

The International College of Economics and Finance

Syllabus for Microeconomics - 2

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Classteachers: Alla A. Friedman, Petr A. Schekochikhin

Course description

Macroeconomics-2 is a one-semester course and it is taught for the third year students in Spring semester. The course focuses on the microeconomics foundations of macroeconomics, demand management policy, the neo-classical (Solow) growth model, inflation and unemployment.

The course is taught in English. The students are also studying for Russian degree in Economics, and knowing Russian terminology through reading in Russian is also required.

Course prerequisites

Students are supposed to be competent in basic economic analysis up to the level of the Introductory Macroeconomics and in calculus taught in the first and second years of studies. Students are also expected to be familiar with constrained optimization studied in the course of Mathematics for Economists during the second year of study and basic game theory tools studied in the course of Microeconomics during the third year.

The course itself provides a basis (and so serves as a prerequisite) for such courses as Monetary Economics, International Economics, Development Economics.

Course objectives

The purpose of the course is to develop the economic way of thinking and make them ready to use logic and methods of economic analysis in their further studies. Specifically the course aims at:

- giving students a solid grasp of macroeconomic analysis at the intermediate-level using both graphical and algebraic techniques;
- ensuring students can apply macroeconomic analysis to the study of contemporary and historical economic problems;
- broadening the students' knowledge in the field of macroeconomics,
- developing the students' abilities to write essays and understand and critically discuss economic literature.

Forms or control and grade determination

Control takes the following forms:

- ⇒ written home assignments (5-7);
- ⇒ essay;

- ⇒ mid-term exam (in the University of London examination format) in the middle of the Spring semester;
- ⇒ University of London exam by the end of the Spring semester.

Course grade is determined by

- ⇒ University of London exam grade (50%),
- ⇒ Mock exam grade (30%),
- ⇒ home assignments (15%);
- ⇒ essay (5%).

Literature

Main texts

1. Macroeconomics. Subject Guide. University of London, 2012.
<https://emfss.elearning.london.ac.uk/course/view.php?id=138>
2. Blanchard O., Macroeconomics. 5Ed. Prentice Hall. 2009. [B]
<http://vig.prenhall.com/catalog/academic/product/0,1144,0131860267-SS,00.html> OR
Blanchard O., Giavazzi F., Amighini A. Macroeconomics: A European Perspective. Financial Times Press, 2010 (Russian translation: О.Бланшар, Макроэкономика, Изд.дом ВШЭ, 2010)
3. Dornbusch R., S. Fischer and R.Startz, Macroeconomics. 10ed. McGraw-Hill, 2008. (DFS)
http://highered.mcgraw-hill.com/sites/0072823402/information_center_view0/
4. Mankiw, N.G., Macroeconomics, 7ed. Worth Publishers. 2010. (M) (Russian translation: Н.Г.Мэнкью, Макроэкономика. Изд-во МГУ, 1994).
<http://bcs.worthpublishers.com/mankiw7/>

Supplementary reading:

1. Mankiw G., A Quick Refresher Course in Macroeconomics, Journal of Economic Literature, 1990, 28, 1645-1660.
2. Pentecost E., Macroeconomics: an open economy approach. Palgrave Macmillan, first edition, 2000.
3. Romer D. Advanced Macroeconomics. McGraw Hill Book Company: London, 4th ed, 2011.

Internet resources

VLE (Online Library of the University of London) <http://my.londoninternational.ac.uk>

Current course materials are posed at the ICEF information system <http://mief.hse.ru>

Key macroeconomic indicators <http://www.economagic.com/>

Russian Federation statistic agency <http://www.gks.ru/>

Central Bank of Russian Federation statistic agency <http://cbr.ru/>

Students supplement to textbook Dornbush R., S. Fisher and R.Starz., Macroeconomics. 10 ed. McGraw-Hill, 2008.

http://highered.mcgraw-hill.com/sites/0072823402/student_view0/index.html

Students' resources to accompany Mankiw, N.G., *Macroeconomics*, 7ed. Worth Publishers. 2010. <http://bcs.worthpublishers.com/mankiw7/>

Course outline

1. Aggregate demand in closed economy: IS-LM model (review)

Goods market and IS curve derivation. Assets market and LM curve derivation. Equilibrium in IS-LM model. Effectiveness of fiscal and monetary policies.

(DFS Ch.9-11, 19; B Ch.3-5; M Ch.10-11)

Further reading

Romer D., Keynesian Economics without the LM curve, *Journal of Economic Perspectives* 14, pp.149-169, 2000.

Hoshi T., A.K.Kashyap, Japan's Financial Crisis and Economic Stagnation, *Journal of Economic Perspectives*, 18 (1), 2004, pp. 3-26.

Ludvigson S.C., Consumer Confidence and Consumer Spending, *Journal of Economic Perspectives*, 18 (2), 2004, pp.29-50.

2. Aggregate demand in an open economy: the IS-LM-BP Model

The IS curve in an open economy. The foreign exchange market and exchange rate terminology. The BP curve and capital mobility. Macroeconomic policy under imperfect capital mobility (comparison with perfect capital mobility and capital control). Exchange rate crisis.

(DFS Ch.12, 20; B Ch.18-21; M Ch.5, 12)

Further reading

Calvo G., F.S.Mishkin, The mirage of exchange rate regimes for emerging market countries, *Journal of Economic Perspectives* 17(4), pp.99-118, 2003.

Mann C.L., Perspectives on the US current account deficit and sustainability, *Journal of Economic Perspectives* 16(3), pp.131-152, 2002.

3. Unemployment and the AD-AS model

Labour market: key concepts (labour force, unemployment rate, participation rate).

The types and causes of unemployment: frictional, structural and classical (or real wage) unemployment. Hysteresis.

The aggregate supply (AS) curve. The long run aggregate supply curve and short run AS curve.

Explanations of upward sloping short run aggregate supply curve. Sticky wages (Keynesian) model. Classical worker misperception model, new Keynesian sticky price model, new classical imperfect information model of short run AS. Expectations and short run AS.

The aggregate demand curve. Explanations of the slope.

Equilibrium in aggregate supply- aggregate demand model. Monetary and fiscal policy in the long run and in the short run. Supply shocks.

(DFS Ch.5,7, 10.4; B Ch.6-7, 13; M Ch.6, 9, 11(Appendix), 13.1)

Further reading

Ball L., N.G.Mankiw, The NAIRU in theory and practice, *Journal of Economic Perspectives*, 16(4) pp.115-136, 2002.

Blanchard O., European unemployment: The evolution of facts and ideas, *NBER Working Paper*, N11750, 2005.

Davis S.J., R.J.Faberman, J. Haltiwanger, The flow approach to labour markets: new data sources and micro-macro links, *Journal of Economic Perspectives* 20 (3), pp.3-26, 2006.

Yellen J., Efficiency wage models of unemployment, *American Economic Review*, 74, May, 1984.

Lucas R., Understanding business cycles, in Estrin S., A.Marin, *Essential Readings in Economics*, Chapter 16, MacMillan Press 1995.

Zarnowitz V., Theory and history behind business cycle: Are the 1990s the onset of the golden age? *Journal of Economic Perspectives*, 13(2), pp.69-90, 1999.

4. Demand management policy

Aggregate demand (AD) shocks. Responses to AD shocks: non-intervention, activist policy. Time lags (inside and outside). Lucas critique.

Policy ineffectiveness proposition.

Monetary policy: targets and instruments.

Rules versus discretion. Time inconsistency problem. Solutions for time-inconsistency problem: constitutional rules, reputation, delegation to an independent authority with different preferences/incentives (independent central banker).

Examples of monetary policy rules.

(DFS Ch.16-17; B Ch.17,23-26; M Ch.4,14-15)

Further reading

Alesina A., The political economy of the budget surplus in the United States, *Journal of Economic Perspectives*, 14(3), pp.3-19, 2000.

Bernanke B.S., F.S.Mishkin, Inflation targeting: a new framework for monetary policy? *Journal of Economic Perspectives*, 11(2), pp.97-116, 1997.

Chari V., J.K.Patrick, Modern macroeconomics in practice: how theory is shaping policy, *Journal of Economic Perspectives*, 20(4), pp.3-28, 2006.

Fisher S., R.Sahay, C.A.Vegh, Modern hyper- and high inflations, *Journal of Economic Literature*, 40(3), pp.837-880, 2002.

Modigliani F., The monetarist controversy, or, should we forsake stabilization policies? *American Economic Review*, 67(2), pp. 1-17, 1997.

Sargent T.J., N. Wallace, Rational Expectations and the Theory of Economic Policy, *Journal of Monetary Economics*, July 1976, pp.199-214.

Taylor J.B. An historical analysis of monetary policy rules, *NBER working paper*, w6768, 1998 (<http://papers.nber.org/papers/w6768>)

Taylor J.B. Reassessing discretionary fiscal policy, *Journal of Economic Perspectives*, 14(3), pp.21-36, 2000.

5. Inflation and Unemployment

Phillips curve. AD-AS model in the long run. Inflation in the long run.

Inflation in the short run.

The costs and benefits of inflation. Seignorage.
The cost of disinflation policy. Rational expectations and Lucas critique.
(DFS Ch.6-7, 11.1-11.2, 19.3; B Ch. 8-9, 14.3-14.4, 22, 25.1; M Ch.4, 13.2)

Further reading

Barsky R.B., L.Kilian, Oil and macroeconomy since the 1970s, *Journal of Economic Perspectives*, 18 (4), pp.115-134, 2004.
Svensson L.E., Escaping from a liquidity trap and deflation: The foolproof way and others, *Journal of Economic Perspectives*, 17 (4), pp.145-166, 2003.
Tobin J., Inflation and unemployment, *American Economic Review*, 62 (1), pp.1-18, 1972.

5. The Neoclassical (Solow) Growth Model

Factors of economic growth, Solow residual.
Stylized facts of economic growth.
Assumptions of the Solow model. Derivation of the capital accumulation equation.
Steady state. Comparative statics (predictions of the model): changes in saving rate, in population growth rate, etc.
The golden rule of capital accumulation.
Solow model with labour augmenting technological progress.
Endogenous growth theory.
(DFS Ch.3-4; B Ch.10-12; M 3.2, 7-8)

Further reading

Barro R.J., X.Sala-i-Martin, *Economic Growth*, McGraw-Hill, 1995 (Introduction).
Baumol W., Productivity growth, convergence, and welfare: What the long-run data show, *American Economic Review*, 76 (5), pp.1072-1085, 1986.
Bosworth B., S.M.Collins, Accounting for growth: comparing China and India, *Journal of Economic Perspectives*, 22(1), pp. 45-66, 2008.
Easterlin R.A., The worldwide standard of living since 1800, *Journal of Economic Perspectives*, 14 (1), pp.7-26, 2000.
Charles J., *Introduction to economic growth*, second edition, Norton 2002, Chapters 1-4.
Romer P., The origins of endogenous growth, *Journal of Economic Perspectives*, 8(1), pp. 3-22, 1994.

6. Microfoundations of aggregate consumption

Keynesian consumption function and Kuznets puzzle. Intertemporal choice model. Life Cycle and Permanent Income theories. PIH under rational expectations.
Barro-Ricardo equivalence. Reasons for the failure of Barro-Ricardian equivalence.
Fiscal policy. Implications of Barro-Ricardo equivalence.

(DFS Ch.13, B Ch.16, 26.2; M Ch.15.4, 16)

Further reading

Barro R., Are Government Bonds Net Wealth? *Journal of Political Economy*, December 1974, pp.1095-1117.

Hall R., Stochastic Implications of the Life Cycle-Permanent Income Hypothesis: Theory and Evidence, *Journal of Political Economy*, December, 1978.

Modigliani F., Life cycle, individual thrift, and the wealth of nations, *American Economic Review* 76(3), pp. 297-313, 1986.

7. Microfoundations of aggregate investment

Yield to maturity and term structure of interest rates. Stock market and the price of stock. Keynesian theory on aggregate investment. The components of investment spending. Neoclassical model of investment. Accelerator models of investment. Tobin's q-theory. (DFS Ch.14, 18.1-18.2; B Ch.14-16; M Ch.4, 17.1)

Further reading

Hall R., D.Jorgenson, Tax policy and investment behaviour, *American Economic Review* 57(3), pp. 391-414, 1967.

8. Money demand and money supply

Functions of money. The transactions demand (Baumol-Tobin model). The speculative theory of money demand: demand for money as a safe asset. The modern quantity theory of money. The monetary base and the money supply. The money multiplier model. Control of the central bank over the money supply. (DFS Ch.15-16; B Ch.4; M Ch.4, 18)

Further reading

Baumol W., The transaction demand for cash: an inventory theoretic approach, *Quarterly Journal of Economics*, 66, pp.545-556, 1952.

Friedman M. (1968) "The Role of Monetary Policy". *American Economic Review*, 58, pp. 1-17.

Tobin J., Liquidity preference as a behaviour towards risk, *Review of Economic Studies*, 25, pp.65-86, 1958.

Essay requirements

Each student is expected to write an essay in Macroeconomics. This should be done as a group assignment. The groups are assigned by the class teacher.

Essay should be on one of the topics considered in the course. The idea is to take the model (approach) presented in the course and illustrate how it can be applied.

Group is expected to write a short essay (about 1000 words), make 5-10 minutes presentation and answer questions. Every member of the team (unless he/she officially refuses from participation and gets 0 for the essay) is expected to demonstrate his/her involvement in the project.

You may use additional materials as necessary but all these materials should be mentioned in references and handed in together with the essay.

Distribution of hours of the course by topics and types of work

№	Topic	Total	Lectures	Classes	Selfstudy
1.	Aggregate demand in closed economy: IS-LM model	14	2	2	10
2.	Aggregate demand in an open economy: the IS-LM-BP model	28	4	4	20
3.	Unemployment and the AD-AS model	28	4	4	20
4.	Demand management policy	28	4	4	20
5.	Inflation and Unemployment	28	4	4	20
6.	The Neoclassical (Solow) Growth Model	28	4	4	20
7.	Microfoundations of aggregate consumption	24	4	4	16
8.	Microfoundations of aggregate investment	14	2	2	10
9.	Money demand and money supply	24	4	4	16
	Total:	216	32	32	152