Monetary Easing in the U.S. and Sudden Stops in Emerging Countries

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January 21, 2015

【Abstract】

I explore how the prolonged monetary easing in the U.S. affects vulnerabilities of emerging markets. To this end, I set up a dynamic general equilibrium model of a small open economy where an occasionally binding international credit constraint induces an abrupt capital outflow and a large-scale economic contraction infrequently. An analysis based on a stochastic simulation shows that an extensive use of monetary easing in the U.S. can make emerging countries more vulnerable to the large scale of capital flow reversals, whereas the frequency of the small corrections of capital flows decreases. Also, when the U.S. raises the short-term interest rate, the incidence of a large-scale financial crisis would increase by about 40% in the presence of the anticipation of an extensive monetary easing.

Keywords: *Sudden Stops, Unconventional Monetary Policy, Financial Crisis*

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