

Fast and loose

The Economist

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- 2001.1: Fed funds rate was cut from 6.5% to 6.0%
- 2003.11: 1.0%
- 2006.8: Fed funds rate was 5.25%
- 2008.3.16: Fed funds rate was 3.25%

Loose? – Taylor rule

- If $\pi = 2\%$, and GDP gap = 0, then $R = 4\%$
- If $\pi = 2\%$, and GDP gap -2% , then $R = 3\%$
- If $\pi = 3\%$, and GDP gap -2% , then $R = 4.5\%$

Too loose?

- Had the central bank followed the rule, rates in 2002 would have been going up not down.