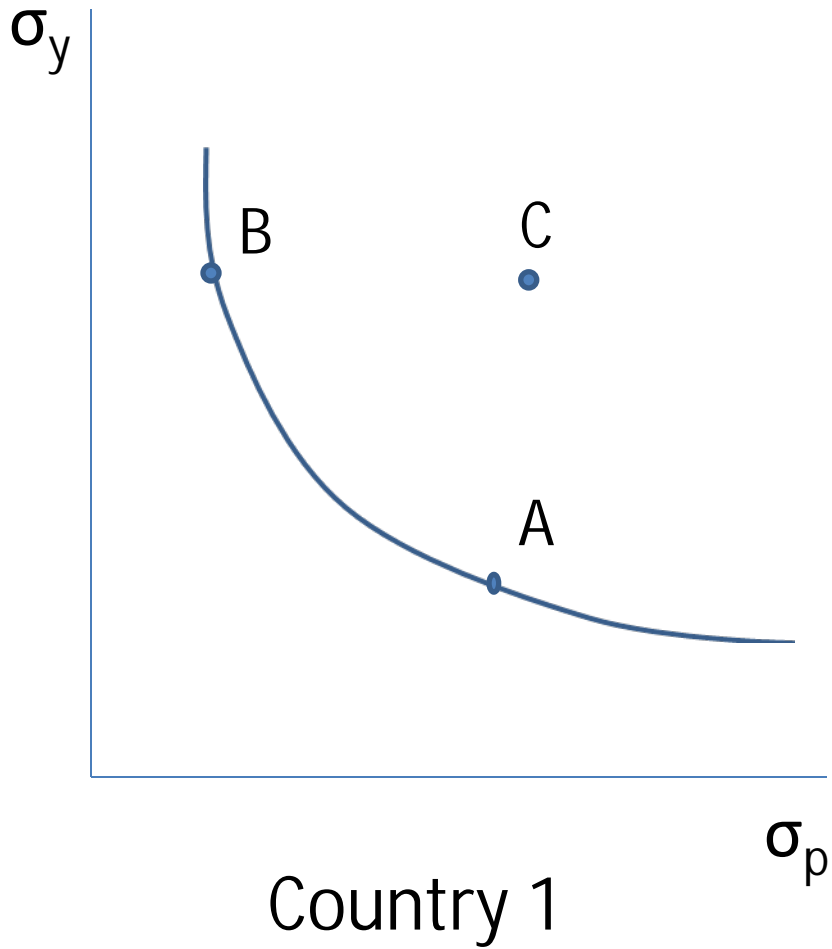
The Breakdown of the NICE System...

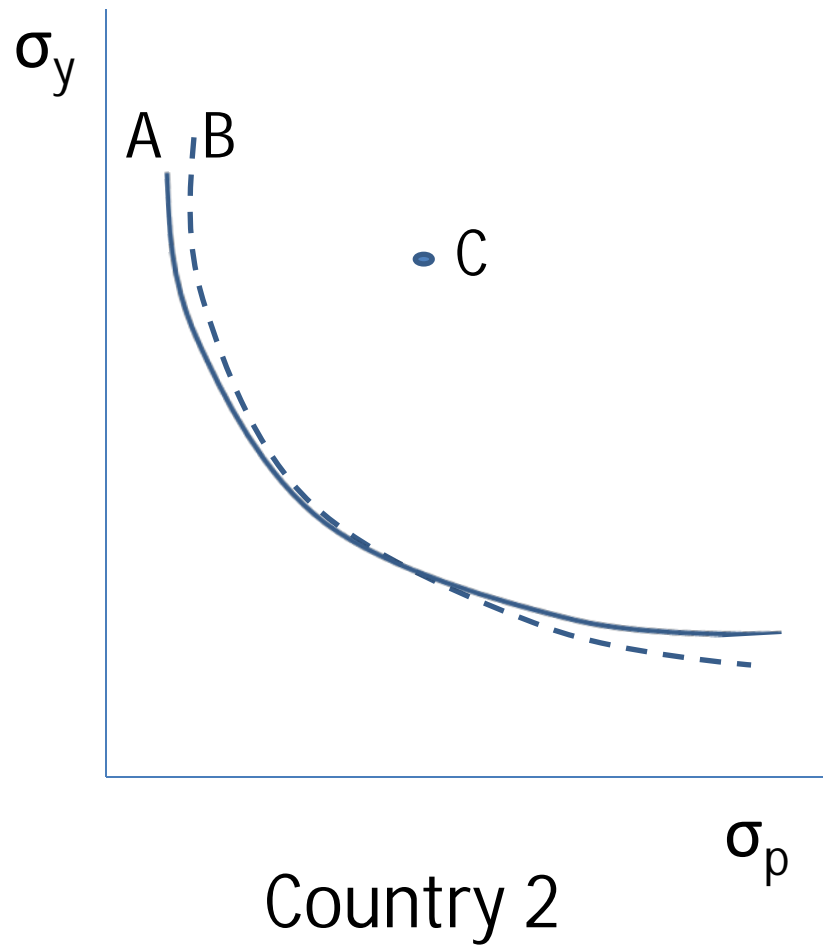
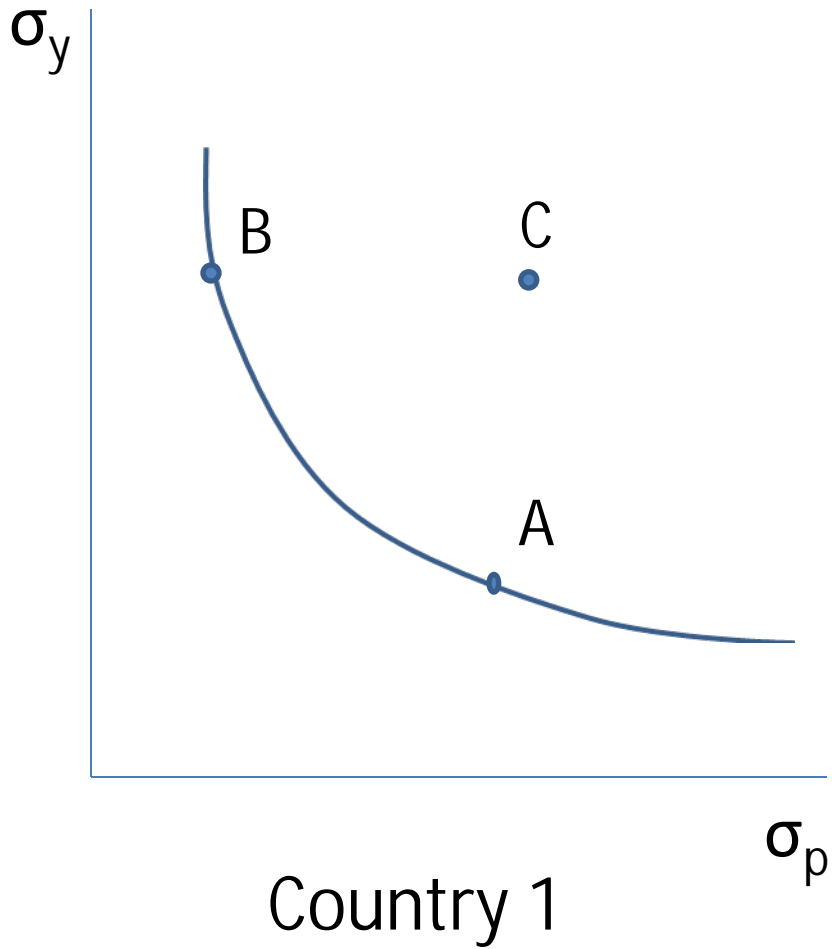


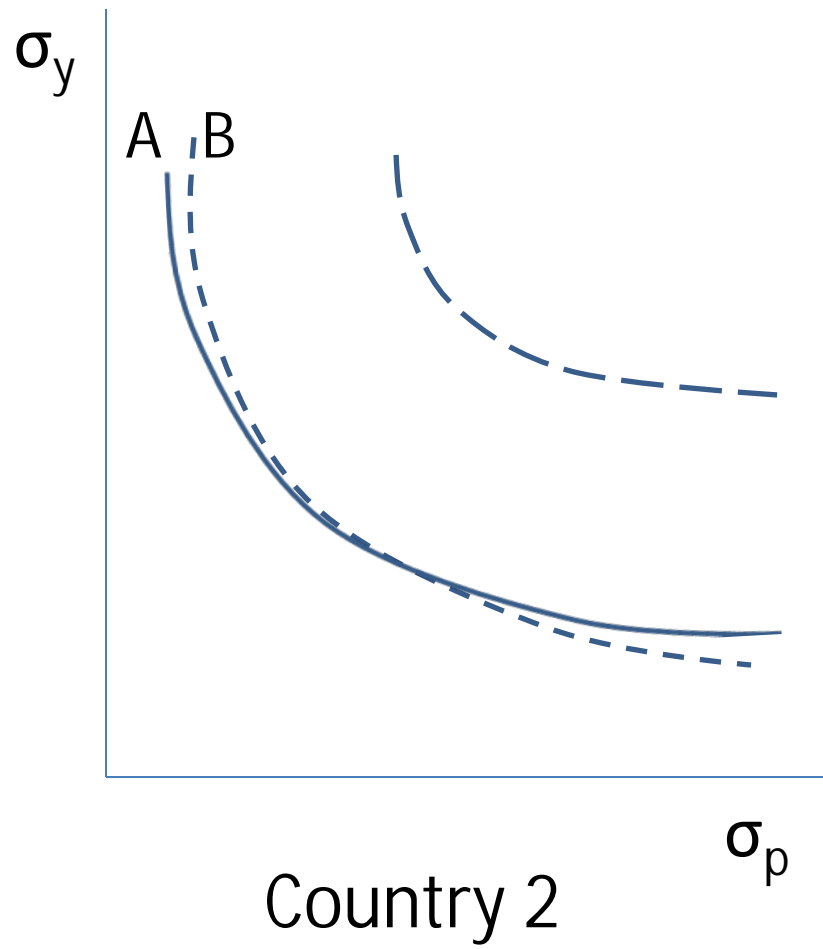
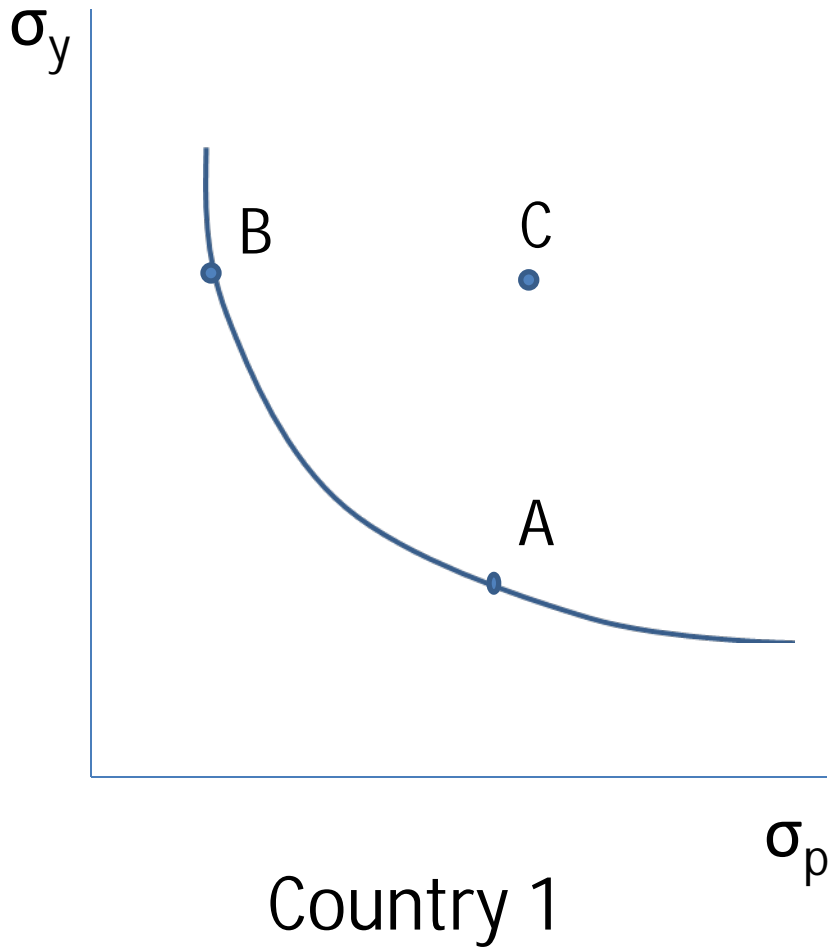
Country 1

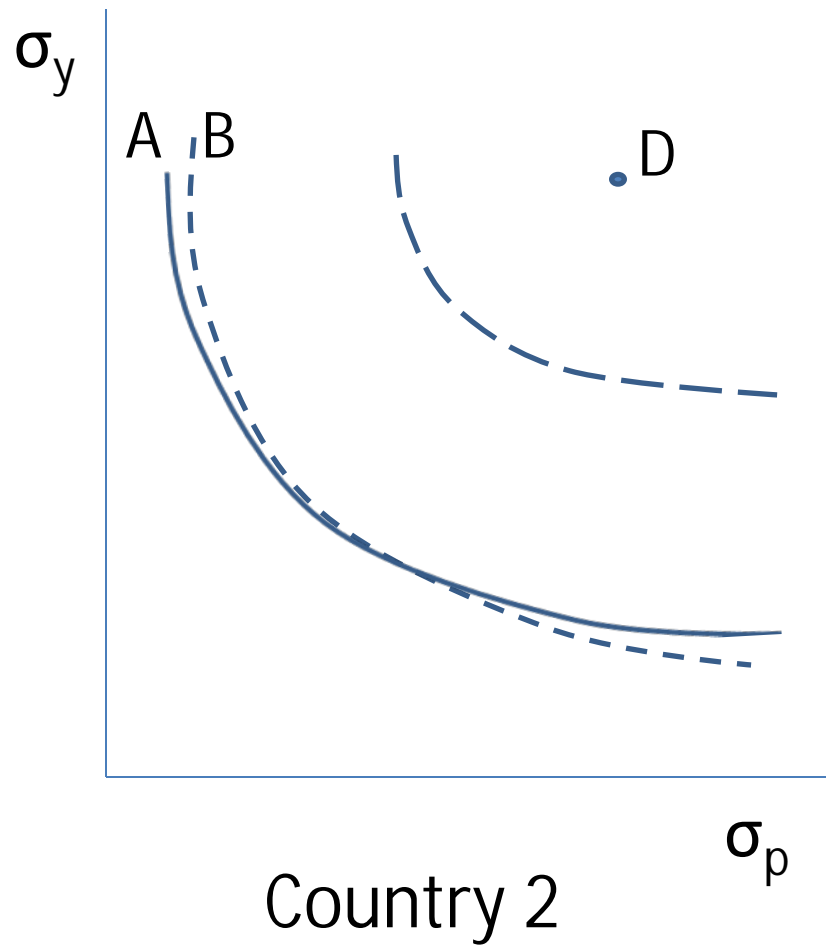
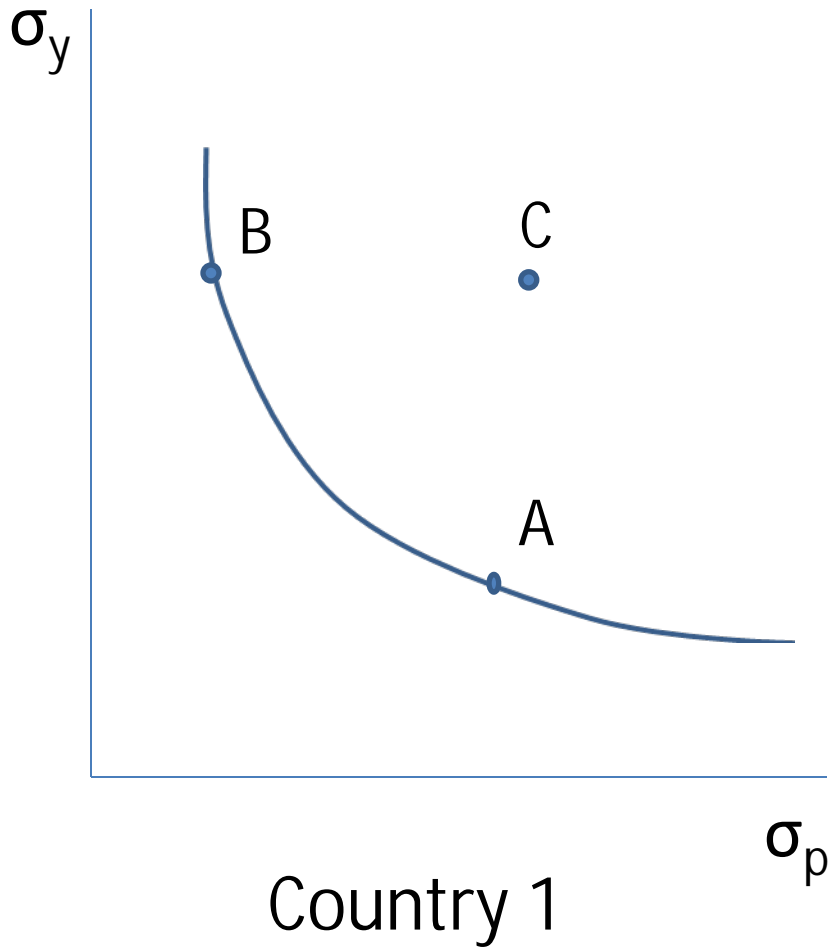


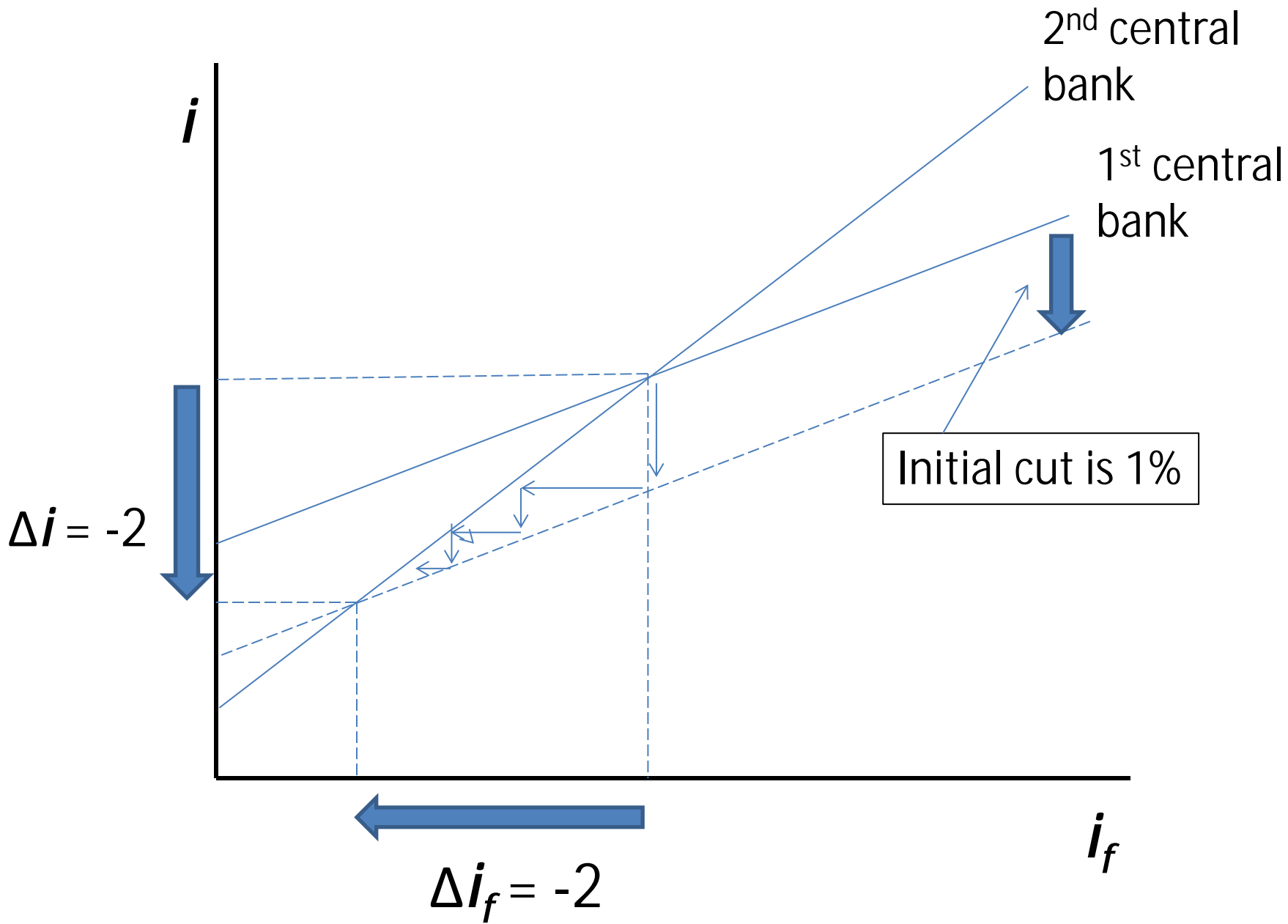
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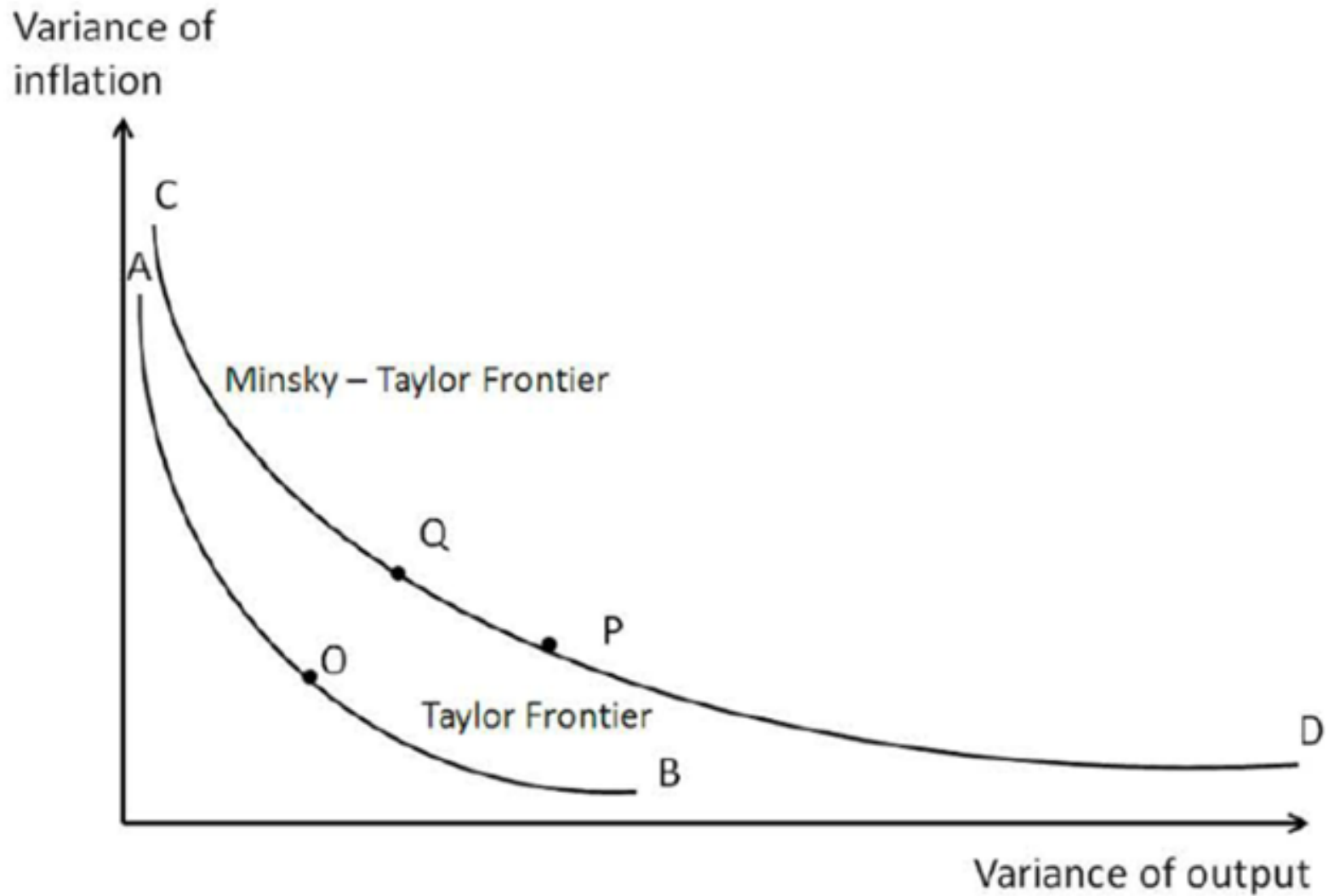








Alternative View: The Tradeoff Curve Shifted



Source: Mervyn King's Stamp Lecture (2012)

Key Points Behind Alternative View

- Rules-based policy is good in normal times,
 - But “times are by no means normal”
 - So we have to deviate
- Global deviation is good (at least for G7)
- “these policies are not ‘beggar-thy-neighbor’ but rather are positive-sum, ‘enrich-thy-neighbor’ actions”

Going forward

- Goal should be an expanded rules-based system similar to the 1980s, 1990s and until recently which would operate near an international cooperative equilibrium.
- International monetary policy coordination—at least formal discussions of rules-based policies and the issues reviewed here—would help the world get to this desirable situation