Policy Forum

Policy Forum: Macroeconomic Policies in the New Normal ¹

Introduction

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This issue of the policy forum focuses on a theme that has become dominant on the policymakers' agenda since the global financial crisis: How to conduct monetary and fiscal policies in an environment characterised by low interest rates and concerns over fiscal sustainability.

A lot of questions regarding how effective these policies are in close and open economies were proposed and discussed in the context of the fourth edition of the Melbourne Institute Macroeconomic Policy Meetings, which took place on 4–5 October 2018. The goal of the event was to provide a forum for academics and policymakers to discuss evidence and insights on the role of fiscal policy before, during and after the global financial crisis. The Meeting featured 11 high quality scientific papers as well as a panel discussion facilitated by Bruce Preston (University of Melbourne) with panelists: Guy Debelle (Reserve Bank of Australia), Anella Munro (Reserve Bank of New Zealand) and Nigel Ray (Australian Treasury). Valerie Ramey (University of California at San Diego) and Simon Gilchrist (New York University) offered keynote speeches on the renaissance in fiscal research after the advent of the crisis (Ramey) and on the real effects of credit booms and busts (Gilchrist). The workshop, organised by Bruce Preston and me, and sponsored by the Reserve Bank of Australia, Reserve Bank of New Zealand, the Australian Treasury, the Department of Economics of the University of Melbourne and the Macroeconomics Unit of the Melbourne Institute, represented an excellent example of a successful interaction between academia and policymaking institutions on a relevant theme such as uncertainty.

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This policy forum contains four papers that are intimately related to this conversation. The paper written by Guay Lim and me, titled ‘What Do We Know About the Macroeconomic Effects of Fiscal Policy? A Brief Survey of the Literature on Fiscal Multipliers’, focuses on recent estimates of fiscal spending and tax-based multipliers and on how non-linearities related to the business cycle, the zero lower bound on the policy rate, the degree of openness of a country with respect to the rest of the world and other conditioning elements can affect the size of the multipliers. A discussion on expected shocks and fiscal plans is also offered. The survey closes with a few directions for future research.

In ‘The Cyclical Behaviour of the Labour Force Participation Rate in Australia’, Richard Evans, Angus Moore and Daniel M. Rees investigate the relationship between labor market participation and economic activity at a cyclical level in Australia. They detect a large and economically important cyclical component of the participation rate. Young people, 25–54 year-old females, and older males are found to be the most responsive groups to variations in economic conditions. Interestingly, if the participation rate did not adjust along the business cycle, expansions would be more inflationary and recessions more deflationary and would generate more involuntary unemployment.

The labor market is also analysed in ‘Contributions of Employment Change to Annual Wage Growth in New Zealand’, a paper written by Dean Hyslop and Amy Rice. They analyse trends in average wage growth in New Zealand over the last 20 years, and they track within-group wage growth and unemployment compositional changes. Real wage growth is found to have been mildly pro-cyclical, with a break during the post-GFC period. According to their estimates, within-group wage growth dominated aggregate wage growth in the analysed period. A deeper investigation on the drivers behind these findings is also provided.

The last paper of the pool is by Martin Fukac, who addresses the question ‘How Much Have Lending Standards Constrained US Recovery After the Financial Crisis?’ By employing a vector autoregression analysis, Martin estimates that the economic contraction of 2008–2009 would have been two percentage points milder in the absence of lending standards shocks, which caused the overheating of the US economy and its subsequent abrupt contraction.

These four papers cover hot topics, and they blend very nicely in this special issue. It was a pleasure to read them and contribute to one of them. I feel privileged I was in the position of managing such an exciting issue of the policy forum. I believe these four contributions will receive a warm welcome by academics and economists working for policy institutions in Australia and around the world.

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