

Accepted Manuscript

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PII: S0022-1996(17)30002-8
DOI: doi:[10.1016/j.jinteco.2016.12.012](https://doi.org/10.1016/j.jinteco.2016.12.012)
Reference: INEC 3014

To appear in: *Journal of International Economics*

Received date: 10 August 2016
Revised date: 17 December 2016
Accepted date: 31 December 2016

Please cite this article as: Céspedes, Luis Felipe, Chang, Roberto, Velasco, Andrés, Financial Intermediation, Real Exchange Rates, and Unconventional Policies in an Open Economy, *Journal of International Economics* (2017), doi:[10.1016/j.jinteco.2016.12.012](https://doi.org/10.1016/j.jinteco.2016.12.012)

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Financial Intermediation, Real Exchange Rates, and Unconventional Policies in an Open Economy*

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This draft: December 2016

Abstract

We discuss unconventional policies in an open economy where financial intermediaries face occasionally binding collateral constraints. The model highlights interactions among the real exchange rate, interest rates, and financial frictions. The real exchange rate can affect international credit constraints via a net worth effect and a novel leverage ratio effect. Unconventional policies are non-neutral if financial constraints bind. Credit programs are most effective when targeted towards financial intermediaries. Sterilized interventions matter because the increased availability of tradables associated with sterilization relaxes financial frictions.

*We are indebted to an anonymous referee and to Jordi Gali, Paolo Pesenti, Gian Maria Milesi-Ferretti and Anton Korinek, for insightful discussions and suggestions. We also thank participants in the 2016 International Seminar on Macroeconomics, the Seventh Workshop of the Latin American Finance Network, and seminars at Brown University, London Business School, the University of Maryland, the IMF, and the Central Bank of Peru. Of course, any errors or omissions remain solely our own.

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