

Discussion of Currency Manipulation

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Gains from Exchange Rate Stabilization

- Trade (Bacchetta, Van Wincoop)
- Nominal Anchor and Credibility
 - The mirage of Fixed Exchange Rate (Obstfeld)
- Financial Market Development
 - Nominal Stability and Endogenous Asset Supply (Gaytan, 2004)
- Growth
 - Long run growth effects of exchange rate regimes (Aghion, Bacchetta, Ranciere, Rogoff, JME, 2009)

Some Frictions Involved

- Deviation from PPP (trade)
- Commitment/Credibility Issue (Nominal Anchor)
- Limited Participation and Non Convexity (Acemoglu-Zilibotti)
- Borrowing Constraints (ABRR)

ABRR

- Current Profits affect future investment and growth
- Stabilizing Profits
 - Real Shocks: Floating Regime
 - Financial Shocks: Fixed Regime
 - Optimal Exchange Policy

Risk-Channel of ER Stabilization

: This paper

- Large country currencies tend to
- Pay little interest rate in good times
- Appreciate in bad times where trade goods are expensive
- Hedge against consumption risk
- Favor capital accumulation (low interest rate)
- Can we « import » this property by pegging.
- What are the effect of the targeted countries

Among Different cases

- **Best Case:** Small country pegging to a large country. Negative cost of stabilization. Reserves accumulation.
 - Small emerging economies pegging
- **Damaging Case:** Country target of stabilization by a large country can lose.
 - Transfer its advantage to the other
 - (China-US). Shift in capital accumulation.

Issues for Discussion (1)

- Evidence:
 - Most evidence comes from the dollar which displays other features (exorbitant privilege)
 - Similar evidence for other relatively large country currency: Euro, South African Rand
- Multi-Lateral issues
 - Two countries pegging to a third one also peg between themselves.
 - Is it optimal? Can it overturn the result.
 - East Asian Countries

Issues for Discussion (2)

- Types of Shocks involved
 - Small shocks (Business Cycles)
 - Large shocks (Financial Crises)
- Ability to peg
 - Cost of Reserves
 - Credibility of Exchange Rate
 - The Case of Dollarization

Issues for Discussion (3)

- Stage of Economic Development and Optimal Exchange Rate Policy
 - When to switch?
- Maximizing World Welfare
 - What should the IMF do in that context