

Monetary and Fiscal Policy Issues in General Equilibrium

Leopold von Thadden

European Central Bank
and

Johannes Gutenberg Universität Mainz
(Fellow, Chair of Macroeconomics)

GSEFM, Field Course
Summer Term 2021

Motivation of the topic:

- In the aftermath of the financial crisis many countries have reached a stage where pressing policy challenges require a thorough understanding of interactions between monetary and fiscal policies

What can you expect from this field course?

- The lectures give a comprehensive **introduction on how to model monetary and fiscal policy issues from a general equilibrium perspective**, covering both positive and normative aspects
- The lectures will use (and where needed explain) concepts and techniques of advanced macroeconomics
- The term papers are expected to cover current research questions

The lecture material covers the following topics:

Part I: Modelling Money in General Equilibrium: a Primer
(*Focus:* How to model money in general equilibrium? Fragility of monetary equilibria, Welfare cost of inflation)

Part II: Money and Public Finance:
Selected Issues from a Positive and a Normative Perspective
(*Focus:* Sargent-Wallace-type budgetary arithmetic, Fiscal theory of the price level, Ramsey-optimal monetary and fiscal policies)

Part III: Unconventional monetary policies
(*Focus:* Effectiveness and limitations of unconventional monetary policies)

Part IV: Monetary unions
(*Focus:* Strategic interactions between monetary and fiscal policies in monetary unions)

Course book: *Carl Walsh, Monetary Theory and Policy, MIT Press, 4th edition, 2017*

- This book gives in chapters 2 and 3 (for part I), chapter 4 (for part II), and chapter 11 (for part III) in many respects a good overview...
- ...but the Lecture notes will discuss a number of the core papers in considerably more detail

Selected core papers:

Part I: Modelling Money in General Equilibrium: a Primer

- Obstfeld, M. and Rogoff, K., Speculative hyperinflations in maximizing models: can we rule them out?, *Journal of Political Economy*, 91/4, 1983.
- Lucas, R., Inflation and welfare, *Econometrica*, 68/2, 2000.
- Ireland, P., On the welfare cost of inflation and the recent behavior of money demand, *American Economic Review*, 99/3, 2009.

Part II: Money and Public Finance:

- Sargent, T. and Wallace, N., Some unpleasant monetarist arithmetic, *Federal Reserve Bank of Minneapolis Quarterly Review*, Fall, 1981.
- Chari, V., Christiano, L., and Kehoe, P., Optimality of the Friedman rule in economies with distorting taxes, *Journal of Monetary Economics*, 37, 1996.

Selected core papers:

Part III: Unconventional monetary policies

- Eggertsson, G. and Woodford, M., The zero bound on interest rates and optimal monetary policy, *Brookings Papers on Economic Activity*, 1, 139 - 211, 2003.
- Curdia, V. and Woodford, M., The Central-Bank Balance Sheet as an Instrument of Monetary Policy, *Journal of Monetary Economics*, 58, 1, 47-74, 2011.

Part IV: Monetary unions

- Chari, V. and Kehoe, P., Time inconsistency and free-riding in a monetary union, *Journal of Money, Credit, and Banking*, 40/7, 1329-1355, 2008.
- Kempf, H. and von Thadden, L., When do cooperation and commitment matter in a monetary union?, *Journal of International Economics*, 91, 252-262, 2013.
- Bletzinger, T. and von Thadden, L., Designing QE in a fiscally sound monetary union, *European Economic Review*, 2021.

Format of the course:

Lectures take place during the first half of the term. There will be seven meetings on **April 13, April 20, April 27, May 4, May 11, May 18, May 25** in room HoF 2.45 / Boston.

There will be a meeting for the presentation of the (initial findings of the) term papers during a special meeting on **July 13** in room HoF 2.45 / Boston.

All meetings take place on **Tuesdays, 4.45 pm - 8 pm** (detailed timing to be communicated during the first meeting).

To be updated in view of Covid-related developments.

Course requirements:

- The final grade will be based on a combination of the **participation in discussions in class (15%)**, a **problem set (15%)**, the **presentation of the term paper (20%)**, and the **quality of the written version of the term paper (50%)**
- The **term paper** can be organized around any quality publication or recent working paper with a clear link to the substance of the course. Preferably, students are invited to select from recent papers with a focus on i) the role of unconventional monetary and fiscal policies or ii) monetary and fiscal policy interactions in monetary unions. An updated list with suggestions for such papers will be posted at the beginning of the course.

Idea: summarize the value added of a paper covering your preferred subject, link it to ongoing research and develop possible directions for (your own?) future research