Monetary Policy in the Dynamic Model

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Example of divine Beveridge-Wicksell model.

dynamic model of slack.

- ☑ divine : inflation is exogenous so Fed only needs to reach full employment to maximize welfare.

- ☑ Beveridge. dynamic model has a Beveridge curve ($\sim$ AS)

$$u(\theta) = \frac{\lambda}{\lambda + f(\theta)}$$

- ☑ Wicksell. AD curve is determined / governed by nominal interest rate.

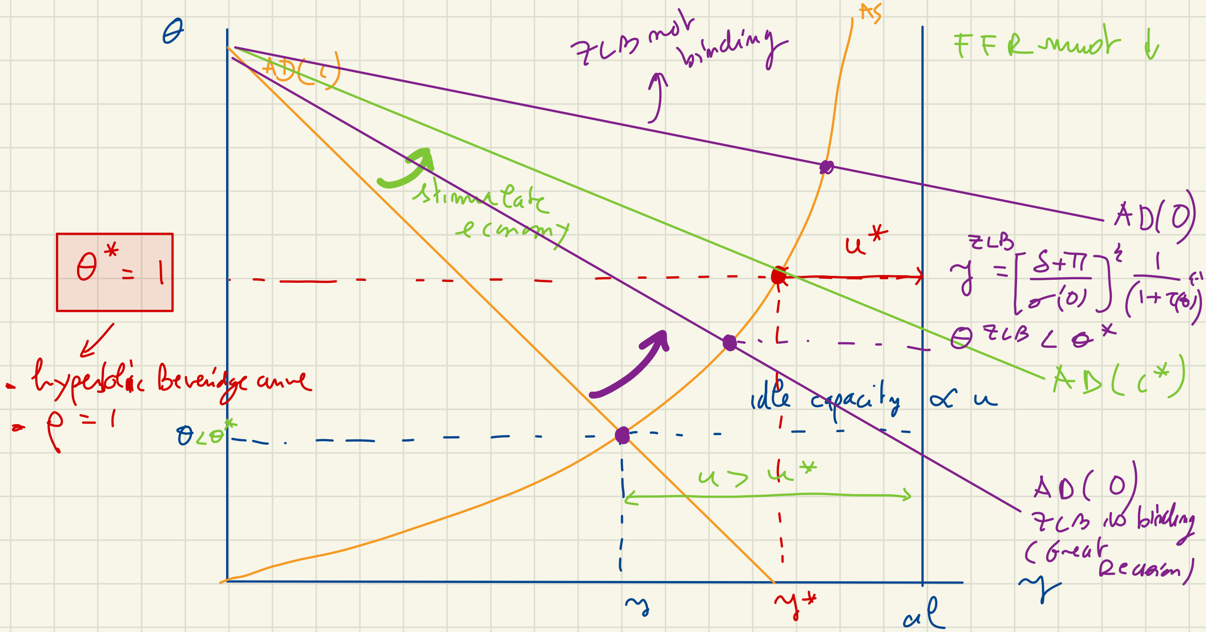
discount rate ε ← shape of utility

$$y^d = \left[\frac{\delta - i + \pi}{\sigma'(0)}\right]^{\varepsilon} \frac{1}{[1+\tau(\theta)]^{\varepsilon-1}}$$

MU wealth

↳ dynamic model is DBW model

↳ formula in sufficient statistics applies to model.


θ
ZLB not binding
FFR must ↓
AS
AD(c)
AD(0)
stimulate economy
u*
y^ZLB = [(δ+π)/σ(0)]^(1/ε) 1/(1+τ(θ))
θ^ZLB < θ*
AD(c*)
idle capacity ∝ u
θ<θ*
u > u*
AD(0)
ZLB is binding
(Great Recession)
y
y*
αl
y
θ* = 1
- hyperbolic Beveridge curve
- ρ = 1