Macroeconomic Themes
Simultaneous Equilibrium

• We worry about different markets *simultaneously*:
  1. Goods and services (the real economy)
  2. Money and bonds (financial markets)
  3. External/international markets (balance of payments)
  4. Labor (supply side – prices are fully flexible in long run)
Simultaneously Determined Variables

• Key question is “What is Exogenous?”
  – “What was the Initial Shock?”
Choosing Assumptions Appropriately

• Choose assumptions and thus model to

Address the Question of Interest

– Examples:

• Exchange Rate Regime (fixed? flexible?)
• Country size (large or small?)
• Prices (fully flexible or not?)
• Central Bank (independent or not?)
Use Identities Freely

• Examples:
  – National Income Accounting Identity
    • $Y = C + I + G + NX$
  – Balance of Payments
    • $c/acc + k/acc + ORS = 0$
Government Budget Constraint

• Method of financing expenditures frequently has dramatic effect
  1. Raising Taxes (a “balanced budget” shift reduces the net impact)
  2. Seigniorage (printing money is eventually inflationary, only possible with dependent central bank)
  3. Issuing Government debt (treasuries have to be paid back eventually, may have crowding out)
Monetary Independence of Central Bank

• New development since 1990, now widespread in OECD

• Growing number of emerging markets too
The Role of the International Environment

• Exchange Rate Regime

• Internal vs. External Constraints and Objectives
Short-Run Costs of Adopting Long-Run Policies for Stability

Geographic Themes

Andrew Rose, Global Macroeconomics Themes
Role of Constraints on Policy

- Government Budget Constraint
- Central Bank Independence
- Exchange Rate Regime and External Environment
- Dynamic Inconsistency: Long and Short-Run