Monetary-Fiscal Crosswinds in the European Monetary Union

Lucrezia Reichlin (London Business School, CEPR)
Giovanni Ricco (University of Warwick, OFCE SciencesPo, CEPR)
Matthieu Tarbé (London Business School)

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Summary

Contribution

- study the monetary-fiscal interaction in the EA through the lens of the aggregate government BC
- new quarterly fiscal dataset
- suggest an empirical framework to study the adjustment of fiscal variables, returns, and inflation to unexpected monetary policy changes

Results

conventional: fiscal policy leans towards the easing
unconventional: muted fiscal response
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- conventional: fiscal policy leans towards the easing
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Would the results remain when extending the analysis to the EA12 or EA19?

Bartsch et al. (2021) find that most often MP and FP pull in different directions for a sample of advanced economies.

**Figure 1:** Share of countries and years with a divergent policy mix (%)
Would the results remain when extending the analysis to the EA12 or EA19?

- heterogeneous macroeconomic situations and debt constraints
- monetary policy does not fit all
- threat of disintegration

**Figure 3:** Taylor rule and target rates; EA unemployment and inflation

Note: Core is Austria, Belgium, France, Finland, Germany, Italy, and the Netherlands. Periphery is Greece, Ireland, Portugal, and Spain. Source: Nechio (2011).
Is MP and FP "coordination" more frequent...

- during tail events?
  - e.g. COVID-19, Great Recession

- in periods of higher public debt?

And should there be more "coordination"?
- implicit versus explicit
- threat to MP independence
- extension of the mandate (e.g. Green MP)
Other questions

What is the role of **heterogeneous output growth**?

Assumption: all countries have the same growth rate at the steady state.

What is the role of **fiscal transfers**?

Assumption: monetary union with transfers.
Other comments

- How to reconcile the short- and long-term evidence?

  Example of unconventional MP easing for Germany:
  - muted fiscal response in the ST
  - (large?) fiscal tightening in the LT

- How to put this evidence of crosswinds for Germany after UMP easing together with common belief that MP in the EA tends to be more favourable to Germany?