Comments on “a model of an optimum currency area”

This study provides a formal model on the costs and benefits of currency areas. Both monetary and real aspects of participation in a currency union are analysed simultaneously. The main novel implication of the model is that the impact of openness on net benefits is ambiguous. In other words, more open economies are not always better candidates for a currency area. The paper is well written and I have only a few comments:

1. The author emphasizes the simultaneous analysis of both real and monetary aspects of currency areas. As such, the analysis is more comprehensive than earlier studies, most of them being based on partial analyses. The results show, however, that most of the earlier conclusions regarding the benefits of currency areas are still valid. Can we conclude from this analysis that regarding the benefits of a currency union interactions between monetary and real aspects play a modest role? If not, can we identify in some way establish their relative importance?

2. In the conclusions several extensions are mentioned, which according to the author are of potential interest. However, it is suggested at the same time that the current study captures the main features. Nevertheless, especially the addition of a third country effect seems relevant here. From the international trade literature it is well known that adding a third country to the analysis potentially could alter conclusions. Hence, can the author give any insight what to expect from such a generalization?

3. Quite often in the paper references are made to the empirical literature. It would be interesting to see (e.g. by simulation) whether the developed model could replicate some of these empirical findings.

4. Related to the previous comment are the surprising empirical findings of Rose (2000). While the detrimental effects of exchange rate volatility on bilateral trade patterns are relatively modest, adopting a single currency has a substantial positive impact on trade. Although there has been much discussion about these empirically found benefits of a currency union, apparently fixed exchange regimes or currency unions are different of nature. The current model is explicitly developed for the latter case, hence it would be interesting to see if the model is capable of reproducing to some extent such empirical findings. In other words, how much should transaction costs decrease to create such large trade benefits?