6. Easy Monetary Policy: Effectiveness and Limits

6.1 Shock and Gradual Monetary Policy.

We begin the positive part of our analysis with a more expansive monetary policy that pushes the overall level of interest rates toward the low end. The measurements that emerge from this analysis refer, first, to the aggregate data for the 12 countries of the Monetary Union, and then to the "two Europes" (or three, as suggested in Chapter 4 of the book). In this context we evaluate the possibilities that can be offered to the different national realities by a more expansive monetary policy put in place for everyone by the ECB.

Precisely, we will measure the macroeconomic performances in reference in particular to five indicators: the rate of growth, the rate of unemployment, inflation, the government deficit and the government debt. Additional considerations and further details can be obtained from the analytical results reported in the Appendix.2

As regards monetary policy, we will take a look at two possible scenarios. In the first case, the European Central Bank “instantly” reduces the entire current system of interest rates by two percentage points (we denote this case as shock monetary policy or as a cold turkey monetary policy). A second case refers to the possibility in which the

---

1 The aggregate statistics for the 12 countries of the Monetary Union are defined as follows. The rate of GDP growth is equal to the growth rate of the sum of GDP levels in every country, calculated in Euro. The aggregate inflation rate is defined as the rate of growth of the sum of the consumer price indices in every country, and the rate of unemployment as the relationship between the number of jobless in the 12 countries and the size of the work force in the corresponding countries.

2 Precisely, the Appendix shows detailed tables containing selected macroeconomic variables concerning the domestic, the foreign, the monetary and the real side of each country economy.
reduction in interest rates, still by 2 points, is put in place gradually over the space of five years (we call this *gradual monetary policy*).

### 6.2 The Impact on Euroland.

Figure 6.1 and Figure 6.2 show the impact of the two economic policy interventions on all the member countries of the Union, while considering the expansions patterns of aggregate series for GDP and unemployment rate.

The darker line (with boxes) refers to the *Shock Monetary Policy*, the lighter line (with balls) represents the *Gradualist Monetary Policy*, while the dashed one (with triangles) is the *Baseline simulation*. Source: Authors’ Simulation with Oxford Economic Forecasting Model (release 2.0).

**Figure 6.1 Easy Monetary Policy: GDP Growth Rate in Euroland**