

Money Creation in a Random Matching Model*

Alexei Deviatov[†]
The New Economic School

November 7, 2006

Abstract

I study money creation in versions of the Trejos-Wright (1995) and Shi (1995) models with indivisible money and individual holdings bounded at two units. I work with the same class of policies as in Deviatov and Wallace (2001), who study money creation in that model. However, I consider an alternative notion of implementability—the ex ante pairwise core. I compute a set of numerical examples to determine whether money creation is beneficial. I find beneficial effects of money creation if individuals are sufficiently risk averse (obtain sufficiently high utility gains from trade) and impatient.

JEL classification: E31.

Keywords: inflation; Friedman rule; optimal monetary policy.

*I would like to thank Neil Wallace for his constant guidance and support with this project. I am also grateful to Dmitry Dolgopyat, Sergei Izmalkov, James Jordan, Thomas Sjöstrom, and to the participants of the Workshop on Money, Banking, and Payments at the Federal Reserve Bank of Cleveland (August 2004) for their valuable comments.

[†]Address: 47 Nakhimovskii Ave., room 1721, The New Economic School, Moscow, 117418, Russian Federation. Tel.: (7 495) 129-1700; fax: (7 495) 129-3722; e-mail: deviatov@nes.ru.