Market Reforms and the Limitations of Monetary Policy: The Case of Colombia

Frank R. Gunter
*Carolyn Fabian Stumph**

In the early 1990s, Colombia moved rapidly to reform its economy including a dramatic opening to foreign trade and capital. This study shows that as a result of this opening, the Colombian economy has become much more economically integrated with that of the rest of Latin America, especially Venezuela and Ecuador. The implications for monetary policy of trade liberalization are then examined. It appears that the cost-benefit trade off may have shifted against the Central Bank's existing policy of steady peso depreciation and in favor of an Argentinean type of currency board. The possible framework of a Colombian currency board is then discussed.

JEL Code: O
Key Words: Colombian monetary policy, currency board, economic integration.

* The authors appreciate the generous financial support of the Martindale Center for the Study of Private Enterprise. Earlier versions of this study were presented at the Lehigh University Conference on the Economic and Social Implications of Colombian Market Reforms in April 1999 and the Southern Economic Association Annual Meeting in November 1999.

Frank R. Gunter, PhD Economics Department Lehigh University 621 Taylor Street Bethlehem, PA 18015 frg2@lehigh.edu.

Carolyn Fabian Stumph, PhD Economics Department Illinois Wesleyan University.