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The Federal Reserve Bank of St. Louis
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St. Louis Fed's *Review*:
An Introduction to Capital Controls
Recent Developments in the Analysis of Monetary Policy Rules
The Role of Supervisory Screens and Econometric Models in Off-Site Surveillance
Testing Long-Run Monetary Neutrality Propositions: Lessons from Recent Research

ST. LOUIS, Mo. — The November/December edition of *Review*, the Federal Reserve Bank of St. Louis' journal of economic and business issues, features the following articles:

• **"An Introduction to Capital Controls."** The Asian crisis and the relatively recent resumption of large international capital flows have revived interest in capital controls — taxes or restrictions in assets like stocks or bonds. Capital controls have been around for a long time and nations have used them for many purposes, including raising revenue, allocating credit domestically, or correcting balance of payments problems. Economist Christopher J. Neely reviews the pros and cons of using capital controls. He concludes that although the issue of whether to use capital controls is complicated, policymakers could better serve their nations' economies by attacking the source of financial distortions or by correcting inconsistent policies.

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• **"Recent Developments in the Analysis of Monetary Policy Rules."** Economist Bennett T. McCallum describes the central aspects of the typical framework used to analyze monetary policy rules. He reviews the methods used to study the effects of policy behavior and provides an example of how two rules can be used to investigate recent monetary policy in Japan. His example shows why it may be important for central banks to develop monetary policy procedures based on monetary-aggregate as well as interest-rate instruments.

• **"The Role of Supervisory Screens and Econometric Models in Off-Site Surveillance."** Off-site surveillance uses financial ratios to identify banks likely to develop problems in safety and soundness. Bank supervisors use two tools to flag developing problems: supervisory screens and econometric models. Despite the fact that models provide more accurate predictions than supervisory screens of which banks will fail or have their supervisory ratings downgraded in the future, supervisors continue to rely heavily on screens. Economists R. Alton Gilbert, Andew P. Meyer and Mark D. Vaughan developed a new econometric model — one designed to forecast downgrades in supervisory ratings — that is more forward-looking than existing models. Although the authors contend that both screens and models add value to off-site surveillance, they conclude that supervisors should rely more heavily on econometric models than they have in the past.

• **"Testing Long-Run Monetary Neutrality Propositions: Lessons from the Recent Research."** Economist James Bullard reviews recent evidence on the long-run neutrality and superneutrality of money. Although he finds the evidence mixed, Bullard determines that considering only lower-inflation countries leads to the conclusion that permanently higher

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money growth or inflation is associated with permanently higher output and permanently lower real interest rates. That result, however, is inconsistent with most other current quantitative business cycle models, which generally predict that permanently higher inflation permanently lowers consumption and output.

Subscriptions to ***Review*** are free and can be obtained by calling (314) 444-8809. The publication is also available on the St. Louis Fed's Web site: www.stls.frb.org.

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