

Optimal Monetary Policy with Redistribution (joint with Wendy Morrison)

Abstract

We study optimal monetary policy in a general equilibrium economy with heterogeneous agents and nominal rigidities. Households differ in type-specific, statecontingent labor productivity and initial firmownership, yet markets are complete.

The fiscal authority has access to a linear tax schedule with non-state-contingent tax rates and uniform, lump-sum transfers. We show that when there are fluctuations in the labor skill distribution, it is optimal for monetary policy to target a state-contingent markup that covaries positively with a sufficient statistic for labor income inequality. In a calibrated version of the model, countercyclical earnings inequality implies countercyclical optimal markups. Therefore, to the extent that redistribution—and not insurance—is the distributional policy goal, optimal monetary policy is output destabilizing.