Credit Spreads and Credit Policies

February 21, 2014, 14h30, ISCTE-IUL, Auditorium ONE01 (Building I)

Pedro Teles
Senior Economist at the Economic Research Department of the Bank of Portugal and Full Professor at the Portuguese Catholic University

Pedro Teles has worked on various issues of monetary and fiscal policy, including the optimality of the Friedman rule, time consistent policies, optimal stabilization policy, optimal currency areas, and instruments of monetary policy. His work is published in the Journal of Political Economy, Review of Economic Studies, Journal of Monetary Economics and Review of Economic Dynamics. He holds a PhD in Economics from the University of Chicago and, between 2001 and 2004, he was a Senior Economist in the Research Department at the Federal Reserve Bank of Chicago.

[Abstract] How should monetary and fiscal policy react to adverse financial shocks? If monetary policy is constrained by the zero lower bound on the nominal interest rate, subsidising the interest rate on loans is the optimal policy. The subsidies can mimic movements in the interest rate and can therefore overcome the zero bound restriction. Credit subsidies are optimal irrespective of how they are financed. If debt is not state contingent, they result in a permanent increase in the level of public debt, in a permanent increase in future taxes and in a permanent reduction in output.