Robust Monetary Policy Under Deep Parameter Uncertainty [*]

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Abstract

In the real world, policy decisions need to be made under considerable uncertainty about the functioning of the economy. Policymakers often have to set their instrument without knowing the true model of their economy, or how their policies will work and affect the variables that they care about. This paper demonstrates the effect of uncertainty about deep parameters in DSGE models on the property of robust monetary policy. We classify the role of parameter uncertainty into the following two categories, (i) uncertainty about the impact of policy to stabilize the target variables, (ii) uncertainty that is related to the inertia of target variables. By dividing the target of uncertainty in this way, we succeed to show the essential reason why different previous papers make different conclusions about the property of robust policy against parameter uncertainty.

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