

Research Update

Economic Analysis and Research Department

www.oenb.at/econ.newsletter

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November 16-17, 2009

OeNB Conference on
Eastern European
Integration



Editorial

by Peter Mooslechner
Director of the Economic Analysis and Research Department

From historical crisis to the need for a summer break ...

What started as a financial turmoil in the summer of 2007 has since then mutated into a full-blown financial and economic crisis of a global nature, resulting in a destabilization of the financial system of previously unknown extent as well as in a wide range of adverse effects on the real economy, hitting areas ranging from the housing market to international trade, industrial production and, finally, labor markets. Even if it is obvious that fundamental uncertainty still prevails, the time may have come to take stock before entering into the third crisis year this summer – and, if possible, to take some days of vacation, too.

Although economics has not been able to prevent the crisis from unfolding – and mainstream economics may even have contributed to its creation – several insights can be taken from the fast growing literature concerning the specifics of a crisis like this one:

- In the advanced countries, there have been 122 recessions since 1960, each lasting one year on average.
- In a typical recession, real GDP falls by about 2% from peak to trough.
- 37 of these recession episodes can be termed “globalized”, meaning that at least half of the globalized economies went into recession at the time.
- Globally synchronized recessions last longer, result in more than twice the loss in output, show much stronger declines in house prices and, in particular, entail a significant contraction of trade flows.
- Over the same period, there were 28 credit crunch episodes, lasting ten quarters on average and resulting in a decline of nearly 20% in real credit.
- Recessions associated with severe financial market problems are longer and deeper than other recessions, mainly because of amplifying effects via financing shortages and asset price collapses.
- In addition, changes in house prices constitute one of the most prominent factors influencing the severity of a recession.

Keeping all these historical elements in mind, it comes as no surprise that the present recession turns out to belong to the most severe ones we have seen in history. Although we all could use a break from the recession now after two years of incredibly intensified analysis and policy efforts, it seems very likely that the crisis will stay with us for some time. Nevertheless, (i) let's continue with our counteracting policy effort, (ii) let's try to avoid additional external shocks over the summer months and (iii) let's hope for a little bit of stabilization and improvement to arrange for some quiet days of summer vacation – which, by the way, will help the tourism industry!

OeNB Governor Nowotny: Central Banks as Crisis Managers and Sources of Stability in Turbulent Times

37th Economics Conference of the OeNB opened by Governor Ewald Nowotny

“To excel in central banking, we need to have the courage to rush in like firefighters and we need to be as vigilant as policemen: Right now we are busy fighting a large fire that has spread across the world; and I would say we have been doing a good job in getting the fire under control. At the same time I can assure you that we have seen to it that money and lending market operations continue to run smoothly and that we promote the resumption of sustainable growth and preserve price stability,” the governor of the Oesterreichische Nationalbank (OeNB), Ewald Nowotny, said in his opening remarks to the 37th Economics Conference of the OeNB in Vienna on Thursday. The theme of this year’s conference, which is held at the Hotel Marriott in Vienna on May 14 and 15, 2009, is “Beyond the Crisis: Economic Policy in a New Macroeconomic Environment.”

Governor Nowotny emphasized that although the current crisis posed tremendous challenges to policymakers, there was a range of instruments available making it possible to counteract adverse developments. The right mix of expansionary monetary and fiscal policies was required to effectively tackle the economic slump. Central banks play a pivotal role in this process.

In his speech, Governor Nowotny explained the use of traditional and nonstandard monetary policy instruments in fighting the crisis and underlined the OeNB’s key function as a central bank in implementing the Eurosystem’s monetary policy and in crisis management at the national level.

Concerns about potential inflationary effects of the current monetary policy stance were unfounded, Nowotny said. Neither short-term inflation expectations nor forecasts of the degree of capital utilization in the real economy, neither credit growth nor monetary growth at present indicate inflation risks. These developments of course must be – and are being – monitored closely to be able to take action fast, if need be. “In the near term we see some signs that price levels might go down in individual euro area countries, which we interpret as an unwinding of increases seen last year in an environment of soaring energy prices. Let me stress, however, that over the medium term I see neither the risk of deflation, nor the risk of inflation,” Nowotny concluded.

For more details see:

http://www.oenb.at/de/service_veranst/fruehere_va/2009/vi09/37_volkswirtschaftliche_tagung.jsp#cm:14-85373

Economic Crisis Unleashes Deep Recession in Austria – Stabilization Expected at Year-End

Economic Outlook for Austria from 2009 to 2011 (June 2009)

According to the June 2009 economic outlook of the Oesterreichische Nationalbank (OeNB), the Austrian economy is projected to enter a deep recession in 2009 owing to the global slump in growth, with real GDP set to shrink by 4.2%. After further declining by a modest 0.4% in 2010, positive real annual GDP growth of 1.2% will reemerge only in 2011.

Compared with the OeNB December 2008 economic outlook, growth expectations for 2009

and 2010 were downgraded by 3.9 and 1.2 percentage points respectively. This major revision reflects the steep slump in the demand for exports and investment – unparalleled in the post-war period. The current downturn is so pronounced that GDP levels seen in 2007 will not return until 2011. HICP inflation will ease from 3.2% in 2008 to a mere 0.4% in 2009 and rise modestly to 1.1% and 1.2% in 2010 and 2011 respectively.

Growth of Real GDP (Seasonally and Working-Day Adjusted)

Quarterly and annual changes in %



Source: Eurostat, OeNB.

Economic mood in the CESEE region darkens, trust in banking sector observed to fall; though degree of euroization remained rather stable - results from the OeNB Euro Survey suggest

In October/November 2008 the third wave of the OeNB Euro Survey conducted in eleven Central, Eastern and South-Eastern European (CESEE) countries, has been carried out. Hence, the survey period coincided with the arrival of the international financial crisis in the region.

Economic confidence weakens

Not surprisingly, respondents' assessment of the current economic situation (as of fall 2008) deteriorated in comparison to the spring wave 2008. In general pessimism remained the dominant sentiment, in particular in Hungary and the SEE countries. A remarkable exception constitutes the Slovak Republic where respondents on average were positive in their economic assessment, likely reflecting the then upcoming accession to the euro area.

Deteriorating trust in banks in most countries

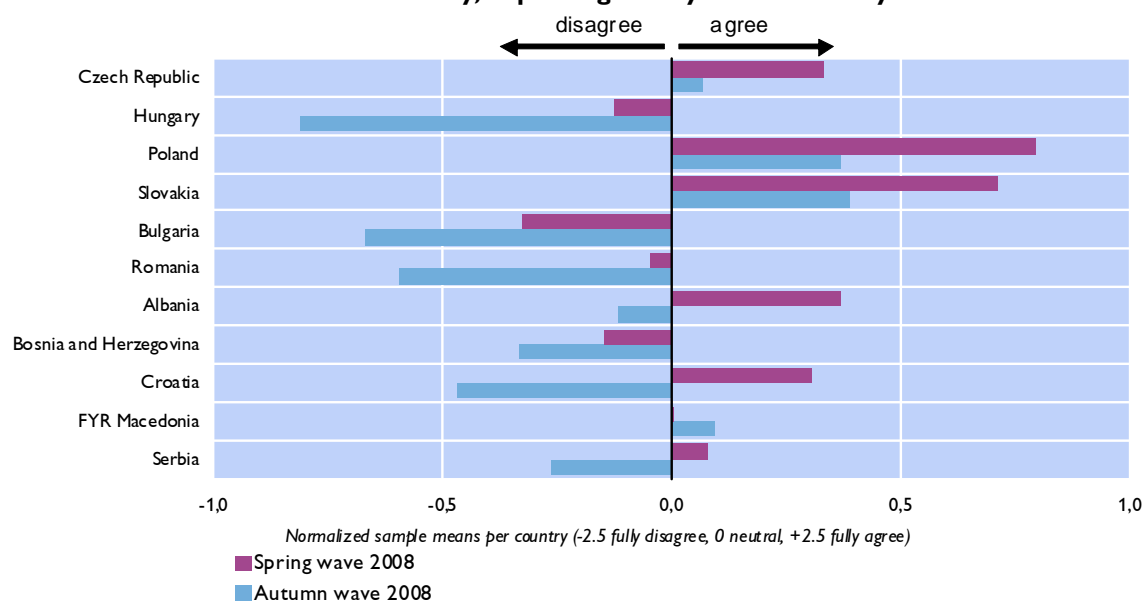
The financial crisis also got manifested in a statistically significant erosion of trust in banks – except for the FYR Macedonia (see Chart). A

relatively strong revocation from a positive to a negative assessment of the domestic banking system, on average, can be observed for Croatia and Albania. Also, in Hungary and Romania answers indicate a relatively strong worsening of trust in banks.

In this context, the question arises whether the observed changes lead to changes in the extent of foreign currency denominated assets holdings? Results indicate that households have not reacted strongly as of fall 2008.

New Results Available in September 2009

A more detailed discussion of the results from the OeNB EuroSurvey Fall Wave 2008 is published in FEEI issue 2/2009. The results from the new survey wave which has been carried out in May and June 2009 will be available in fall 2009. Results of sentiment indicators will be published at the beginning of September at ceec.oenb.at.

Consent to the statement: "Currently, depositing money at banks is very safe"

Source: OeNB Euro Survey Spring Wave 2008 and Autumn Wave 2008.

From Financial Crisis to Global Economic Crisis

The Austrian financial system is facing its most serious challenges in decades, according to the 17th issue of the Financial Stability Report, released on July 6, 2009. The international economic crisis also reached the Austrian economy, with Austrian real GDP declining since the fourth quarter of 2008. The financial crisis adversely affected corporate financing conditions. In particular, borrowing in the equity market almost came to a standstill. Although bank lending continued to grow, banks tightened their credit standards. In the household balance sheets, the recession materialized especially in the form of heavy valuation losses for capital market securities. New household borrowing, by contrast, went down significantly. However, the foreign currency share of household financing remained high.

The financial crisis and the downturn in the real economy had a clearly adverse effect on banks' profitability. In particular, marked valuation losses in trading income and higher loan loss provisions reduced profitability. In 2008, nevertheless, the Austrian banking system still generated a profit, albeit a considerably diminished one.

The CESEE business of banks active in the region accounted for a significant share of this profitability. Profits generated in this segment largely offset falling profits in others. In view of the gloomy economic outlook, international financial markets' risk aversion to this region increased sharply. Austrian banks' investment in CESEE countries increasingly came under the spotlight of critical international attention. This group of countries should not, however, be seen as a homogeneous region. Instead, the financial crisis affected individual countries to widely varying degrees. Furthermore, the activities of the IMF and the EU in the region created confidence and helped reduce significantly the likelihood of extremely negative developments.

The implementation of the bank support package helped prepare banks for an increase in loan loss provisions. Since the fourth quarter of 2008, both capital ratios and core capital ratios, after decreasing in previous periods, have risen via increased internal financing (retained earnings) and external financing (by core shareholders and by means of government participation capital).

The OeNB's biannual Financial Stability Report provides regular analyses of Austrian and

international developments with an impact on financial stability. In addition, it includes studies offering in-depth insights into specific

topics related to financial stability. The Financial Stability Report can be downloaded from the OeNB's website at www.oenb.at

OeNB's research output presented at Noeg Conference

The quality and the quantity of the OeNB's economics department were demonstrated at the Annual Meeting of the Austrian Economic Association which took place in Linz, May 22-23, 2009. Eight papers by OeNB economists were presented and discussed, covering topics from inflation and wages, pricing of risk or money demand.

Jürgen Janger and Philipp Schmidt-Dengler examined the link between the price level, inflation, and variability of the price level with competition intensity. Testing predictions derived from standard oligopoly theory, they find that competition reduces the variability of the price level; the evidence of the effect of competition on inflation is somewhat mixed.

Burkhard Raunig compared the market pricing of the default risk of banks to that of other firms. He finds that market participants indeed viewed banks differently and that they drastically changed their mind during the recent turmoil that started in August 2007.

Helmut Stix presented joint work together with **Ulf von Kalckreuth** and **Tobias Schmidt** (both Deutsche Bundesbank). They shed light on how individuals choose payment instruments and why cash remains so important in some European countries. Their results indicate that cash usage is compatible with rational decision making.

Markus Knell studied the relation between real wage rigidity and nominal price and wage

rigidities. His findings suggest that the standard model omits institutional characteristics that are crucial for cross-country differences in real wage rigidity.

Claudia Kwapil presented her paper on the response of Austrian firms to demand shocks. Based on a survey among 560 firms, the preferred reaction to demand reduction is cost cutting and downsizing employment is preferred to cutting wages; this is in line with previous studies from other countries.

Julia Wörz and Katalin Polgar (ECB) analyzed the relationship between trade and wages at the industry level in EU25. They find that increased trade penetration changes the composition of tasks towards more productive, more skill-intensive activities by replacing low-wage jobs, especially in the EU10 countries.

Thomas Scheiber presented a joint paper with **Helmut Stix** on euroization in eleven Central, Eastern and Southeastern European countries. Their results indicate that euroization is highly correlated with the quality of past economic governance, reflecting past periods of instabilities.

Wolfgang Pointner and Alfred Stiglbauer examined changes in the Austrian wage structure. Using data from the survey of earnings structure, they find only a small increase in wage inequality in Austria between 1996 and 2002 and that higher female participation reduced wages below the median.

Professor Peter L. Bossaerts gave three lectures on the topic "Experimenting with Financial Markets"

On June 9th and 10th, Professor Peter L. Bossaerts (California Institute of Technology, Pasadena), this year's OeNB Gastprofessor 2009, gave three lectures on the topic "Experimenting with Financial Markets". The point of departure of Professor Bossaerts' lectures was the modern

asset pricing theory. The theory abounds with sophisticated mathematical models that make strong predictions about asset price determination and that have given rise to concise formulae that have been and are widely used in the financial industry and

especially in risk management. Despite their analytical elegance, the existing empirical evidence (e.g. of the CAPM) is rather disappointing. Professor Bossaerts argues that a large part of this empirical failure has to do with the fact that these studies are based on field data that can only be used to test the theoretical models under strong auxiliary assumptions (e.g. that the observations are equilibrium outcomes, that expectations are formed rationally, that people have no cognitive biases etc.). In order to conduct clear-cut tests of the models, Peter Bossaerts strongly argued to employ experimental methods that allow to control for most additional factors and to arrive at undistorted results. He presented some newly developed software tools that make it possible to easily implement a double-auction market that can be used to test asset pricing behavior.

Professor Bossaerts' own research has shown, e.g., that the pricing predictions of the CAPM do

surprisingly well in such an experimental market, while the individual allocations of assets are in contrast to the theoretical model. He also shows that the results indicate that one has to reject a commonly heard assumption in mainstream finance, that only the marginal investor matters, in favor of the view from general equilibrium theory that all agents matter. Further experiments that were discussed by Peter Bossaerts dealt with information aggregation and with markets for loans under adverse selection. Experimental financial markets allow to emphasize the successes and failures of the mathematical, general-equilibrium-based theoretical models. They are thus an important and promising field of study that can be helpful to point out the direction of future research in financial economics.

Sir Tony Atkinson gave 14th Global Economy Lecture at OeNB

On May 7, 2009, the 14th Global Economy Lecture was held at OeNB. The Global Economy Lecture is organized jointly by the WIIW and OeNB. Sir Tony Atkinson, Professor of Economics and Fellow of Nuffield College, Oxford spoke about the "The Global Distribution of Income: Past Trends and Future Prospects." Opening remarks were held by Doris Ritzberger-Grünwald, Head of the OeNB's Foreign Research Division, and Michael Landesmann, Director of WIIW.

In his lecture, Sir Tony Atkinson analyzed the distribution between countries, the "international distribution," as well as the distribution within countries. For the distribution between countries, he compared GDP per capita across countries and described the evolution of the share of the richest 12 countries in total world income. Sir Tony Atkinson analyzed the distribution within countries using Lorenz curves and Gini coefficients, as well as the share of total income earned by top earners in a country.

The above measures yield a clear picture regarding the international distribution of income. Following the Industrial Revolution, international incomes have diverged until the middle of the

20th century, with inequality declining in the second half of the past century. This was largely due to large countries becoming middle income countries. However, richest countries kept getting a larger share of global income and the poorest countries were left further behind during this period.

Within-Country inequality substantially declined in industrialized countries until the last quarter of the 20th century. During the past 30 years we have seen an increase in both overall inequality (as measured by the Gini coefficient) and the shares of top income earners in Anglo-Saxon countries. The Nordic countries and Germany have experienced a somewhat later rise in inequality. Hence, there is some evidence for U-shape in the evolution of inequality. This is explained with top capital and wage incomes first declining, and in particular top wage incomes increasing again in recent years.

Finally, Sir Atkinson discussed what will be the likely impact of the current crisis on income distribution. Evidence from past Banking-crisis induced recessions show an increase in inequality. Sir Atkinson argued that a similar effect must be expected as a result of the current crisis.

The ensuing discussion focused on the role of policy – in particular tax reforms – in the evolution of the observed trends. In light of the current financial crisis it was pointed out that one

needs to look carefully at both wealth and income. The question how much was lost by whom is difficult to answer as most available wealth statistics do not mark to market.

OeNB Annual Report 2008



The OeNB's Annual Report 2008 was released in May 2009. It provides a broad review of Austrian monetary and economic conditions, new developments in financial markets in general and in financial market supervision in particular as well as of the OeNB's responsibilities and its role as an international partner in cooperation and dialogue.

http://www.oenb.at/en/presse_pub/period_pub/unternehmen/geschaeftsbericht/geschaeftsbericht_2008.jsp

OeNB Periodical Publications

http://www.oenb.at/en/geldp_volksw/vowi_pub/volkswirtschaftliche_publicationen.jsp

Monetary Policy & the Economy, Q2/09

Economic Crisis Unleashes Deep Recession in Austria - Stabilization Expected at Year-End; Economic Outlook for Austria from 2009 to 2011 (Christian Ragacs, Klaus Vondra)

Inflation Expectations: Role and Measurement for Monetary Policy (Ernest Gnan, Johann Scharler, Maria Antoinette Silgoner)

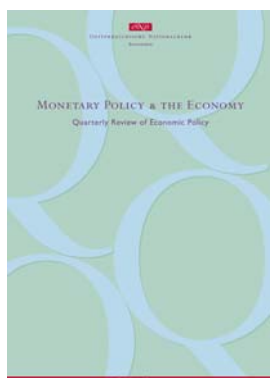
Unifying EU Representation at the IMF - A Voting Power Analysis (Peter Brandner, Harald Grech)

The Role of Exchange Rate Movements in the Euro Area (Paul Gaggl)

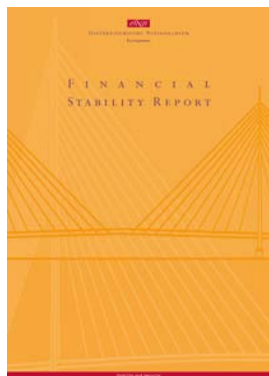
How Austrian Firms Have Responded to Softening Demand - Survey Results (Claudia Kwapil)

Housing Wealth of Austrian Households - Results of the OeNB's Housing Wealth Survey 2008 (Pirmin Fessler, Peter Mooslechner, Martin Schürz, Karin Wagner)

Beyond the Crisis: Economic Policy in a New Macroeconomic Environment; Summary of the OeNB's 37th Economics conference (Ernest Gnan, Burkhard Raunig)



Financial Stability Report 17 (July 2009)



Banking and Financial Stability in Russia and the Euro Area amid International Financial Market Turbulences (Stephan Barisitz, Gernot Ebner, Mathias Lahnsteiner, Johannes Pann)

Direct Cross-Border Lending by Austrian Banks to Eastern Europe (C. Pühr, M. Schwaiger, M. Sigmund)

Modeling Credit Risk through the Austrian Business Cycle: An Update of the OeNB Model (Michael Boss, Gerhard Fenz, Johannes Pann, Claus Pühr, Martin Schneider, Eva Ubl)

EU Bank Packages: Objectives and Potential Conflicts of Objectives (Michaela Posch, Stefan W. Schmitz, Beat Weber)

A First Glimpse at the Impact of the Crisis on Austria's Financial Sector (M. Schürz, M.S.Schwaiger, J. Übeleis)

Focus on European Economic Integration 2/2009



European and Non-European Emerging Market Currencies: Forward Premium Puzzle and Fundamentals (Peter Backé, Franz Schardax)

The 2008 Fall Wave of the OeNB Euro Survey in Central, Eastern and Southeastern Europe - A First Glimpse into Households' Reactions to the Global Financial Crisis (Sandra Dvorsky, Thomas Scheiber, Helmut Stix)

Fiscal Position and Size of Automatic Stabilizers in the CESEE EU Member States - Implications for Discretionary Measures (Markus Eller)

Focus on European Economic Integration 3/2009

Evaluating Inflation Determinants with a Money Supply Rule in Four New EU Member States (Aaron Mehrotra, Tomas Slacik)

Economic Growth Determinants in European Regions: Is Central and Eastern Europe Different? (Jesus Crespo-Cuaresma, Gernot Doppelhofer, Martin Feldkircher)

Macrofinancial Development and Systemic Change in CIS Central Asia (Stephan Barisitz)

OeNB Working Papers

http://www.oenb.at/en/presse_pub/research/020_workingpapers/working_papers_2009.jsp

Working Paper 154

"Country Size, Currency Unions, and International Asset Returns" (May 14, 2009) by Tarek A. Hassan)

The fact that economies differ in size has important implications for international asset returns. I solve for the spread on international bonds and stocks in an endowment economy with complete asset markets and non-traded goods. The model predicts that larger countries have lower real interest rates because their bonds provide insurance against shocks that affect a larger fraction of the world economy. Larger countries' bonds must therefore pay lower excess returns in equilibrium and uncovered interest parity fails. By a similar logic, stocks in the non-traded sector of larger countries also tend to pay lower excess returns. If asset markets are segmented, the

introduction of a currency union lowers real interest rates and expected returns on stocks in the non-traded sector of participating countries. I test the predictions of the model for a panel of OECD countries and show that they are strongly supported by the data: Investors earn lower excess returns on bonds and stocks in the non-traded sector of larger countries. Similarly, excess returns on EMU member countries' bonds and stocks in the non-traded sector fell after European monetary integration.

Working Paper 155

“Systemic Risk: Amplification Effects, Externalities, and Policy Responses” (May 14, 2009) by Anton Korinek

The worst financial crises since the Great Depression has forced central bankers and policymakers across Europe and around the globe to take unprecedented policy measures to deal with systemic risk, i.e. the risk that the financial system ceases to perform its function of allocating capital to the most productive use because of financial difficulties among a significant number of financial institutions. This paper develops a parsimonious model of systemic risk in the form of amplification effects whereby adverse developments in financial markets and in the real economy mutually reinforce each other and lead to a feedback cycle of falling asset prices, deteriorating balance sheets and tightening financing conditions. The paper shows that the free market equilibrium in such an environment is generically inefficient because constrained market participants do not

internalize that their actions entail amplification effects. Therefore they undervalue the social benefits of liquidity during crises and take on too much systemic risk. We use our framework to shed light on a number of current policy issues. We show that banks face socially insufficient incentives to raise more capital during systemic crises, that bailouts which are anticipated can be ineffective, and that expectational errors are considerably more costly during crises than in normal times. Furthermore we develop an analytical framework for macro-prudential capital adequacy requirements that take into account systemic risk. We also analyze a new channel of financial contagion and explain why private agents will take insufficient precautions against contagion from other sectors in the economy.

Working Paper 156

“Financial Networks, Cross Holdings, and Limited Liability” (May 29, 2009) by Helmut Elsinger

I discuss a network of banks which are linked with each other by financial obligations and cross holdings. Given an initial endowment the value of the obligations and the equity values of the banks are determined endogenously in a way consistent with the priority of debt and the limited liability of equity. Even though neither equity values nor debt values are necessarily unique the value of debt and equity holdings of outside investors is uniquely determined. An algorithm to calculate debt and equity values is developed.

External Publications by Staff Members

“The Impact of Reference Norms on Inflation Persistence When Wages are Staggered”

Markus Knell and Alfred Stiglbauer

European Central Bank Working Paper Series No 1047, April 2009

In this paper we present an extension of the Taylor model with staggered wages in which wage-setting

is also influenced by reference norms (i.e. by benchmark wages). We show that reference norms can considerably increase the persistence of inflation and the extent of real wage rigidity but that these effects depend on the definition of reference norms (e.g. how backward-looking they are) and on whether the importance of norms differs between sectors. Using data on collectively bargained wages in Austria from 1980 to 2006 we show that wage-setting is strongly influenced by reference norms, that the wages of other sectors seem to matter more than own past wages and that there is a clear indication for the existence of wage leadership (i.e. asymmetries in reference norms).

“The Work-and-Spend Cycle in a Globalized World”

Markus Knell

Economics Bulletin, 2009, Vol. 29 no.1 pp. 492-499

In this paper we show that globalization might cause an inefficient reduction of working time regulation. The argument rests on the assumption that people care about their relative standing and that national policymakers fail to completely internalize the consumption externality of the increasingly international reference standards.

“An Integrated Approach to Stress Testing: The Austrian Systemic Risk Monitor”

Martin Summer (with Michael Boss, Gerald Krenn and Claus Puhr)

Stress Testing the Banking System, edited by Mario Quagliariello, Cambridge University Press, p. 202-237

“Globalization, the output-inflation tradeoff, and inflation”

Harald Badinger

European Economic Review, iFirst, published online, doi:10.1016/j.euroecorev.2009.03.005

This paper provides comprehensive evidence on the relation between inflation and globalization, defined here as trade and financial openness, using a large cross-section of 91 countries over the period 1985 to 2004. We establish two main empirical regularities: Both higher trade and financial openness i) reduce central banks' inflation bias, yielding lower average inflation and ii) are associated with a larger output-inflation tradeoff. This evidence is at odds with the standard Barro-Gordon framework, which would require globalization to have a negative effect on the output-inflation tradeoff to yield lower equilibrium inflation, but it is consistent with a recent strand of new Keynesian models emphasizing the role of imperfect competition and nominal rigidities. Our findings also support the relevance of the time inconsistency hypothesis, which underlies the theoretical models predicting a relation between globalization and inflation. For the OECD subsample, however, we do not find an effect of openness on inflation (the output-inflation

tradeoff), suggesting that these countries have created an institutional framework for central banks that eliminates distortions due to the time inconsistency problem.

“Country size and trade effects of the Euro”

Harald Badinger (with Fritz Breuss)

Weltwirtschaftliches Archiv, 2009, iFirst, published online 20 May 2009, DOI 10.1007/s10290-009-0013-6

This paper investigates whether small countries gain relatively more than large countries from an 'expansion' of their market through the creation of a single currency. The introduction of the euro offers a particularly valuable source to test this hypothesis, which we motivate using the theoretical model by Casella of the year 1996. Our results from a panel data analysis, using both aggregate and disaggregated trade data, point to a statistically significant but quantitatively moderate small country bonus. On average, the euro has led to an improvement of the small euro area's relative export performance by 3–9%.

“Globalization, Taylor rules, and inflation”

Harald Badinger

Applied Economics Letters, published online 09 May 2008, DOI: 10.1080/13504850701720114

This article provides evidence that globalization has contributed to global disinflation by making policy makers more aggressive towards fighting inflation. We estimate Taylor rules for 83 countries over the period 1985 to 2004 and find that the relative weight attached to the output gap is negatively related to trade and financial openness in a simple cross-section model. This result does not hold up for the OECD subsample, suggesting that this group of countries has successfully solved the time inconsistency problem and uncoupled central bank behaviour from otherwise relevant determinants of the inflation bias.

“Fiscal rules, discretionary fiscal policy, and macroeconomic stability: an empirical assessment for OECD countries”

Harald Badinger

Applied Economics, 41(7), 2009, 829-847

Does aggressive use of discretionary fiscal policy induce macroeconomic instability in terms of higher output and inflation volatility? Three main conclusions arise from our cross section and panel analysis for a sample of 20 OECD countries: first, discretionary fiscal policy has a significant and sizeable effect on volatility of GDP (per capita) and all of its components. Second, there is no direct effect on inflation volatility; since output volatility is an important determinant of inflation volatility, discretionary fiscal policy indirectly exacerbates inflation volatility. These results turn out robust with respect to alternative fiscal policy measures and endogeneity concerns. Finally, many of the fiscal rules introduced since 1990 appear to have reduced the use of discretionary fiscal policy.

“Estimation of higher-order spatial autoregressive panel data error component models”

Harald Badinger (with Peter Egger)

CESifo Working Paper No. 2556

This paper develops an estimator for higher-order spatial autoregressive panel data error component models with spatial autoregressive disturbances, SARAR(R,S). We derive the moment conditions and optimal weighting matrix without distributional assumptions for a generalized moments (GM) estimation procedure of the spatial autoregressive parameters of the disturbance process and define a generalized two-stages least squares estimator for the regression parameters of the model. We prove consistency of the proposed estimators, derive their joint asymptotic distribution, and provide Monte Carlo evidence on their small sample performance.

List of all Publications since 2001 (by staff of the Economic Analysis and Research Section):

http://www.oenb.at/de/img/publications_2009_2_fin_tcm14-99334.pdf

Upcoming and Recent Events

The following events are organized by the OeNB. Please note that attendance is by invitation only. If you are interested in participating in one or more of the events, please send an e-mail to econ.newsletter@oenb.at

September 28, 2009	East Jour Fix: “Credit Default Swaps - Blessing or Curse?”
October 30, 2009	Friday Seminar: Information, heterogeneity and market incompleteness, held by Liam Graham (University College London)
November 13, 2009	Friday Seminar: Large Bayesian VARs, held by Domenico Giannone (European Central Bank)
November 16-17, 2009	OeNB Conference on Eastern European Integration
November 27, 2009	Friday Seminar: TBA, held by Volker Nitsch (Technical University Darmstadt)
December 11, 2009	Friday Seminar: TBA, held by Felix Kübler (University of Zurich)
Recent Events: April 17, 2009	Friday Seminar: Sales and Monetary Policy, held by Kevin Sheedy, London School of Economics (LSE)
May 7, 2009	Global Economy Lecture held by Tony Atkinson
May 8, 2009	Friday seminar: Systemic risk as renegotiation breakdown, held by Alfred Lehar, University of Calgary
May 14-15 , 2009	OeNB Economics Conference
May 22, 2009	Friday seminar: Information and Bubbles - Results from a Beauty Contest Experiment, held by Urs Birchler, Schweizerische Nationalbank
June 5, 2009	Friday seminar: Anatomy of financial crashes: an agent based model of the leverage cycle, held by Stefan Thurner, Universität Wien

June 8, 2009	Economic Forecast for Austria
June 19, 2009	Friday seminar: How Linkages Fuel the Fire: The Transmission of Financial Stress from Advanced to Emerging Economies, held by Stefan Danninger, International Monetary Fund

OeNB Courses at the Joint Vienna Institute (JVI)

August 31 - September 4, 2009	OeNB Summer School "The Current Financial Crisis - What can Structural Models tell us?"
September 21 - 25, 2009	Macro-Financial Stability, Exchange Rate Regimes, and Road to the Euro
October 5- 8, 2009	Cash Circulation and Payment Systems in Austria
November 9 - 13, 2009	Monetary and Financial Statistics Collected and Compiled by the ESCB
November 23 - 26, 2009	Economic and Monetary Integration in Europe
November 30 - December 2, 2009	Translation in a Central Bank Setting

For further details see: http://www.jvi.org/fileadmin/jvi_files/JVI_Program2009.pdf

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