

The alternative view is that beggar-thy-neighbor impacts are greater when using unconventional instruments. The difficulty arises in evaluating whether the use of such instruments is consistent with the normal policy framework or represents an attempt mainly to weaken the currency and boost exports in the absence of a positive domestic demand response. The same causes that justify recourse to unconventional policies make the inflation-targeting compass lose precision. When inflation significantly undershoots its target and central banks resort to instruments with which they have little experience, it is much harder to say whether a policy stance is in line with the IT framework or whether it represents an attempt at competitive devaluation.

In addition, spillovers may work differently in times of crisis. During a crisis, local credit demand is likely to be weak and banks' willingness to lend domestically will be especially limited. For every additional dollar of liquidity that is created by monetary policy, a larger share will end up abroad in crisis times than in normal times, thereby depreciating the exchange

rate at the expense of trade partners. It follows that spillovers are potentially larger during episodes of local financial distress.

The presence of international spillovers suggests that coordination can lead to better global outcomes. In addition, the current situation highlights the need for principles and procedures for deciding when an unconventional monetary policy is beggar-thy-neighbor in its effect. In turn, these principles should form the basis for corrective action.

Conclusion

The cross-border spillovers from monetary policy provide yet another reason for rethinking not just the domestic monetary policy framework but also mechanisms for ensuring compatibility between large-country policies. We will turn to recommendations that follow from this analysis in Chapter Five. But before offering recommendations, we turn to a discussion of some additional policy burdens on central banks in the aftermath of the crisis.