Rewrite analysis

FOREIGN UNCONSTRAINED

RAMSEY

PROPOSITION

Union gap are close

INTREPRATION

Fully optimal to close union gaps.

Even when higher degree of openness.

Even when h>0.5? Yes because you just amplify Foreign fluctuation.

Also when h>0.5 and pursue an equally-weighted objective -> optimal to depart from 0 gaps 🡪 Explain why.

But the most important thing : When asymmetry in price rigidity 🡪 depart from Union gaps 🡪 Explain why (see long paragraph). Use the model in gap form to explain why.

OSR

Regarding Welfare

Not too costly to use a OSR setup instead of Ramsey setup. Detail ambiguous role of parameters changes.

Regarding Union gaps.

Perform as Ramsey => No difficulty to close Union gaps. Important result. As Ramsey, depart from 0 gap when observe rigidity.

Regarding Coefficient.

PROPOSITION Symmetric coef

Same as symmetric. Not intuitive since the shcok is affecting foreign => suggest rule should be updated following shocks.

Different coefficient when asymmetry => support idea of country specific rule when asymmetry. Explain the logic : Home is less subject to inflation => policy can be conduct differently.

Sensitivity. Very sensisitve when Monetary policy follows a Taylor rule. But when inertia => Target of optimal coefficient is in a small range.

FOREIGN CONSTRAINT

Q of political incentive

Investigate welfare improval at nunion level.

CEV HOME

Is it perceive at very costly to follow union-oriented objective? Not necessarily.

COEF HOME

Are the coef significantly different when Home pursue Union objective.

No clear result in political incentive when foreign is constrained

CONCLUSION

What we have done and found?

We have developed a two-country currency union model and investigated the dynamics and welfare properties of simple fiscal rules. We show how our model extend the small open economy. Our result suggests that there is room for country-specific and time-specific fiscal rule.

Limitation?

We consider one type of shock. We do not overcome the problem of the simplicity of rule : rule based on gaps are not realistic.

Incomplete model : distortionary tax, debt, non ricardian