JOURNAL ARTICLE

Common agency with Rational Expectations: Theory and Application to a Monetary Union

Get access

,

The Economic Journal, Volume 113, Issue 489, July 2003, Pages 539–549,
https://doi.org/10.1111/1468-0297.t01-1-00143
Published: 10 July 2003 **Article history** ▾

Abstract

We extend the theory of common agency to the situation where the principals' payoffs are affected by their *ex ante* expectations of the agent's *ex post* choice. We show how the usual truthful schedules must be modified to account for the rational expectations constraint. We apply the model to a monetary union where member governments influence the policy of the common central bank using incentive contracts. We examine how the outcomes depend on different delegated objectives of the bank, and find that some often-advocated rules create an excessive deflationary bias.

Issue Section: Articles