DISSERTATION ABSTRACT

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My dissertation is comprised by three papers that look at monetary policy, international economics, and adaptive learning. The first two papers estimate New Keynesian DSGE models in order to examine the causes of the Great Inflation in the U.S., and the fear of floating phenomenon pervasive in emerging markets. The Great Inflation analysis incorporates policymakers that are learning adaptively about the state of the economy. The third paper evaluates the desirability of policy rules that respond to wage inflation in a model with staggered price and wage setting in the context of determinacy and stability under adaptive learning. The first and last papers of my dissertation contribute to the studies of the implications of adaptive learning on monetary policy. My dissertation results support Sargent's (1999) view that adaptive learning is a relevant mechanism affecting inflation policy.

My job market paper, **"Policy Preferences and Policymakers' Beliefs: The Causes of the Great Inflation in the U.S."**, examines the causes of the rise and fall of inflation during the 1970s and 1980s, considered under the term of the "Great Inflation," in the United States. The monetary policy literature has proposed two potential channels through which monetary policy played a role in the rise and fall of inflation in the U.S. during the 1970s and 1980s. One approach holds that monetary policymakers during the 1970s preferred stabilizing output while post 1979 they preferred inflation stabilization (Cecchetti, et al. 2007). An alternative explanation contends that the Federal Reserve held misperceptions about the state of the economy and the transition equations for the economy. Erroneous beliefs about the state of the economy and the transition equarions could lead policymakers into creating excessive inflation that will be reversed once beliefs are aligned with outcomes via an adaptive learning process. To disentangle the effects of these two hypotheses, this paper develops a medium scale macroeconometric model that incorporates real-time learning by policymakers as well as a (potential) shift in policymakers' preferences. Empirical results support both views: distorted beliefs led policymaker's to underestimate the persistence of inflation and to incorrectly perceive an unfavorable tradeoff between inflation and the output gap; these misperceptions were accompanied by a stronger preference for output stabilization during the 1970s than the 1980s. Combined these two channels illustrate the role played by monetary policy in propagating and ending the Great Inflation.

My second paper, **"Fear of Floating or Monetary Policy as Usual? A Structural Analysis of Mexico's Monetary Policy"**, looks at the Mexican economy experience before and after the financial and balance of payments crisis. I estimate a structural model that includes a Taylor rule as the expression of the evolution of monetary policy. Estimates of the monetary policy rule allow us to assess the extent to which the interest rate responds to inflation or to the exchange rate in the post crisis period, whereby we can evaluate the Mexican central bank's claim that post 1994 the monetary policy authority targeted inflation or if it acted in accordance to fear of floating . The empirical analysis suggests that the central bank of Mexico did not respond strongly to movements in the exchange rate during the floating exchange rate regime, especially compared with the high degree of exchange rate targeting observed in the managed exchange rate regime. Thus, the evidence does not add support to the claim that monetary policy in Mexico reflects a fear of floating.

The third paper, **"A New Keynesian Model with Staggered Wage and Price Contracts under Learning"** studies the implications for economic dynamics when the central bank sets its nominal interest rate target in response to variations in wage inflation. I provide results on the existence, uniqueness, and stability under learning of rational expectations equilibrium for alternative specifications of the manner in which monetary policy responds to economic shocks where price and wage rigidities are present. Monopolistically competitive producers set prices via staggered price contracts and households set nominal wages in the same fashion. In this setting the conditions for determinacy and learnability of rational expectations equilibrium differs from a model where only prices are sticky. I find that, when the central bank responds

to wage and price inflation and to the output gap a Taylor principle for wage and price inflation arises, but it is not necessarily related to stability under learning dynamics.