

Comments

Hamza Malik's paper is a valuable extension of dynamic general equilibrium model with its application for emerging market economies. The model has been constructed around a number of plausible assumptions including monopolistic competition, imperfect substitution of domestic and foreign goods, differentiated variety of goods, and rigidities in prices. Addition of foreign assets position through the introduction of domestic and foreign bonds with risk premium further enhances the realism of this model for policy simulations.

Despite all these strengths, Malik cautions us that conclusions should not be taken as general propositions, notwithstanding the robustness of results to minor changes in assumptions about parameterization. This point has been emphasized by McCallum (1997), in which the key stumbling block for policy formation is the limited knowledge of the way the macro economy works. Results that are highly model-specific are of limited use.

One of the policy conclusions of Malik's paper that advises central bank to lower the interest in the presence of excess appreciation is most troublesome. While the conclusion is perfectly logical within the context of specific formulation, I strongly suspect that it can be reversed with further extension of the model by incorporating more realistic behavior of macroeconomics in developing countries. I think the troublesome conclusion can easily be reversed if classic inflationary bias is introduced in the model.

Another related weakness is the absence of government or at best, its implicit benign presence in the model. I believe that incorporation of domestic assets in a way that makes fiscal deficits possible will take care of this weakness as well as that of absence of inflationary bias. I do understand that by introducing financial intermediaries and capital, model may become too complicated and may lose its intuitive appeal. However, some thoughts on these lines may considerably enhance the usefulness of computable general equilibrium models.

Finally, I congratulate the author to formulate this model in an analytically tractable and intuitively clear manner, and believe that it is a significant contribution to the literature of dynamic computable general equilibrium models.

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Reference

McCallum, B. (1997). *Issues in the Design of Monetary Policy Rules*. NBER Working Paper No. 6016. Massachusetts: NBER.