Macro Public Finance I
EUI, February & March 2016

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Time and Location: Tuesday 17.15-19.15

Course Overview: This class will cover a range of questions related to fiscal policy issues: what should be the optimal plan for labor taxes, capital taxes, transfers, public debt, government spending? We will cover both models with a representative agent and models with heterogeneous agents. We will focus on fiscal plans with commitment only.

Syllabus: The exact ordering and content of the class will be adjusted weeks after weeks.

1. Optimal fiscal plans with time-zero commitment

   (a) A warm-up: we review the well-known papers of Chamley and Judd and discuss their results on capital taxes; we use this as an opportunity to review the Primal Approach.

   - The canonical papers:
     - Chamley, Christophe, *"Optimal Taxation of Capital Income in General Equilibrium with Infinite Lives,"* Econometrica, 54, 3 (May 1986), 607-622.
     - Judd, Kenneth L., *"Redistributive Taxation in a Simple Perfect Foresight Model,"* Journal of Public Economics, 28,1 (October 1985), 59-83.
   - More recent papers:
     - Straub, Ludwig & Werning, Ivan, *"Positive Long Run Capital Taxation: Chamley-Judd Revisited,"* NBER Working Paper No. 20441, 2014.

   (b) Optimal responses of tax and public debt to shocks in models with a representative agent.

   - Complete markets:
     - With debt and labor taxes: Lucas, Robert Jr. & Stokey, Nancy L., 1983. *"Optimal fiscal and monetary policy in an economy without capital,"* Journal of Monetary Economics, Elsevier, vol. 12(1), pages 55-93.
     - Adding capital taxes: Chari, V V & Christiano, Lawrence J & Kehoe, Patrick J, 1994. "*Optimal Fiscal Policy in a Business Cycle Model,"* Journal of Political Economy, University of Chicago Press, vol. 102(4), pages 617-52, August.
     - Adding endogenous government spending: Ferriere, Axelle & Karantounias, Anastasios, *"Fiscal austerity in ambiguous times"*, Working paper (2016)
   - Incomplete markets
     - With debt and labor taxes: Aiyagari, S.R, Marcet, A., Sargent, T.J, and Juha Seppala (2002): *"Optimal Taxation without State-Contingent Debt"*, Journal of Political Economy, 110, 1220-1254.
     - Adding capital taxes: Farhi, Emmanuel. 2010. *"Capital Taxation and Ownership when Markets are Incomplete,"* Journal of Political Economy, 118 (5): 908-948.

   (c) Optimal taxes and transfers with heterogenous agents.

- Complete markets: Ivan Werning, 2007. *"Optimal Fiscal Policy with Redistribution,"* The Quarterly Journal of Economics, Oxford University Press, vol. 122(3), pages 925-967.
- Incomplete markets: Anmol Bhandari & David Evans & Mikhail Golosov & Thomas J. Sargent, 2016. *"Taxes, Debts, and Redistributions with Aggregate Shocks,"* Working paper.

2. Fiscal plans in Aiyagari models.

   - Dynamic lump-sum taxes:
     - Jonathan Heathcote, *"Fiscal Policy with Heterogeneous Agents and Incomplete Markets"*, Review of Economic Studies January 2005, 72, p. 161-188.
     - Greg Kaplan & Gianluca Violante, *"A Model of the Consumption Response to Fiscal Stimulus Payments"*, Econometrica, Vol. 82(4), July 2014, 1199-1239.
   - Capital taxes:
     - Conesa, Juan Carlos, Sagiri Kitao, and Dirk Krueger. 2009. *"Taxing Capital? Not a Bad Idea after All!"*, American Economic Review, 99(1): 25-48.
     - David Domeij & Jonathan Heathcote, *"On the Distributional Effects of Reducing Capital Taxes,"*International Economic Review May 2004, 45/2, p. 523-554.
   - Progressive taxes:
     - Jonathan Heathcote & Kjetil Storesletten & Gianluca Violante, *"Consumption and Labor Supply with Partial Insurance: An Analytical Framework"*, American Economic Review, Vol. 104(7), July 2014, 2075-2126.
     - Axelle Ferriere & Gaston Navarro, *"The Heterogeneous Effects of Government Spending: It's All About Taxes"*, Working Paper.
   - The role of public debt:
     - S. Rao Aiyagari & Ellen R. McGrattan, *"The Optimum Quantity of Debt*, October 1998, Journal of Monetary Economics, 42(3): 447-469.
     - Martin Floden, *"The Effectiveness of Government Debt and Transfers as Insurance"*, Journal of Monetary Economics, August 2001, 48(1), 81-108.

Grading: During this class, you will be asked to replicate a paper using an Aiyagari framework (you will choose within some of the papers listed above; this can be handled in teams of maximum two students), plus you will be asked to present a paper (20mn) or prepare a referee report, depending on the number of students who register in this class. If we do presentations, they will occur during the lectures.