

Macroeconomic Policy for Stagflation

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Abstract

If oil price increases generate a stagflation, which means economic a coincidence of recession and inflation, individual traditional macroeconomic policy is difficult to cope with the stagflation. In this paper, we show that policy mix can completely counter the stagflation. Our finding shows that such a policy mix must be a simultaneous implementation of monetary tightening and fiscal expansion. To show the existence of our policy mix, we construct a dynamic stochastic general equilibrium model and analytically investigate effects of oil price shocks.

Keywords: oil price shock; stagflation; fiscal policy; DSGE modeling