The Taylor Rule is (almost) Everywhere in Monetary Economics (but there is Still Room to Expand Market Share !)

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The Two Most Consequential Papers in Monetary Economics in last 75 Years

- Friedman (1968): Introduced natural rate of unemployment (u*) and natural rate of interest (r*), with a vertical long-run Phillips Curve.

- Taylor (1993): The Taylor Rule , the Taylor Principle, inflation targeting = 2

Friedman’s Framework

•u* and r* as economic destinations, not policy rule inputs.

•Advocated k-percent money growth rule, which worked better in theory than practice (1970s-1980s)

Taylor’s Framework

•Anchors nominal policy rate to neutral real interest rate (r*) plus inflation target.

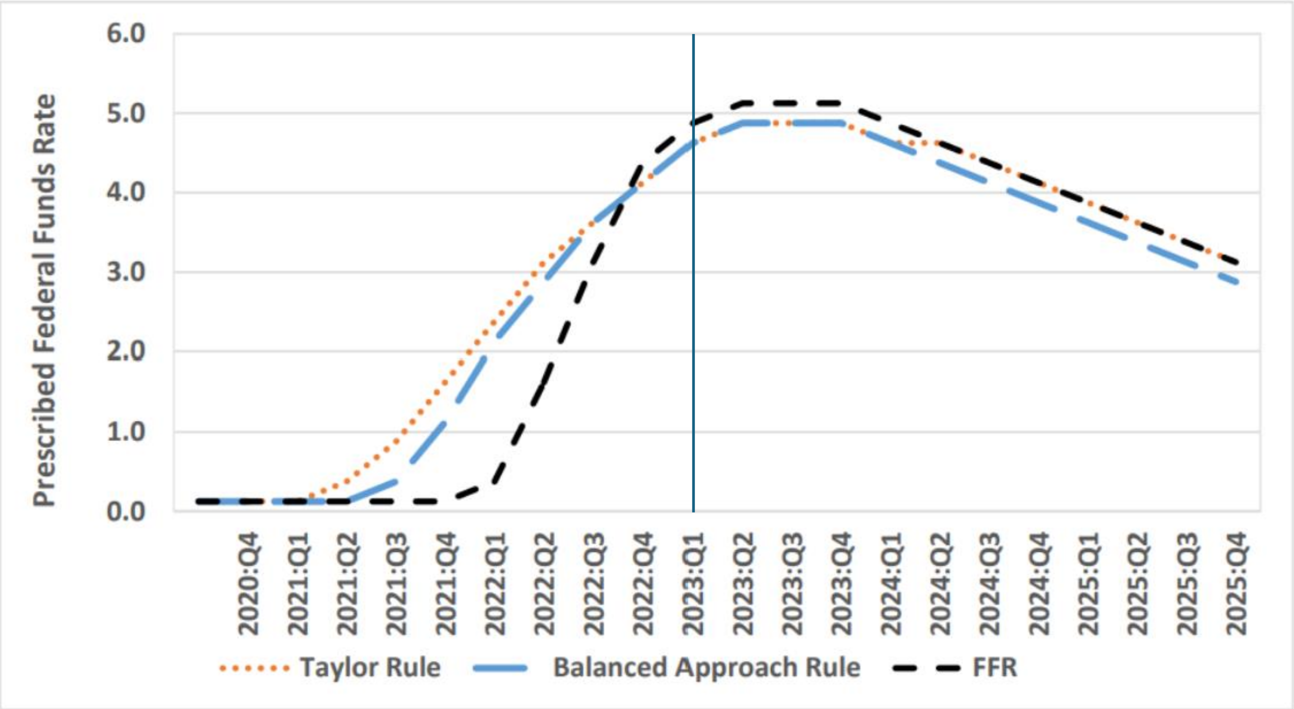
•Follows Taylor Principle: Raise nominal rate more than one-for-one when inflation exceeds target.

•Leans against output/unemployment gaps (u – u*) supporting price stability and dual mandate.

Taylor Rule is (almost) Everywhere

- Central to Woodford’s monetary and Cochrane’s fiscal theories of price level.
- Empirical benchmark for effective real world monetary policy (when not at zero lower bound).
- Optimal in New Keynesian models (CGG)
- Robust across macroeconomic specifications (CEE) and for open as well as closed economies
- Essential in Yield curve models and bond pricing (AP)
- Ubiquitous in central bank briefing books

Papell and Prodan suggest a straightforward way that policy rules be added to the existing SEP



There is much more to say but I am running out of time

So let me conclude by wishing the Taylor Rule a very happy 32nd birthday

….and another 75 years!