

Outline for Course on Macroeconomics (II)

Course Given By: Ethan Kaplan ekaplan@econ.berkeley.edu
Heather Congdon Fors heather.congdon@economics.gu.se

Brief Course Description: This course is the second-half of the introductory Macroeconomics Ph.D. sequence at Gothenburg University. Whereas the first half of the course focuses on growth theory and the theory of fluctuations, this half will focus on the theory of unemployment, monetary policy, and international macroeconomics. The main questions which the course addresses are: what are the causes of unemployment and how can monetary and fiscal policy be used to reduce unemployment? There will also be a small empirical section on macro-econometrics. The course is divided into 12 lectures, covering 9 topics. We begin with an empirical overview of the Great Depression in the United States when unemployment was extremely high and growth very low for many years as well as the experience with “Euroscleurosis” with high unemployment and moderate growth in countries such as Spain during the 1980s and early 1990s. In section II, we move on to the neo-classical synthesis of the Keynesian model. Section III discusses the underlying assumptions about price rigidity made by the neo-classical synthesis of the Keynesian model. Much of modern neo-Keynesian macroeconomics in the 1980s and into the 1990s has focused on “micro-founding” macroeconomic models with price rigidity. Section IV then moves to a more detailed discussion of micro-founded theories of unemployment. Section V discusses the role of monetary policy in reducing unemployment, covering both the Keynesian Phillips curve as well as the Lucas Supply Curve explanations for the observed negative relationship between unemployment and inflation. Section VI turns to a discussion of empirical macro-econometrics, with a particular focus on identifying the role of monetary policy on unemployment reduction. Section VII discusses modern developments in monetary theory and the conduct of monetary policy with particular focus on inflation targeting, central bank independence, central bank transparency, interest rate rules, and seignorage. Section VIII examines the impact of monetary and fiscal policy in an international environment, discussing both the Mundell-Fleming result about the relative power of monetary and fiscal policy in flexible versus fixed exchange rates as well as the overshooting result of Dornbusch concerning the over-reaction of exchange rates to changes in the money supply. Lastly, Section IX concludes by discussing the importance of and sources of nominal as well as real rigidities in generating theories of non-neutral monetary policy.

Course Requirements: Grading will be based upon 4 homework assignments, a final exam, and class participation. The grade breakdown will be: 60% homework and 40% final examination.

Course Arrangement: The course has an instructor (Ethan Kaplan) and a section leader (Heather Congdon Fors).

Course Schedule:

Tuesday, April 5th 10-13: Lecture 1 -	Ethan Kaplan: Sections I, II
Wednesday, April 6th 10-13: Lecture 2 -	Ethan Kaplan: Sections II, III
Thursday, April 7th 10-13: Lecture 3 -	Ethan Kaplan: Section IV
Tuesday, April 19th 10-13: Lecture 4 -	Ethan Kaplan: Section IV (Homework #1 Due in Class)
Wednesday, April 20th 10-13: Lecture 5 -	Ethan Kaplan: Section V
Thursday, April 21st 10-13: Exercise 1 -	Heather Congdon Fors
Tuesday, May 3rd 10-13: Lecture 6 -	Ethan Kaplan: Section VI (Homework #2 Due in Class)
Wednesday, May 4th 10-13: Lecture 7 -	Ethan Kaplan: Section VI
Monday, May 16th 10-13: Exercise 2 -	Heather Congdon Fors
Tuesday, May 17th 10-13: Lecture 8 -	Ethan Kaplan: Section VII (Homework #3 Due in Class)
Wednesday, May 18th 10-13: Lecture 9 -	Ethan Kaplan: Section VII
Thursday, May 19th 10-13: Exercise 3 -	Heather Congdon Fors
Wednesday, May 25th 10-13: Lecture 10 -	Ethan Kaplan: Section VIII
Tuesday, May 31st 10-13: Lecture 11 -	Ethan Kaplan: Section VIII/IX
Wednesday, June 1st 10-13: Lecture 12 -	Ethan Kaplan: Section IX (Homework #4 Due in Class)
Wednesday, June 1st 14-17: Exercise 4 -	Heather Congdon Fors

Topic Outline

(** refers to required reading)

- (I.) Data on Macro: Great Depression and European “Euroscleurosis”**
 - (1.) ** Solon, Gary, Robert Barsky and Jonathan Parker, “Measuring the Cyclicity of Wages: How Important is Composition Bias?”, *Quarterly Journal of Economics*, (Feb., 1994), pp. 1-25.
 - (2.) ** Chapters 5.5, 5.6 of Romer Text.
 - (3.) ** Time Series Data Sheets (Handouts).

- (II.) Classical Model:**
 - (1.) **Chapter 5.1 of Romer Text.

- (III.) Different Assumptions About Price Rigidity (Output, Capital, Labor):**
 - (1.) ** Chapter 5.3 of Romer Text.

- (IV.) Unemployment**
 - a. Definition
 - b. General Equilibrium Approach
 - c. Efficiency Wage:

- (1.) **Shapiro, Carl and Joseph Stiglitz, “Equilibrium Unemployment As a Worker Disciplining Device”, *American Economic Review* (June, 1984), pp. 433–444.
- (2.) Chapters 9.2, 9.3, and 9.4 of Romer Text.
- d. Implicit Contracts
 - (1.) **Chapter 9.5 of Romer Text.
- e. Insider/Outsider
 - (1.) **Chapter 9.6 of Romer Text.
- f. Search
 - (1.) **Diamond, Peter, “Aggregate Demand Management in Search Equilibrium”, *Journal of Political Economy*, (Oct., 1982), pp. 881-894.
 - (2.) Chapter 9.8 of Romer Text.
- g. Hysteresis
 - (1.) Blanchard, Olivier and Lawrence Summers, “Hysteresis in Unemployment”, *NBER Working Paper 2035*, (1986).
 - (2.) **Chapter 9.7 of Romer Text.
- h. Aggregate Demand
 - (1.) Blanchard, Olivier and Nobuhiro Kiyotaki, “Monopolistic Competition and the Effects of Aggregate Demand”, *American Economic Review*, (September, 1987), pp. 647-666.
 - (2.) Cooper, Russell and Andrew John, “Coordinating Coordination Failures in Keynesian Models”, *Quarterly Journal of Economics*, (August, 1988), pp. 441-463.
 - (3.) Weitzman, Martin, “Increasing Returns and the Foundation of Unemployment Theory”, *Economic Journal*, (Dec., 1982), pp. 787-804.

(V.) Philips Curve, Inflation and Monetary Policy I

- a. Phillips Curve: Phillips Curve w/ Monetary Policy: Empirics and Explanations
 - (1.) Phillips, A. W., “The Relation Between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom, 1861-1957”, *Economica*, (Nov., 1958), pp. 283-299.
 - (2.) **Chapter 5.4 of Romer Text.
- b. Lucas Supply Curve and Critique of Lucas Supply Curve:
 - (1.) Lucas, Robert E., “Expectations and the Neutrality of Money”, *Journal of Economic Theory*, (1972: 4), pp. 103-124.
 - (2.) **Chapters 6.1-6.3 of Romer Text.
 - (3.) **Mankiw, N. Gregory, “The Inexorable and Mysterious Tradeoff Between Inflation and Unemployment”, Mimeo, (2000), <http://post.economics.harvard.edu/faculty/mankiw/papers/royalpap.pdf>
 - (4.) Woodford, Michael, “Imperfect Common Knowledge and the Effects of Monetary Policy”, Mimeo, 2001, <http://www.princeton.edu/~woodford>.

(VI.) Empirics of Monetary Policy

- a. Traditional
 - (1.) **Phillips, A. W., “The Relation Between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom, 1861-1957”, *Economica*, (Nov., 1958), pp. 283-299.
 - (2.) **Chapter 6.3 of Romer Text.
- b. Lucas Critique
 - (1.) **Lucas, Robert E., “Econometric Policy Evaluation: A Critique”, *Carnegie-Rochester Conference Series on Public Policy*, (1976), pp. 19-46.
- c. VARS:
 - (1.) Rudebusch, Glenn, “Do Measures of Monetary Policy in a VAR Make Sense?”, *International Economic Review*, (Nov., 1998), pp. 907-931.
 - (2.) Sims, Christopher, “Money, Income, and Causality”, *American Economic Review*, (Sep. 1972), pp. 540-552.
 - (3.) **Sims, Christopher, “Macroeconomics and Reality”, *Econometrica*, (Jan. 1980), pp. 1-48.
 - (4.) **Stock, James and Mark Watson, “Vector Autoregressions”, *Journal of Economic Perspectives*, (Autumn, 2000), pp. 101-115.
- d. Other Identification Mechanisms:
 - (1.) **Prescott, Edward, “Theory Ahead of Business Cycle Measurement”, *Carnegie-Rochester Series on Public Policy*, (1986: 25), pp. 11-44.
 - (2.) **Romer, Christina and David Romer, “Does Monetary Policy Matter? A New Test in the Spirit of Friedman and Schwarz”, *NBER Macroeconomics Annual*

(VII.) Monetary Policy II

- a. Review of Keynesian Theory
 - (1.) Chapter 5.1 of Romer Text.
- b. Costs of Inflation
 - (1.) Chapter 10.9 of Romer Text.
- c. Conservative Central Bankers
 - (1.) Barro, Robert, “Reputation in a Model of Monetary Policy With Incomplete Information”, *Journal of Monetary Economics*, (Jan., 1986), pp. 3-20.
 - (2.) **Rogoff, Kenneth, “The Optimal Degree of Commitment to a Monetary Target”, *Quarterly Journal of Economics*, (Nov., 1985), pp. 1169-1189.
 - (3.) **Chapters 10.4-10.5 of Romer Text.
- d. Critiques of Rational Expectations:
 - (1.) Woodford, Michael, “Imperfect Common Knowledge and the Effects of Monetary Policy”, Mimeo, 2001, <http://www.princeton.edu/~woodford>.

- e. Central Bank Transparency
 - (1.) Morris, Stephen and Hyun Shin, "Social Value of Public Information", *American Economic Review*, (December, 2002), pp. 1521-1534.
 - (2.) **Svensson, Lars, "Social Value of Public Information: Morris and Shin (2002) Is Actually Pro Transparency, Not Con", February 2005, <http://www.princeton.edu/~svensson/>
- f. Interest Rate Rules
 - (1.) **Taylor, John, "Discretion Versus Policy Rules in Practice", *Carnegie-Rochester Series on Public Policy*, (1993: 39), pp. 195-214.
 - (2.) **Taylor, John, "An Historical Analysis of Monetary Policy Rules", *NBER working paper 6768*, (Oct., 1998).
- g. Inflation Targeting
 - (1.) **Bernanke, Benjamin and Mark Gertler, "Inflation Targeting: A New Framework for Monetary Policy?", *Journal of Economic Perspectives*, (Spring, 1997), pp. 97-116.
 - (2.) **Chapter 10.7 of Romer Text.
- h. Seignorage: Developed and Less Developed Countries, the WTO, and the World Bank/IMF
 - (1.) **Chapter 10.8 of Romer Text.

(VIII.) International

- a. Mundell-Fleming
 - (1.) **Chapter 5.2 of Romer Text.
- b. Overshooting
 - (1.) Dornbusch, Rudiger, "Expectations and Exchange Rate Dynamics". *Journal of Political Economy*, (Dec., 1976), pp. 1161-1176.
 - (2.) Eichenbaum, Martin and Charles Evans, "Some Empirical Research on the Effects of Monetary Policy Shocks on Exchange Rates", *Quarterly Journal of Economics*, (Nov., 1995), pp. 975-1009.

(IX.) Real Rigidities and Nominal Rigidities

- a. Real Rigidities
 - (1.) **Blanchard, Olivier and Nobuhiro Kiyotaki, "Monopolistic Competition and the Effects of Aggregate Demand", *American Economic Review*, (September, 1987), pp. 647-666.
 - (2.) **Cooper, Russell and John Andrew, "Coordinating Coordination Failures in Keynesian Models", *Quarterly Journal of Economics* (August, 1988), pp. 441-463.
 - (3.) **Chapters 6.4 and 6.11 in Romer Text.

b. Nominal Rigidities

(1.) Mankiw, N. Gregory, "Small Menu Costs and Large Business Cycles: A Macroeconomic Model of Monopoly", *Quarterly Journal of Economics*, (May, 1985), pp. 529-539.

(2.) Mankiw, N. Gregory and Ricardo Reis, "Sticky Information Versus Sticky Prices: A Proposal to Replace the New Keynesian Phillips Curve", *Quarterly Journal of Economics*, (Nov., 2002), pp. 1295-1328.

(3.) Taylor, John, "Staggered Wage Setting in a Macro Model", *American Economic Review*, (May, 1979), pp, 108-113.

(4.) **Chapters 6.8 and 6.9 of Romer Text.