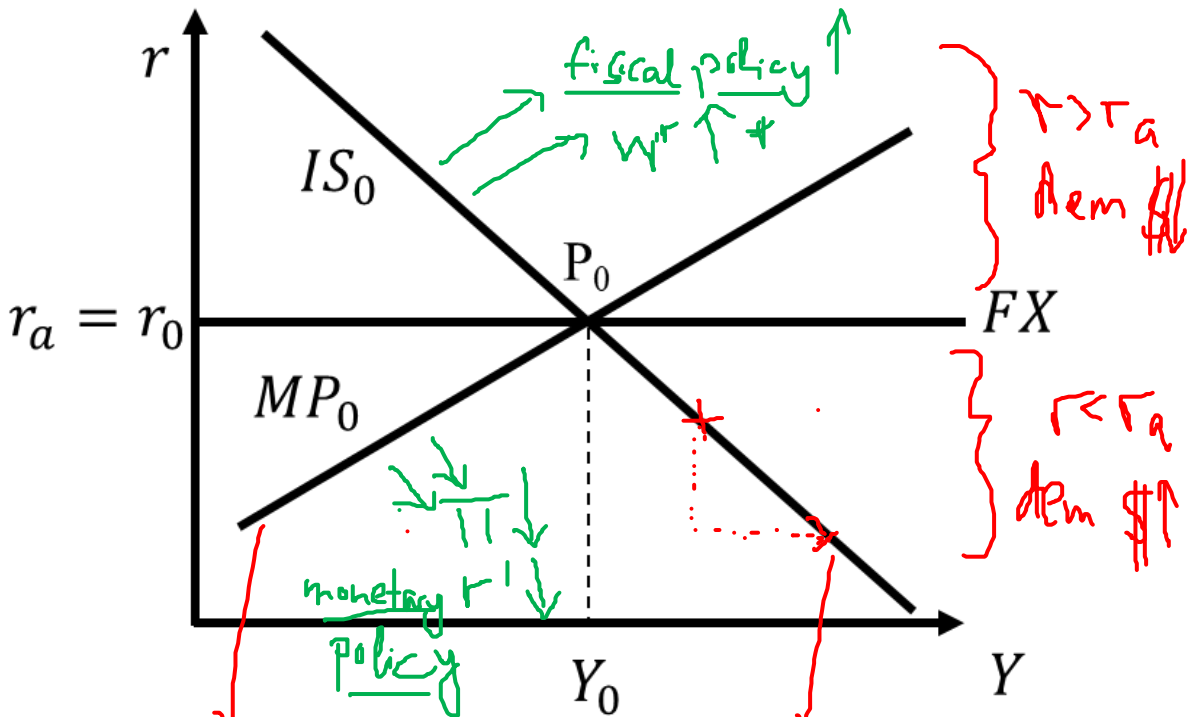


Summer term 2020

## Chapter #4



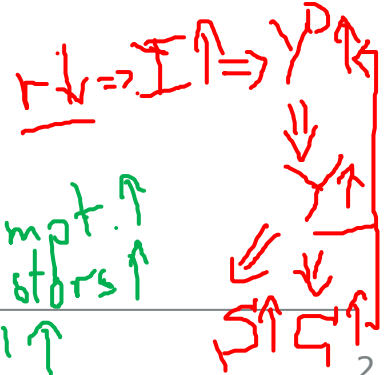


reaction

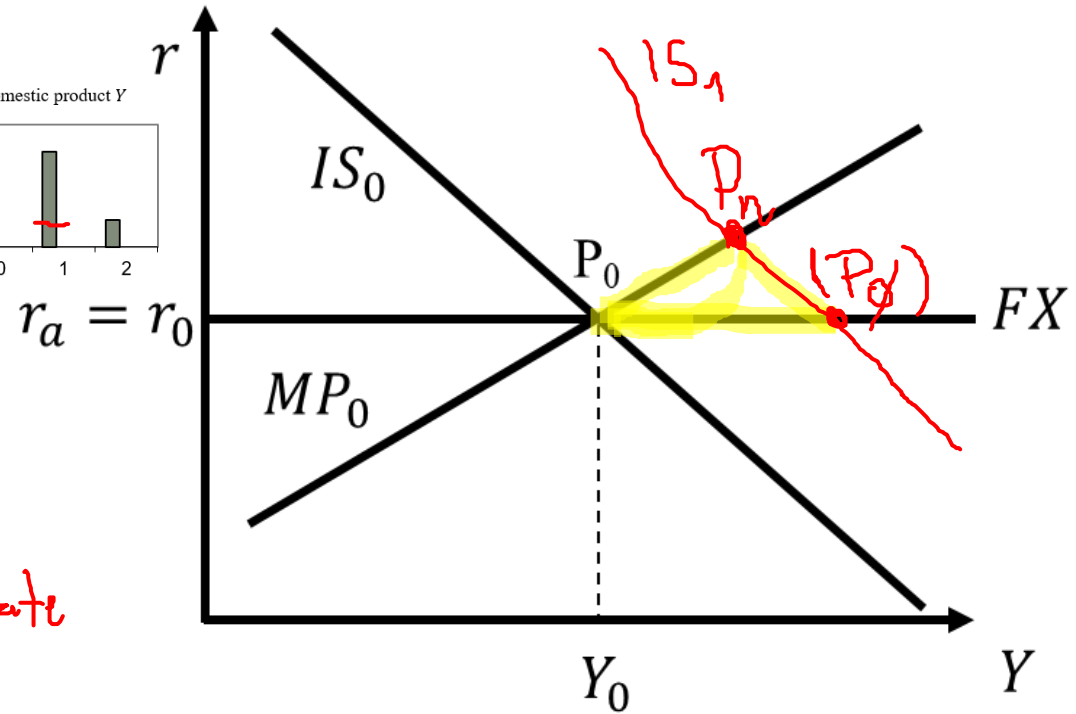
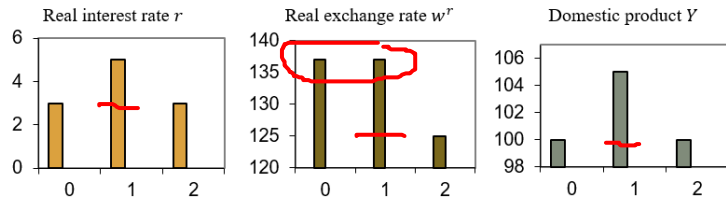
$$r = r' + \lambda_p (Y - \bar{Y}) + \lambda_i (\pi - \pi^*)$$

(CB)

\* auton. consumpt. ↑  
 expect. investors ↑  
 shocks to  $X_1$  ↑



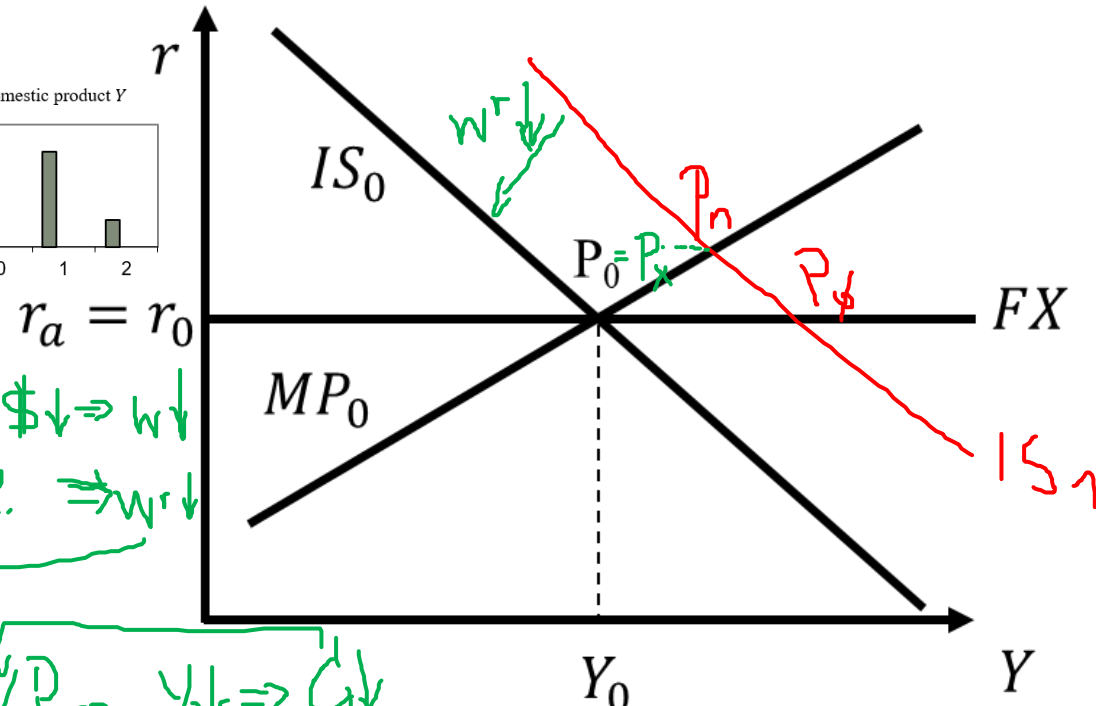
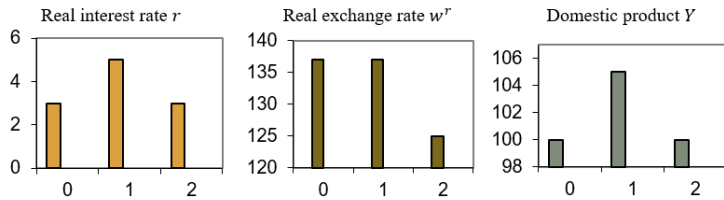
# Problem 4.1



$t=1$  fiscal policy  
expansive  
 +  
 fixed exchange rate  
 +  
 with neutralisation

$t=1$  (1) fiscal policy  $\rightarrow Y \uparrow \rightarrow F \rightarrow C \rightarrow S \rightarrow \uparrow$   
 (2) CB:  $Y \uparrow \rightarrow r \uparrow \rightarrow I \downarrow \Rightarrow Y \downarrow \Rightarrow Y \downarrow - X \downarrow$   
 (3)  $t > r_a \Rightarrow \text{dem } \text{€} \uparrow \text{ \$} \downarrow \Rightarrow \text{sell } \text{€} + \text{buy } \text{\$} \Rightarrow R \uparrow \Rightarrow \text{liquidity taking} \uparrow$   
 (4) demand  $F \downarrow \Rightarrow \text{neutr } F \downarrow$

# Problem 4.1



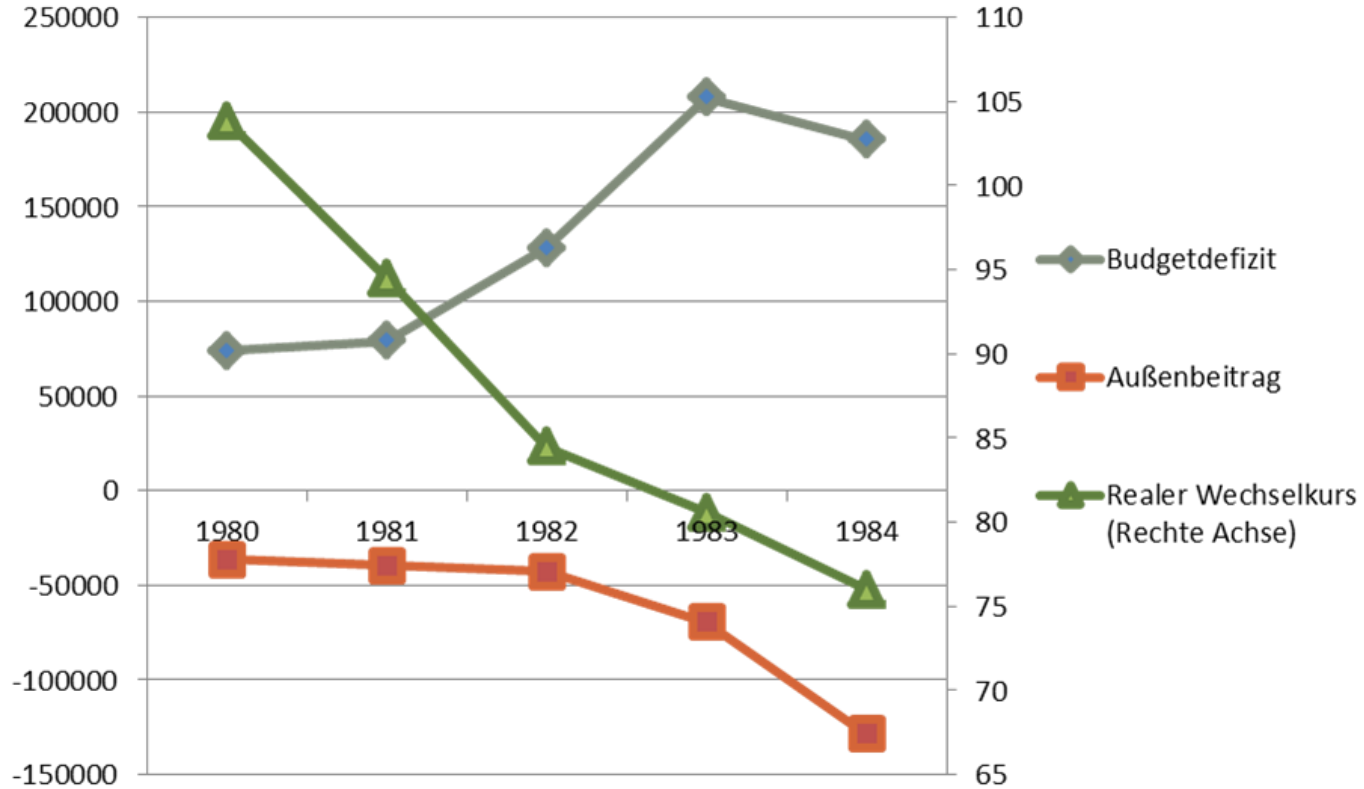
$C, \uparrow \rightarrow r_a \rightarrow \text{dem } \$ \downarrow \Rightarrow w^r \downarrow$   
 no infl.  $\Rightarrow w^r \downarrow$

$\rightarrow X \downarrow, Z \uparrow \Rightarrow Y \downarrow \Rightarrow C \downarrow, S \downarrow$   
 $KI \uparrow$   
 CB:  $Y \downarrow \Rightarrow r \downarrow \Rightarrow I \uparrow$

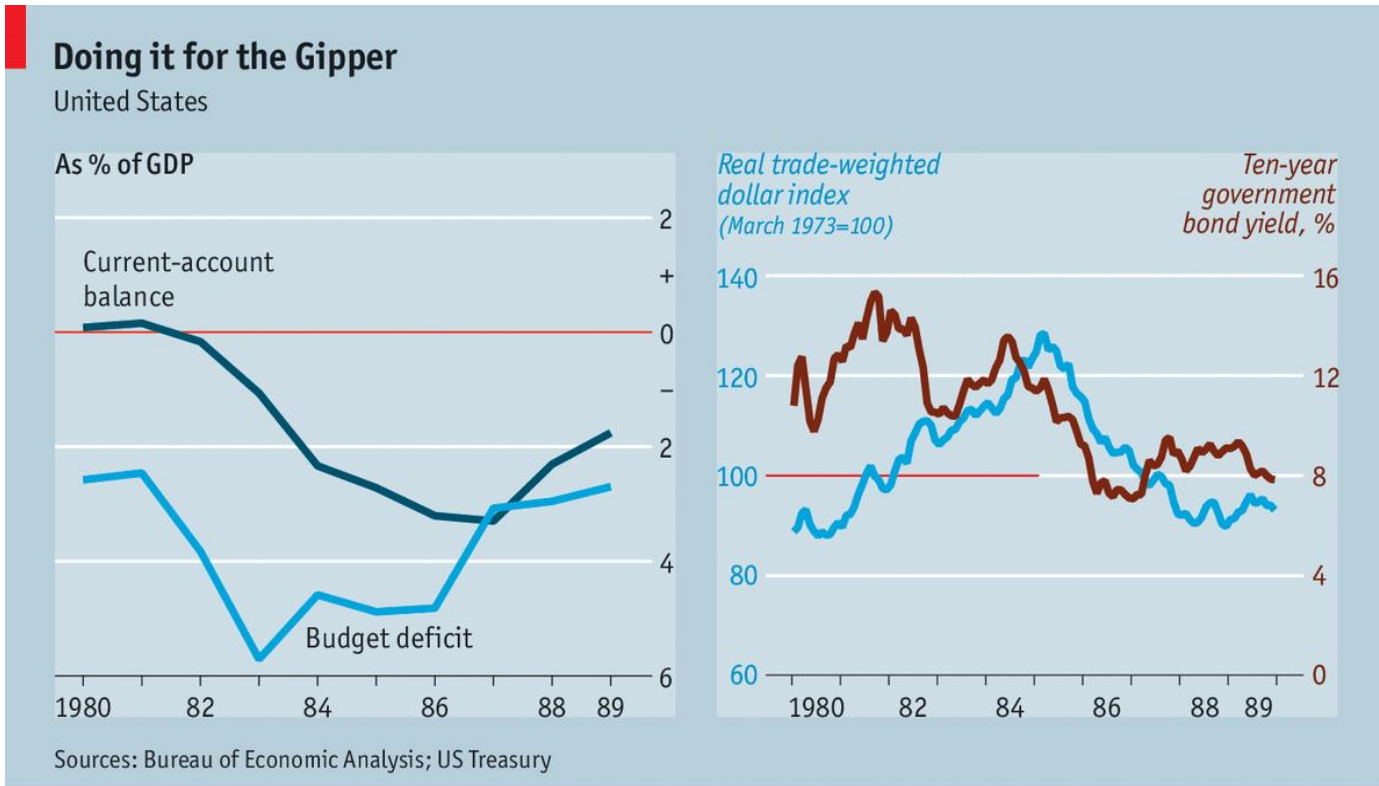
$\rightarrow$  current accounts (deficit)  $X \downarrow, Z \uparrow$

$\rightarrow$  budget deficit due to expansive fiscal policy  
 (tax revenues unchanged because  $Y$  unchanged)

# ■ Twin Deficit



# ■ That Eighties Show



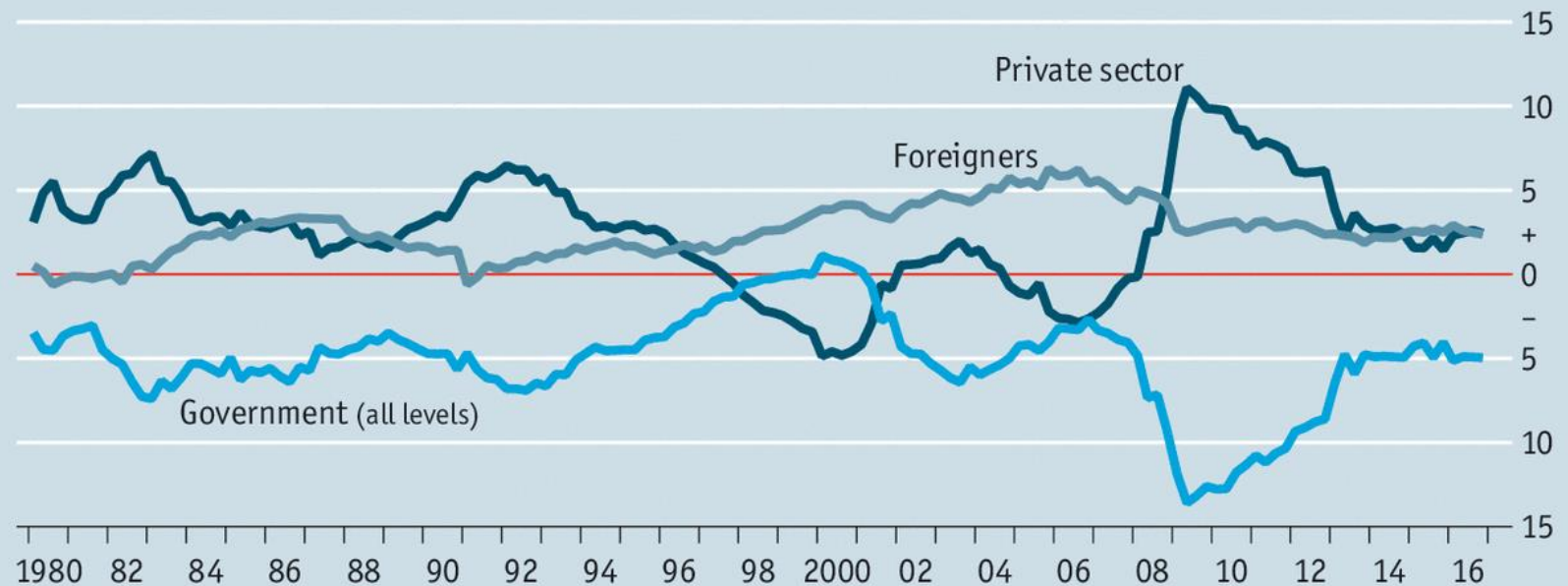
Economist.com

# ■ The contradiction at the heart of Trumponomics

*You can't have tax cuts, an investment boom and a smaller trade deficit*

## Zero-sum game

United States, net lending by sector, % of GDP



Source: Bureau of Economic Analysis

Economist.com

## ■ Different possibilities

