General Discussion*

Participants focused their comments primarily on Canadian policy issues. David Laidler was skeptical about the paper's fixed-cost assumption. He related it to what he considered the assumption of "laziness" by some authors, and he argued that such an assumption is more plausible in the manufacturing sector than in the primary sector. Consequently, he felt that an expanded model with fixed costs embedded in the manufacturing sector would be more useful in the Canadian policy context.

Michael Devereux appreciated the model's fixed-cost characteristic, because he saw it as capturing bankruptcy considerations or irreversibility aspects that current macro models may be missing. Gabriel Srour explained that differences in fixed costs could be explained by the inability of firms to change rapidly. Thus, fixed costs represent certain rigidities of process rather than "laziness." Under this assumption, the model showed that monetary policy will sometimes encourage less efficient firms to overproduce and more productive firms to underproduce. Srour agreed that this idea of efficiency could be important when looked at between two sectors.

Devereux emphasized Laidler's concern about investigating the appropriate sector and addressed Cédric Tille's work regarding shocks that hit one sector relative to another. Devereux commented that having many different types of shocks becomes problematic for monetary policy, given one policy tool, but he felt that this model could be used to analyze such questions. Srour acknowledged Tille's contribution to his own analysis of the effects of elasticity of substitution between sectors.

* Prepared by Jeremy Friesen and James Rossiter.

Laidler suggested that another important policy question is exchange rate sensitivity to commodity prices, given a possible secular decline of commodity export dependence. The thought was that intersectoral labour mobility would be a useful tool with which to approach this question. He further suggested that the model be expanded to look at the effects of international labour mobility in addition to sectoral labour mobility. He saw the need for the model to reflect *varying degrees* of mobility rather than full mobility or none at all. Srour stated that he too was interested in international labour mobility being incorporated into the model, but thought that perhaps it was less of a current policy concern for Canada.

Devereux questioned the use of a flexible-wage equilibrium as a valid benchmark, citing recent work by Obstfeld and Rogoff. Srour addressed this point by noting that the mathematical solution to the welfare-maximizing equilibrium could have been used as a benchmark and, in fact, the two did yield dissimilar results in the model, although they were equal in some specifications. It was Srour's view, however, that monetary policy should try to replicate market conditions and that any welfare-optimization issue was not clearly a monetary policy problem and could be dealt with in another policy form and with other policy tools.