Comment on Jordi Galí: Monetary Policy and Bubbles in a New Keynesian Model with Overlapping Generations

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- Relatively small departure from conventional NK model suffices to admit bubbles.
- Consider stochastic bubbles of two kinds:
  - The unstable solutions that arise in the model's bubble region.
  - Stochastically popping (but otherwise stably growing) bubbles near the low-interest bubble-free region.
- Clear and simple policy recommendation, confirming Galí (AER 2014) in a more relevant business cycle setting: Aggressively stabilize inflation (don't lean directly against the bubble).

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4. Why can't we have (more) determinacy by fixing the target for the long-run real interest rate?

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    - Different from Domeij-Ellingsen; we study the transition paths following a single large bubble shift.

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  - The mortality of individuals (OLG) not really important.
  - The key is the incomplete asset market; can't buy stocks of all nonexistent firms: This is realistic!
- Hence, present framework is a justified simplification – it's the Santos-Woodford requirements that are too strong.

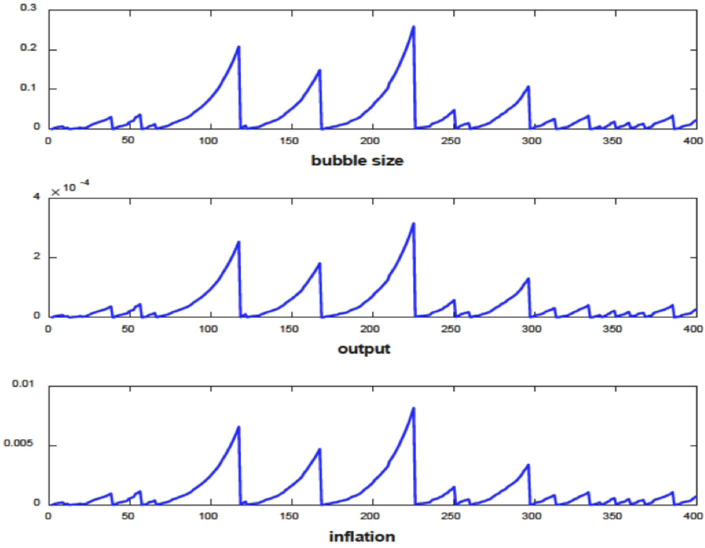

Figure: 5