



UNIVERSITY OF TECHNOLOGY
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Fiscal Policy: Post or New Keynesian?

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26th FMM Conference, 22 Oct 2022, Berlin

***Disclaimer:** The views expressed herein do not necessarily reflect those of wonderful coauthors, who shall not be held responsible for any **oversimplification** or **incomplete reading** of the literature by the **presenter**.*

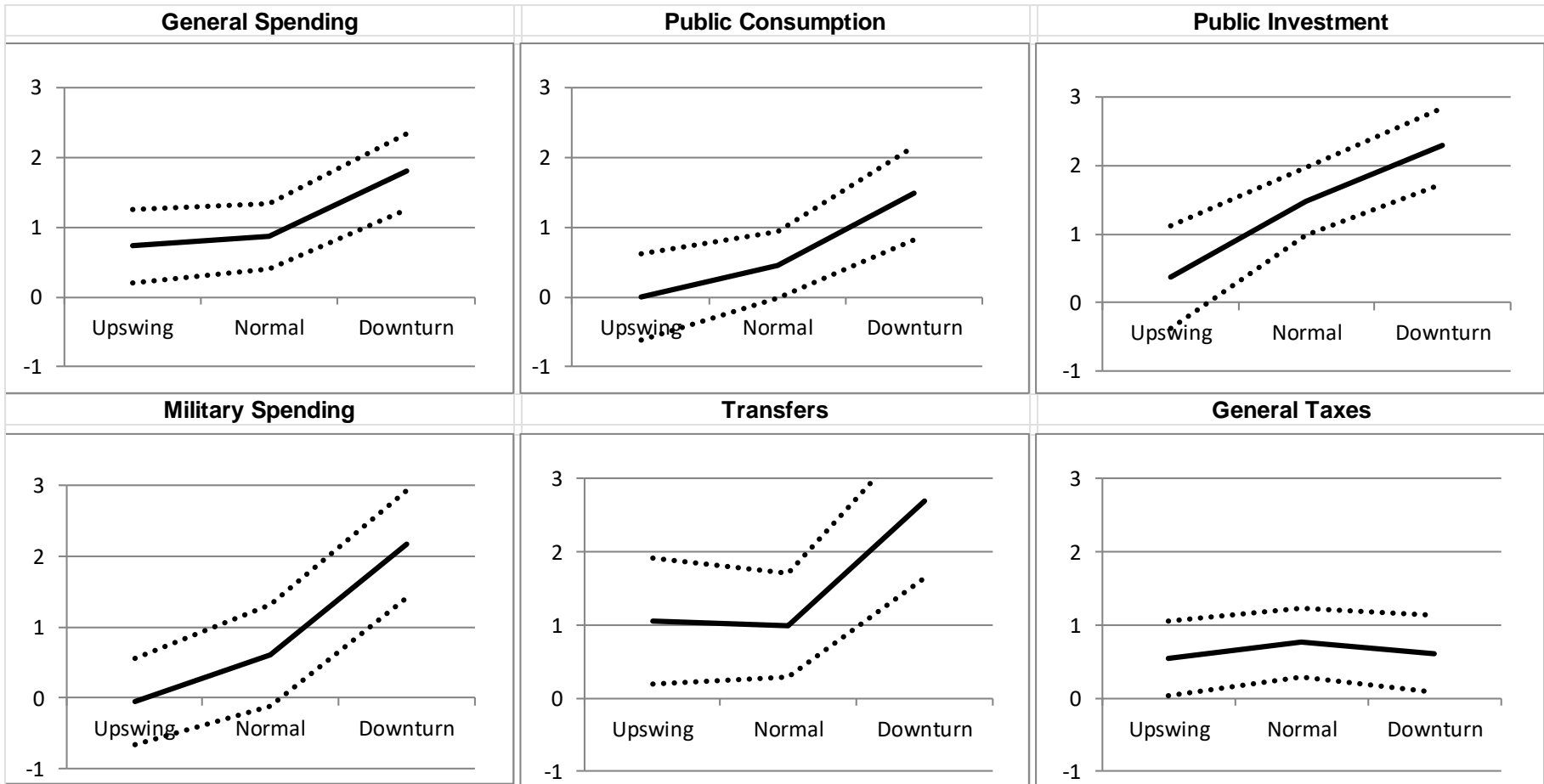
Outline

1. The Macro Perspective
2. The Micro Perspective
3. Implications for Current Policies

The Macro Perspective

Fiscal Multipliers – Regime Dependence

Meta Regression Analysis of >1800 multiplier estimates

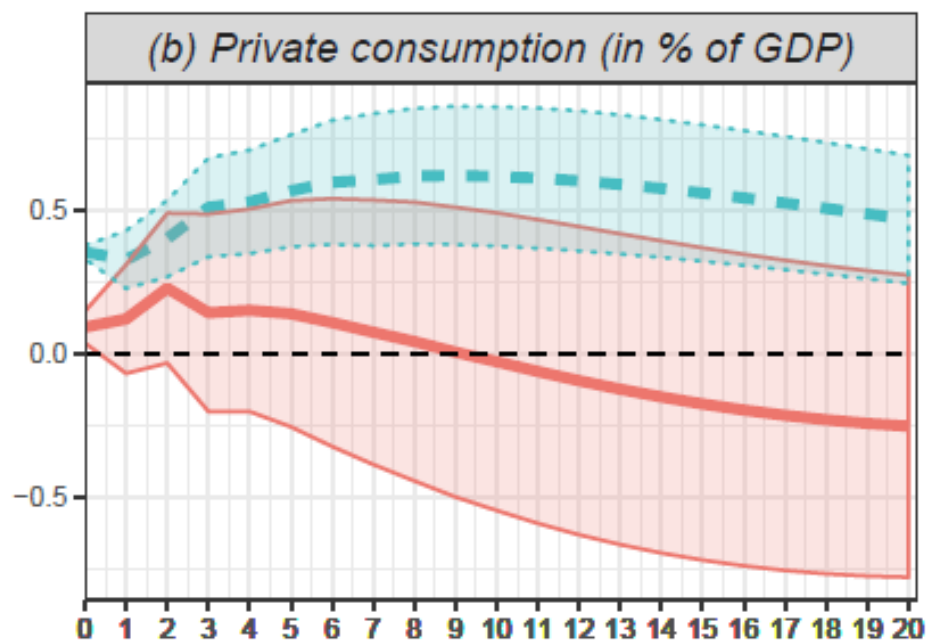
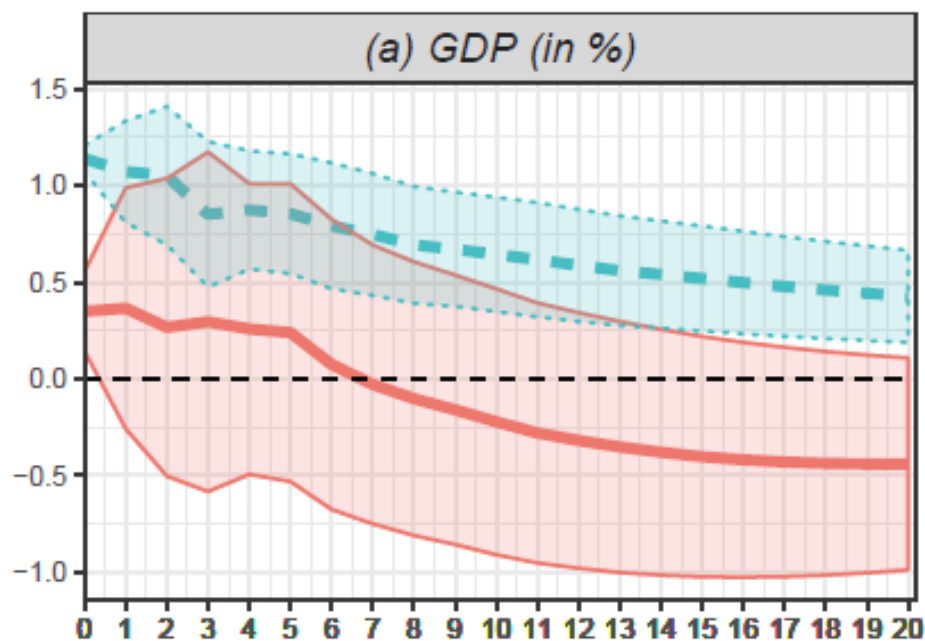


Source: [Gechert/Rannenberg \(2018\)](#)

Closer Look on Taxes vs Transfers











Social Security Contributions and Transfers: Germany

Revenues Expenditures



Fiscal Multipliers

Post Keynesian (PK) or New Keynesian (NK)?

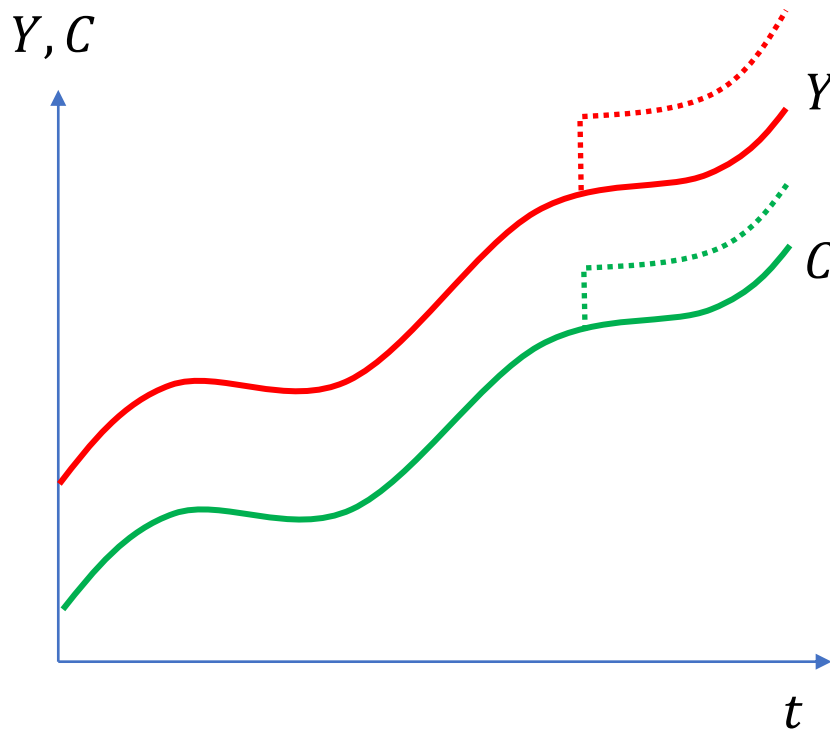
Evidence	PK Model	NK Model
1. Normal times spending multiplier $m \approx 1$	 (open econ)	
2. Crisis times spending multiplier much higher		 (ZLB)
3. Normal times spending multiplier > tax multiplier		
4. Crisis times tax multiplier flat in comparison		 (ZLB)
5. Transfer Multiplier > Tax Multiplier	 (heterog MPC)	 (HtM)

The Micro Perspective

Consumption Function: Permanent Income Shock

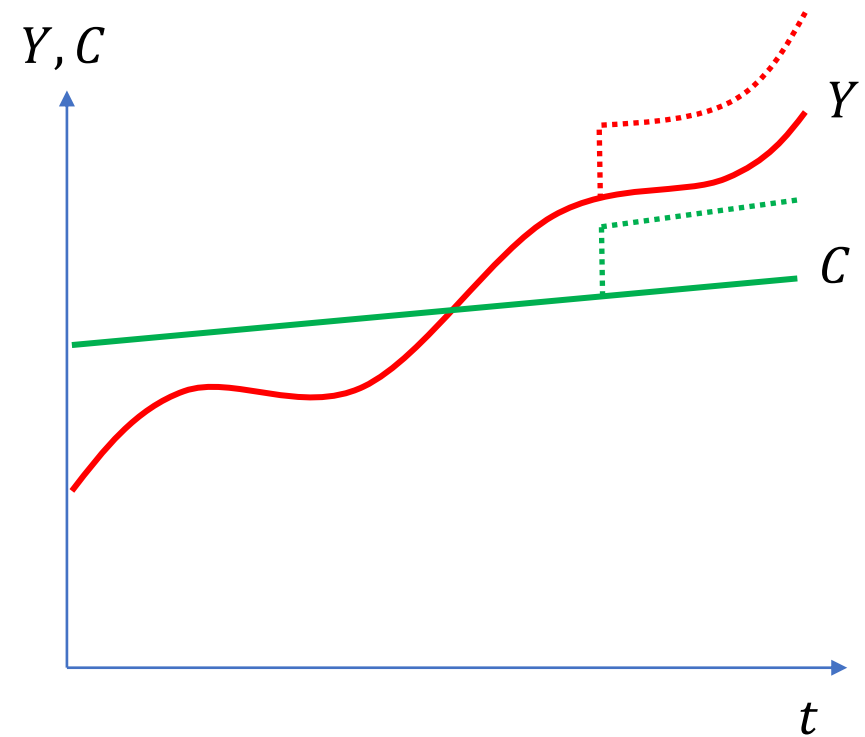
Post Keynesian $C_t = c \cdot Y_t$

$MPC = c$



New Keynesian $\bar{C} = \bar{Y}$

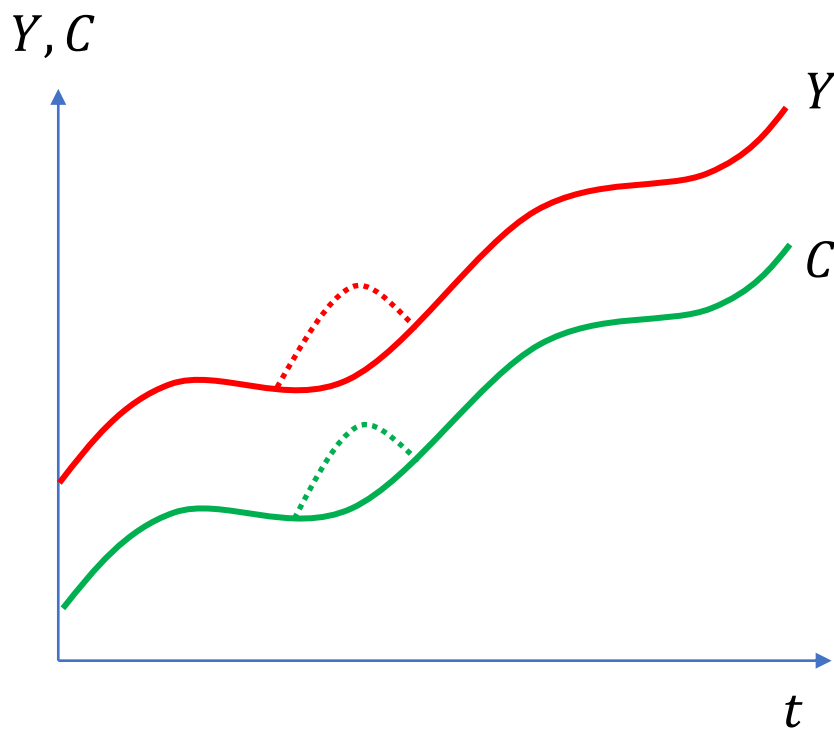
$MPC = 1$



Consumption Function: Transitory Income Shock

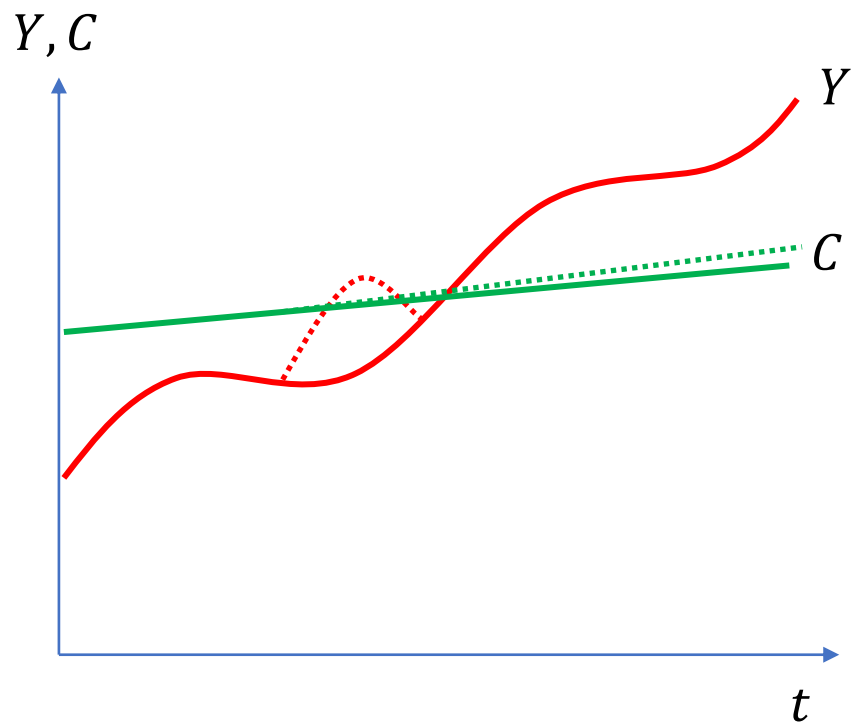
Post Keynesian $C_t = c \cdot Y_t$

$MPC = c$



New Keynesian $\bar{C} = \bar{Y}$

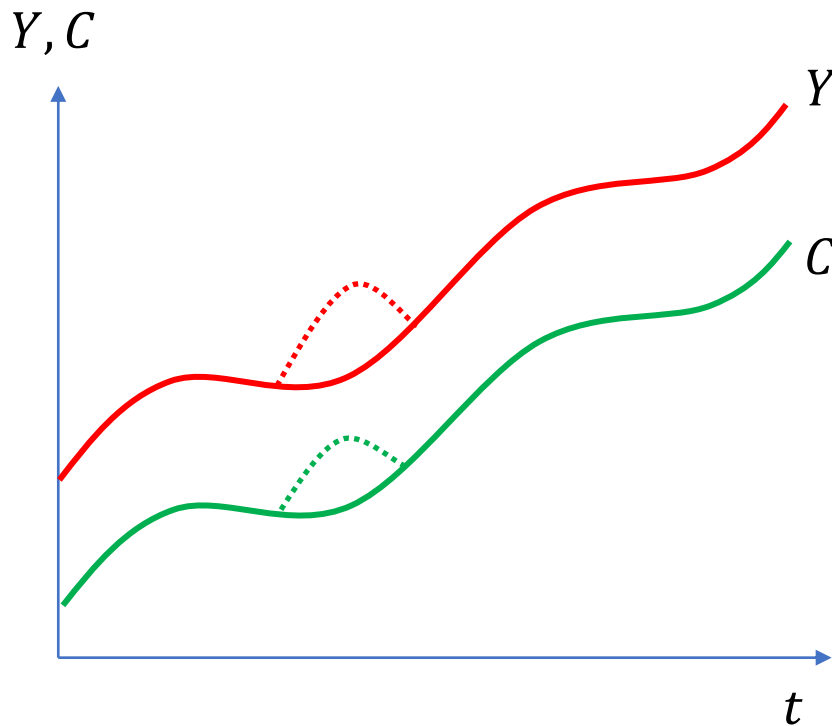
$MPC \approx 0$



Consumption Function: Transitory VAT Cut

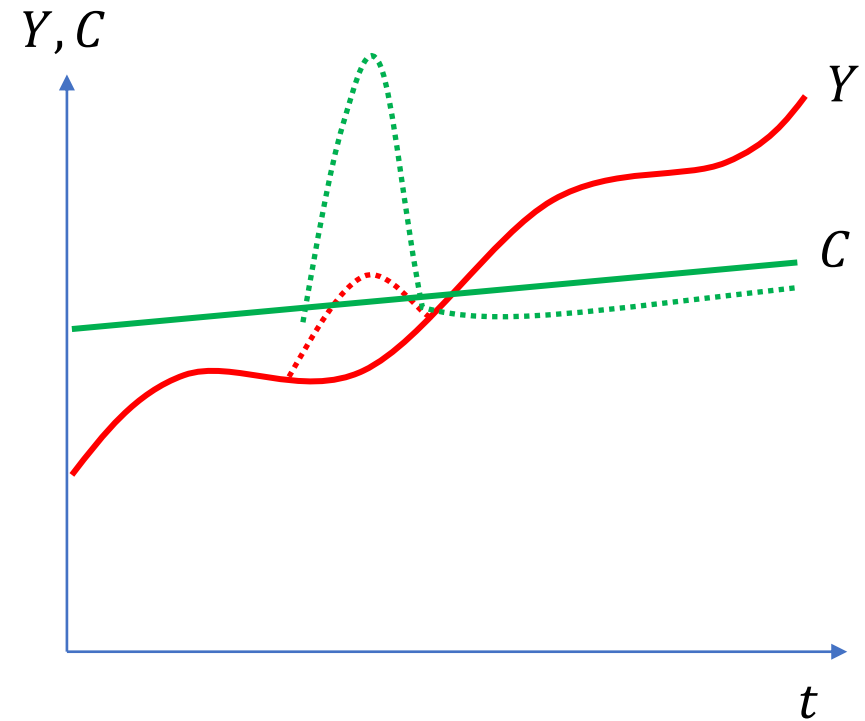
Post Keynesian $C_t = c \cdot Y_t$

$MPC = c$



New Keynesian $\bar{C} = \bar{Y}$

$MPC > 1$



Empirics Again

–Large literature on transitory **US Consumer Checks**

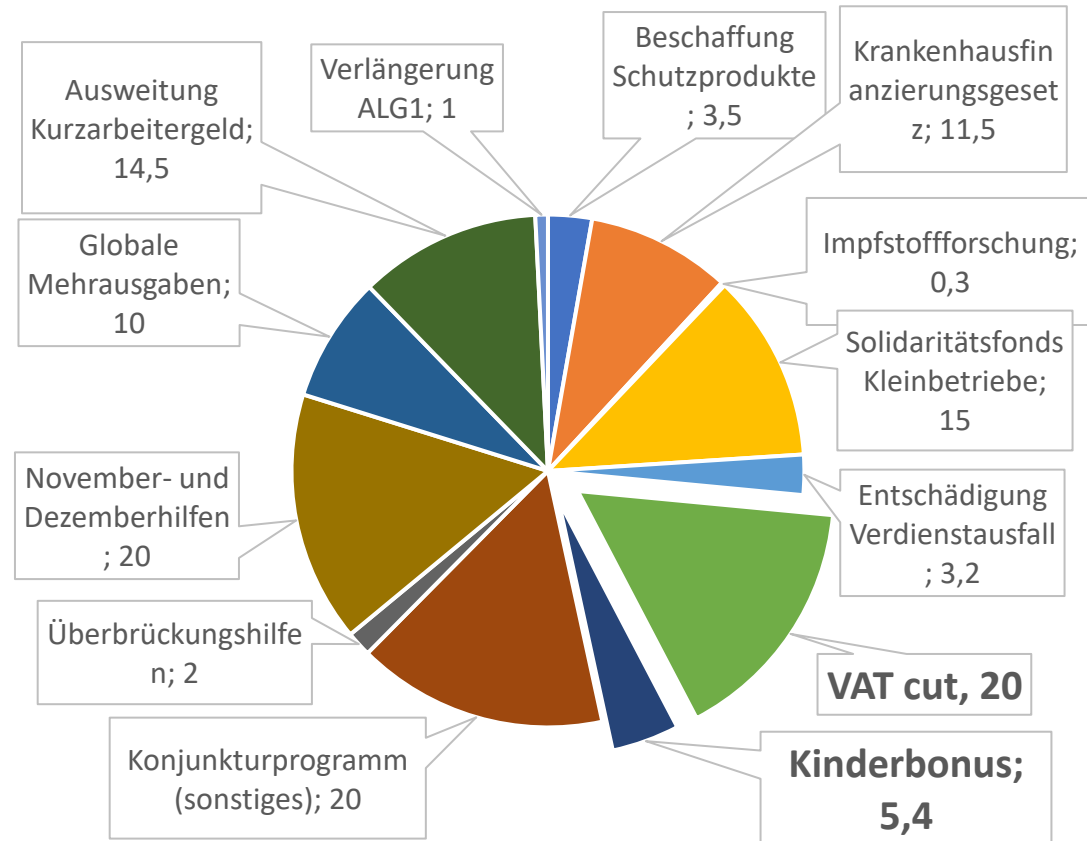
- Parker et al. 2022, Baker et al. 2020, Coibion et al. 2020, Broda et al. 2014, Sahm et al. 2010, Shapiro & Slemrod 2009, ...
- Some international evidence, but scarce (ITA: Jappelli & Pistaferri 2014, 2020; UK: Bunn et al. 2018; GER: Goldfayn-Frank et al. 2022)
- $MPC > 0$,
- $MPC \gg 0$ for households with low / no liquid wealth
- Falsification of both PIH and simple Keynesian consumption function

–Temporary **VAT cut** as „Unconventional Fiscal Policy“

- Scarce evidence (Baker et al. 2019, D'Acunto et al. 2021, 2018, Bachmann et al. 2021)
- They tend to find strong New Keynesian intertemporal substitution effects

German Stimulus Package 2020

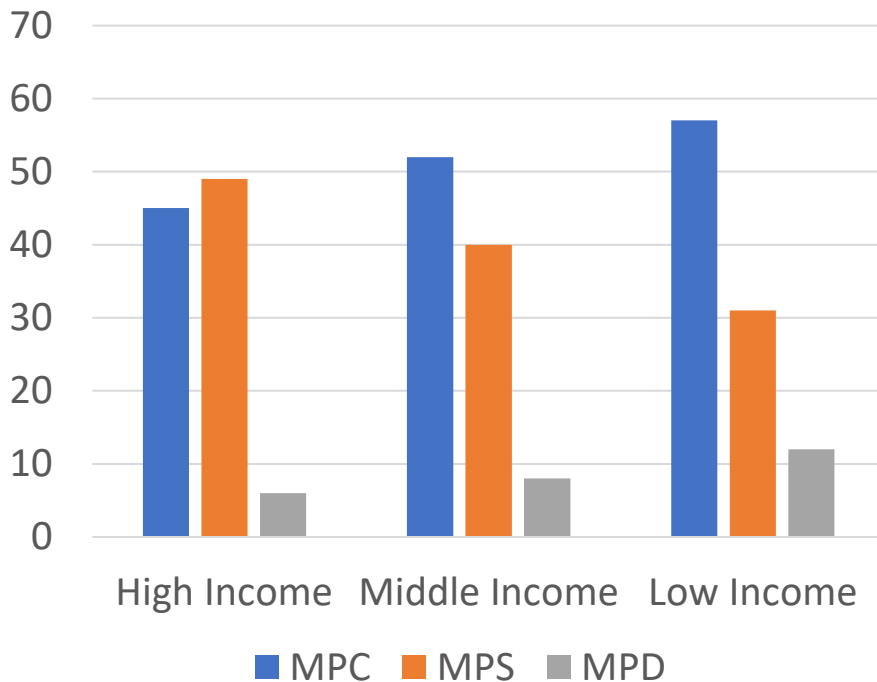
- In sum ca. €125Bn (3.5% of GDP) in 2020.
- „Kinderbonus“ 2020, € 5.4 Bn (0.16% of GDP)
- Temporary VAT cut ca. € 20 Bn (0.6 % of GDP) Jul-Dec 2020
- Interesting test bed for competing consumption theories



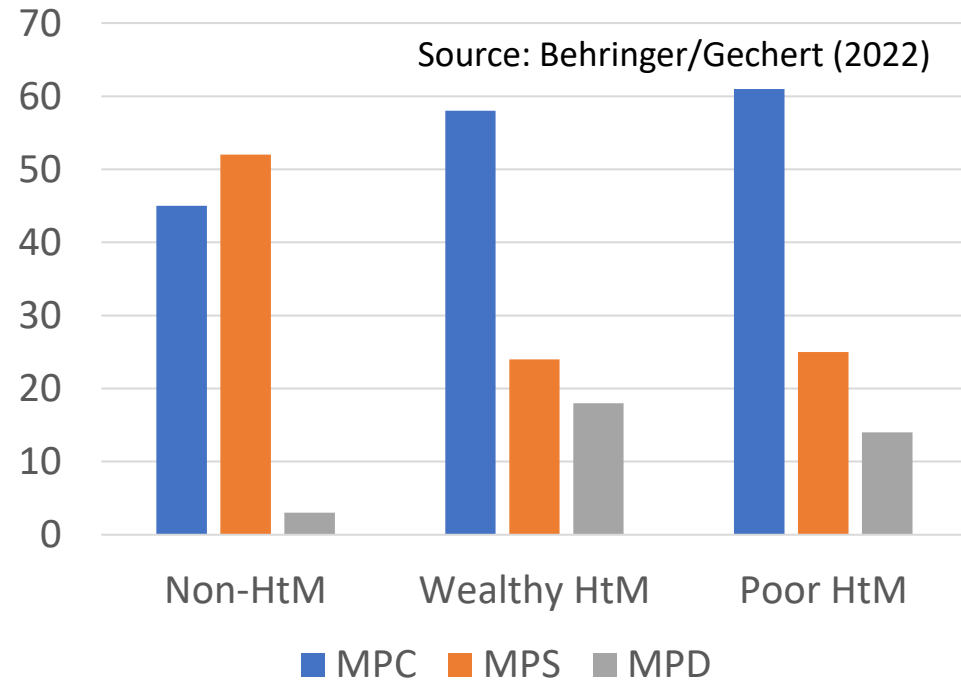
Source: DIW (2020), own calc

Kinderbonus: Marginal Propensities to Consume, Save, Repay Debt

By Household Income



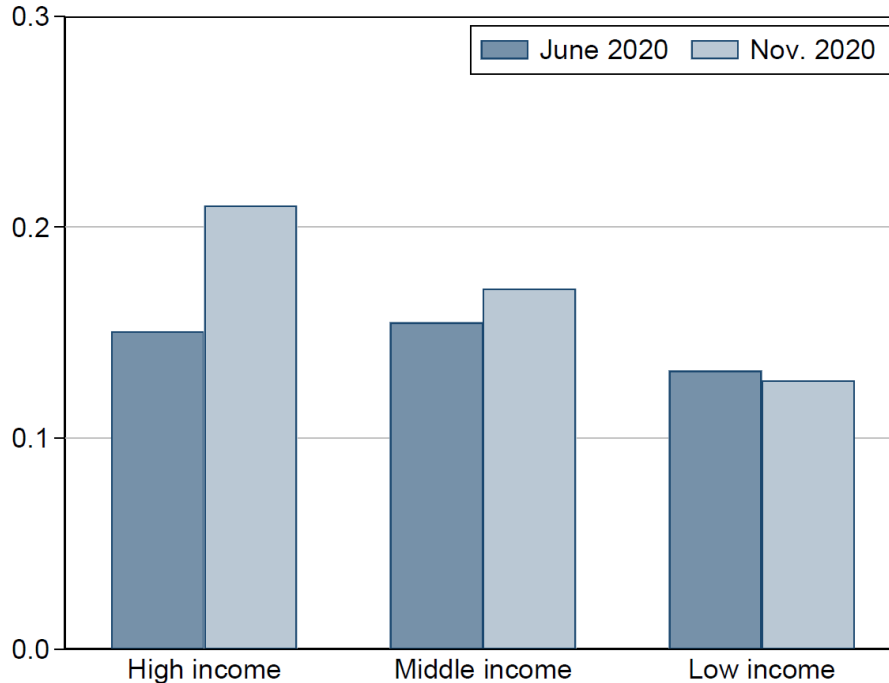
By Financial Wealth Group



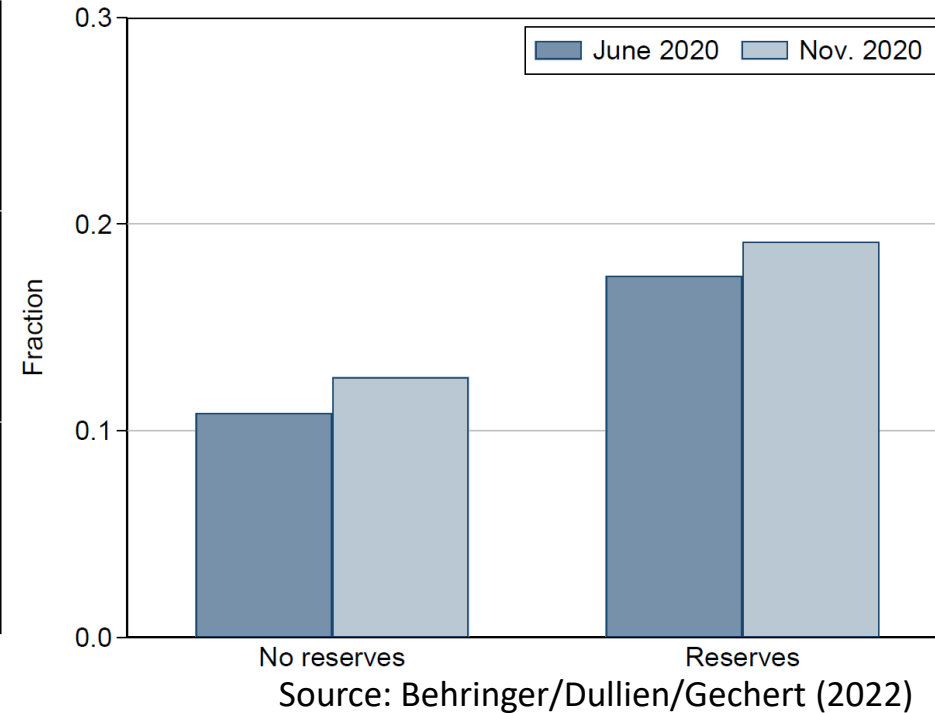
- $MPC \gg 0$ for all groups
- HH with high incomes / liquid reserves tend to save the bonus
- HH with small incomes / no liquid wealth tend to consume / repay debt
- Strong concerns about future / high financial stress / debt burden $\rightarrow MPC \uparrow$

Preponement by HH income / wealth

By Income








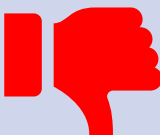


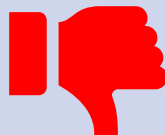
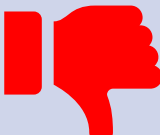


By Financial Wealth Group



Source: Behringer/Dullien/Gechert (2022)

- Some, but weak intertemporal substitution effects
- Preponement stronger with higher current incomes, liquid reserves

Consumption Behavior

Evidence	PK Model	NK Model
Transitory transfer: average $MPC \approx 0.5$		
$MPC \downarrow$ with wealth		 (TANK)
$MPC \downarrow$ with current income		
$MPC \uparrow$ with greater fears, financial stress, debt burden		 (TANK, HANK)
Some, but weak intertemporal substitution with VAT cut	 (no)	 (strong)
Use of VAT cut rises with cash on hand		

Behavioral Concepts Beyond Baseline NK or PK Models

Realistic Microfoundations

- Credit/Liquidity Constraints
(Deaton 1991, Jappelli & Pistaferri 2014)
- Precautionary / Buffer-Stock Saving
(Carroll 1997, Gechert & Siebert 2021)
- Stone-Geary-Preferences, basic consumption needs, saving as a luxury good
(Carroll 1998, Campanale 2018)
- Mental Accounting
(Thaler 1990, McDowall 2020)

Behavioral Concepts Beyond Baseline NK or PK Models

Consequences for Consumption

- Explicit life-cycle perspective of consumption
- Consumption tracks current income closely
- Liquid wealth important for consumption
- Transitory income shocks:
 - Average $MPC > 0$
 - Low income / liquid wealth HH: $MPC \gg 0$
- Transitory VAT cut: Future income, price, interest rate changes ...
 - ... more important than in the PK model
 - ... less important than in NK model

Including Behavioral Elements in PK and NK Models

PK, selected from Lavoie (2022)

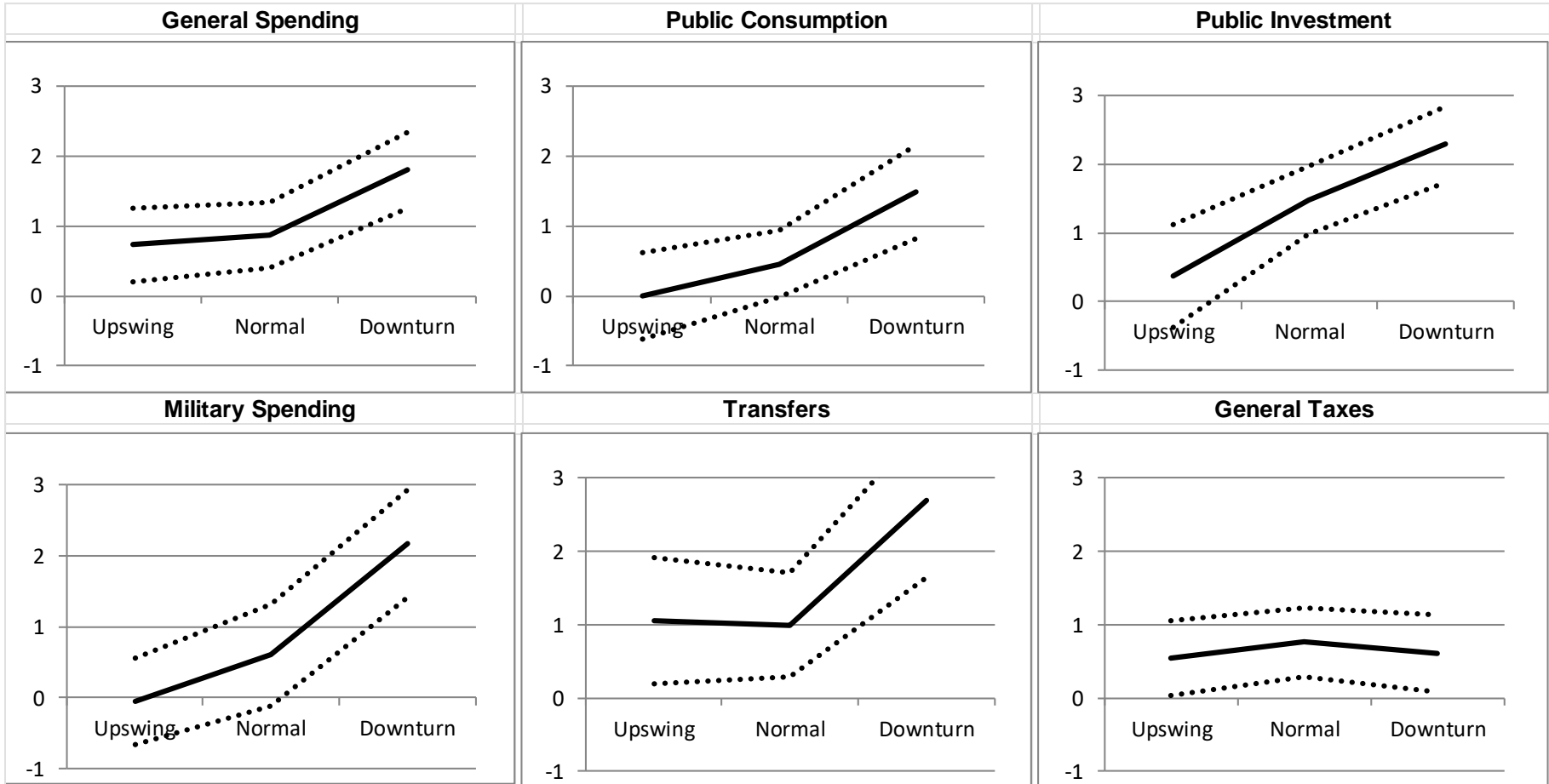
- Procedural rationality and satisficing, separability of needs (→Mental Accounting)
- Pyramide of needs (→Stone-Geary preferences)
- Yet no life-cycle model of consumption or intertemporal choices.

HANK (Hagedorn et al. 2019)

- Heterogeneous agents according to their productivity, discount rate and assets
- Incomplete financial markets, non-insurable income risk
- Precautionary saving motive
- Endogenous credit constraints
- Dynamic Keynesian Cross Effects
- Muted intertemporal substitution
- Still over-reliance on exp. future income, interest rates, prices

Implications for Current Policies

In which regime are we right now?



Fiscal policy under supply shortages and lurking recession

With a focus on the EU

–Short-term

- Targeted consumer tax cuts (→basic consumption needs) / subsidies that reduce measured inflation.
- ... but no outright price caps to fossiles, which might undermine saving incentives.
- Redistributive transfers / social security acting as income insurance, not necessarily as stimulus.

–Medium-term

- Industrial policies / public investment to gain independence from fossiles and restructure European growth model.
- Expect a higher frequency of negative shocks → public debt concerns? → Tax the rich

→ Is this Post or New Keynesian?

We are all Keynesians now

Effective Demand Failures and the Limits of Monetary Stabilization Policy[†]

The challenge for stabilization policy presented by the COVID-19 pandemic stems above all from disruption of the circular flow of payments, resulting in a failure of what Keynes (1936) calls “effective demand.” As a consequence, economic activity in many sectors can be inefficiently low, and interest-rate policy cannot eliminate the distortions—not because of a limit on the extent to which interest rates can be reduced, but because interest-rate reductions fail to stimulate demand of the right sorts. Fiscal transfers are instead well suited to addressing the fundamental problem, and can under certain circumstances achieve a first-best allocation of resources. (JEL E23, E32, E43, E52, E62, E63, H63)

<https://doi.org/10.1257/aer.20201529>