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

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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.

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