“Surfing the Waves of Globalization: Asia and Financial Globalization in the Context of the Trilemma”
by Joshua Aizenman, Menzie Chinn, and Hiro Ito

Comments by Sergio Schmukler

8th Research Meeting of the NIPFP-DEA Program
New Delhi
March 15 and 16, 2011
Comments

- Very nice paper
- Difficult exercise to undertake
- Lots of results
- Very interesting findings
- Many results, most of them very sensible and consistent with expectations
- Very useful for policymakers
- Given amount of results and expertise of the authors, somewhat difficult to comment
Role of international reserves (IR)

- Paper introduces IR to the trilemma as a fourth element
- Three other elements are openness, monetary policy, and exchange rate policy
- But given level of openness, IR are part of the monetary and exchange rate policy
- Is it really a fourth element?
- Are diamonds a reflection of how countries choose within the triangles?
- Especially during the recent period of financial integration
- And at any time, given sluggishness and monotonicity of openness
Comments

Closed to Capital Movement

Moneatary Independence

Exchange Rate Stability

Floating Exchange Rate

Financial Integration

Fixed Exchange Rate
Comments

- Closed to Capital Movement
- Fixed Exchange Rate
- Floating Exchange Rate
- Monetary Independence
- Exchange Rate Stability
- More Use of Reserves
- Financial Integration
- Fixed Exchange Rate
Comments

More on reserves

- Used for several purposes
- For mercantilist goal, for undervalued exchange rate
- For crisis prevention
- As mean of saving abroad
- Here, only to stabilize exchange rate?

Exchange rate stability

- “Instability” could be good or bad, depending on the context
- Should policymakers care about this volatility - context specific
- Volatility high in many countries with no major consequences, witness many developed countries. If so, why?
- How are the crises considered?
Comments

Asia
- What is different from Asia?
- While the discussion is Asia specific, the results seem more general
- Are other EMs becoming more like Asia?

Developed economies
- What do the results look like without Europe?
- Why not including them in the sample?
- Why not pool all countries?

Time periods
- Are 5-year averages enough to compute volatility measures?
- Is there anything particular about the time periods analyzed?
Comments

What are the policy implications?

- Does convergence to the middle make sense?
- Does paper argue in favor of holding large reserves?
- Up to what point? What to do beyond it?
- Gives lots of flexibility, plus countries do not seem to have been penalized
- Even if costly, the accumulation of more reserves appears to yield some benefit, even with higher inflation
Many results and many conclusions, hard to digest

- What is the bottom line of the authors?
- Some implications speculative, like effect on cost of capital
- Some parts repetitive
- Would be useful to understand more
Comments

Reference to trilemma paper but explanation not very clear

Use of dependent and explanatory variables not always transparent

- E.g., why use volatility for inflation and output and level for inflation only?
- Would it be useful to look at output growth rates?
- Use of many explanatory variables
- Capital flows a measure of financial openness too
- What are the relevant channels to study?
- Why does exchange rate volatility affect investment?
- More tied to theory or some ex-ante hypotheses, ideas?
Comments

- Economic size of coefficients
  - E.g., does use of reserve fully mitigate policies, up to a point?
- Use of level or flow of reserves as relevant variable?
- Endogeneity
  - Potential for reversed causality
  - E.g. inflation volatility and exchange rate stability
  - Mentions GMM but results are not reported
- Inflation volatility
  - Why using inflation volatility in both sides of the regression?
  - What are the differences between the two variables?
  - What are the implications?
Thank you!