Discussion of
"Optimal policy and simple rules: A unified approach"
by Øistein Roisland and Tommy Sveen

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Oslo, June 24, 2010

Introduction

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- To do so: Modify loss function of policymaker.

Overview

1 Monetary policy under uncertainty

2 Approach of the paper

3 Selected results

4 Questions, (potential) issues and suggestions

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    $\implies$ Robust policy is found by solving a game between a policy maker who attempts to minimize loss and nature that chooses a model from the model space so as to maximize loss.
    $\implies$ No model probabilities need to be specified.

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  $\Longrightarrow$ Kuester and Wieland (2010): Such an agnostic policymaker [i.e. a policymaker that considers it impossible to define a sensible prior distributions over the model space] could instead ask how to insure herself against worst-case scenarios, i.e. worst-case models.

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  $\implies$ Goal of the paper: "Combine the best from these two worlds".

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    $\Longrightarrow$ Question: How does policy relate to robust policy derived from standard Bayesian approach?

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    $\implies$ Idea of minimax approach.

Selected results

- Interest rate rule in z_t is classic Taylor rule:

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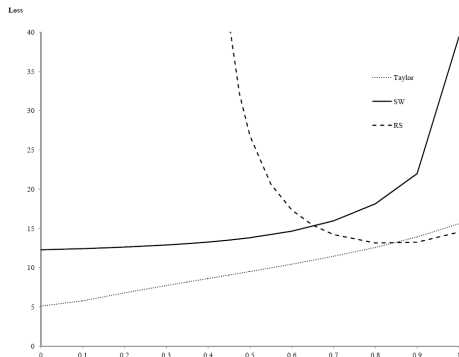
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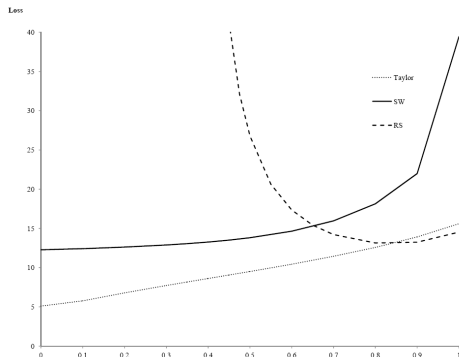
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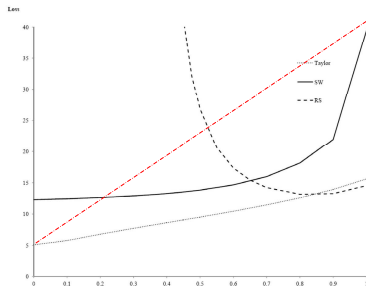

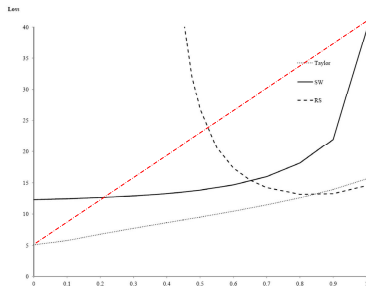Figure 1: Average loss evaluated in the alternative models as a function of the weight on the classical Taylor rule.

$\implies$ Recommendation: Policymaker should choose $\theta \in [0.4, 0.65]$.

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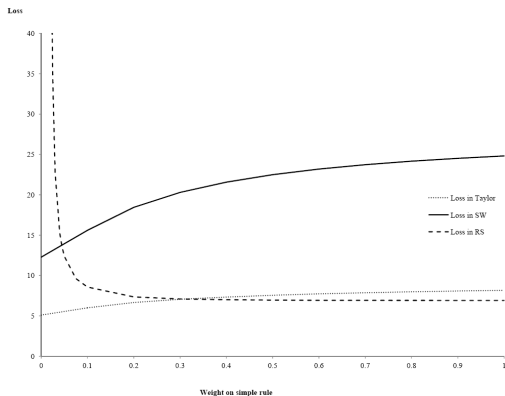
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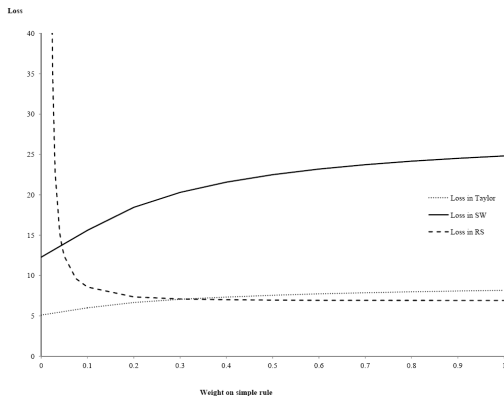
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$\implies$ Recommendation: Policymaker should choose $\theta \in [0.018, 0.045]$.

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- Use priors on alternative models?

$\implies$ Quasi-Bayesian approach?

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- Illustration of one potential problem with "worst-case scenario".

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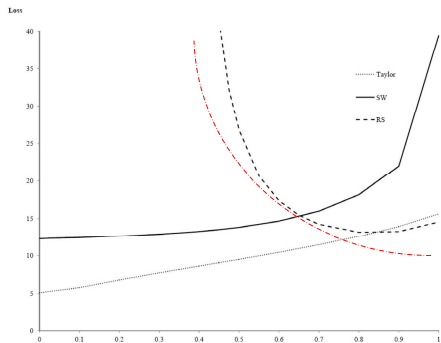
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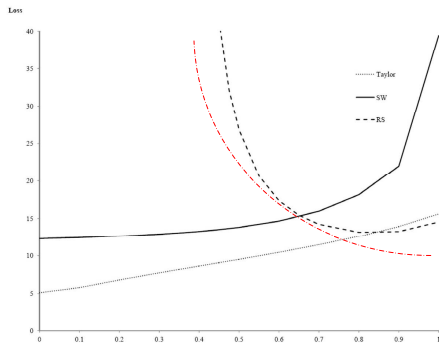- Interest rate rule in z_t is classic Taylor rule:

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$\implies$ Base worst-case scenario on RS model.

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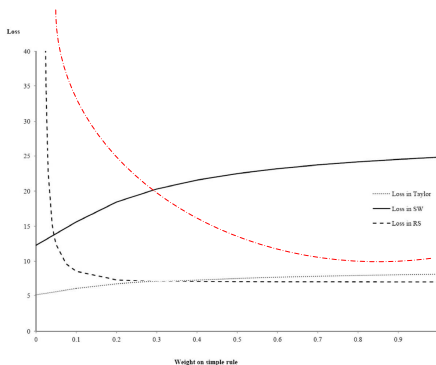- Interest rate rule in z_t is optimized simple interest rate rule from RS (1999) model.

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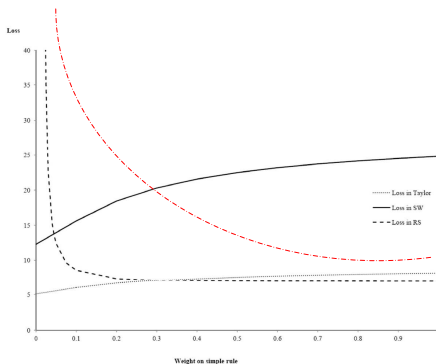- Interest rate rule in z_t is optimized simple interest rate rule from RS (1999) model:

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  $\Longrightarrow$ Specific to chosen approach?