What determines the price level?

September 12, 2015
Why is this important?

- The real world: Japan, US, Europe.
- Theoretical models with indeterminate price level, “equilibrium selection” hand-waving.
How fiscal backing eliminates indeterminacy

- Paper money without fiscal backing is rare and short-lived.
How fiscal backing eliminates indeterminacy

- Paper money without fiscal backing is rare and short-lived.

- An expected stream of primary surpluses creates a hole in private sector intertemporal budget constraints that creates a demand for assets in excess of what the private sector provides.
How fiscal backing eliminates indeterminacy

- Paper money without fiscal backing is rare and short-lived.

- An expected stream of primary surpluses creates a hole in private sector intertemporal budget constraints that creates a demand for assets in excess of what the private sector provides.

- This is not “taxes payable with money”.
How fiscal backing eliminates indeterminacy

• Paper money without fiscal backing is rare and short-lived.

• An expected stream of primary surpluses creates a hole in private sector intertemporal budget constraints that creates a demand for assets in excess of what the private sector provides.

• This is not “taxes payable with money”.

• Sims (2013)
“Active”, “passive”, and “Ricardian” policies

- Leeper quadrants. (plot, equations) (Leeper (1991))
“Active”, “passive”, and “Ricardian” policies

• Leeper quadrants. (plot, equations) \textit{Leeper} (1991)

• \textit{Cochrane} (2011)

• \textit{Sims} (1994)

• \textit{Benhabib, Schmitt-Grohé, and Uribe} (2001)
Reinterpreting inflation history

• Sargent (1982)
Reinterpreting inflation history

- Sargent (1982)
- Bianchi and Ilut (2013), Bianchi (2010)
- Sims (2011)
A standalone central bank?

- Perhaps the idea behind the ECB.
A standalone central bank?

- Perhaps the idea behind the ECB.
- Sims and Del Negro (2013)
Optimal fiscal policy

- Sims (2001)
- Sims (2013)
- Leeper and Zhou (2013)
References


Schmitt-Grohé, S., and M. Uribe (2004): “Optimal fiscal and


