

What drives the Business Cycle?

One of the most fundamental questions in macroeconomics relates to the origins of business cycles. Real business cycle models focus on technology shocks, while New-Keynesian models attribute a larger role to demand shocks. Can empirical evidence help us distinguish between business cycle theories? What are the issues that empirical research faces?

Recommended reading:

- Gali, J. (1999), *Technology, Employment, and the Business Cycle: Do Technology Shocks Explain Aggregate Fluctuations?* American Economic Review, 89(1), 249-271.
- Angeletos, G.-M., Collard, F. and Dellas H. (2021): *Business-Cycle Anatomy*. American Economic Review, 110 (10), 3030–70.

On Phillips Curves and Inflation

What causes inflation in modern economies? The New-Keynesian Phillips curve posits that inflation is driven by expected inflation, slack in the economy, and supply shocks, e.g. cost-push shocks. What is the state of the empirical evidence for such a Phillips curve? Is the Phillips curve dead or has the slope of the Phillips curve flattened? These issues are of first-order importance for central bankers that need to achieve their price stability mandates.

Recommended reading:

- Hazell, J. and Herreno, J. and Nakamura, E. and Steinsson, J. (2022): *The Slope of the Phillips Curve: Evidence from U.S. States*. The Quarterly Journal of Economics, Volume 137, Issue 3, Pages 1299-1344.
- Furlanetto, F., Bergholt, B., and Grange, E. (2024) *Did Monetary Policy Kill the Phillips Curve? Some Simple Arithmetics*. Review of Economics and Statistics, forthcoming.

Identifying the Effects of Monetary Policy

Identifying the effects of monetary policy shocks in macroeconomics can be difficult. Researchers are faced with the endogeneity and feedback effects of monetary policy. Which approaches can applied econometricians use to model the effects of changes in monetary policies on other macroeconomic variables? Which economic theories are they based on?

Recommended reading:

- Ramey V.A. (2016) *Macroeconomic Shocks and Their Propagation*. In: Handbook of Macroeconomics, Ed. 2A, pp. 71-162.
- Bauer, M. D. and Swanson, E. T. (2023): *A Reassessment of Monetary Policy Surprises and High-Frequency Identification*. NBER Macroeconomics Annual, volume 37, pp. 87-155.

Monetary Policy Rules: The Systematic Component in Monetary Policy

The conduct of monetary policy is endogenous to the state of the economy. When the economy “overheats,” with output growing above potential and inflation rising, the central bank typically raises its policy rate. Conversely, in downturns with below-target inflation, the policy stance becomes more expansionary. Research has shown that central banks often behave in a rule-like manner. A well-known example of such behavior is the Taylor rule. But what exactly is the Taylor rule, and how closely does it approximate optimal policy? Moreover, can empirical evidence help us answer these questions?

Recommended reading:

- Nakamura, E., Riblier, V and Steinsson, J. (2025) *Beyond the Taylor Rule* 2025 Jackson Hole Economic Policy Symposium.
- Barnichon, R. and Mesters, G. (2023) *A Sufficient Statistics Approach for Macro Policy*. American Economic Review, 2023, vol 113 (11), pp. 2809-45.

Hysteresis: Scarring Effects of Transitory Shocks

Can massive temporary shocks inflict permanent damage on economies? This is a key concern for policy makers. However, typical characterizations of the business cycle assume that cyclical shocks have temporary effects and do not cause long-term damage to an economy. This textbook notion has come under pressure again in the last decade as the global economy was struggling with a very slow recovery to the great financial crisis (GFC). Especially, the economies of the euro zone have been hit hard with the double-dip recession when the GFC was followed up by the euro crisis.

Recommended reading:

- Eo, Y. and Morley, J. (2022): *Why has the US Economy stagnated since the Great Recession?* The Review of Economics and Statistics, 104, 246-258.
- Furlanetto, F. et al. (2025) *Estimating Hysteresis Effects*. AEJ: Macro, vol. 17, no. 1, (pp. 35-70)

The Global Role of the US Dollar

Fluctuations in the US dollar play an essential role in the international monetary system. With the explosive growth of global financial markets, the US currency has gained a predominant position in emerging market economies as well as advanced economies. Through which channels does the US dollar impact these economies? What are its implications for the dollar exchange rate?

Recommended reading:

- Miranda-Agrippino, S. and Rey, H. (2020) *US Monetary Policy and The Global Financial Cycle*. Review of Economic Studies, 87, 2754-2776.
- Georgiadis, G., Müller, G. and Schumann, B. (2024) *Global Risk and the Dollar*. Journal of Monetary Economics, vol. 144.

Safe Assets and the Convenience Yield

Safe assets play a significant role in the global economy. The US is the central supplier of these safe assets and earns a convenience yield for issuing safe dollar assets. What implications does this have for the dollar exchange rate and US monetary policy?

Recommended reading:

- Krishnamurthy A. and Lustig, H. (2019) *Mind the Gap in Sovereign Debt Markets: The U.S. Treasury basis and the Dollar Risk Factor*. 2019 Jackson Hole Economic Policy Symposium.
- Engel, C. and Wu, S. P. Y. (2023): *Liquidity and Exchange Rates: An Empirical Investigation*. The Review of Economic Studies, Volume 90, Issue 5, Pages 2395-2438.

What drives Long-Term Inflation Dynamics?

Long-term, or trend inflation reflects the slow-moving forces that persist beyond short-run business cycle fluctuations. Understanding what drives long-term inflation is crucial because trend inflation guides monetary policy decisions and shapes expectations, which themselves reinforce inflation dynamics. Empirical research needs to identify the drivers of trend inflation to allow central banks to improve their policy design and credibility.

Recommended reading:

- Kamber, G. and Wong, B. (2020) *Global factors and trend inflation*. Journal of International Economics, 122, 103265
- Ascari, G. and Fosso, L. (2024) *The international dimension of trend inflation*. Journal of International Economics, 148, 103896