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Recent Issues in Macroeconomics: Post-Financial Crisis*

Editor's Introduction to the Special Issue

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The recent global financial crisis has been marked by prolonged deep recessions in advanced countries. Academic researchers and policy makers have devoted much of their time and efforts to understand the effectiveness and consequences on emerging countries of non-standard macroeconomic policies adopted by advanced countries. The main goal of the annual conference of Seoul Journal of Economics 2014 is to invoke comprehensive and thorough discussions among academic researchers and policy makers on the recent development in macroeconomics with special emphasis on the role of macro-prudential policies in emerging-market countries. Given that many emerging-market countries have been severely hit by economic crises even in the 1990s and 2000s, central banks in those countries have begun to adopt the so-called macro-prudential

* The studies in this special edition help us understand how the profession has made progress in the understanding of recent issues in macroeconomics and that important policy prescriptions can be drawn from this understanding. However, the studies also provide a clear picture of the limitations of the existing research on the subject and show that this subject remains a fertile area for extensive future research. This special issue was supported by the National Research Foundation of Korea Grant funded by the Korean government (NRF-2014S1A3A2044637).

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policies earlier and more heavily than advanced countries. The goals and targets of macro-prudential policies in emerging-market countries tend to place relatively more weights on issues associated with the controls of capital flows and foreign-exchange markets. The studies presented in this Special Edition Issue discuss and survey the research frontier on this subject.

The studies are selected from the proceedings of a conference organized jointly by Seoul Journal of Economics and a research project of the Social Science Korea program called Search for a New Framework in the Analysis of the Korean Economy: Based on a New Perspective about Emerging-Market Countries. The conference was held on July 2 and 3, 2014, in Seoul, Korea, and was organized by Tack Yun. The conference program included nine articles, six of which appear in this symposium. All the studies were subject to the same editorial and refereeing process of regular submissions to Seoul Journal of Economics.

Fujimoto, Munakata, and Teranishi (2015) analyze the optimal macro-prudential policy for the Korean economy. The important theoretical framework in this study lies in the introduction of a centralized credit market with search frictions in which a matching function determines the total amount of credit contracts between banks and firms. The authors use their model to compute the welfare levels that can be obtained under macro-prudential and monetary policy rules with and without credit terms. The main result of this study is that the macro-prudential and monetary policy rule with credit terms can raise social welfare at a level higher than the estimated Taylor rule can do when the structural parameters of the model are calibrated for the Korean economy.

Jung (2015) presents a DSGE model with nominal price rigidity in which households prefer catching up with the Joneses for their consumption of non-durable goods. These households also have a logarithmic function for owning housing stock. He also makes a distinction between debt-to-income (DTI) and loan-to-value (LTV) constraints for households that act as permanent borrowers because of a relatively low value of their time discount factor. Given that the Korean government has used LTV and DTI ratios as its macro-prudential tools, Jung analyzes the macroeconomic effects of several behavioral rules of DTI and LTV ratios. The results of his analysis can be summarized as follows: First, time-varying macro-prudential policies tend to be more effective in stabilizing household debt than time-invariant macro-prudential policies. This result holds whether or not the macro-prudential policy authority considers

the labor income of the borrower on top of the LTV ratio. Second, the macro-prudential policy rule with the pure LTV ratio moderates the household debt in response to the house demand shock better than the macro-prudential policy rule that considers both the labor income of the borrower and the market value of the house. Third, the macro-prudential policy that considers both the labor income of the borrower and the market value of the house is better in moderating the household debt in response to the productivity shock than the other types of macro-prudential policies. In summary, macro-prudential policies that react to the credit growth stabilize the swings of household debt more effectively than those that respond to changes in the housing price.

The main topic of Jungbin Hwang and Jae-Young Kim (2015) is the empirical analysis of risk spillover effects across financial markets, and risk is measured by using the value at risk (VaR) that can capture some extreme behavior of an asset. The key hypothesis of this study is that an extreme downside movement of returns in a market measured by a VaR has negative effects on other markets, causing similar movement of returns in the latter. The empirical findings of this study confirm that during the recent crisis period, an extreme downside movement in a major market affected other markets and that such effects became stronger. The analysis of this study is useful in the contagion of different markets, especially for crisis periods. The inclusion of the following points in the revision would help readers obtain a better understanding of the important results of this study.

Soyoung Kim (2015) analyzes the time-varying nature of international monetary policy options available for emerging countries during the post-Bretton Woods era, in view of the trilemma. Upon the liberalization of the emerging countries' capital account, emerging countries suffered from excess volatility and economic crisis, leading to the pileup of international reserves. A fundamental reform on the international monetary and global liquidity provision systems will help emerging countries cope with liberalized capital accounts. If the implementation of such a reform will take a long time, properly developed financial safety nets can benefit emerging countries in the interim. When this option is not available, emerging countries have no choice but to impose capital controls. As a result, advanced countries should understand the options of emerging countries and strive with these countries to implement an international monetary system reform that can reflect the recent worldwide developments.

Mihye Lee and Su-mi Na (2015) examine the downward nominal wage

rigidity in Korea by using both aggregate and individual level data. The results show that, on average, wages have been flexible. However, micro-data suggest that nominal wages are downwardly rigid most of the time. They also emphasize that the downward nominal wage rigidity can be different across industries at industry and individual levels in each industry: The downward nominal wage rigidity is higher in the service sector than in the manufacturing sector at the individual level even though the manufacturing sector exhibits smaller volatility in its wage growth rate than the service sector.

Yun (2015) develops an equilibrium model of central-bank swap lines that helps understand the observed recent behaviors of foreign reserves and analyze the potential effect of the Federal Reserves' foreign-exchange swap lines on determining international reserves and exchange rate. In the Fed's swap lines, foreign central banks distribute U.S. dollars to local financial institutions with "variable-rate" auctions, while they make currency swap contracts with the Federal Reserve. Different lending rates were set for different central banks, and the Federal Reserve did not take credit risks that might arise from lending to local financial institutions. These features of actual swap lines are incorporated into a theoretic model of swap contracts for central banks, which turns out to be similar to the debt contract model of Bernanke, Gertler, and Gilchrist (1999). An implication of this model in determining exchange rates is that the currency of a country is appreciated with the amount of its current and future international reserves but depreciated with its monetary aggregates when the debt capacity of international reserves is binding, which might be true even in the absence of foreign-exchange swap lines.