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Fiscal and Monetary Policies in Complex Evolving Economies

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Abstract

What is the most appropriate combination of fiscal and monetary policies in economies subject to banking crises and deep recessions? We study this issue using an agent-based model that is able to reproduce a wide array of macro and micro empirical regularities. Simulation results suggest that policy mixes associating unconstrained, counter-cyclical fiscal policy and monetary policy targeting employment is required to stabilize the economy. We also show that “discipline-guided” fiscal rules can be self-defeating, as they depress the economy without improving public finances. Finally, we find that the effects of monetary and fiscal policies become sharper as the level of income inequality increases.

Keywords: agent-based model, fiscal policy, monetary policy, banking crises, income inequality, austerity policies

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