Lingnan University 嶺南大學 香港 Hong Kong

Faculty of Business 嶺南大學商學院

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Hong Kong Institute of Business Studies

OPTIMAL FISCAL POLICY: IMPLEMENTING A RAMSEY PLAN

ABSTRACT

Lucas and Stokey (1983) motivated governments to confirm an optimal tax plan by rescheduling government debt appropriately. Debortoli et al. (2021) showed that does not work when an initial government debt is so high that a Ramsey planner sets the tax rate above the peak of the Laffer curve. A Ramsey plan can be implemented even in that case by adding instantaneous debt to Lucas and Stokey's contractible subspace and requiring that continuation governments preserve the purchasing power of instantaneous debt. Using the purchasing-power-adjusted instantaneous debt balance as the state variable, we formulate a Ramsey plan with a Bellman equation and use it to study deterministic settings that feature right continuous with left limit (C`adl`ag) initial term debt structures and government spending processes. We extract implications about tax smoothing and effects of fiscal policies on bond prices.

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BIOGRAPHY

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Wei Jiang joined the Department of Industrial Engineering and Decision Analytics at the Hong Kong University of Science and Technology as an Assistant Professor in August 2019. He received Ph.D. in Quantitative Finance from National University of Singapore (2018), and both M.S. in Financial Mathematics (2012) and B.S. in Mathematics (2009) from Peking University. Prior to his Ph.D. study, he worked as a Financial Analyst in China Merchants Finance Holding Co., Ltd.

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