# Money-financed Fiscal Stimulus with Future Tax Adjustment

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Abstract

Money-financed fiscal policy is typically constrained by legal and institutional arrangements that prevent money issuance from being detached from future fiscal adjustment. Using a canonical New Keynesian model, this paper studies whether money-financed fiscal stimulus remains effective when money creation is accompanied by the same future tax adjustment that would arise under debt financing. We find that imposing such tax adjustment has limited effects on the short-run impact of money-financed fiscal stimulus, for both tax cuts and government purchases, and in both normal times and a liquidity trap. Although future tax increases reduce the long-run cumulative effect, money financing with fiscal adjustment remains more expansionary than debt financing in our baseline setting. The mechanism is that future tax increases generate deflationary pressure, which weakens the expansionary effect over time, but also raise real money balances and thereby sustain monetary accommodation. A key policy implication is that the effectiveness of money financing with fiscal adjustment depends on how gradually taxes are adjusted, since the timing of lump-sum taxes affects money growth and therefore real allocations under sticky prices.

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