

Ulrich Volz Prospects For Monetary Cooperation and Integration in East Asia MIT Press 2010

"Today, regional monetary cooperation and integration is being discussed in virtually all parts of the world..." & cooperation broader than coordination follows Schelkle (2001) "monetary integration comprises all forms of coordinated currency stabilization" p³

"Monetary policy coordination is a highly sensitive field that requires mutual trust and understanding..." p³

ASEAN + 3 decision Feb 09

"institutionalize regionalism for the first time" establishing a common agency for surveillance of regional financial markets

"open process without pre-determined outcome" p⁴

"The interest... in regional monetary cooperation and integration... so has been ^{fuelled} by the suitability of the institutional monetary systems" For E Asia also the 97 crisis and the rise of China

"Regionalization of the world economy" China as an economic challenge discussion of FDI flows "Even though there is no clear evidence of crowding out, the fears persist" 43

"the notion ... that ASEAN countries need to restructure and integrate their economies in order to stay competitive ..." 43

In Jan 07 ASEAN agreed to speed up AEC from 2020 to 2015 "in response to the growing economic power of China and India" (Barton 2007)
China also an opportunity

Most Asian countries now have more trade with China than with Japan or US [the declining importance of intra industry trade]

"OCA theory has several theoretical short comings that have led to an over emphasis on the effectiveness of independent monetary and exchange rate policy as stabilization instruments and an under valuation of the benefits of monetary integration"
static.

"taking a dynamic perspective can turn some of the wisdom of OCA theory on their head..." p 49

"Surprisingly, financial sector effects ~~have~~ of monetary integration have received relatively little attention in the OCA literature, which has predominantly focused on real economic effects" 52
economize on holding int res

Standard Criteria

- 1 Similarity of market and business cycles
Mundell ~~1973~~ (1973) countries
ultra regional with sharing p 35
- 2 Factor mobility, and flexibility of wages
and prices
- 3 openness
- 4 product diversification
- 5 cooperation and compactness of ultra-currency
area trade - ex rate vol limits
ultra industry ~~ex~~ trade in differentiated
but substitutable products more than
homogeneous goods (Bayoumi, Eichengreen,
& Mauro 2001).
- 6 Similarity of stage of economic development
and past macro policies.
may provide explanation in potential difficulties
- 7 Development and similarity of financial
markets
note that underdeveloped financial
markets increase the costs of exchange rate
flexibility "and the benefits of monetary
integration will inversely increase" 59
[This doesn't necessarily follow]
financial development affects transmission
of monetary policy
- 8 Fiscal Transfer Mechanisms
notes only water for temporary shocks

" from a trade perspective, it is more crucial for East Asian countries to maintain intraregional exchange rate stability than to maintain stability toward the dollar" 73

" dist of China's trade across markets relatively similar " to most ASEAN

Growth and inflation correlations 1980 to 2007
pair wise no period ~~breaks~~ breaks

" A group of countries that displays relatively high positive GDP growth correlations in East Asia consists of Hong Kong, Indonesia, Japan, Korea, Malaysia, the Philippines, Singapore, and Thailand 85

" not much different than those between Western European countries 85

get generally some results for S shock correlations. Demand shock correlations lower

unemployment rates as indicators of flexibility generally lower in A than E

" On the whole, factor market flexibility appear greater in East Asian countries when compared to the European Union " 98

" Most of the indicators show that while East Asia certainly does not constitute an OCA, it is not faring too badly - also in comparison with Europe " 101

"Overall, ... East Asia is not much further away from optimality than today's euro area was maybe ten or twenty years ago" 100

Ch 6 "A ~~to~~ Reconsideration of Costs and Benefits" require a fundamental reconsideration

- 1 The death of the Phillips Curve
- 2 An understanding of the exchange rate as an asset price

"With the exchange rate driven predominantly by ~~by~~ asset market developments that are not only based on economic fundamentals and rational behavior, the exchange rate cannot be regarded as a reliable instrument for adjustment to real shocks - and hence it cannot be lost as a policy instrument" 106

It can become a cause of delusion
 July Schelkle 2001a

Schelkle (2001b, 27) "Taking the exchange rate as an asset price seriously turns the basic message of the OCA approach on its head"

Rose (2001:194) "Rather than being part of the solution $\{$ floating rates $\}$ are frequently part of the problem

"In practice, they just as often introduce shocks... $\{$ and $\}$ provide insulation"

3 The Lucas Critique

and time inconsistency levalore
 "The structure of an economy is endogenous to the economic policies applied to it" Schelkle 2001 6 18

"The endogenous change of OCA parameters during the process of monetary integration ... need not necessarily lead to an optimization of the currency area" 108

exchange rate spillover effects

He finds a strong trade creation effect in EA from similar ex rate regions
 user implied rate in basket as the measure
 p 111

Effects of trade & fin int on business cycles
 building on IMF, Imbr (04,06)

user FDI as measure of fin int.

He ~~uses similarity of currency regimes~~
 finds more trade + FDI leads to less specialization

He adopts "the region's exchange rate policy can be described by the East Asian dollar standard, ... in which all East Asian countries with the exception of Japan, operate more or less tight pegs to the US dollar" 132

Indonesia, K, S + Thai same set & vote
 of 70 to 90% Japan 66%

99 to 08

Cambod rici 98.36

K 81. e 1.7 4 15

S 73 e 15.6 4 7.4

Thai 79 e 6.8 11.1

Estimates E & A monetary independence

cooperation approach 133-140

Cambodia 98.2 3.8

Indonesia 68.7 2 10.35

vote for dollar falling

recently below 60 for K + 70 for T

He argues ~~EA~~ stabilizing the RER may
 be more important for most Asian
 economies than inflation targeting

Ho looks for "features that could enhance
 the viability and credibility of an
 EMS-style monetary system in
 today's world" 178

"[The ERM] crisis was a result of
 the system's inability to find a
 cooperative response to a shock
 [from German fiscal policy] that
 increased asymmetries within the system" 178
 coordination failure

Lesson for EMS type system cooperation has
 to be "fully relied upon" 179

CeMCoA BoJ in Nov '05

need for flexibility and
re-alignments - need to be able
to de-protection
fluctuating margins
Krugman target zone honey moon
iffit
wider bands

"The rules of the system must be put
straight, without room for interpretation"
183

Support funds EMS STF
< controls

"A crucial precondition for any regional
monetary arrangement to be successful is
a far-reaching consensus on policy
preferences" 186

EA should follow a gradual approach

"Creating a regional exchange rate system
in East Asia under present conditions
would most certainly end in crisis" 186
186

"A step wise approach to monetary integration
(Coordinated) adoption of currency baskets

Could first involve the regional
flanked by financing facilities under the
CMI and a further enhancement of
regional surveillance mechanisms" 188
Over time coordinate baskets and introduce bands

• escape the dollar trap

"Currency baskets would provide an elegant way out of the dollar dependency" 187

"An Williamson ⁽²⁰⁰¹⁾ points out ~~(2000)~~, a common basket would offer the important advantage of ensuring that the exchange rates of East Asian countries in relation to each other are not destabilized by shocks to the dollar/yen/euro rates. This would prevent inadvertent competitive devaluation or the suspicion of environmental competitive devaluation that could result from differential pegging policies" 189

But couldn't this be offset if there's a lot of flexibility with respect to the basket?

The similar trade structures should make it easier to get agreement

Replace "The East Asian dollar standard would be replaced by an 'East Asian basket standard'" 195 then introduce the ACU as a virtual basket currency to be used as a regional benchmark index to distinguish individual or regional movements in exchange rates and could become a parallel currency

The ACU might be used more by the private sector than the ECU because none of the Asian currencies has a strong incumbency advantage

Both China and Japan support the ACU to reduce reliance on the dollar

London 2004 p 251 "There is no 'Asian way' that draws nations together, no common point of view that is intrinsically different from that of the West" 2003

The Chinese trade tribute system
 ADB 2007 survey of opinion leader relations perceived as strong or very strong

Trade and investment	57%	75% in North
money & finance	36	34% in South
infrastructure	26	
public goods	19	

76% to think important to create regional institution for econ dialogue and surveillance

67% legal liability esp regional

37% common currency

Exchange rate fluctuations are more costly for production net worth trade

Hayakawa and Kimura Kimura (2008)

Average trade openness in 07 ASEAN 129%
 K 76 C 67 J 31

"Japanese corporations are likely to become increasingly entangled in government-led economic cooperation..." 210-11

"a clear and coherent Japanese vision regarding East Asian integration and Japan's role therein is lacking to date" 211

"the fear to be preempted or sidelined by the other country seems to be the driving force for both China and Japan to engage in regional cooperation" 212

The 08-09 crisis "is likely to act as a catalyst and speed up the delinking from the dollar" 214

"it is worthwhile remembering that the main impetus to European monetary integration was the collapse of the Bretton Woods system" 215