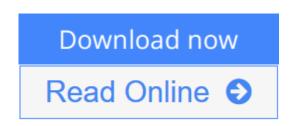


# The Role of Policymakers in Business Cycle Fluctuations

By Jim Granato, M. C. Sunny Wong



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This book's central theme is that a policymaker's role is to enhance the public's ability to coordinate their price information, price expectations, and economic activities. This role is fulfilled when policymakers maintain inflation stability. Inflation persists less when an implicit or explicit inflation target is met. Granato and Wong argue that inflation persistence is reduced when the public substitutes the prespecified inflation target for past inflation. A by-product of this co-ordination process is greater economic stability. In particular, inflation stability contributes to greater economic output stability, including the potential for the simultaneous reduction of both inflation and output variability - inflation-output co-stabilization (IOCS). Granato and Wong use historical, formal, and applied statistical analysis of business-cycle performance in the United States for the 1960 to 2000 period. They find that during periods when policymakers emphasize inflation stability, inflation uncertainty and persistence were reduced.

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#### Review

"Granato and Wong have written an elegant volume that outlines a useful theoretical construct of the issues faced by policymakers in managing business cycles. The implications of their approach go beyond predictions of inflation and output performance. They also extend to recommendations about institutional reform and the role of the political process. Graduate students and academics that teach and think about macroeconomic policy issues will find this book to be a valuable addition to the literature." - Pierre Siklos, Wilfrid Laurier University, Canada

"This splendid work of scholarship will be of considerable interest to both economists and political scientists. The argument relates a specific rule-based monetary policy to inflation and output performance on the one hand, and to the expectations and activities around stable and predictable monetary policies." - William R. Keech, Carnegie Mellon University

"Innovative in the way it blends historical, mathematical, and statistical analyses and insightful in how it shows that rule-guided policy produced information coordination, Granato and Wong's book is a major contribution to political economy. The Role of Policymakers in Business Cycle Fluctuations will be a valuable resource to scholars who want to understand policy and macroeconomic outcomes in the United States in the Greenspan era and in the years to come." - John Freeman, University of Minnesota

"Based on rigorous models and compelling econometric evidence, Granato and Wong's argument is that low inflation and stability of output are mutually reinforcing, with accuracy of inflation expectations playing a key role in producing this outcome. The authors weave together impressive theoretical, historical, and statistical support for their thesis." - Henry Chappell, University of South Carolina

"This book provides an accessible and learned guide to the explosion of recent research on the modern theory of macroeconomic stabilization policy. The authors weave discussions of data, history, politics, and macroeconomic theory together in ways that emphasize the key role of private-sector expectations, and show how policymakers can play an important role in coordinating those expectations to minimize volatility." -James Bullard, Federal Reserve Bank of Saint Louis

"Granato and Wong forcefully challenge assumptions about how economic agents form and update their expectations in response to policymaker behavior. Combining insigns and methodologies from economics, statistics, and political science, they show how a policy emphasis on price stability contributes to sustained periods of economic growth. Their models of information, coordination, and learning represent the frontiers of political economy research. This work will serve as a touchstone for a generation of scholars interested in the political determinants of economic performance." - William Bernhard, University of Illinois, Urbana-Champaign

#### About the Author

Jim Granato is a Visiting Scientist and Political Science Program Director at the U.S. National Science Foundation (NSF). He is the author or co-author of numerous publications in academic journals such as American Journal of Political Science, Economics and Politics, Journal of Theoretical Politics, Political Analysis, Political Research Quarterly, and Public Choice. M. C. Sunny Wong is Assistant Professor of Economics at the University of Southern Mississippi. His primary research has focused on adaptive learning dynamics in monetary policy and he is also interested in the areas of foreign direct investment (FDI) and economic growth. Professor Wong has published research articles in journals such as the Southern Economic Journal, Political Reswarch Quarterly, and Journal of Macroeconomics.

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