

# Currency Wars, Trade Wars and Global Demand

*Author: Olivier Jeanne*

*Discussant: Federica Romei*



- Assume identical SOEs subject to a demand shock
  - Interest rate
  - Tax on imports
  - Tax on exports
  - Tax on capital flows
- What would they do?



- If ZLB does not bind
  - Manipulate terms of trade in their favour
- If ZLB binds
  - Increase taxes on imports -> Welfare decreasing from a global perspective
  - Drop taxes on exports -> Welfare increasing from a global perspective
- NOT ALL THE TRADE WARS ARE THE SAME!



# My Discussion

- Why do countries use tax on imports?
- Possible second paper



- “...sadly import tariffs seem to be the instrument of choice in the real world, and global demand shortage is conducive to tariff wars...” [Olivier Jeanne]
- Why does it happen since taxes on imports may decrease home consumption?



# Possible explanation

- Assume some households are Hand-to-Mouth
  - They cannot access the financial market
  - They consume their income (High MPC)
- Some other households are Ricardian
  - They access the financial markets
  - They consume their permanent income (Low MPC)



# Tax on imports

- Ricardian households
  - Decrease their consumption (Euler equation)
  - Increase consumption of home goods
- Hand-to-mouth
  - Increase consumption of home goods
  - Increase their consumption (Indirect effect)



- By using the tax on imports, domestic planner can take advantage of domestic the indirect effect
- Hence, domestic planner may find it optimal to use this instrument
- Still, it can have negative externalities on other countries
  - Domestic planner does not consider the RoW indirect effect
- Hence, suboptimal from a global perspective



# Possible second paper

- Assume a cost-push shock under inflation targeting (Fornaro and Romei, 2022 - Bianchi and Coulibaly, 2023)
- Assume that inflation cannot move
- Interesting to study how to use these import/export taxes
- Most likely, drop in import taxes and increase in export taxes



# Conclusions

- Very interesting paper!
- Full of intuitive and clear results
- Useful model to study more recent crises