THREE ESSAYS ON TIME CONSISTENCY

OF MONETARY POLICY IN OPEN ECONOMY

A Summary of Dissertation

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Summary

This dissertation aims to study the time consistency problem of monetary policy in two-country model. We raise two research questions: 1) Is the Friedman rule less likely to be sustained under cooperation than under non-cooperation when the governments lack commitment technology? 2) Is delegation more effective to solve the time consistency when the economy becomes more open?

Chapter 1 describes the motivation, research objectives, methodology, and organization.

Chapter 2 investigates the time-consistency problem of monetary policy under open economy. We first consider the consequences and the solutions in the general macroeconomic framework, and then examine the role of open economy in solving the time-inconsistent monetary policies. Three main consequences have been pointed out in the literature: inflationary bias, expectation trap, and free rider. To eliminate the problem, different types of commitment technologies have been suggested: rules, reputation, maturity structures of public debt, and monetary delegation method. An open economy sheds more light on resolving the problem.

Chapter 3 uses a microfounded New Keynesian two-country model to revisit the counterproductive cooperation when governments cannot commit to their future monetary policy. When monopolistic distortions are large, the optimal policy under commitment is characterized by the global Friedman rule irrespective of policy regime. The counterproductive cooperation between governments displays in two aspects: under cooperation, the discretionary outcome may be worse, and the global Friedman rule is less likely to be sustained than under non-cooperation.

Chapter 4 assesses the effects of openness on the effectiveness of delegation in solving the time-inconsistency problem of monetary policy. We built a micro-founded New Keynesian two-country model with a government structure including a government and a central bank. We explicitly formulate delegation process which allows the government to reappoint the current central bank with a reappointment cost. Our findings are two-fold: when the economy becomes more open, a lower threshold of reappointment cost parameter is required for central bank appointment being sustained and when the reappointment cost is less than such a threshold, the current central bank is less likely to be reappointed.

Chapter 5 provides conclusions and policy implications.