Following the Leader? The Relevance of the FED Funds Rate for Inflation Targeting Countries

Rodrigo Caputo† Luis Oscar Herrera‡
Central Bank of Chile Central Bank of Chile
August 21, 2016

*Previously circulated as “Efficient CPI-based Taylor Rules in Small Open Economies”. We are grateful to Sofía Bauducco, Pierpaolo Benigno, Luis Catão, Andrea Gerali, José De Gregorio, Bernardo Guimaraes, Jaime Hurtubia, Ricardo Lagos, Jean-Paul L’Hullier, Alfonso Irarrázabal, Francesco Lippi, Andrea Tiseno and Diego Saravia for insightful suggestions and fruitful discussions. We have benefited from comments by seminar participants at the Central Bank of Chile, the Norges Bank, the Einaudi Institute, the Bank of Italy, the University of Chile, the LAMES-LACEA 2012 meeting, and the Catholic University of Chile. We are grateful to Carlos Medel, Carlos Salazar and Agustín Díaz who, at different stages of the project, provided outstanding research assistance. The views expressed here are those of the authors and do not necessarily reflect the position of the Central Bank of Chile or its board members.

†rcaputo@bcentral.cl
‡lherrera@bcentral.cl

Paper Highlights
Our paper contains theoretical and empirical contributions to understand the monetary policy design in emerging and developed economies. In particular:
1. We derive an efficient CPI inflation-based Taylor rule in the context of a small open economy model.
2. The policy rule derived can be used to understand the way in which monetary policy is conducted in inflation targeting countries.
3. We use panel data techniques to empirically estimate a policy rule like the one we derived, for a set of 23 emerging and developed economies.
4. We conclude that, despite the difference between emerging and developed countries, central banks react to expected CPI inflation as well as to the foreign interest rate (Fed funds rate).
5. In the case of emerging economies the response to foreign variables is, as suggested by theory, zero once CPI inflation is replaced by domestic inflation.

Abstract
In a New-Keynesian model for a small open economy, we derive a CPI inflation-based Taylor rule that implements the flexible price allocation. We conclude that, in this rule, the natural rate of interest should be linked to the foreign interest rate and to domestic productivity shocks. This rule ensures that the CPI real rate moves in order to induce movements in consumption that are coherent with the flexible price allocation. The empirical evidence shows that inflation-targeting central banks respond to movements in the Fed funds rate, besides reacting to expected CPI inflation and to the domestic output gap. This is true for developed and emerging economies. Furthermore, we find that in emerging countries the response to foreign variables is not different from zero, as suggested by theory, when domestic inflation, rather than CPI inflation, is introduced in the policy rule.

JEL classification: E52, E58, F41
دریافت فوری متن کامل مقاله

امکان دانلود نسخه تمام متن مقالات انگلیسی
امکان دانلود نسخه ترجمه شده مقالات
پذیرش سفارش ترجمه تخصصی
امکان جستجو در آرشیو جامعی از صدها موضوع و هزاران مقاله
امکان دانلود رایگان ۲ صفحه اول هر مقاله
امکان پرداخت اینترنتی با کلیه کارت های عضو شتاب
دانلود فوری مقاله پس از پرداخت آنلاین
پشتیبانی کامل خرید با بهره مندی از سیستم هوشمند رهگیری سفارشات