UNIVERSITÄT PASSAU

Wirtschaftswissenschaftliche Fakultät

Summer term 2020

Chapter #5
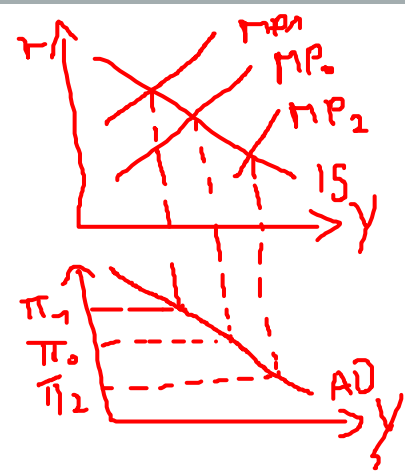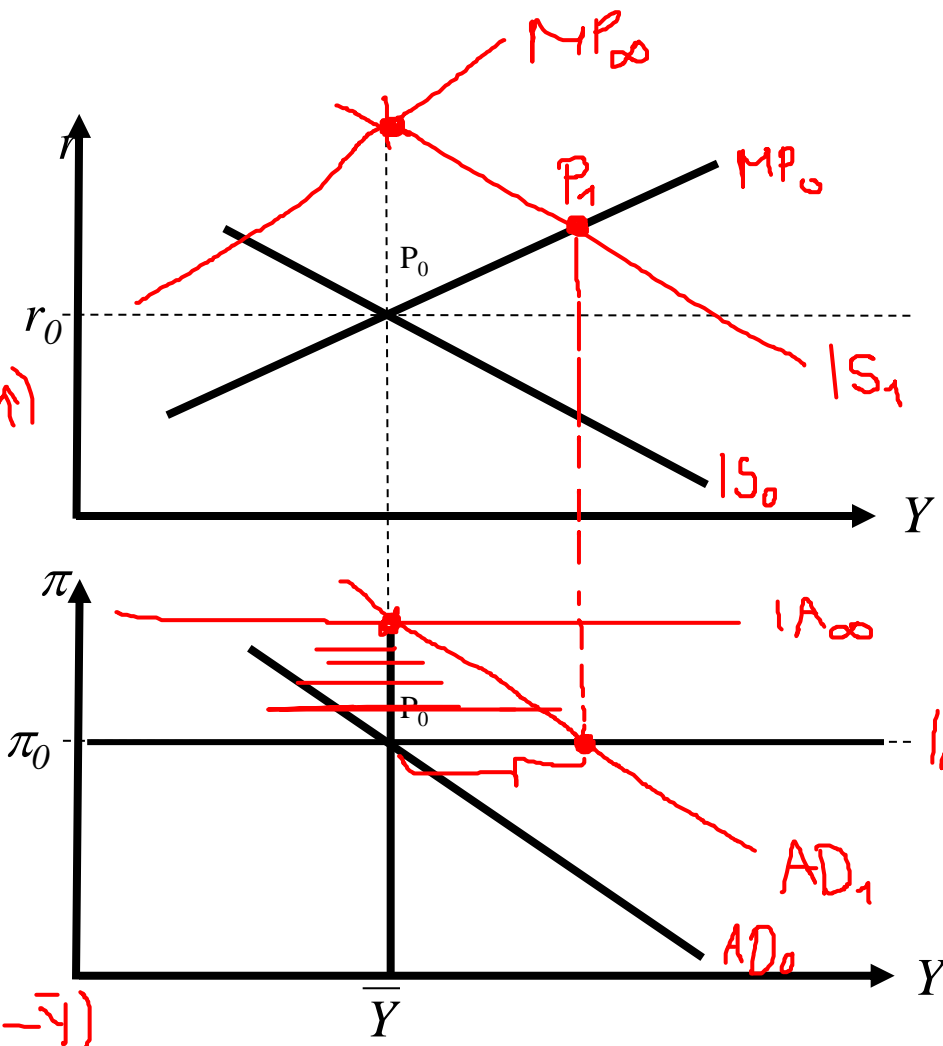
David Parkins

Closed economy

Period 1
$IS\uparrow \Rightarrow Y\uparrow$
$CB: Y\uparrow \Rightarrow r\uparrow \Rightarrow I\downarrow$

Period 2 – ∞
$Y_{-1} > \bar{Y} \Rightarrow \pi\uparrow (IA\uparrow)$
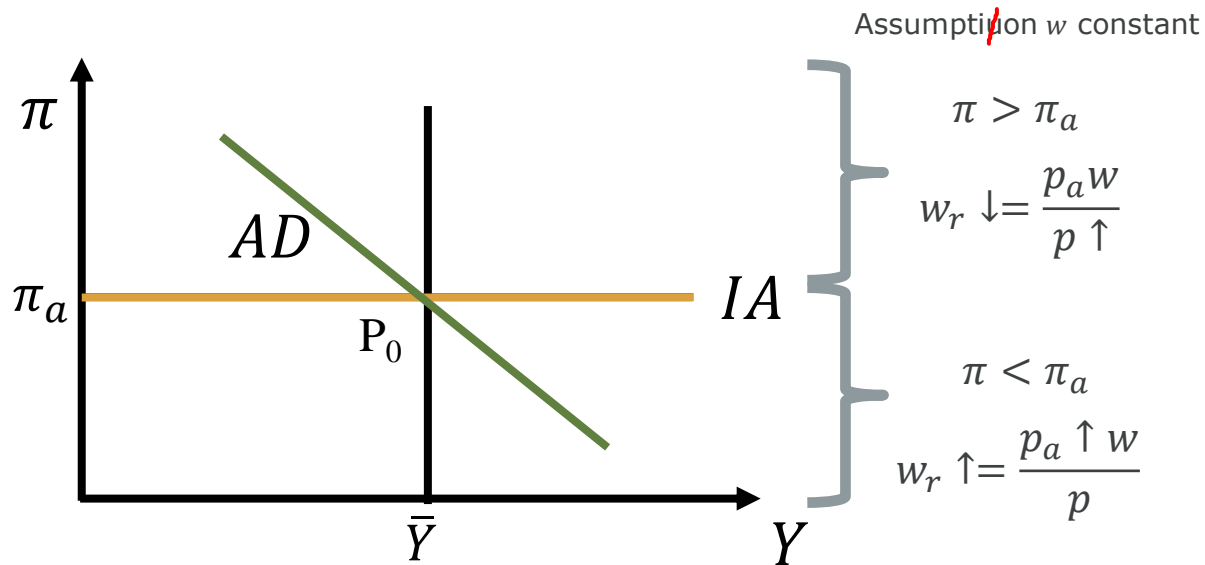$CB: \pi\uparrow \Rightarrow r\uparrow \Rightarrow I\downarrow$
until $Y = \bar{Y}$

AD: $\pi\uparrow \longrightarrow Y\downarrow$
I $CB: r\uparrow \Rightarrow I\downarrow$

$IA:$ $Y \longrightarrow \pi$
$Y_{-1} > \bar{Y} \Rightarrow \pi\uparrow$
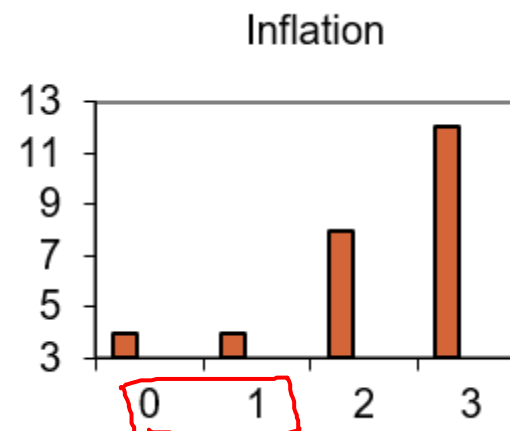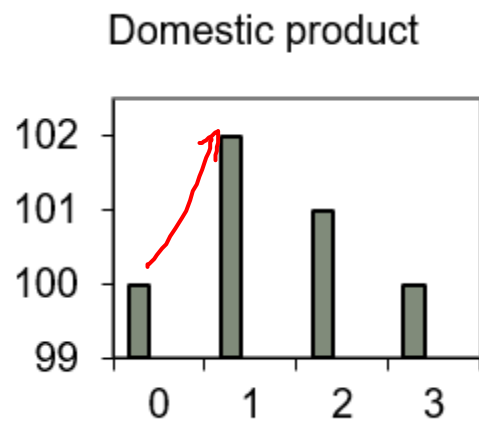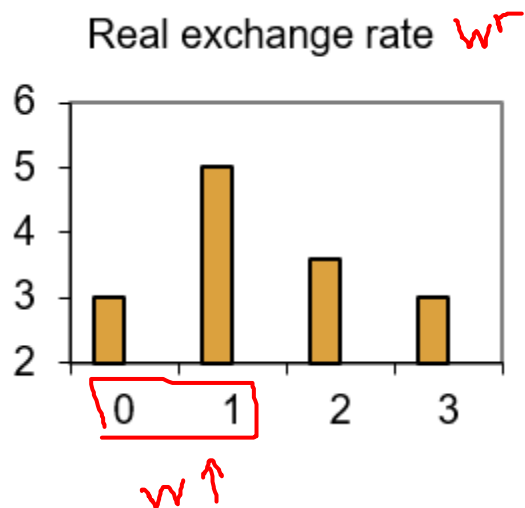$\pi_t = \pi_{t-1} + \delta(Y_{-1} - \bar{Y})$

MP_∞

P_1

MP_0

r_0

IS_1

IS_0

P_0

Y

π

IA_∞

P_0

π_0

$IA_0 = IA_1$

AD_1

AD_0

$\bar{Y}$

Y

Inflation and real exchange rates

$r \neq r_a \Rightarrow w \uparrow \searrow w^r \uparrow\downarrow$

$\pi_1 \neq \pi_a \nearrow$

Assumption w constant

$\pi > \pi_a$

$w_r \downarrow = \dfrac{p_a w}{p \uparrow}$

$\pi < \pi_a$

$w_r \uparrow = \dfrac{p_a \uparrow w}{p}$

Problem 5.1

MP + flex => boosting
FP + flex => Crowding out

Real exchange rate w^r

Domestic product
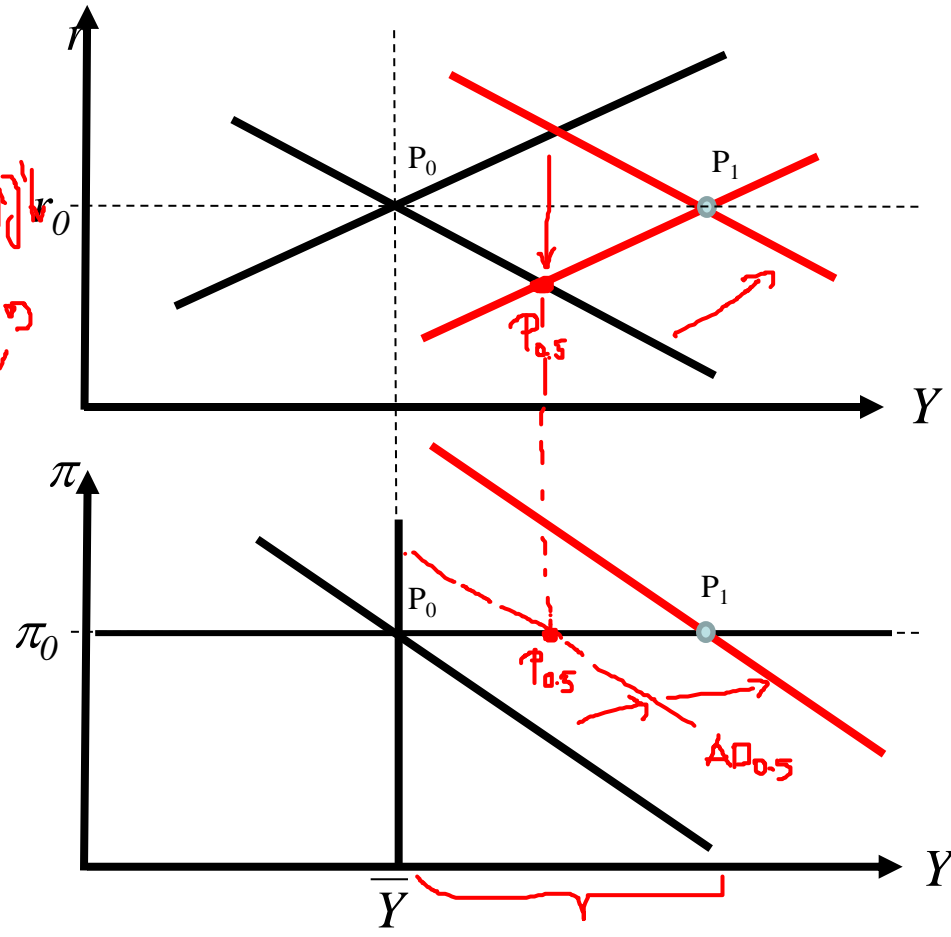
Inflation

w↑

■ 5.1a+b) Period 0

5.1a+b) Period 1

CB: $r \downarrow$ (MP$\downarrow$) AD$\uparrow$
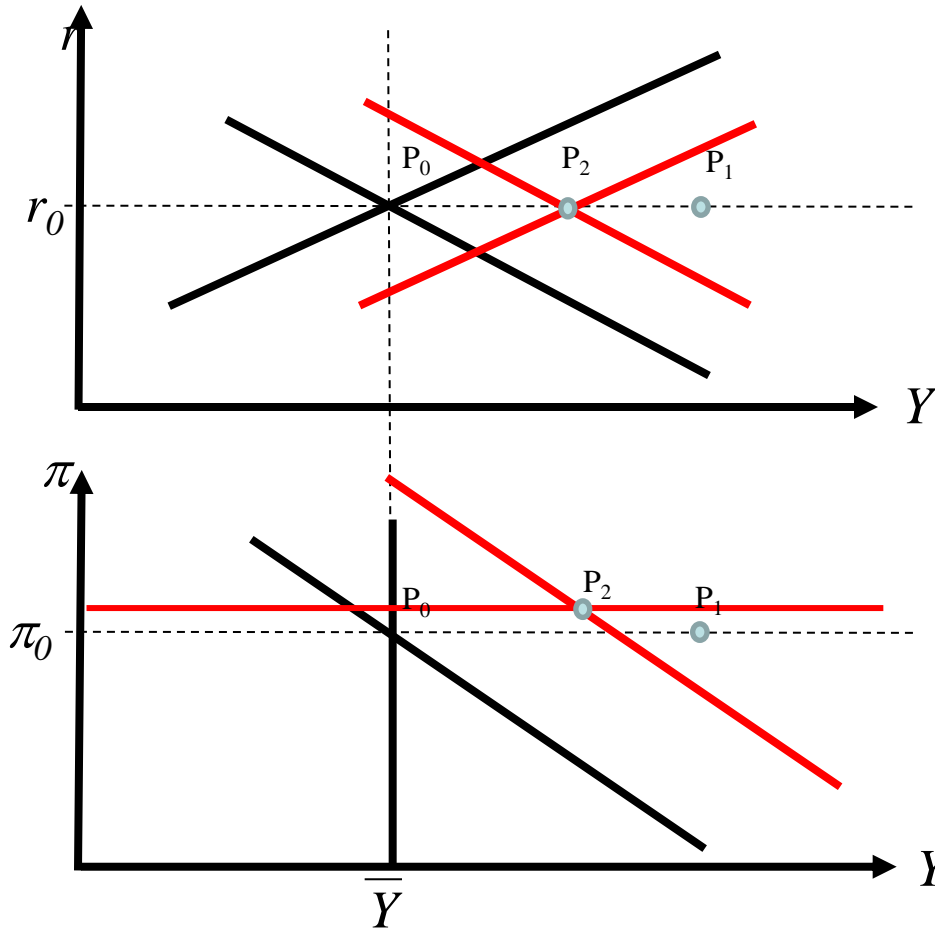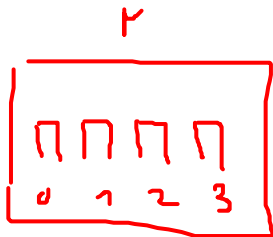$\Rightarrow I \uparrow \Rightarrow Y \uparrow$

FX: $r < r_a \Rightarrow$ dem $\$\uparrow$
$\Rightarrow w\uparrow \Rightarrow w^r\uparrow \Rightarrow X\uparrow$
$\Rightarrow Y\uparrow$ (IS$\uparrow$ AD$\uparrow$)

CB: $Y\uparrow \Rightarrow r\uparrow \Rightarrow I\downarrow$

P_1

P_0 P_1

r_0

$P'_{0.5}$

Y

π

P_0 P_1

π_0

$\pi_{0.5}$

$AD_{0.5}$

$\overline{Y}$ Y

■ 5.1a+b) Period 2

Handwritten annotations (right side):

$Y_{-1} > \bar{Y} \Rightarrow |A\uparrow \ \pi\uparrow$

$CB: \pi\uparrow \Rightarrow \dfrac{r\uparrow \Rightarrow I\downarrow}{(MP\uparrow)}$

$\pi > \pi_a \Rightarrow W^r\downarrow$

$\uparrow p_a\dfrac{\bar{W}}{p\uparrow\uparrow}$ $(IS\downarrow)$ $AD\downarrow$

$\Rightarrow X'\uparrow\uparrow\uparrow \Rightarrow Y\downarrow$

$CB: Y\downarrow \Rightarrow r\downarrow \Rightarrow I\uparrow$

Continues until $Y = \bar{Y}$

5.1a+b) Period 3

crawling peg