You are kindly invited to attend a Joint Seminar of the National Bank of Belgium, CES-KUL, Ecares-ULB and UCL

by

Michael B. Devereux (University of British Columbia) joint paper with David Cook

on

Optimal Fiscal Policy in a World Liquidity Trap

Abstract

We construct a model of the international transmission of ‘liquidity trap’ shocks, and examine the case for international coordination of fiscal policy to respond to the liquidity trap. Integrated financial markets tend to propagate liquidity traps. In a global environment, fiscal policy may be effective in raising GDP when the economy is stuck in a liquidity trap, but it does so in a ‘beggar thy neighbor’ fashion; when one economy is in a liquidity trap, the cross country spillover effect of fiscal policy is negative. We examine the welfare optimizing policy response to a liquidity trap when countries coordinate on fiscal policy. Fiscal policy may be an effective tool in responding to a liquidity trap, although it is never optimal to use fiscal expansion sufficiently to fully eliminate a downturn. Moreover, there is little case for coordinated global fiscal expansion. For the most part, the country worst hit by a liquidity trap shock should use its own policies to respond, without much help from foreign policies.

The seminar will take place on Thursday, **21 October 2010** from **16.30 until 18.00**. The seminar will be held in the Auditorium of the National Bank of Belgium (Room A), Entrance: Warmoesberg 61, Brussels.

Please reply by email to Yvette.Vandenbosch@nbb.be if you wish to participate to this seminar. With name and car plate number to access the NBB Parking Warmoesberg 41.

Kind regards,
H. Dewachter (KUL), R. Kollmann (ULB), C. Poily (UCL) and R. Wouters (NBB)