

Welfare Costs

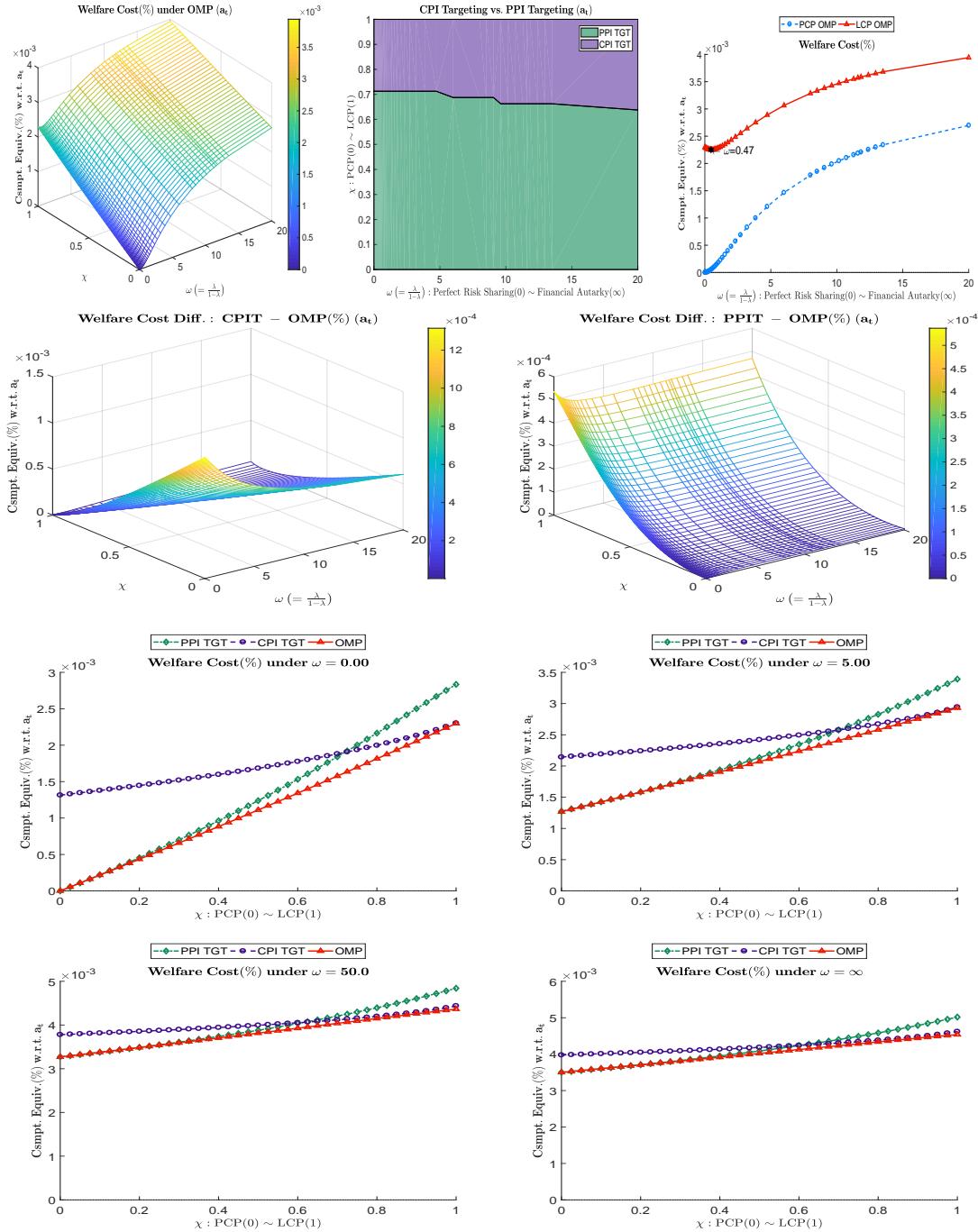
under different degrees of pricing-to-market

and varying degrees of risk sharing

with respect to

a Home Productivity Shock

Figure 18: Welfare Costs with respect to a Home Productivity Shock



Note — χ denotes the degree of pricing-to-market from PCP ($\chi = 0$) to LCP ($\chi = 1$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect risk sharing ($\omega = 0$) to financial autarky ($\omega = \infty$). Welfare costs are measured in consumption equivalent η^C (equation (40) in the main text). The first panel on the top display welfare costs under optimal monetary policy. The second panel on the top presents the range of χ and ω where CPI targeting incurs lower welfare cost than PPI targeting and vice versa: green area for PPI targeting and violet for CPI targeting. The first and second figures in the second row shows the difference of welfare costs of CPI and PPI targeting from that of optimal policy. *PPI TGT* denotes strict PPI inflation targeting; *CPI TGT* denotes strict CPI inflation targeting; *OMP* represents optimal monetary policy.

Welfare Costs

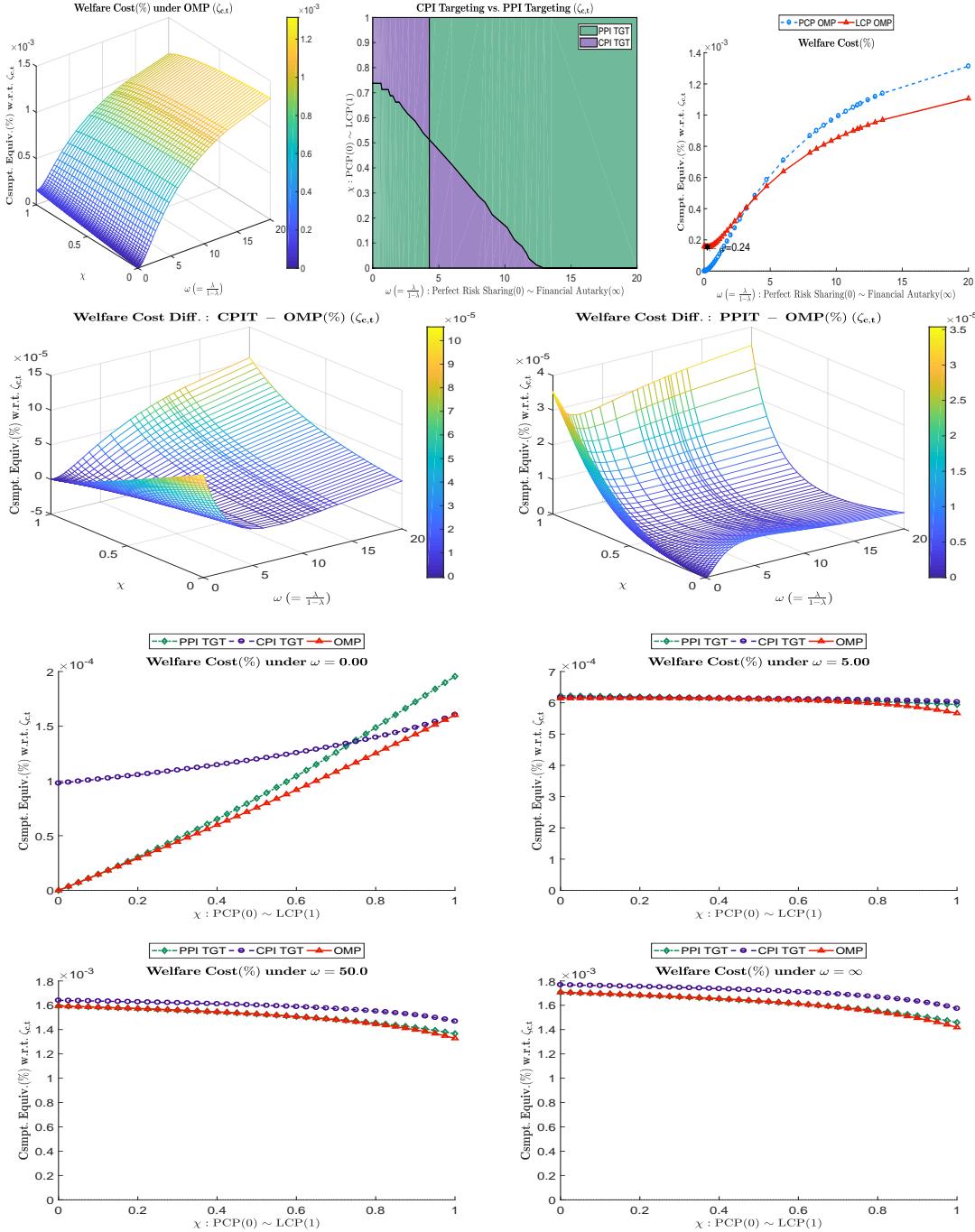
under different degrees of pricing-to-market

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a Home Preference Shock

Figure 19: Welfare Costs with respect to a Home Preference Shock



Note – χ denotes the degree of pricing-to-market from PCP ($\chi = 0$) to LCP ($\chi = 1$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect risk sharing ($\omega = 0$) to financial autarky ($\omega = \infty$). Welfare costs are measured in consumption equivalent η^C (equation (40) in the main text). The first panel on the top display welfare costs under optimal monetary policy. The second panel on the top presents the range of χ and ω where CPI targeting incurs lower welfare cost than PPI targeting and vice versa: green area for PPI targeting and violet for CPI targeting. The first and second figures in the second row shows the difference of welfare costs of CPI and PPI targeting from that of optimal policy. *PPI TGT* denotes strict PPI inflation targeting; *CPI TGT* denotes strict CPI inflation targeting; *OMP* represents optimal monetary policy.

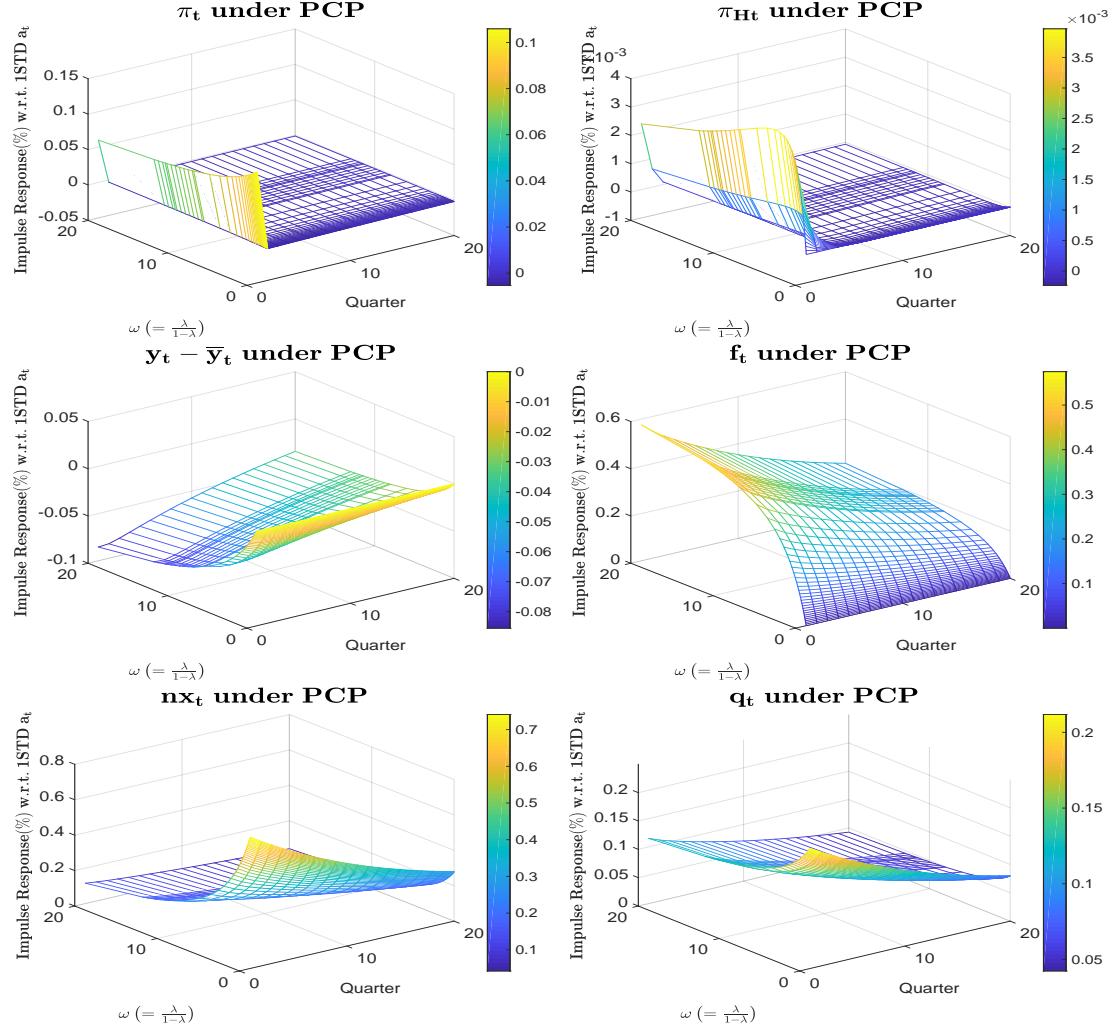
Impulse Responses

under PCP and different degrees of risk sharing

with respect to

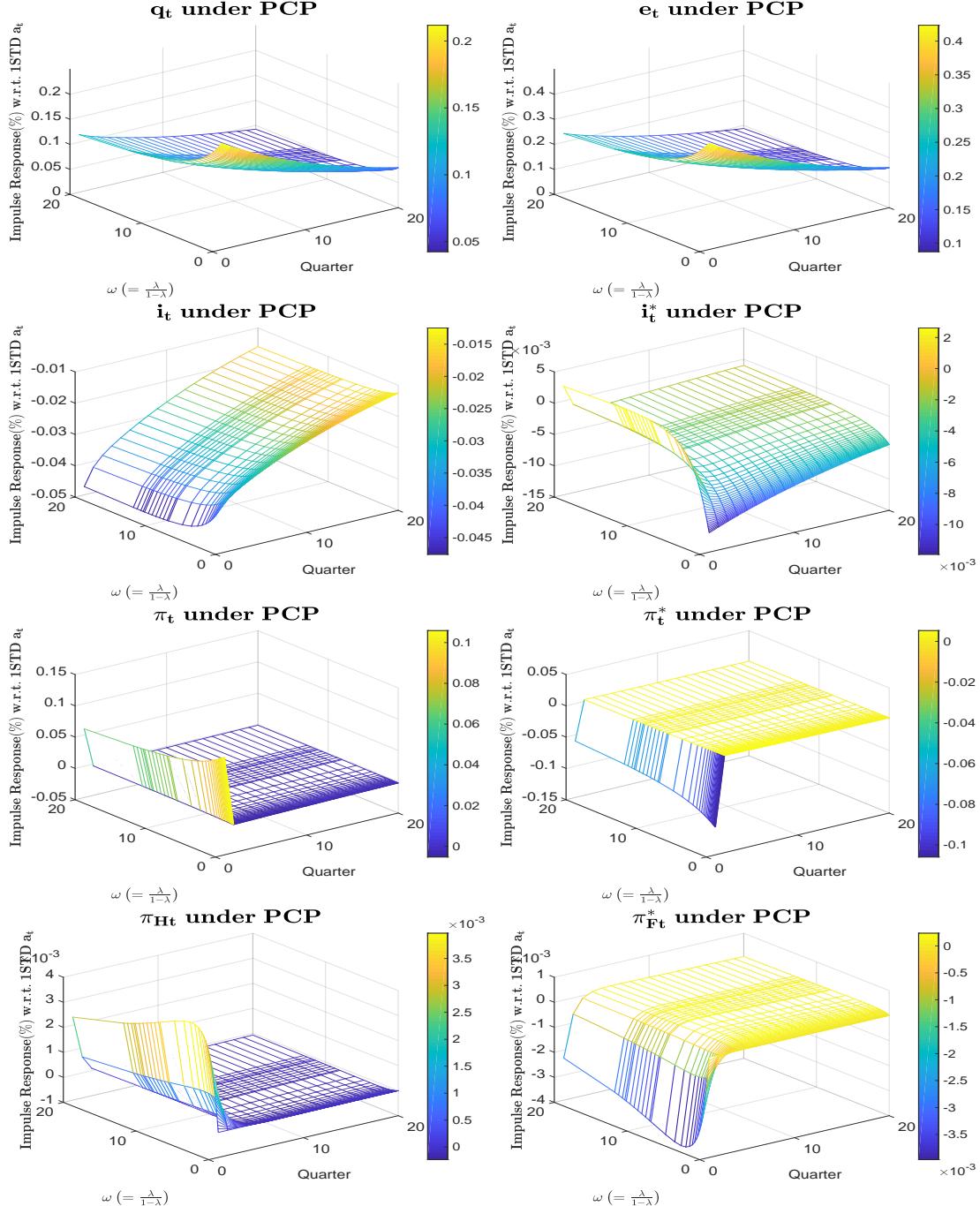
a 1 STD Home Productivity Shock

Figure 20: [PCP] Impulse Responses of Policy Targets with respect to a 1 STD Home Productivity Shock



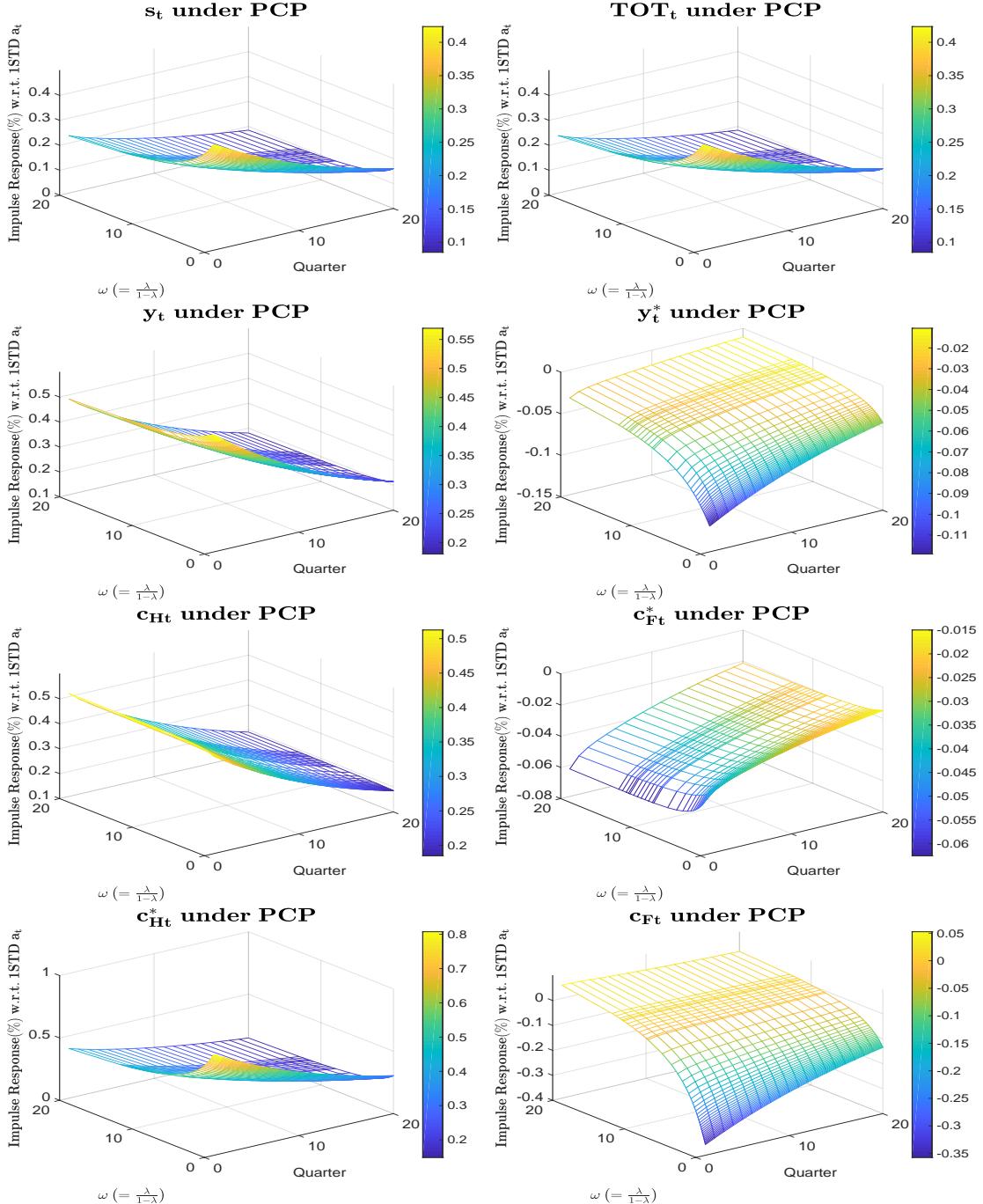
Note – PCP denotes producer currency pricing ($\chi = 0$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ); y_t Home output and \bar{y}_t its efficient counterpart; f_t demand imbalance; nx_t net exports; q_t real exchange rate.

Figure 21: [PCP] Impulse Responses of Policy Instruments with respect to a 1 STD Home Productivity Shock



Note – PCP denotes producer currency pricing ($\chi = 0$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). q_t denotes real exchange rate and e_t nominal exchange rate; i_t nominal interest rate (QoQ); π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ). Variables with asterisk denote Foreign counterparts.

Figure 22: [PCP] Impulse Responses of Output with respect to a 1 STD Home Productivity Shock



Note – PCP denotes producer currency pricing ($\chi = 0$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). s_t denotes the price of imported goods relative to domestically-produced goods in Home; TOT_t Home terms of trade; y_t Home output; c_{Ht} Home demand for Home produced goods; c_{Ft} Home demand for Foreign produced goods; c_{Ht}^* Foreign demand for Home produced goods; c_{Ft}^* Foreign demand for Foreign produced goods. Variables with asterisk denote Foreign counterparts.

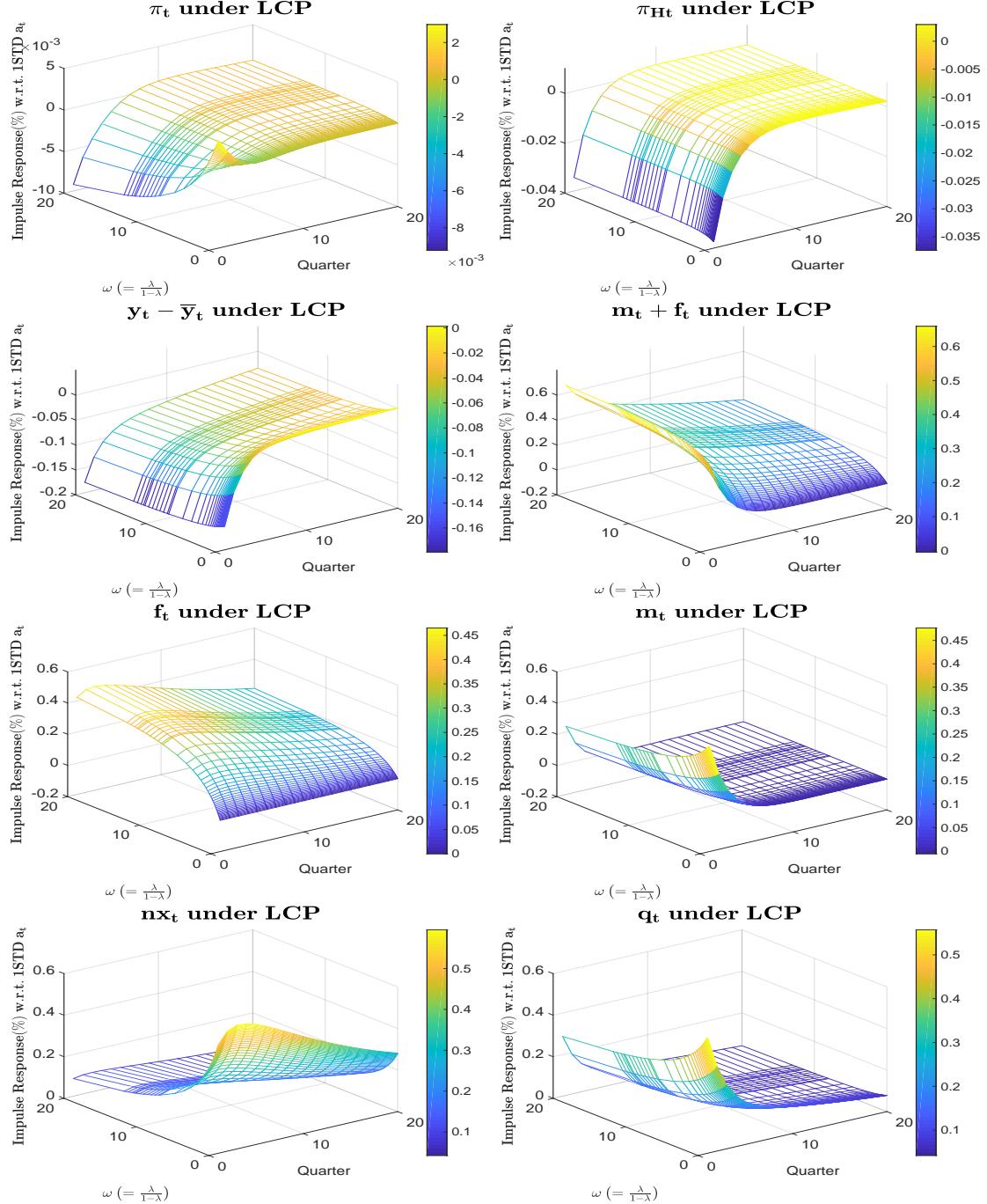
Impulse Responses

under LCP and different degrees of risk sharing

with respect to

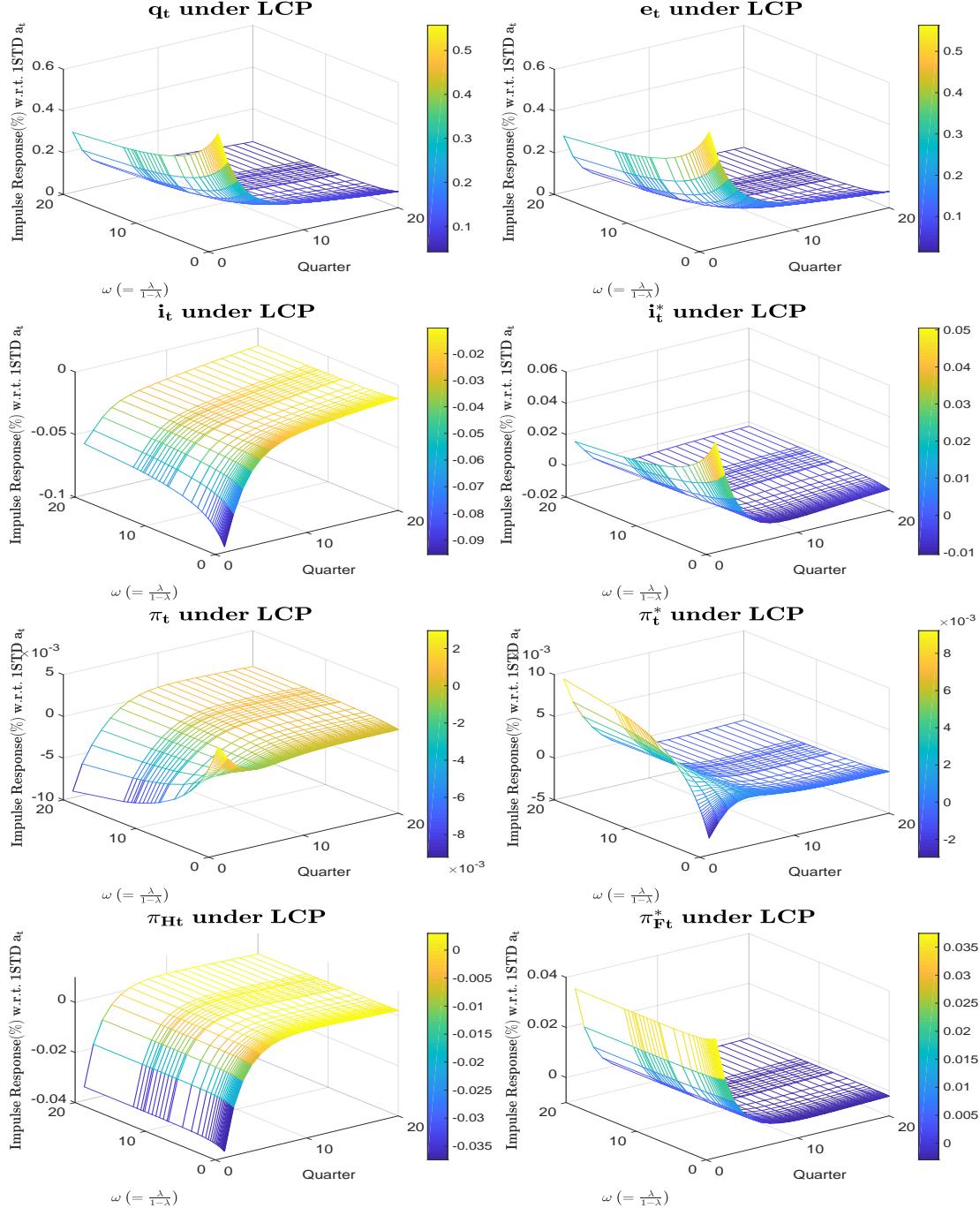
a 1 STD Home Productivity Shock

Figure 23: [LCP] Impulse Responses of Policy Targets with respect to a 1 STD Home Productivity Shock



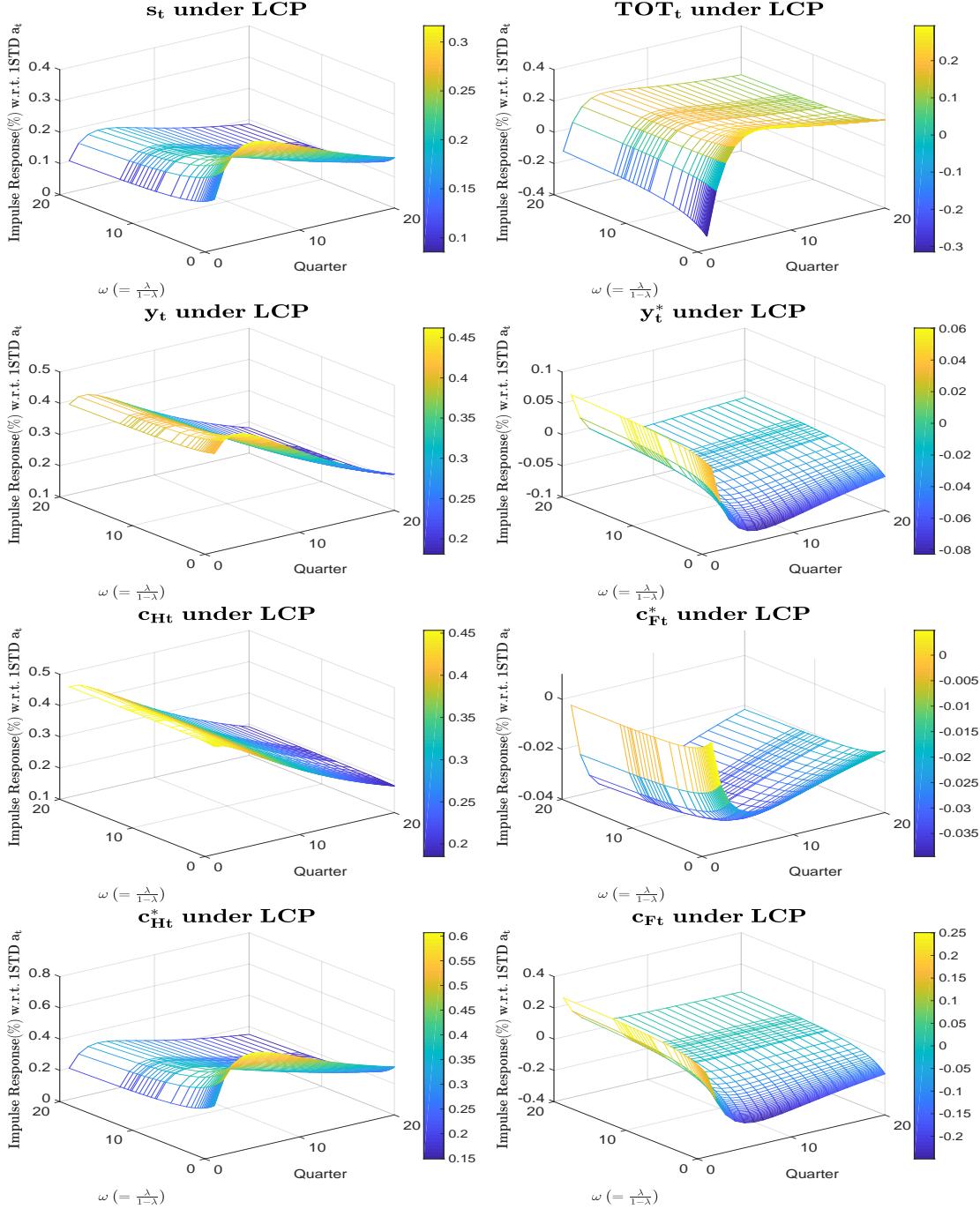
Note – LCP denotes local currency pricing ($\chi = 1$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ); y_t Home output and \bar{y}_t its efficient counterpart; f_t demand imbalance; m_t currency misalignment; nxt net exports; q_t real exchange rate.

Figure 24: [LCP] Impulse Responses of Policy Instruments with respect to a 1 STD Home Productivity Shock



Note – LCP denotes local currency pricing ($\chi = 1$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). q_t denotes real exchange rate and e_t nominal exchange rate; i_t nominal interest rate (QoQ); π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ). Variables with asterisk denote Foreign counterparts.

Figure 25: [LCP] Impulse Responses of Output with respect to a 1 STD Home Productivity Shock



Note – LCP denotes local currency pricing ($\chi = 1$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). s_t denotes the price of imported goods relative to domestically-produced goods in Home; TOT_t Home terms of trade; y_t Home output; c_{Ht} Home demand for Home produced goods; c_{Ft} Home demand for Foreign produced goods; c_{Ft}^* Foreign demand for Foreign produced goods; c_{Ht}^* Foreign demand for Home produced goods. Variables with asterisk denote Foreign counterparts.

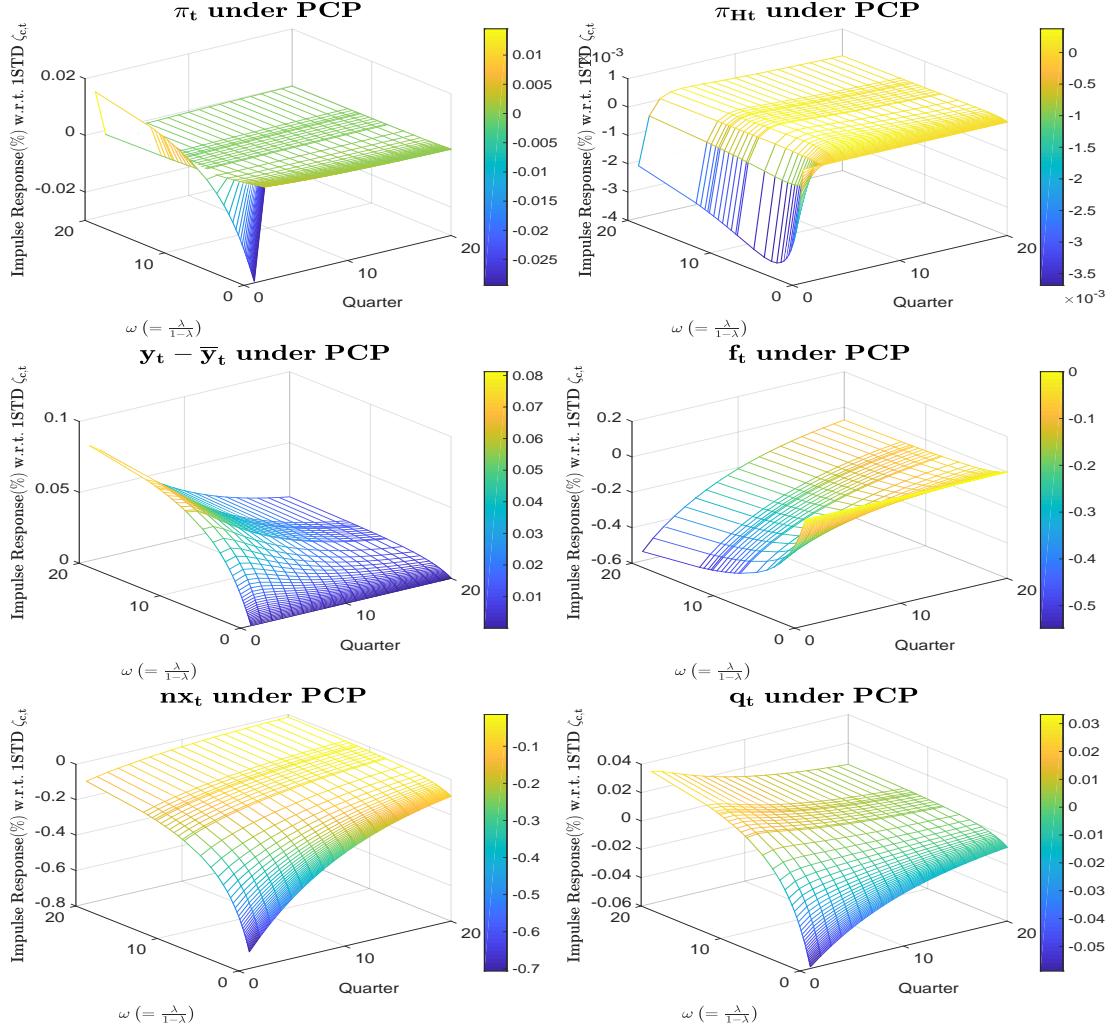
Impulse Responses

under PCP and different degrees of risk sharing

with respect to

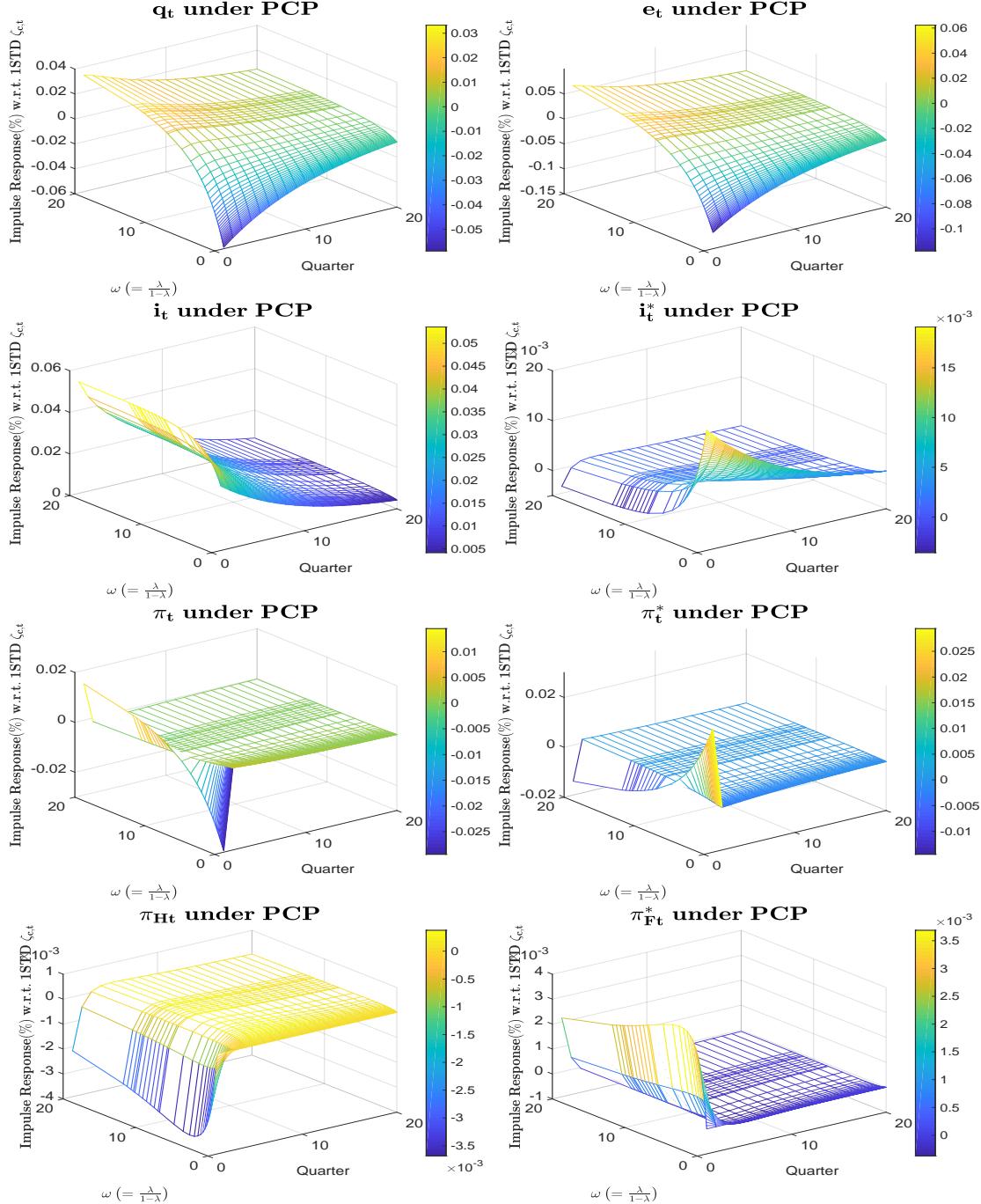
a 1 STD Home Preference Shock

Figure 26: [PCP] Impulse Responses of Policy Targets with respect to a 1 STD Home Preference Shock



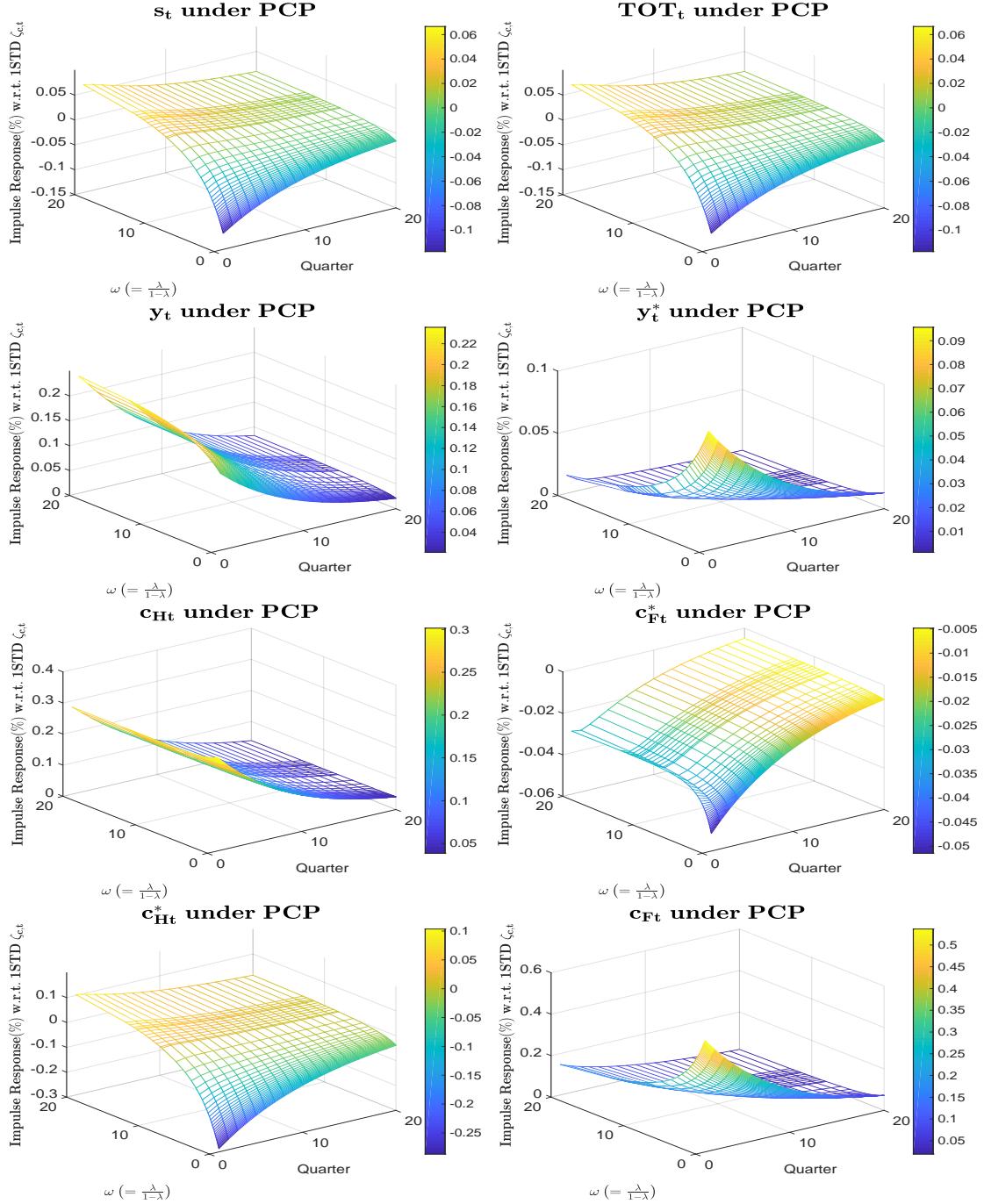
Note – PCP denotes producer currency pricing ($\chi = 0$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ); y_t Home output and \bar{y}_t its efficient counterpart; f_t demand imbalance; nx_t net exports; q_t real exchange rate.

Figure 27: [PCP] Impulse Responses of Policy Instruments with respect to a 1 STD Home Preference Shock



Note – PCP denotes producer currency pricing ($\chi = 0$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). q_t denotes real exchange rate and e_t nominal exchange rate; i_t nominal interest rate (QoQ); π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ). Variables with asterisk denote Foreign counterparts.

Figure 28: [PCP] Impulse Responses of Output with respect to a 1 STD Home Preference Shock



Note – PCP denotes producer currency pricing ($\chi = 0$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). s_t denotes the price of imported goods relative to domestically-produced goods in Home; TOT_t Home terms of trade; y_t Home output; c_{Ht} Home demand for Home produced goods; c_{Ft} Home demand for Foreign produced goods; c_{Ht}^* Foreign demand for Home produced goods. Variables with asterisk denote Foreign counterparts.

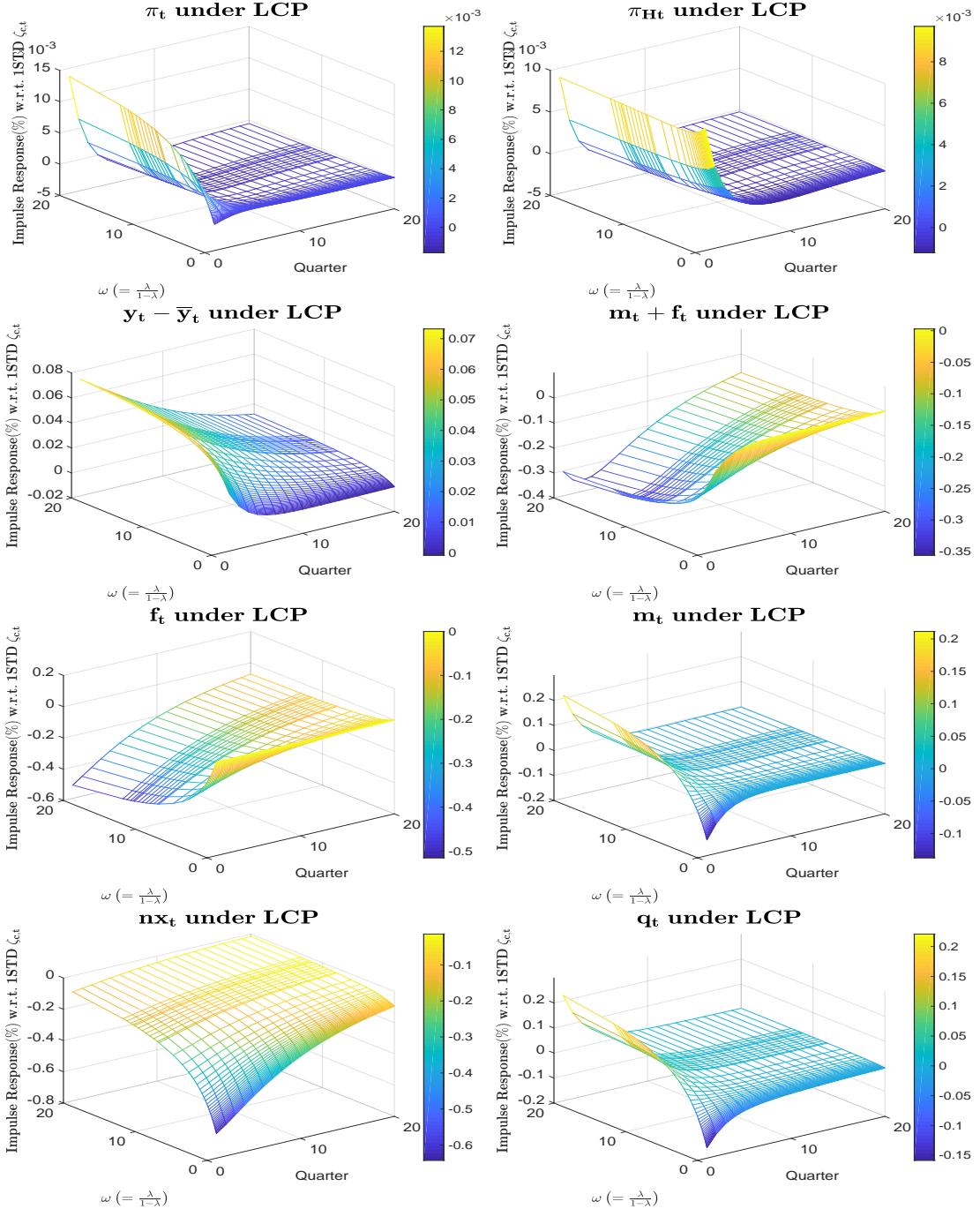
Impulse Responses

under LCP and different degrees of risk sharing

with respect to

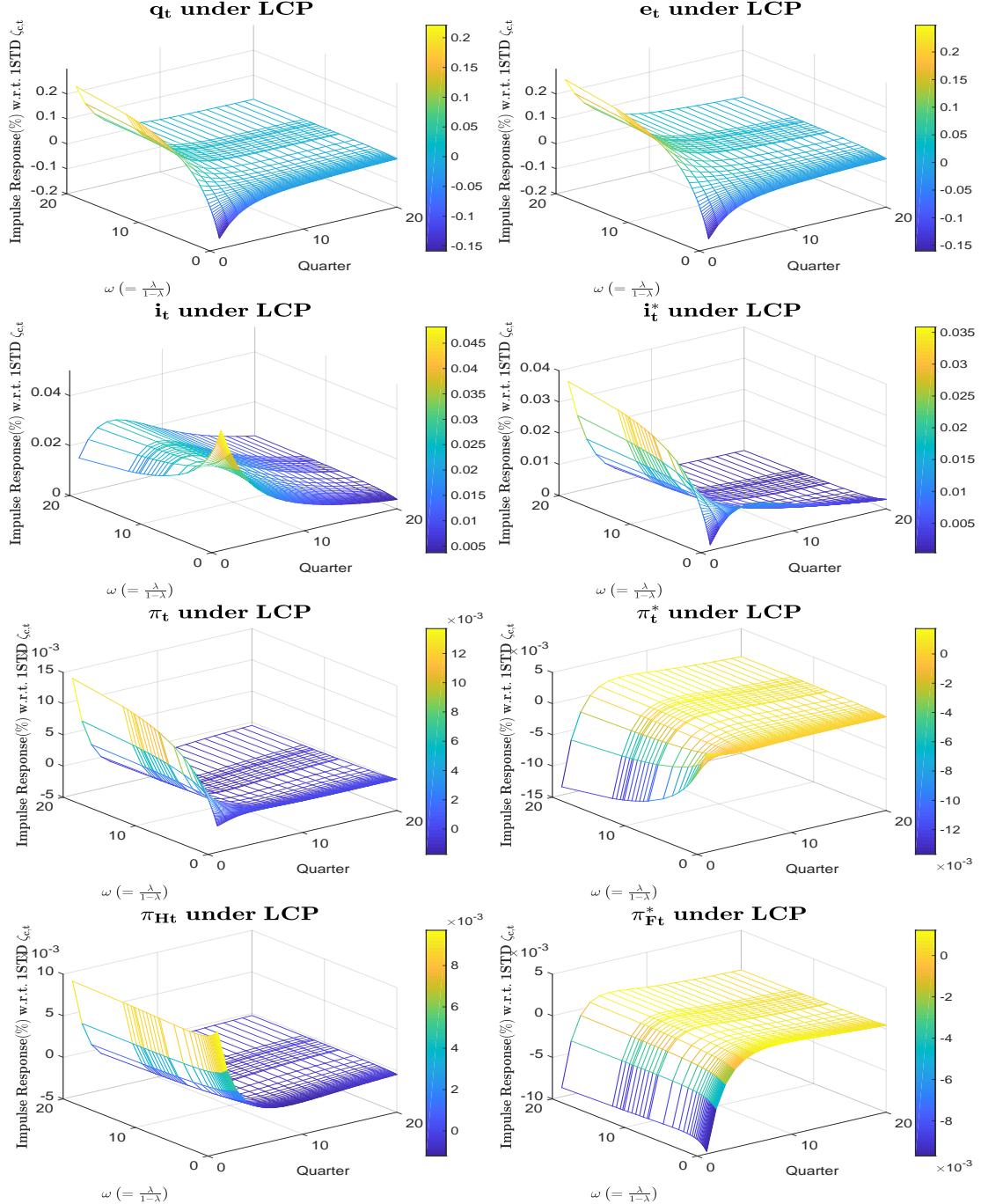
a 1 STD Home Preference Shock

Figure 29: [LCP] Impulse Responses of Policy Targets with respect to a 1 STD Home Preference Shock



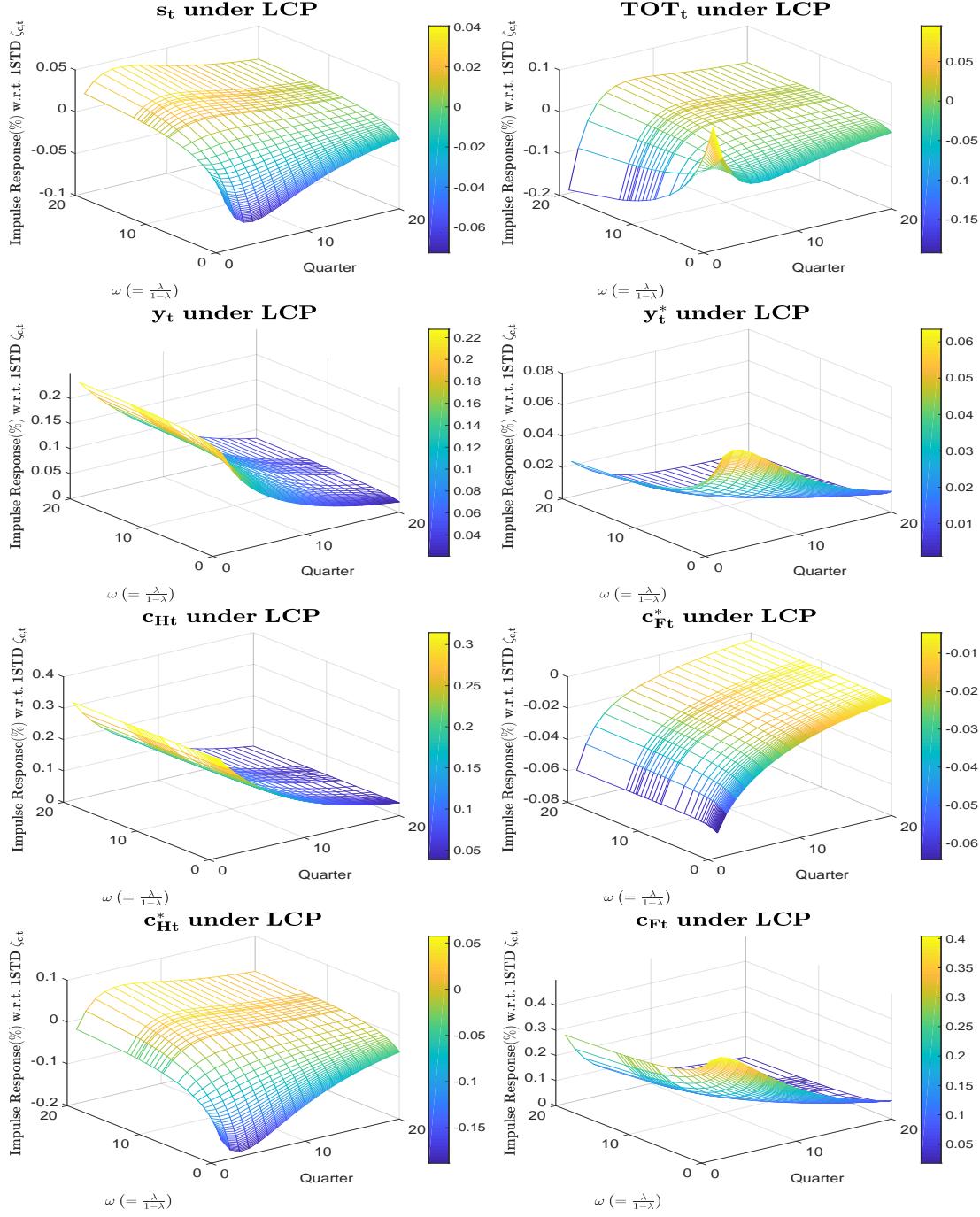
Note – LCP denotes local currency pricing ($\chi = 1$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ); y_t Home output and \bar{y}_t its efficient counterpart; f_t demand imbalance; m_t currency misalignment; nx_t net exports; q_t real exchange rate.

Figure 30: [LCP] Impulse Responses of Policy Instruments with respect to a 1 STD Home Preference Shock



Note – LCP denotes local currency pricing ($\chi = 1$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). q_t denotes real exchange rate and e_t nominal exchange rate; i_t nominal interest rate (QoQ); π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ). Variables with asterisk denote Foreign counterparts.

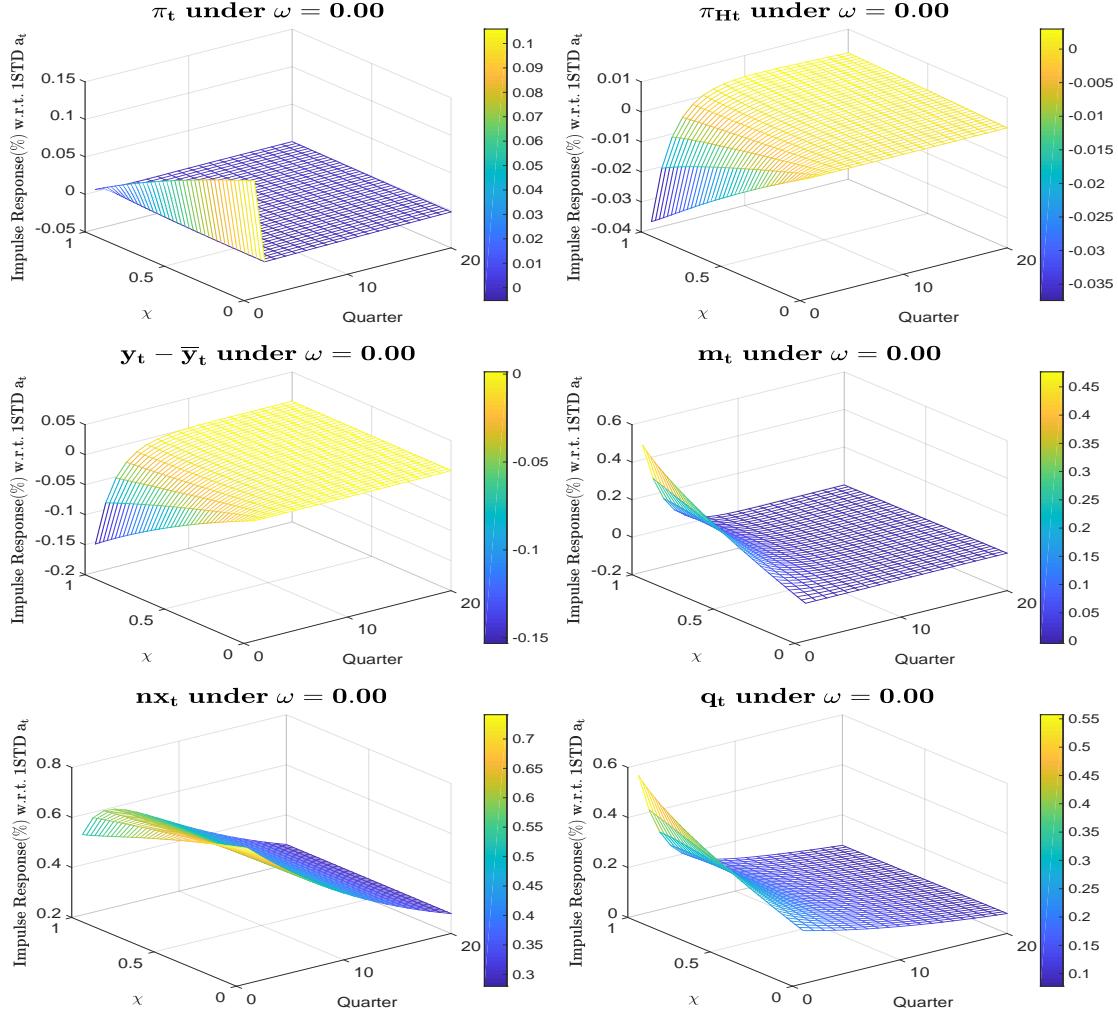
Figure 31: [LCP] Impulse Responses of Output with respect to a 1 STD Home Preference Shock



Note – LCP denotes local currency pricing ($\chi = 1$). $\omega \equiv \frac{\lambda}{1-\lambda}$ represents the degree of financial market integration ranging from perfect financial integration ($\omega = 0$) to financial autarky ($\omega = \infty$). s_t denotes the price of imported goods relative to domestically-produced goods in Home; TOT_t Home terms of trade; y_t Home output; c_{Ht} Home demand for Home produced goods; c_{Ft} Home demand for Foreign produced goods; c_{Ft}^* Foreign demand for Foreign produced goods; c_{Ht}^* Foreign demand for Home produced goods. Variables with asterisk denote Foreign counterparts.

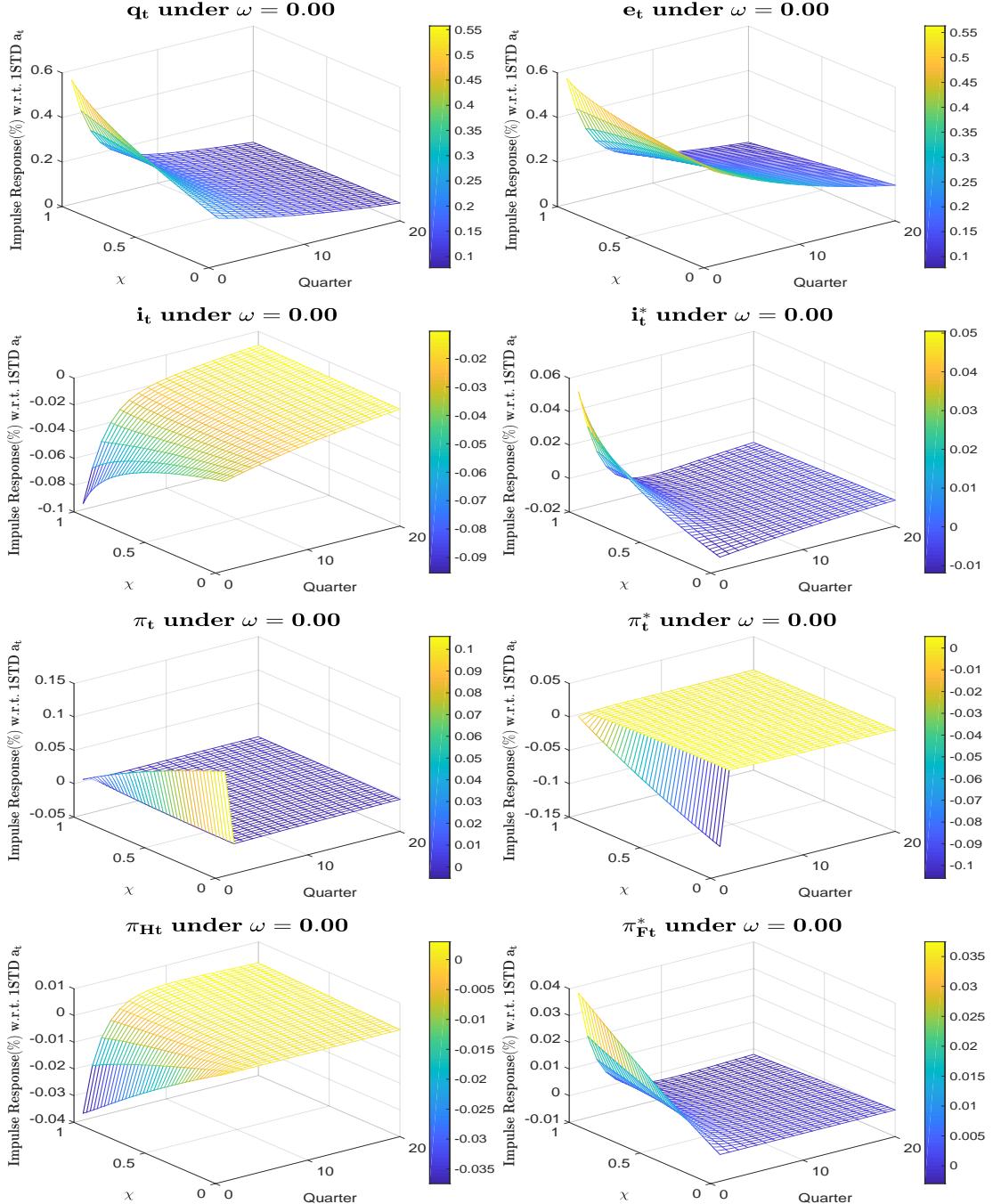
Impulse Responses
under perfect risk sharing
and varying degrees of ERPT
with respect to
a 1 STD Home Productivity Shock

Figure 32: Impulse Responses of Policy Targets with respect to a 1 STD Home Productivity Shock under Perfect Risk Sharing



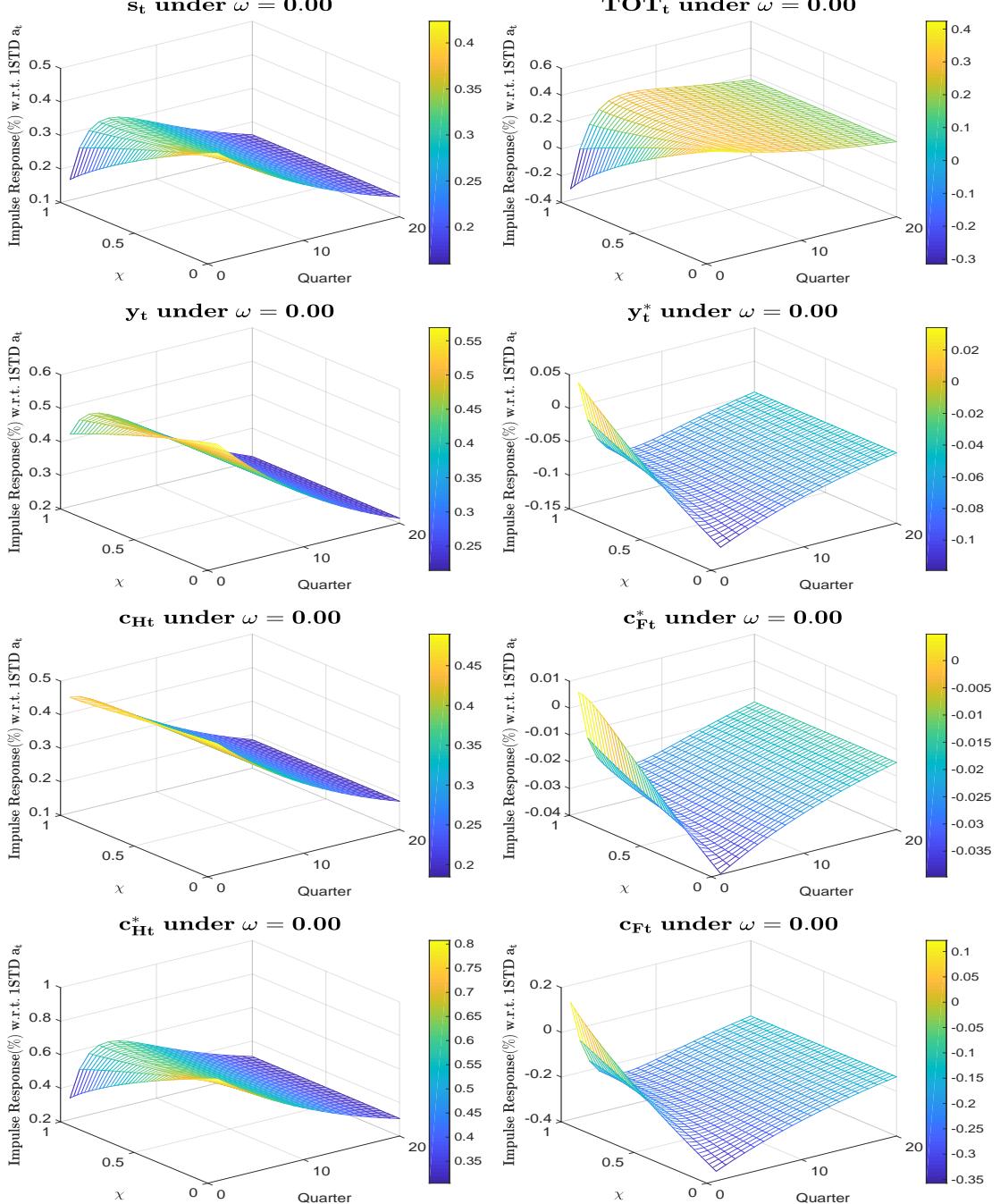
Note – χ denotes the degree of pricing-to-market from PCP ($\chi = 0$) to LCP ($\chi = 1$). π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ); y_t Home output and \bar{y}_t its efficient counterpart; m_t currency misalignment; nx_t net exports; q_t real exchange rate.

Figure 33: Impulse Responses of Policy Instruments with respect to a 1 STD Home Productivity Shock under Perfect Risk Sharing



Note – χ denotes the degree of pricing-to-market from PCP ($\chi = 0$) to LCP ($\chi = 1$). q_t denotes real exchange rate and e_t nominal exchange rate; i_t nominal interest rate (QoQ); π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ). Variables with asterisk denote Foreign counterparts.

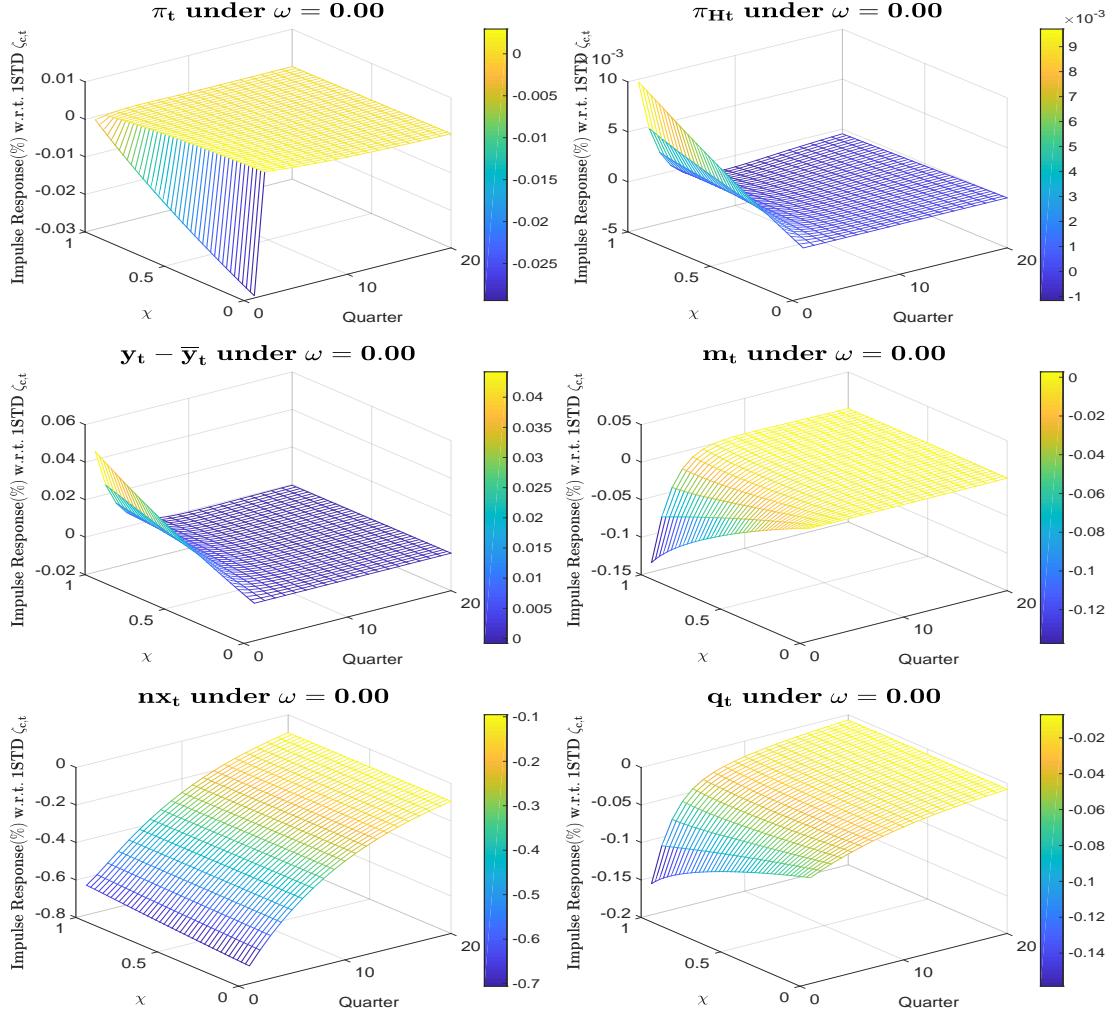
Figure 34: Impulse Responses of Output with respect to a 1 STD Home Productivity Shock under Perfect Risk Sharing



Note – χ denotes the degree of pricing-to-market from PCP ($\chi = 0$) to LCP ($\chi = 1$). s_t denotes the price of imported goods relative to domestically-produced goods in Home; TOT_t Home terms of trade; y_t Home output; c_{Ht} Home demand for Home produced goods; c_{Ft} Home demand for Foreign produced goods; c_{Ft}^* Foreign demand for Foreign produced goods; c_{Ht}^* Foreign demand for Home produced goods. Variables with asterisk denote Foreign counterparts.

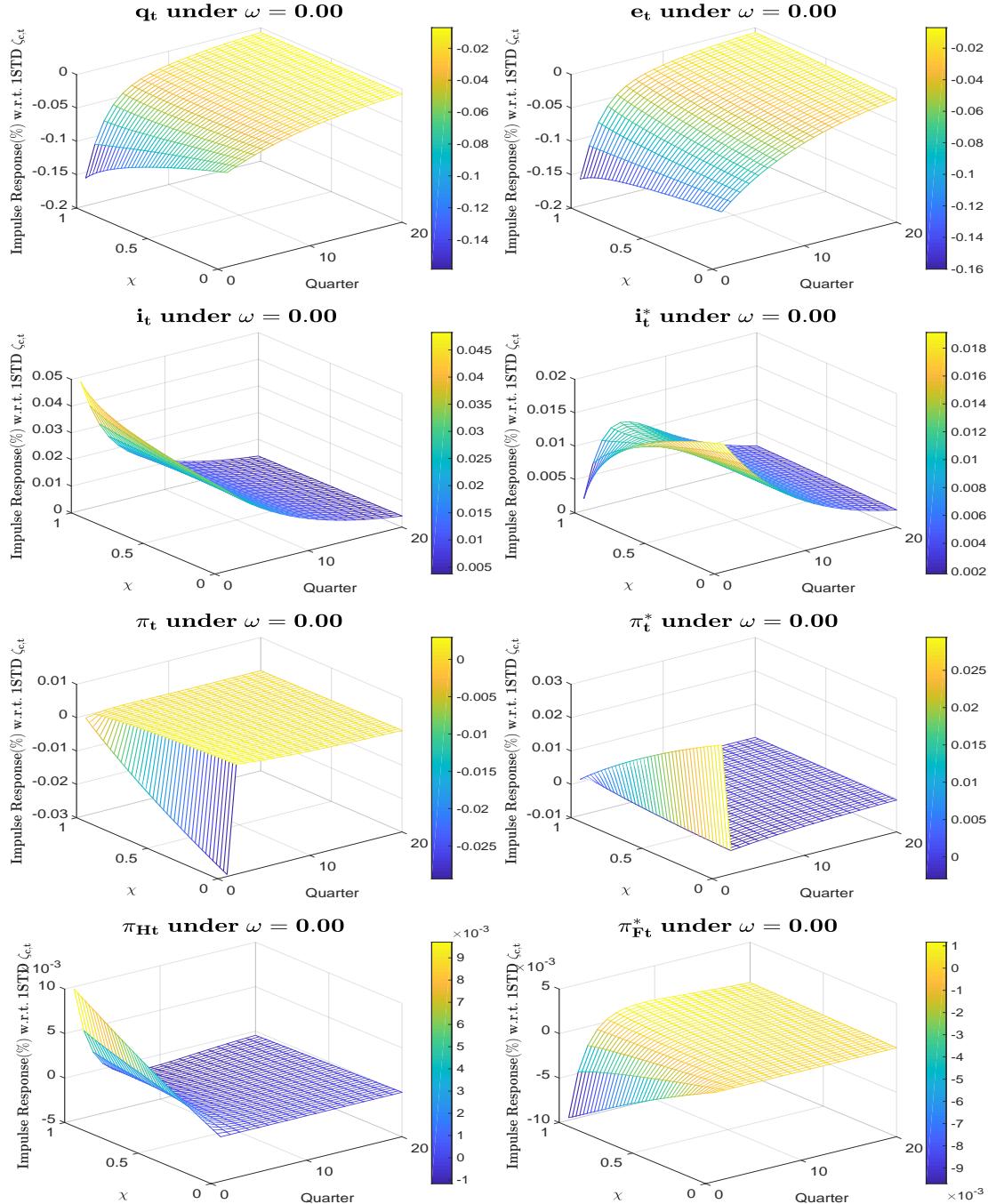
Impulse Responses
under perfect risk sharing
and varying degrees of ERPT
with respect to
a 1 STD Home Preference Shock

Figure 35: Impulse Responses of Policy Targets with respect to a 1 STD Home Preference Shock under Perfect Risk Sharing



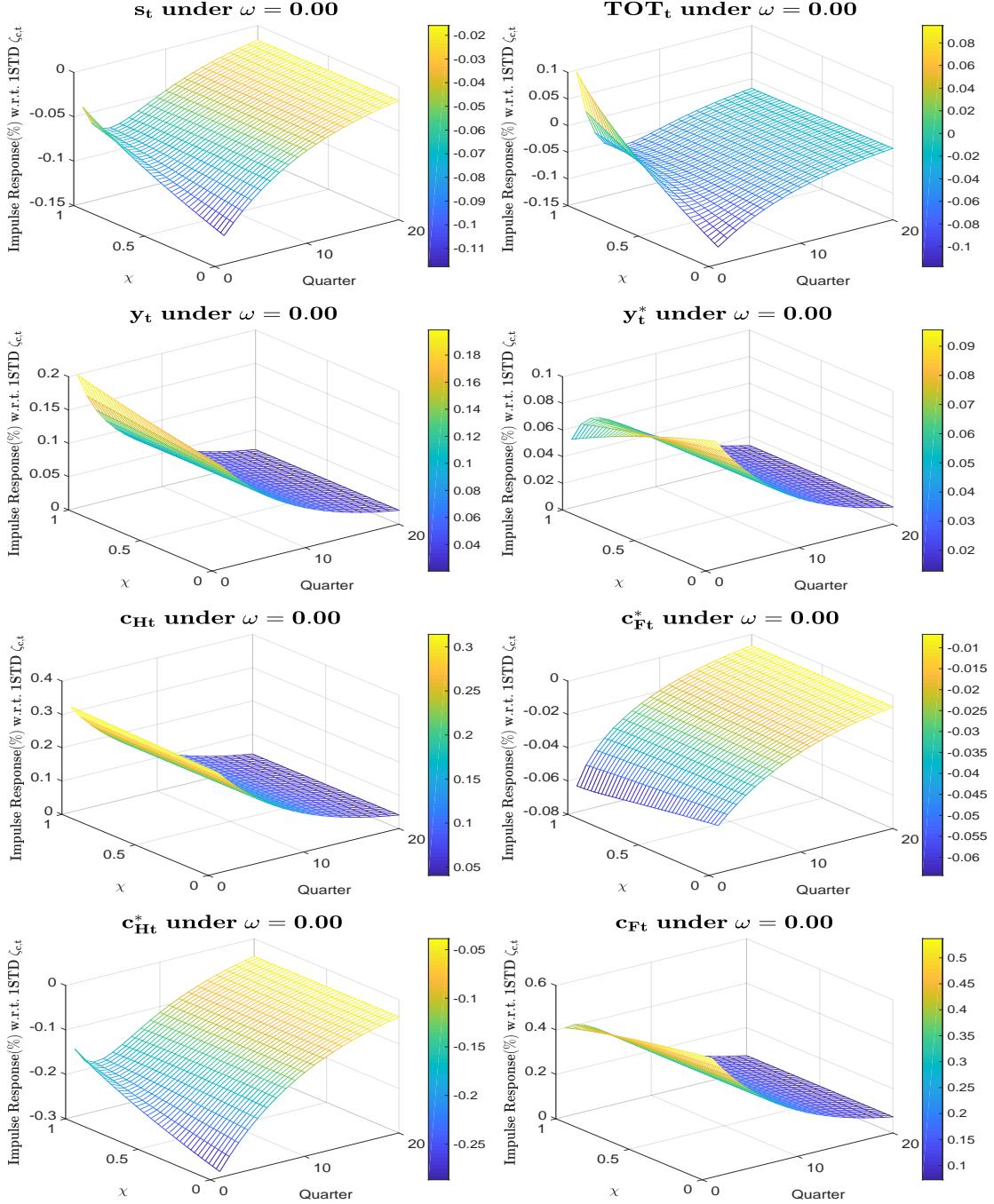
Note – χ denotes the degree of pricing-to-market from PCP ($\chi = 0$) to LCP ($\chi = 1$). π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ); y_t Home output and \bar{y}_t its efficient counterpart; m_t currency misalignment; nx_t net exports; q_t real exchange rate.

Figure 36: Impulse Responses of Policy Instruments with respect to a 1 STD Home Preference Shock under Perfect Risk Sharing



Note – χ denotes the degree of pricing-to-market from PCP ($\chi = 0$) to LCP ($\chi = 1$). q_t denotes real exchange rate and e_t nominal exchange rate; i_t nominal interest rate (QoQ); π_t denotes Home CPI inflation rate (QoQ); π_{Ht} Home PPI inflation rate (QoQ). Variables with asterisk denote Foreign counterparts.

Figure 37: Impulse Responses of Output with respect to a 1 STD Home Preference Shock under Perfect Risk Sharing



Note – χ denotes the degree of pricing-to-market from PCP ($\chi = 0$) to LCP ($\chi = 1$). s_t denotes the price of imported goods relative to domestically-produced goods in Home; TOT_t Home terms of trade; y_t Home output; c_{Ht} Home demand for Home produced goods; c_{Ft} Home demand for Foreign produced goods; c^*_{Ft} Foreign demand for Foreign produced goods; c^*_{Ht} Foreign demand for Home produced goods. Variables with asterisk denote Foreign counterparts.