

Discussion of
J. Bullard and E. Schalling's
"Monetary Policy, Determinacy, and Learnability in the
Open Economy"
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In a New Keynesian open economy model, the authors study

- determinacy of REE
- convergence to REE under learning

under a variety of policy rules

- Taylor rules
- exchange rate rules
- Targetting rules
- coordination or competition among countries

Extending many papers in the literature (Evans and Honkapohja, Bullard and Mitra, Orphanides and Williams, Ferrero, Aoki, ...) to open economy.

Comments

What is the reason this paper should be published?

1. It shows there can be policy interactions among countries.

Ok, but ... not very surprising.

Could be achieved with a much simpler model. For example

- Assume shocks are serially uncorrelated, learning parameters go from 20 to 4.
- Can you simplify model to a Cagan-type money demand. Go from 20 to 2 parameters.
- With two parameters one can analyze behavior of economy in a two-dimensional graph.

2. To have a collection of results allowing us to study actual behavior of exchange rate, inflation and output with a model of learning.

This should be real objective.

This paper is just a first step.

Even as a first step, it would be nice to have

- more intuition for convergence or divergence
- 2. in a simple example

Some possibilities:

- does exchange rate have very strong low frequency movements in the model?
Probably.
- Is the relationship between inflation and exchange rate as in the data?
Will depend on parameters.
- can you generate currency crisis?.
Probably, just as Marcet and Nicolini (2003) generate hyperinflations.
- when is business cycle transmission in the model similar to the data?

- On fixed exchange rates, can we explain China now vs. Argentina in the 90's?

Why did Argentina have a financial crisis but China is doing so well?

- different policy?

It would seem 100% backing of monetary base would work in favor of Argentina.

- bad priors on Argentina?

(in ECB language: *inflation expectations were not anchored* in Argentina)

If so, why is it that eleven years of good behavior did not erase these priors?

- different fiscal policy?, how does it translate into shocks in the model?
- they are in fact the same.

Perhaps eigenvalue of B is very close to 1.

China did not have a financial crisis ... yet?

Near-rationality

If model is used for real data, one must check near-rationality of learning scheme.

Indeterminacy

Does not mean much per se.

Just means there is unfinished work.

But in this paper

Indeterminacy = instability under learning.

so all work has been done here!.

Speed of Convergence

Within models that converge, speed of convergence can be very different.

If learning is stable but one eigenvalue of B is close to 1, very slow convergence.

For policy recommendations and applications to real data speed of convergence is very important (Ferrero 2004).

Would like to see "iso-speed" curves.