The International Spillovers of Synchronous Monetary Tightening

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Abstract

We use historical data and a calibrated model of the world economy to study how a synchronous tightening of monetary policy can amplify cross-border transmission of monetary policy. The empirical analysis shows that historical episodes of synchronous tightening are associated with tighter financial conditions and larger effects on economic activity than asynchronous ones. In the model, a sufficiently large synchronous tightening can disrupt intermediation of credit by global financial intermediaries causing large output losses and an increase in sacrifice ratios, that is, output lost for a given reduction in inflation. We use this framework to study the gains from coordination that would arise if countries set interest rates cooperatively rather than autonomously adjusting rates to stabilize domestic conditions.

KEYWORDS: Monetary Policy; International Spillovers; Inflation; Panel Data Estimation; Open Economy Macroeconomics.

JEL CLASSIFICATION: C33. E32. E44. F42.

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