Discussion of "The Elusive Gains from Nationally Oriented Monetary Policy" by Martin Bodenstein, Giancarlo Corsetti, and Luca Guerrieri

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SUMMARY

This paper

- **solves** for optimal cooperative and non-cooperative MP in an open NK model
- **finds** that non-coordinated policy can be much worse than coordinated policy

Approach

- a dynamic stochastic model with two countries and two goods
- some analytical formulas + numeric solution + many robustness checks

A very interesting paper on an important question!

Discussion

1. Overview
2. Comments

Model

1. Households: infinitely lived households with log utility and habits

2. Goods: home and foreign (both traded)

3. Production: $Y_t^H = A_t^H L_t^H, \; Y_t^F = A_t^F L_t^F$

4. Prices: goods prices and wages are sticky as in Calvo

5. Monetary policy: non-cooperative optimum, cooperative optimum, IT

6. Fiscal policy: monopolistic subsidies

7. International asset markets: Incomplete, complete, auatarky

Main Results

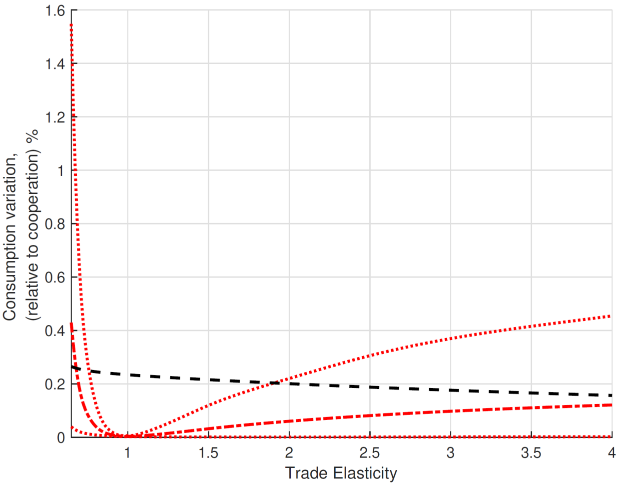
Inter-temporal and intra-temporal elasticity of substitution = 1 (Cole-Obsfeld, 1991)

$$U_i^{\text{coop}} = U_i^{\text{non-coop}}$$

Inter-temporal and intra-temporal elasticity of substitution $\neq 1$

$$U_i^{\text{coop}} > U_i^{\text{non-coop}} \text{ and (potentially) } U_i^{\text{coop}} \gg U_i^{\text{non-coop}}$$

Main result: illustration



Question: where are the bounds on the costs of the business cycles?

UNDERSTANDING MAIN RESULT

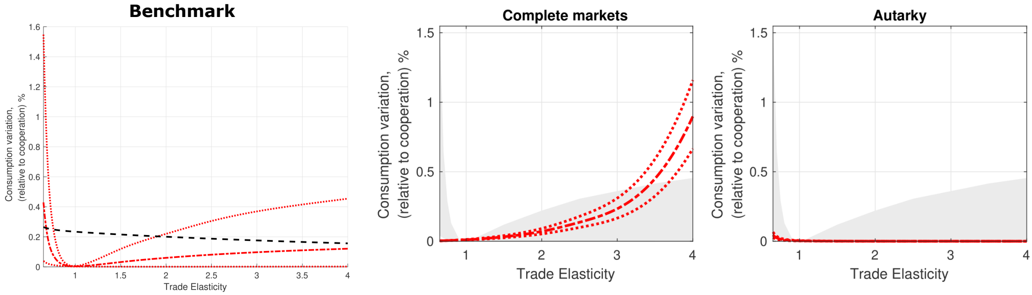
Distortions

1. Sticky prices ⇒ Aggregate demand externality: Keynes

2. Incomplete markets ⇒
   non-welfare neutral pecuniary externality: Greenwald-Stiglitz 1986
3. Monopoly power over domestically produced goods ⇒
   terms of trade manipulation: Mill 1844; Bagwell-Staiger 1999
4. Monopoly power over bonds ⇒
   inter-temporal terms of trade manipulation Costinot-Lorenzoni-Werning 2014

Spillovers due to 2, 3, 4

Comment 1: Which spillover is the most important?



- Incompleteness is important but not crucial
- Autarky exercise is informative but it restricts current account
- Proposal: a continuum of countries each producing a differentiated good
  - + Comment 1b: not all countries are big to influence world interest rate

Comment 2: Size of the coordination benefit

Relative costs

- Benefits of coordination similar or larger to costs of business cycles

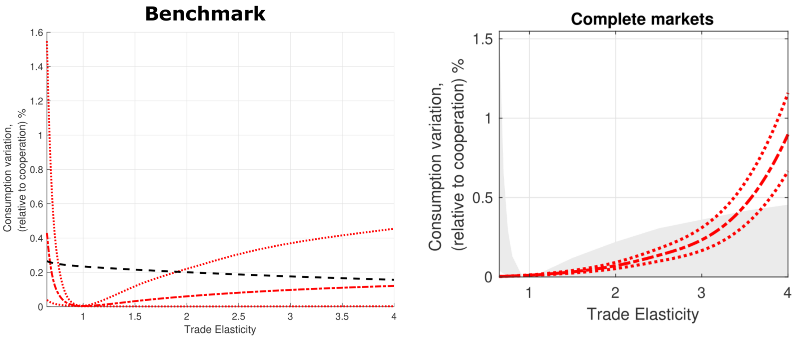
Absolute costs

- Costs of business cyclces are small: 0.2% of equivalent consumption variation
- Is the model an appropriate benchmark?

Bigger costs of business cycles

- Large shocks (disasters)
- Persistent shocks (long-run risks)
- Heterogenous households (HANK)

Comment 3: Benefits of financial integration



Is financial integration detremental under non-coopertaive monetary policy?

Comment 4: Why do countries use IT?

Why do countries not coordinate?

- This paper: Deviation from a coordination is profitable

Also this paper

- Inflation targeting is very close to coopertive solution
- Why do countries not deviate from inflation targeting?
- Or maybe they do?

Comment 5: correlated shocks

What are the benefits of coordination under correlated shocks?

- Global financial crisis

- COVID

- A current rise in inflation around the world

CONCLUSION

- A very interesting and relevant paper!
- Comments: disentangle spillovers, absolute size, fin. integration, why IT?