

Effects of Exit Strategy of the Quantitative Easy Monetary Policy on East Asian Currencies

Comment by Jianping Ding

Shanghai University of Finance and Economics

The main conclusion:

- It is concluded that East Asian countries would face capital outflows to depreciate their home currencies while they would have upward pressure against their own interest rates if the FRB adopted an exit strategy of the quantitative easy monetary policy to raise the interest rate in the near future.

Panic of currency depression and slump of stock price in all Asian countries?

- Moreover, it finished further increases in monetary base in October 2014. They have fear that the FRB's action might make the money flow backward from emerging market countries into the United States to depreciate their currencies and to decrease stock prices.

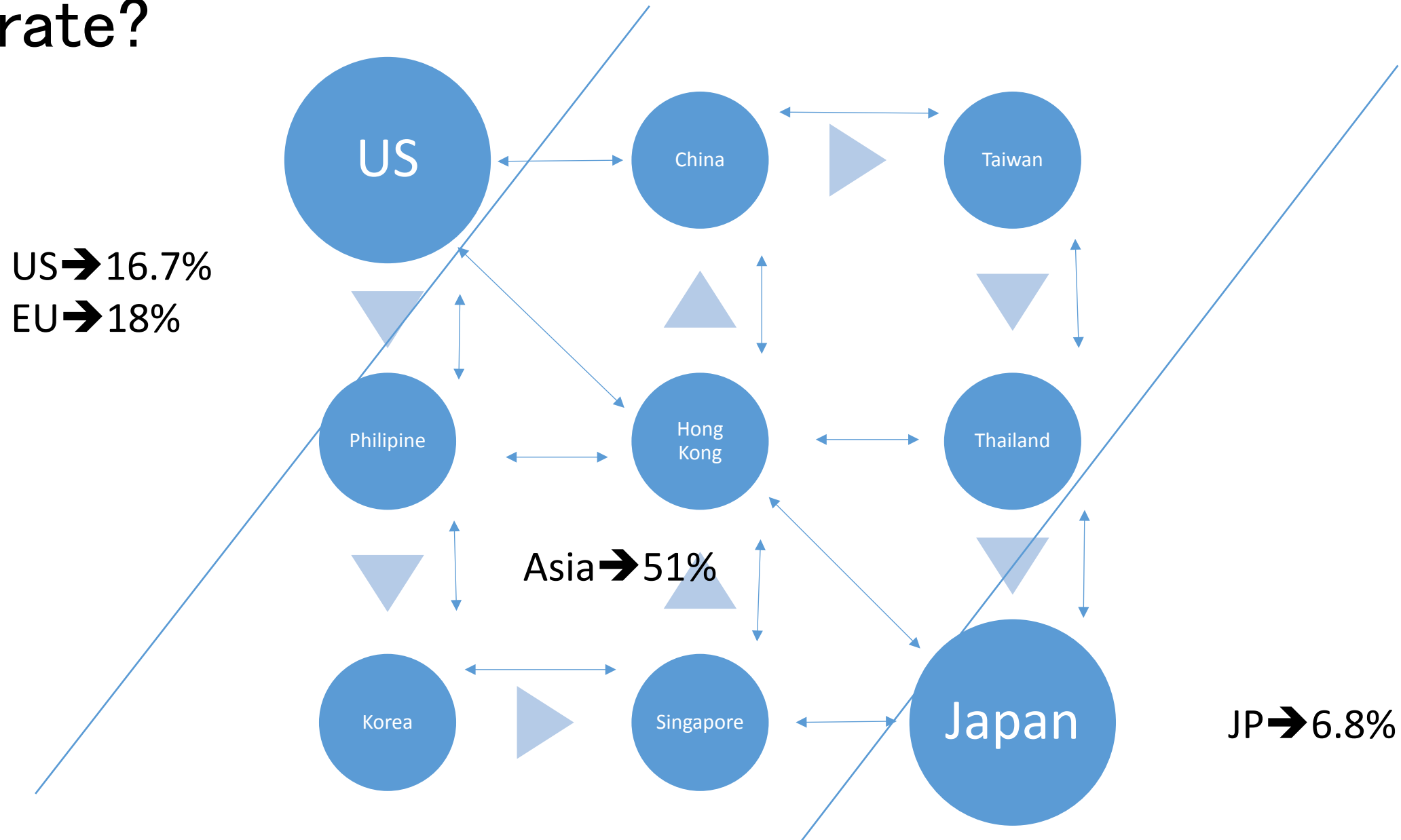
Fear of “Currency–Carry–Trade” in Asia

- The carry trades affected capital flows within East Asian region. Moreover, they had some relationship with changes in capital flows or rebounds of capital flows. Typical cases in 2005, 2007. The sudden reverse of capital flow.

The big gap in Asian currencies: source of crisis?

- The largest deviation indicator differential was larger than 60% point between the most overvalued currency (the Japanese yen) and the most undervalued currency (the Vietnamese dong) in 2011.
- In history (1997), the Asian financial crisis, the Japanese yen and USD moved also in opposite direction, and this sparked the Asian crisis originated in Thailand and Korea.
- East Asian currencies showed asymmetric responses against the global financial crisis.

N-participants' Game? If Fed raises its interest rate?



All correlation tests on the exist strategy

- Fed increase interest rate by 2% → East Asian countries would have to follow afterwards.
- Interest rate (ten days) ✓
- Exchange rate → ... (small) ✗
- Financial account → (positive, some) ✗

If Japan does otherwise (not follow)?

- The Bank of Japan seems to keep its quantitative and qualitative easing monetary policy for the time being in order to accomplish 2% of inflation target.
- Other East Asian currencies will appreciate and their interest rate will rise subsequently.
- The scenario before Asian financial crisis in 1997.

Krugman described the scenario

- Japanese Yen depreciated and USD appreciated, other the Asian countries had to appreciate their currencies and found their export price “Jump” (price out of market). Thus their exports could hardly have access to the United States and Europe.
- Will the scenario happen next year if the Fed rises its interest rate.

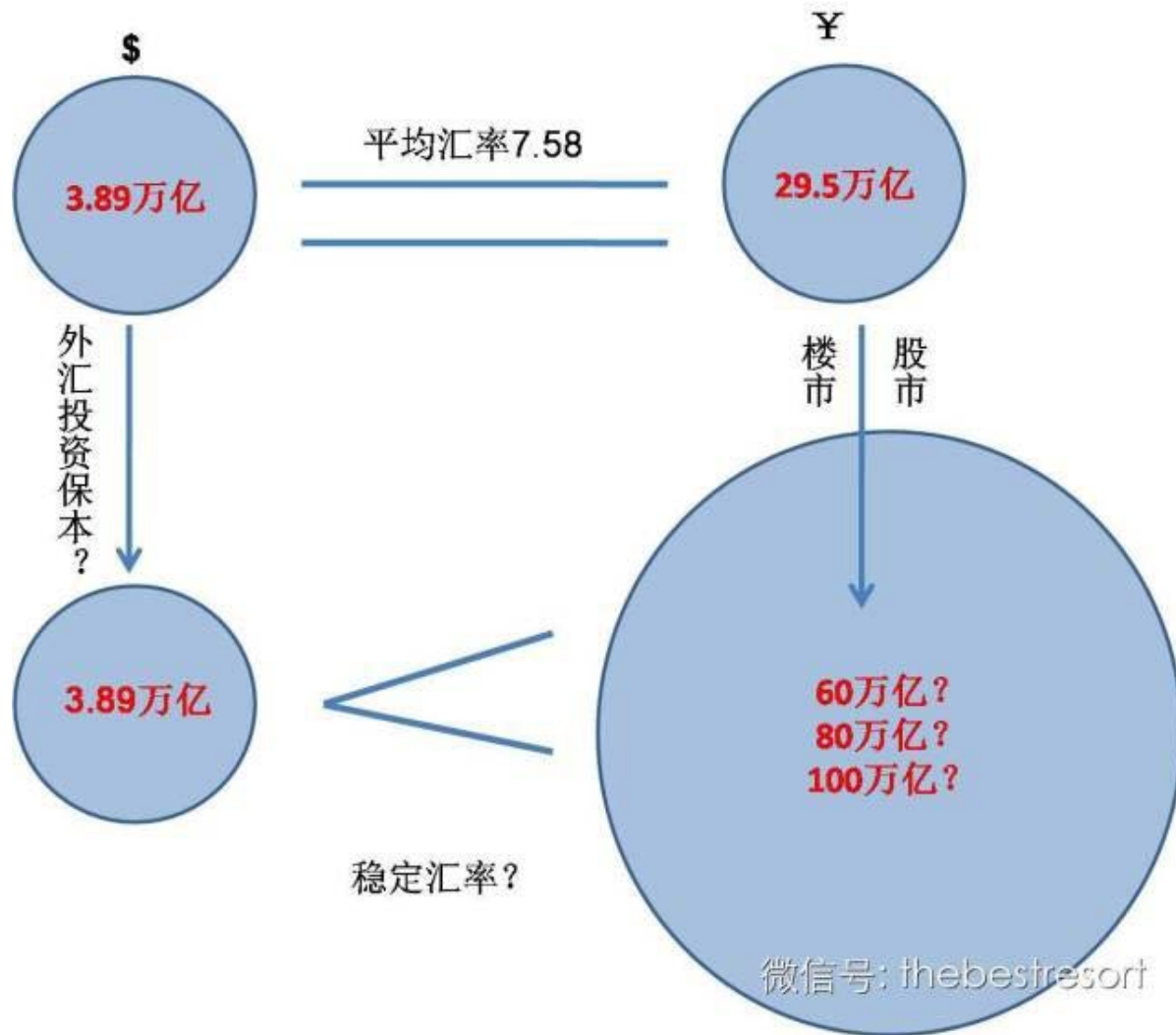
Scale and timing?

- **Scale:** Flow of capital out of Japan and its scale. Is there indirect estimation of the scale? If the scale is not so large, the impact to other exchange rate and interest rate will not volatile as expected.
- **Timing:** The economic cycles in Asian countries are not in syndrome and symmetry.
- **Pricing to the market strategy and temporary capital control on sudden change of capital flow would be more likely.**

Is AMU taking input-output-tables into consideration?

- It is a big project to estimate input-output-tables into consideration since 5-year change make a big difference in some Asian countries.
- Pair-wise comparison of pass-through effect is also necessary to establish micro foundation to support this estimation.

Crisis to CNY(RMB)? → Depreciation ?



Nearly 4 billion USD reserve won't help "self-fulfilling" capital flight