

Macroeconomic instability, government budgetary policy and overlapping generations economy

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ABSTRACT

Using Reichlin's overlapping generations model (1986) with capital-labor substitution as studied in Cazzavillan (2001), this paper explores how government budgetary policies, that is, endogenous capital income taxes vs the fixed tax rate on capital income influence the occurrence of macroeconomic instability such as indeterminacy, local bifurcations and multiple steady states, depending on the elasticity of capital-labor substitution. As is well understood in Ramsey optimal growth model, it will be shown that the fixed income tax rate is strongly recommended relative to endogenous income taxes from the view of macroeconomic stability.

J.E.L. Classification:

Key words: Indeterminacy, Hopf-, Flip-, transcritical and saddle-node bifurcations, multiple steady states, government budgetary policies and overlapping generations model
