Discussion of

“**Monetary and Fiscal Policy with High Inflation**”

By Tommaso Monacelli

Ippei Fujiwara

Keio University / ANU / ABFER / CEPR

RIETI-CEPR Symposium

Monetary and fiscal policies against inflation

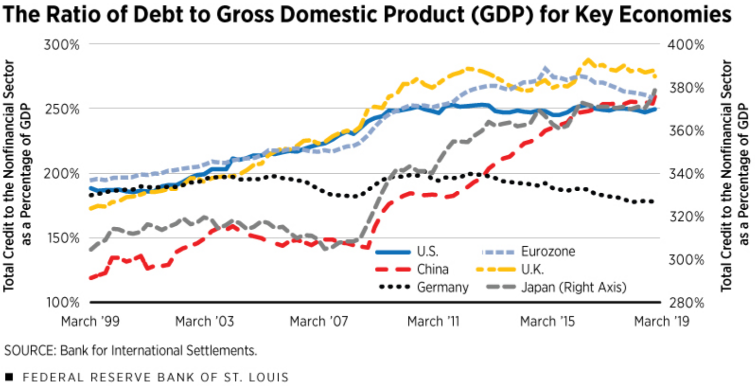
- Traditional view: Leeper (JME1991)
  - Monetary policy must be *active* $\Rightarrow$ *Taylor principle* ($\Uparrow \pi \Rightarrow \Uparrow r \Rightarrow \Downarrow c$)
  - Fiscal policy must be *passive* $\Rightarrow$ *Ricardian*

- Explicit consideration of redistribution motive
  - *Substitute* in the short-run
    - Monetary policy must be *active* $\Rightarrow$ *Taylor principle* ($\Uparrow \pi \Rightarrow \Uparrow r \Rightarrow \Downarrow c$)
    - Fiscal policy $\Rightarrow$ redistribution after supply shock $\approx$ insurance ($\Uparrow \pi \Rightarrow \Uparrow f$ or $g \Rightarrow \Uparrow c$)
  - *Complement* in the long-run
    - Fiscal policy must be *passive* $\Rightarrow$ *Ricardian* ($\Uparrow \pi \Rightarrow \Uparrow \tau \Rightarrow \Downarrow c$)

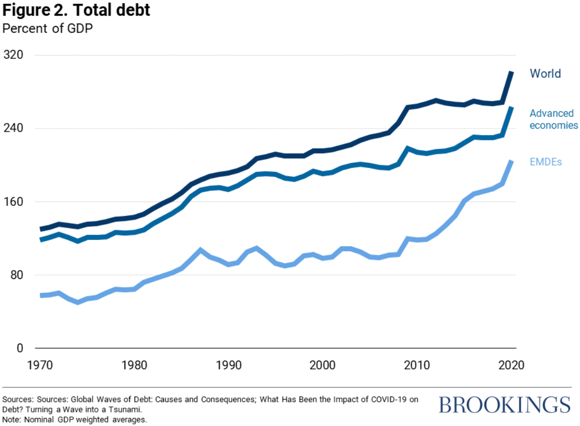
Summary

- A very nice paper with
  - relevance to the current policy debate: policy-mix against supply side inflation
  - clear explanation of optimal policy-mix through T(H)ANK model
    - Two agents: Saving agents vs Hand-to-mouth agents
    - Micro-founded quadratic loss function showing the tradeoff in stabilization among price, output, and inequality
- Very important messages
  - "Fiscal policy should be expansionary in periods of high supply-side inflation"
  - BUT "Long-run expectations of debt stabilization is key"
    - "Persistent high inflation is always and everywhere a fiscal phenomenon"

Comment 1: Time inconsistency

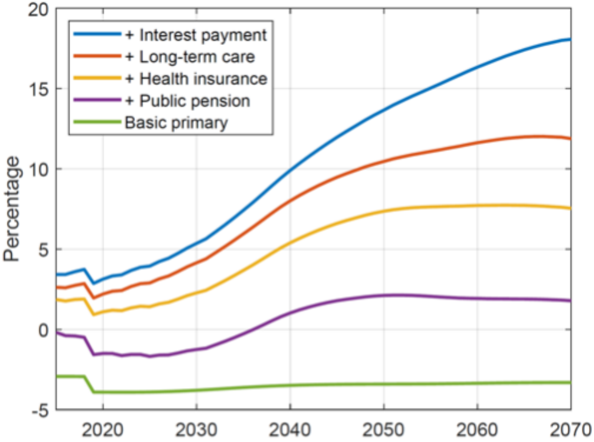


Comment 1: Time inconsistency



- Unprecedented events happen almost every decade: GFC, COVID19, Ukraine,...
- Can we have the short-run expansionary fiscal policy but with the long-run fiscal contraction?

Japan: Aging and fiscal sustainability



source: RIETI

- Structural factors, such as (super) aging, makes fiscal consolidation even more challenging

Comment 2: Elasticity of H's income to agg. income

Assume $\underbrace{\chi > 1}_{\substack{\text{H income reacts} \\ \text{more than proportionally} \\ \text{to aggr. income}}}$

- This leads to *ex post* heterogeneity in consumption $\Rightarrow$ relatively smaller H's consumption
- Ait-Sahalia, Parker and Yogo (JoF2004)
  - "The risk aversion implied by the consumption of luxury goods is more than an order of magnitude less than that implied by national accounts data"
  - "For the very rich, the equity premium is much less of a puzzle"
- Parker and Vissing-Jorgensen (AER2009)
  - "The consumption of high-consumption households is more exposed to fluctuations in aggregate consumption and income than that of low-consumption households in the Consumer Expenditure (CEX) Survey"
  - "The exposure to aggregate consumption growth of households in the top 10 percent of the consumption distribution in the CEX is about five times that of households in the bottom 80 percent"