

Macro Roundup Article

Headline: [The Effect of Monetary Policy Assumptions on Fiscal and Macroeconomic Analysis](#)

Article Link: <https://budgetlab.yale.edu/news/240716/effect-monetary-policy-assumptions-fiscal-and-macroeconomic-analysis>

Author(s)	Ernie Tedeschi and John Ricco
Publication	The Budget Lab
Publication Date	July 17, 2024

Tweet: [. @ernietedeschi and @riccoja argue that a Fed “captured” by political pressure would lead to median inflation 0.6% higher after six years.](#)

Summary: A “captured” Fed would be one less responsive to inflationary impulses, which allows inflationary pressure to build unchecked. To test the implications of capture, we ran a monetary policy rule that allows for a spectrum of political “capture” through a series of stochastic simulations in FRB/US, the Fed’s macroeconomic model. In these simulations, FRB/US picks random historical economic shocks to key variables occurring between 1970 and 2023 and applies them to its forward forecast. We ran 1,000 such simulations each assuming $C = 0$ (no political capture) and alternatively $C = 0.85$ (high political capture). $C = 1$ implies extreme perfect capture, in which the Fed only responds asymmetrically to low inflation and high unemployment. Figure 2 illustrates the results. The x-axis shows cumulative 6-year inflation, while the y-axis denotes the probability of each outcome in our simulations. A captured Fed skews economic outcomes towards more inflation over time. In our simulations, low inflation was just as likely under our two capture assumptions. But the median inflationary outcome was +0.6pp higher after six years under high capture. And the outlier 95th percentile outcome was almost 2pp higher under high capture.

Related Articles: Fiscal Dominance and the Return of Zero-Interest Bank Reserve Requirements and Changing Central Bank Pressures and Inflation and Living with High Public Debt

Primary Topic: Monetary Policy

Topics: GDP, Inflation, Monetary Policy, Op-Ed/Blog Post, Politics, Weekly

Permalink: <https://www.edwardconard.com/macro-roundup/ernietedeschi-and-riccoja-argue-that-a-fed-captured-by-political-pressure-would-lead-to-median-inflation-0-6-higher-after-six-years?view=detail>

Featured Image Link: <https://www.edwardconard.com/wp-content/uploads/2024/07/22417-the-effect-of-monetary-policy-assumptions-on-fiscal-and-macroeconomic-analysis-featured-thumbnail-image.png>