Abstract

This paper proposes a new way to evaluate significance of incompleteness of exchange rate pass-through, on both export and import sides, on responses of macroeconomic variables to both external and internal disturbances. Our approach involves Bayesian estimation of a relatively small scale open economy New Keynesian model which features incomplete nominal exchange rate pass-through. This model is estimated using the Japanese data. It is found that pass-through is indeed incomplete, on both the export and import side of the Japanese economy. In response to a shock to the foreign exchange market which lowers the value of the yen by 1%, export prices increase by about 0.5%, while import price increases are slightly larger. This limits the influence of monetary policy on both kinds of prices.