

Monetary Equilibria in a Cash-in-Advance Economy with Incomplete Financial Markets

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Abstract

The general equilibrium model with incomplete financial markets (GEI) is extended by adding fiat money, fiscal and monetary policy and a cash-in-advance transactions technology. Existence and multiplicity of equilibria in such economies is studied under different combinations of fiscal and monetary policy: the central bank either pegs the interest rate or money supply while the fiscal authority sets a Ricardian or a non-Ricardian fiscal plan. We prove the existence of equilibria in all four scenarios. In Ricardian economies, the conditions required for these results are not more restrictive than in the standard GEI. In non-Ricardian economies, the sufficient conditions are slightly more demanding. It is shown that the equilibrium under a Ricardian fiscal policy does not determine the overall price level and the equivalent martingale measure.

Key Words: Money, Incomplete Markets, Monetary Policy, Fiscal Policy, Indeterminacy, Gains to Trade.

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