Central Banking: Perspectives from Emerging Economies

Discussion of Paper by Menzie Chinn

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Main conclusions

- Emerging markets are different
- Inflation targeting has proven a durable framework
- Trilemma binds more strongly

Discussion

- How robust are these conclusion?
- What should be the agenda?

Different, yes, but how much?

- Less developed financial markets
- Susceptibility to rapid capital flow reversals
- Procyclical fiscal policies
- Inability to borrow internationally in domestic currency
- Minimal ability to influence global markets

Comparison with the eurozone

	Emerging Markets	Eurozone
Financial Markets	Have a come a long way	More advanced than emerging, but significantly so?
Capital Flow Reversals	More prone to reversals but less hurt by Great Recession	Less prone and so policy complacency till big reversal, but same mechanism
Procyclical Fiscal Policies	Yes, but less so over time	Procyclicality is embedded in fiscal framework
Inability to borrow in domestic currency	Less so over time	Yet they borrowed in dollars to create grave peril
Minimal ability to influence financial markets	Yes.	Any more so than emerging markets?

Inflation Targeting Durable?

- Those that target and don’t target show little difference in response to inflation
- Oddly, those that target inflation pay more attention to the output gap
- Before the crisis, both paid attention to the exchange rate
- After the crisis, inflation is unrelated to interest rate setting
- Inflation targeting: a loose framework that means different things to different people.

The Trilemma Debate Today

- Helen Rey, August 2013
  - US monetary policy determines global financial cycle
  - Imposes binding constraint on domestic monetary policy
  - Independence possible only through capital controls
- Klein and Shambaugh, September 2013
  - Capital controls do not work
  - Even modest exchange rate flexibility helps
- Forbes, Fratzscher, Straub, December 2013
  - Capital controls do not work on macro targets
  - But can help reduce financial vulnerability: credit growth, currency mismatches.

The “Rakesh Mohan View”

- Emerging market policymakers aim for:
  - moderate levels monetary independence and financial openness
  - some degree of exchange rate stability
- Thus, leaning against the trilemma
  - while accumulating sizable foreign exchange reserves
  - As an integral element of monetary policy management

The debate

- Emerging/advanced distinction is a overstated
- Inflation targeting is a useful rhetorical device
- The real action: dilemma/trilemma
  – US monetary policy may reflect domestic concerns but has global implications
  – Japan and Euro area: smaller but real consequences
  – Global monetary coordination : politically impossible?
  – Rounding the trilemma corners: options?