Adverse selection
in banking systems, 177
effect on banks' vulnerability, 177
Allocation of resources
induced by interest group lobbying, 265
Pareto-efficient, 265–266
Asset markets, international
in analysis of fiscal policy transmission, 11
in analysis of monetary policy transmission, 10
Balance of payments. See also Current account
adjustment to imbalances, xvi–xvii
current account estimates, 310
monetary and nonmonetary gold flows in, 305
monetary approach to, xvi
Balance-of-payments crises
conditions for, 133
Mundell's analysis, 431–432
perfect-foresight equilibrium model, 441–442, 444–445
size of response parameters (Mundell), 432
Banking crises
 costs of (1980s–1990s), 172
defined, 183
developing country macroeconomic conditions surrounding, 185–190
economic conditions as predictors of East Asian (1997), 198
in emerging markets, 178–183
external debt as contributor to, 193–196
factors contributing to, 172–175
macroeconomic effects, 176
Banking systems
under currency board, 124–132
developing countries need protection from contagion, 198–199
interbank market, 176–177
moral hazard in developing country, 175
supervision and regulation in emerging market countries, 182–183
weakness as predictor of currency crises, 123
Banks
consequences of failures of, 176
fragility of, 176–177
response to idea of lender-of-last-resort, 180–181
services provided by, 176
Bellagio Group, 65
Bond issues, euro-denominated private, 422–423
Bretton Woods system
capital controls under, 64
collapse (1971–73), 54, 66, 426
creation of IMF, 64
as gold-exchange, or gold-dollar, standard, 53
gold-foreign exchange reserves ratios during, 69–85, 90–101
limits on holding, buying, and selling gold, 64
pegged exchange rates under, 63–64
Capital controls
under Bretton Woods, 64
under European Union, 263
Subject Index
Capital flows
Mundell’s analysis of speculative, 432
Mundell’s studies of inflows of capital, 277
Rybczynski-based link between trade volumes and, 276–277
Capital immobility, Feldstein-Horioka hypothesis, 315–322
Capital markets, European distortions affecting, 267
Capital mobility
effect of inflows on trade between United States and some Latin American countries, 280–300
exchange rates as stabilizers with shocks and, 431–432
less than perfect, xv
Mundell-Fleming model, 273
Mundell’s model of perfect, xii–xiii
Mundell’s studies of, 273
perfect or near-perfect, 432
Central banks
under currency board, 132
demand for gold, 54
emergence of modern, 55
functioning as currency board, 127–133
gold reserve requirements (1880–1972), 107–109
justification for holding gold reserves, 67–69
as lenders of last resort under different exchange rate regimes, 124–125, 133–134
in model of balance-of-payments crises, 433, 438–440
motives of interwar, 60
role in concept of fixed exchange rates, xiii–xiv
sale of gold reserves (1990–1997), 67
shift from gold to gold-exchange standard, 56–59
shift in composition of and demand for total reserves (1885–1995), 69–85
stabilizing role in speculative environment, 432
supporters of rational expectations approach, 255
Consumers
in model of monetary policy transmission, 18–21
Consumption choice bundle
effect of tariffs on, 468–469
with endogenous terms of trade, 485–492
with exogenous terms of trade, 479–485
in labor market search model, 470–479
Currency. See also Devaluation; Exchange rates; Foreign exchange reserves; Optimum currency areas
devaluation probabilities in exchange rate-based stabilizations, 435–436, 439–440
euro as, 413, 416, 418, 423
Currency boards
banking systems under, 124–132
central bank functioning as, 127–133
Currency crises. See also Speculative attacks, currency
under currency board, 124
first-generation model of speculative attacks, 207, 208–215
fiscal policy during, 441
intertemporal microfoundations of, 434
link to financial sector crises, 123
policy determinants of, 456–462
predictability, 231–236
predictions of model under uncertainty, 434
as predictors, 198, 435
response of exchange rate policy in, 439–440
Currency reform, Germany (1948), 153–161
Current account
identification of monetary shock effects on, 396–400
monetary and nonmonetary gold flows in data for, 305–313
Data sources
analysis of capital and trade flows in some Latin American countries, 280–281
analysis of current account response to monetary shocks, 394–395
Australian current account, 309–310
Canada’s balance of payments, 310
effect of exchange rate regime on banking crises, 190
empirical evidence of macroeconomic policy transmission, 12
estimates of gold in current accounts of European countries, 310–313
for gold flows in balance of payments, 306–313
gold inventories, 313, 315
for identification and dating of banking crises, 184
monetary policy transmission mechanism, 10
proposals for development of, 268–269
Devaluation
expectations of, 234
of fixed exchange rate, 209–210
model to predict timing of, 232
Distortions, economic
affecting European economies, 266–268
caused by interest groups, 264–265
proposed economic analysis of, 268–270
redistributive effects, 265
Distribution
of gold reserves (1927–30), 61–62
role of government in, 259–261, 265
Division of labor
with fragmentation of production, 365–367
Dollar, U.S.
de facto standard, 66
pre-1997 East Asian currencies pegged to, 424–425
East Asian countries
after speculative attacks, 424
pre-1997 linked macroeconomic policies, 424–425
proposed common monetary standard, 427–428
Economic and Monetary Union (EMU)
common monetary standard prior to, 423–424
Economic policy
IMF-recommended structural reform, 256–257, 259, 263
proposed research program and reform, 268–270
World Bank recommendations for structural reform, 257, 259
Economic policy theory
analysis of distortions, 264–268
issues and areas to analyse, 257–259
Mundell tradition, 253–255
Economic shocks. See also Monetary shocks
effect on macroeconomic policy, 9–16
effect on terms of trade, 178–179, 184
impact on emerging market economies, 178–179
stabilization related to exchange rates with exogenous, 431–432
Emerging market countries
causes of banking crises in, 178–190
effect of economic shocks on, 178–179
macroeconomic policy in, 178
problems of banking in, 176–177
Euro
advent (1999), 413, 416
impact on U.S. dollar, 418
as regional currency, 423
European Commission
decisions based on economic principles, 263–264
Exchange rate regimes
as contributor to banking crises, 190–193
potential effect on banks in emerging markets, 179–181
role in developing country banking crises, 190–193, 197–198
Exchange rates. See also Currency;
Foreign exchange reserves
post–World War I, 59
response to monetary shocks of nominal and real, 31, 40–42
shadow exchange rate, 210, 215–218
use of pegged and flexible rates, 179–181
Exchange rates, fixed
business-cycle behavior with, 434–435
call option in currency crises, 214
conditions for domination of flexible exchange rate, 431
demand for reserves during periods of, 69–87
devaluation in financial crisis, 209–210
effect of tightening commitment to, 223
fragility of regimes, 236
with lender of last resort, 133–134
in model of business cycles and balance-of-payments crises, 438–442
Exchange rates, fixed (cont.)
in model using first- and second-
generation models, 229–231
Mundell’s contribution to, xiii
optimal commitment to, 224–229
stability and predictability of, 53
stabilizing properties of, 432
while sterilizing, 212–213
Exchange rates, floating or flexible
demand for reserves during periods of,
69–87
domination by fixed exchange rate, 431
effect of managed floating regime, 53
in financial crisis, 209–210
gold in regime of, 66–69
with lender of last resort, 134–136
Mundell’s contribution, xiv–xv
Factor mobility
complementarity between international
trade and, 274–277
Mundell’s contribution to ideas of
international, xx, 365
relation to trade in HOS model, 277
substitutability of international trade
and, 273–274
Factors of production
international fragmentation, 369–371
international trade with fragmentation,
371–380
Federal Reserve System
creation and guarantee function, 60
Feldstein-Horioka capital immobility
hypothesis, 315–17, 322
Financial sector. See also Banking systems
effect on banks of domestic structure of,
181–182
relation of exchange rate regime to
fragility of, 123–124
role in banking crises of domestic, 196–
197
role in banking crises of domestic and
external, 174–175, 196–197
Firms
in model of monetary policy
transmission, 23
PTM and non-PTM, 27–29
Fiscal policy
during currency crises, 441
effect of pricing-to-market, 11
European Union treatment of income,
267
Maastricht Treaty, 258, 424
model of business cycles and balance-
of-payments crises, 440–442
monetary dynamics, xv–xviii, xxi
Mundell-Fleming model, xii–xv
transmission, 10–11
Foreign direct investment (FDI)
effect on trade of own- and other-
industry FDI, 292–297
effect on trade of own- and other-sector
FDI, 289–292, 298–300
inflow effect on trade between United
States and some Latin American
countries, 280–300
model of inflow effect on volume of
trade, 277–280
sectoral composition of trade and
(1972–1994), 283–286
testing effects on trade of, 286, 288–294
U.S. capital flows by region and sector
Foreign exchange reserves. See also
Currency; Exchange rates
commitment in speculative attack to,
214
in first-generation models of speculative
attack, 213–215
gold in, 308
as share of total reserves (1880–1996),
69–85, 90–101, 110–111
sterilizing attack on, 212–213
Free rider problem, 269
Germany, West. See also Monetary policy,
German postwar
downbreakdown of postwar monetary
system, 155–156
with postwar currency reform, 155–161
rationing, wage and price freeze
(1935–1944), 154–155
Globalization
meaning of, 365–366
welfare gains from, 367
Gold
under Bretton Woods, 63–64
in central banks’ reserve portfolios, 67
dollar price in interwar period, 60
future monetary role of, 84
gold cover ratio in interwar period,
60–61
holdings by monetary authorities, 53–55
monetary role (1870–1914), 305
role in floating exchange rate regime, 66–69
in share of total reserves (1885–1995), 69–85
as traded commodity (1870–1914), 305
Gold Bloc, 71
Gold convertibility
abandonment (1930s), 63
under gold-dollar standard, 63
post–World War I, 59
Gold-dollar standard
post–World War II, 63–66
Gold-exchange standard
collapse and disintegration (1930s), 54, 65
dependence on foreign exchange reserves, 61–63
of Mundell, 53
prewar and interwar, 53, 56–63
shift to, 56–58
timing in development of, 69–85
Gold Pool, 66
Gold reserves
central bank requirements for (1880–1972), 107–109
central bank sales of (1990–1997), 67
central banks’ collective responsibility, 68–69
gold as war chest, 69
international distribution (1927–1930), 61–62
persistence of retaining, 67–68
post-1971 value, 66–67
Gold standard
capital immobility hypothesis under, 315–318, 322
development of international, 55–56
gold as official international settlement under, 305
gold-for-euro foreign exchange reserves under, 90–101, 110–111
interwar, 60, 321–322
shift to gold-exchange standard, 56–58
Government
economic role in the economy, 259–262
justifications for intervention, 259–262
in model of monetary policy transmission, 22–23

Heckscher-Ohlin-Samuelson (HOS) model, 274–277
Information
bank operation in environment of asymmetric, 177
cascades in currency attacks, 219–220
Insurance
in asset markets, 11
cross-country consumption, 21–22
Interest groups
distortions created by, 264–268
free rider problem, 269
incentives of, 264–265
Interest rates
in labor market search model, 473
levels in speculative attacks on currency, 211–213
related to banking crises in developing countries, 185–190, 198
response to monetary shocks, 31, 41
before and during speculative attack, 234
International Monetary Fund (IMF)
Articles of Agreement creating SDR, 65
creation under Bretton Woods, 64
Keynesian economics, Mundell’s contribution to refinement of, 253–254
Labor markets
distortions affecting European, 267
effect of division of labor on, 365–367
Mundell’s contribution to concept of mobility in, xviii–xix
Labor market search model
effect of endogenous terms of trade, 485–492
of intertemporal maximization, 470–479
model of effect of exogenous terms of trade, 479–485
Latin American countries
FDI effects on trade (1972–1994), 286–300
Law of one price (LOOP)
deviations from, 10
prices satisfying and deviating from, 18–19, 23–26
Maastricht Treaty. See also Economic and Monetary Union (EMU)
fiscal constraints, 424
fiscal policy provisions, 258
Macroeconomic policy
effect of transmitted shocks on, 9–16
in emerging market countries, 178
empirical evidence of international transmission of, 11–16
limits and objectives of, 256
policy transmission mechanism
(Obstfeld-Rogoff), 17–49
Macroeconomics
dynamic models, 9–10
microeconomic analysis of, 268
open economy (Obstfeld-Rogoff), 9–10
Markets. See also Asset markets,
International; Labor market; Money market;
 Pricing-to–market (PTM)
clearing in model of monetary policy transmission, 27–28
government intervention to correct failure, 259–261
market classification principle, xvi
Mobility. See Capital mobility; Factor mobility; Labor markets
Monetary dynamics (Mundell), xv–xvii
Monetary overhang
European strategy to deal with, 163–165
factors contributing to postwar European, 145–153
measurement and dissolution of, 147–150
Monetary policy. See also Fiscal policy effect when pricing-to-market, 10–11
with fixed exchange rate regime, xiv
international transmission of shocks to, 9–11
monetary dynamics, xv–xviii, xxi
monetization during World War II in Europe, 145
Mundell-Fleming model, xii–xv
political economy of choices for reform, 163–165
politicized interwar, 60
reform in Europe (1944–1952), 160–163
reforms (1940s–1950s), 145–147
Monetary policy, German postwar
in Allied occupation zones (1948), 156
currency reform (1948), 153–154, 156–161
reform in Germany, 153–159
before and during World War II, 154–156
Monetary policy transmission model
 calibration, 29–31
equilibrium, 28–29
quantitative evaluation, 31–49
two-country model of mechanism, 17–29
Monetary shocks
current account response to, 393
effect of trade in noncontingent nominal bonds, 40–41
effect on current account variation, 399–400, 405–406
expansion effect in monetary policy transmission model, 31–40
government spending effect in model of monetary policy transmission, 42–49
identification of effects on current account, 396–400
in monetary policy transmission model, 31–42
pricing-to-market in model of monetary policy transmission, 41–42
response of exchange rates to, 31, 40–42
response of interest rates to, 31, 36, 37, 41
Monetary standard
pre-1997 East Asian, 424
proposed for East Asia, 427–428
Monetary system, international gold-based, 54
Money market
in first-generation models of speculative attacks, 208–215
Money supply. See Monetary overhang
Moral hazard
in banking systems, 177
in developing country banking systems, 175
effect on banks, 177
Mundell-Fleming model, xii–xv, 9–11, 123, 273, 393, 431, 467, 506
Mundell-Tobin effect, xix
Subject Index

Nonlinearity
in extended first-generation model of speculative attack, 216–220
in first-generation models of speculative attack, 215
in second-generation model of speculative attack, 220–223

Optimum currency areas, xviii–xix, xxi
literature of, 228
Mundell’s 1961 model, 228–229, 415
time span of, 123, 415
Optimum Currency Areas conference (1970), 413–416

Price controls
in Europe during and after World War II, 145
price setting in model of monetary policy transmission, 23–26
Pricing-to-market (PTM)
in analysis of monetary and fiscal transmission effects, 10–11
defined, 10
link to monetary transmission mechanism, 10–11
in monetary policy transmission model, 11, 23–26
PTM and non-PTM firms, 26–29
Private sector
model of business cycles and balance-of-payments crises, 436–438
Privatization, 267–268
Production process
fragmentation of, 365–368
pricing of products in international trade, 369–371
Property rights
in market-traded and fixed exchange rate policy, 214
PTM. See pricing-to-market (PTM)
Purchasing power parity (PPP)
in monetary policy transmission model, 22
Rational expectations
approach, 254–255
equilibrium in model of business cycles and balance-of-payments crises, 445–447
Ricardian model, 277, 288
Risk premium
in first-generation models of speculative attack, 213, 215
Rybczynski theorem, 276–277

Shocks. See Economic shocks; Monetary shocks
Special Drawing Rights (SDRs), 65–66
Speculative attacks, currency
in Europe (1990s), 233
first-generation models, 207, 208–215
information cascades, 219–220
macroeconomic effects (Mundell’s model), 435, 456–462
option pricing, 214
predictability, 231–236
relevance of analysis of, 432
second-generation models, 207–208, 220–223
selling at shadow price, 210
Stabilization policy
exchange rate-based, 431–432, 434–435, 438–440
model of business cycles and balance-of-payments crises, 438–442
monetary dynamics, xv–xviii, xxi
Mundell-Fleming model, xii–xv, xx
Sterilization
in first-generation models of speculative attacks, 212–213
Stolper-Samuelson theorem, 274
Tariffs
consumption choice bundle effect, 468–469
effect on employment in labor market search model, 470–479
effect on intertemporal utility, 493–494
effect on reservation wage, 468–469
effect on steady state utility, 492–493
effect with endogenous terms of trade, 485–492
effect with exogenous terms of trade, 479–485
in Mundell-Fleming model, 467
Technologies, fragmented or integrated, 367–368
Terms of trade. See also Tariffs
country influence in model of labor market search, 470–479
effect of shocks to, 178–179, 184
effect on consumption choice bundle
Terms of trade (cont.)
with exogenous, 479–485
response to monetary shocks, 31, 42
Trade, international. See also Capital
mobility; Factor, mobility; Foreign
direct investment, (FDI); Monetary
shocks; Tariffs; Terms, of trade
complementarity between factor
mobility and, 274–277
effect of liberalization on, 367
FDI inflow effect between United States
and some Latin American countries,
280–300
with fragmentation, 371–379
intensive growth of, 366
pricing of products sold in, 369–371
sectoral net export position of Latin
American countries (1972–1994),
286–287
substitutability of factor mobility and,
273–274
testing effect of FDI on, 286, 288–294
Treaty of Rome (1958)
aricultural subsidies and tariffs, 266–
267
Triffin Dilemma, 61, 64

Uncertainty
balance-of-payments crises under, 436–
442
in first-generation models of speculative
attack, 213–215
predictions of currency crises under,
434
Unemployment
intertemporal search unemployment
theory, 468–469
United States
effect of FDI on trade with Latin
American countries, 286–300
FDI flows to various regions (1973–
1994), 281–284
sectoral composition of FDI to Latin
sectoral composition of trade and FDI
to Latin American countries, 283–286

Vector auto-regression (VAR)
identification with restrictions on
variable relationships, 400–404
identification with restrictions on
variables, 396–400

pricing-to-market monetary policy
shocks, 11–16

Wealth effect
in model of business cycle transmission
and balance of payments, 433, 444–445