

Interest Rate Cuts vs. Stimulus Payments: A Macro Equivalence Result

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Abstract: I extend the textbook New Keynesian model to allow for a general form of Ricardian non-equivalence. In this setting I prove that, as soon as households are not perfectly Ricardian, any aggregate allocation that is implementable via nominal interest rate policy is also implementable by adjusting uniform lump-sum transfer payments. It follows that conventional fiscal policy using stimulus checks can perfectly substitute for monetary policy when interest rates are constrained by an effective lower bound. I further show that, in a simple model of Ricardian non-equivalence due to uninsurable household income risk, the mapping from infeasible interest rate policy to equivalent transfer payments is fully characterized by a small number of empirically measurable sufficient statistics. I document that this simple sufficient statistics characterization remains nearly exact even in a rich Heterogeneous Agent New Keynesian (HANK) model.

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