

Anderson Graduate School of Management
UCLA

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MGMT 406

THE GLOBAL ECONOMY

Spring 2014

The purpose of this course is to develop the analytical framework required for understanding the way changing macroeconomic conditions in the *world economy* affect the environment faced by modern decision makers and business leaders. Issues related to central banks' behavior (quantitative easing, interest rate adjustment and other), economic growth, inflation, interest rates behavior, exchange rates determination, global competitiveness, unemployment and the external sector (international reserves and the like) will be explored. At the end of the course it is expected that students will be able to critically assess how possible developments in the world economy -- such as the change in the monetary policy stance by the European Central Bank or the Federal Reserve, for example -- will affect the business environment relevant to their specific industry.

This course has two important characteristics: First, its emphasis is decisively and unmistakably international. The vast majority of examples and case studies will deal with the international economy. The approach taken here recognizes, from the very beginning, that teaching macroeconomics from a closed economy perspective does not make much sense. Second, this course is eminently practical; concepts and models will only be discussed to the extent that they have direct bearing in the understanding of real life situations. An important consequence of this practical perspective is that students will be required to undertake a number of empirical projects throughout the course.

I expect that all students will actively participate in class discussions.

There is no text book; instead there are a series of articles. There are two types of readings: (1) Analytical and academic articles that provide background for our class discussion; and (2) technical reports by investment banks that deal with current developments in the world economy. The latter are in "real time," in the sense that they will cover issues that are important during that particular week.

A word about reading: There is quite a bit of material to read. Everything is important, but some articles are more important than others. You should learn how to differentiate between "important" and "very important." If in doubt, ask me or the TA.

Every academic assigned reading is on line. All you need to do is follow the links. Every report/article/paper “in real time” covering the contingency will be posted on the course’s web site.

Grading Policy

- There will be two exams.
- Three (group) homework assignments.

The final grade will be determined in the following way:

- Midterm 20% (May 10)
- Final 40%
- Class Participation 20%
- Homework 20%

If you are unable to take the midterm, the final exam will count for 70% of the grade (unless you make a special arrangement with me). The Final will be a “take home” exam.

I will not “cold call” on you, but I expect everyone to participate actively in class discussions. Class participation will be critical in determining the fate of marginal grades cases.

It is possible that one of the sessions will be on-line, rather than on campus. If that is the case, I will let you know well in advance, so you can plan your travel, other courses, and other activities.

Office Hours

My office is located in C-508, and my phone number is 206-6797. My E-mail address is sedwards@agsm.ucla.edu.

Organization of the Course and Syllabus

The course is organized in several “modules.” Each module covers a specific set of concepts and tools. Modules do not necessarily correspond to specific sessions or weeks. Covering some modules may take more than one session, covering other modules may only take part of a session. The time devoted to each module is not pre-determined; it depends on how the class proceeds, on how many questions students have and how many current applications we discuss.

COURSE OUTLINE

In what follows I provide a detailed outline of the topics that we will cover in this course. There is ***no*** correspondence between the different topics and the week in the quarter. We will move at our own pace, often covering more than one topic in one week. However, I do provide the approximate time to be spent in each module.

MODULE 1: Introduction to global macroeconomics (Approximately half a session)

A. Concepts and issues

The global economy and risks

- Credit
- Political
- Currency

Macroeconomics vs. microeconomics

Macroeconomics and forecasting

Closed vs. open economy perspectives

Long vs. short run analyses.

Partial vs. general equilibrium analysis

Macroeconomic data, basic relations and concepts

GNP

GDP

Consumption

Investment

Government expenditure

Net exports and trade balance

Savings

B. Readings:

How Would Modern Macroeconomic Schools of Thought Respond to the Recent Economic Crisis?

<http://research.stlouisfed.org/pageone-economics/uploads/newsletter/2009/200911.pdf>

Useful Websites:

<http://www.bea.gov/> (Bureau of Economic Analysis - data on GDP and other macro data)

<http://minneapolisfed.org/research/data/us/> (Minneapolis Fed data base and commentary).

MODULE 2: INFLATION, DEFLATION AND MONETARY POLICY (approximately one session)

A. Concepts and issues

Price indexes

CPI

PPI

Core inflation

Sixteen percent trimmed mean CPI

How inflation affects business decisions

MODULE 3: MONETARY POLICY AND CENTRAL BANKS (Approximately one session)

A. Concepts and issues

Base money

M1

M2

Money multiplier

Federal Funds target interest rate

Open market operations

Yield curve and the transmission mechanism of monetary policy

International comparisons

Can emerging countries have an independent monetary policy

B. Readings:

Federal Reserve Board, “Monetary Policy,” in <http://www.federalreserve.gov/policy.htm>

Federal Reserve Bank of San Francisco: “What is the Fed?” in <http://www.frbsf.org/education/teacher-resources/what-is-the-fed>

Federal Reserve Bank of Cleveland: “Measuring Inflation,” in http://www.clevelandfed.org/research/data/us-inflation/cpi.cfm?dcs.nav=local?WT.oss=inflation%20measuring&WT.oss_r=3120

Gary H. Stern “The Transition to Low Inflation: Progress and Pressures,” in <http://minneapolisfed.org/pubs/ar/ar1984.cfm>

Arthur J. Rolnick, “An Anti-Inflation Policy is a Pro-Growth Policy” in <http://minneapolisfed.org/pubs/fedgaz/97-04/edi-ajr.cfm>

“U.S. Monetary Policy: An Introduction” in www.frbsf.org/publications/federalreserve/monetary/index.html

MODULE 4: INFLATION, UNEMPLOYMENT AND MONETARY POLICY: THE “TAYLOR RULE” (Approximately half a session)

A. Concepts and issues

Taylor rule

Monetary accommodation

Taylor rules in the real world

How to use the Taylor Rule to estimate the “natural” rate of interest

B. Readings:

Federal Reserve Board, “Taylor Rules” 2007, in
<http://www.federalreserve.gov/pubs/feds/2007/200718/200718pap.pdf>

Uncertainty and Monetary Policy in
<http://www.frbsf.org/publications/economics/letter/2005/el2005-33.html>

Inflation Expectations: How the Market Speaks
<http://www.frbsf.org/publications/economics/letter/2005/el2005-25.html>

MODULE 5: TRADITIONAL THEORIES OF INFLATION (Approximately half a session)

A. Concepts and issues

The Quantity Theory of Money

Velocity of circulation

Full employment

The demand for money

- Transactions motive
- Precautionary motive
- Unit of account

Opportunity cost of holding money

Inflation as a Tax

Interest rates, yields and bonds

Readings:

Interview with Former Federal Reserve Vice Chairman Roger W. Ferguson, Jr. in
<http://www.minneapolisfed.org/pubs/region/00-06/ferguson.cfm?js=0>

Federal Reserve Bank of San Francisco, “Monetary Policy, Money and Inflation,” 2012, in
<http://www.frbsf.org/economic-research/publications/economic-letter/2012/july/monetary-policy-money-inflation/>

MODULE 6: MODERN THEORIES OF INFLATION: THE ROLE OF THE GLOBAL ECONOMY (Approximately half a session)

A. Concepts and issues

The law of one price
 Goods arbitrage
 Purchasing power parity (PPP)
 Absolute version of PPP
 Relative version of PPP

B. Readings:

J. Gagnon and J. Ihrig, “Monetary Policy and Exchange Rate Pass-Through,” 2004, in
<http://www.federalreserve.gov/pubs/ifdp/2001/704/ifdp704r.pdf>

Michael R. Pakko and Patricia S. Pollard, “For Here or To Go? Purchasing Power Parity and the Big Mac” in
<http://research.stlouisfed.org/publications/review/96/01/9601mp.pdf>

Michael R. Pakko and Patricia S. Pollard, “Burgernomics: A Big Mac™ Guide to Purchasing Power Parity”, in
<http://research.stlouisfed.org/publications/review/03/11/pakko.pdf>

MODULE 7: ALTERNATIVE EXCHANGE RATE REGIMES AND INFLATION (Approximately half a session)

A. Concepts and issues

Alternative exchange rate regimes
 Pegged exchange rates
 Monetary approach to the balance of payments
 Pricing to market
 Deviations from PPP
 Inflation and the exchange rate
 Tradable and non-tradable goods
 The relative price between tradable and non-tradable goods (the Real Exchange Rate)

B. Readings:

M, chapters 15, 19 (19.1).

[Bergsten, Fred, “Alternative Exchange Rate Regimes”, 1999, in
 http://www.iie.com/publications/testimony/testimony.cfm?ResearchID=346](http://www.iie.com/publications/testimony/testimony.cfm?ResearchID=346)

Rose, A. "Exchange Rate Regimes in the Modern Era," UC Berkeley, 2011, in <http://faculty.haas.berkeley.edu/arose/FFF.pdf>

MODULE 8: BALANCE OF PAYMENTS ACCOUNTING (Approximately half a session)

A. Concepts and issues

Imports
Exports
Trade balance
Service account
Transfers
Financing account
International reserves
Balance of payments

B. Readings:

"International Economic Accounts", in
(You need to be familiar with the structure of the accounts, however you don't need to know all of the details)

<http://www.bea.gov/international/>

"What Is the Balance of Payments?", Norman S. Fieleke in
<http://www.bos.frb.org/economic/special/balofpay.pdf>

Balance of Payments Statistics Newsletter
<http://www.imf.org/external/pubs/ft/bop/news/pdf/1205.pdf>

MODULE 9: CURRENCY RISK AND EXCHANGE RATES IN THE LONG RUN (Approximately one session)

A. Concepts and issues

Real exchange rate (RER)
RER and exports
RER and imports
RER and sustainable current account balance
From the RER to the NER

B. Readings:

"The Real Exchange Rate: Definitions and Calculations", Ahmet N. Kipici and Mehtap Kesriyeli
in

<http://www.tcmb.gov.tr/yeni/evds/teblig/97/reel.pdf>

Long-run Determinants of East Asian Real Exchange Rates

<http://www.frbsf.org/econsrch/wklyltr/wklyltr98/el98-11.html>

MODULE 10: INTEREST RATES, EXCHANGE RATES AND ASSET MARKETS IN THE GLOBAL ECONOMY (Approximately one session)

A. Concepts and issues

Nominal interest rate

Real interest rate

Fisher equation

Risk neutrality

Risk aversion

Currency risk

Uncovered interest rate differentials

Carry trade

Exchange rate volatility and “news”

B. Readings:

Interest Rates and the Economy

<http://money.howstuffworks.com/interest-rate.htm>

Jaramillo, L. and C.M. Tejada, “Sovereign Credit ratings and Spreads in Emerging Markets,”

IMF WP, 2011, in

<http://www.imf.org/external/pubs/ft/wp/2011/wp1144.pdf>

MODULE 11: FISCAL POLICY: STIMULI AND THE MULTIPLIER (Approximately half a session)

A. Concepts and issues

Fiscal multiplier

Crowding out

Countercyclical macroeconomic policy

Historical discussion (Great Depression and other historical episodes)

Deficits and debt

Sustainable long term deficits and debt sustainability

B. Readings:

IMF, "Fiscal Policy for the Crisis," 2008, in
<http://www.imf.org/external/pubs/ft/spn/2008/spn0801.pdf>

Spillimbergo, A. et al. "Fiscal Multipliers," IMF, 2009, in
<http://www.imf.org/external/pubs/ft/spn/2009/spn0911.pdf>

"The Unpleasant Arithmetic of Budget and Trade Deficits", Gary H. Stern, President, Federal Reserve Bank of Minneapolis in <http://minneapolisfed.org/pubs/ar/ar1986.cfm>

MODULE 12: UNEMPLOYMENT (Approximately half a session)

A. Concepts and issues

Labor force
 Rate of participation
 Discouraged worker
 Additional worker
 Natural unemployment rate
 Labor market distortions and unemployment

B. Readings:

U.S. Department of Labor, Bureau of Labor Statistics Home Page, <http://www.bls.gov/>

Bureau of Labor Statistics, "Latest News Release. The Employment Situation" in
<http://www.bls.gov/news.release/pdf/empsit.pdf>

MODULE 13: THE GOLDMAN-SACHS MODEL OF ECONOMIC GROWTH (Approximately one session)

A. Concepts and Issues

Aggregate production function
 Sources of Growth
 Capital Accumulation and Growth
 Employment creation and growth
 Total factor productivity (TFP) growth
 Determinants of TFP
 - Trade policy.
 - Educational policy.
 Savings
 Private savings
 Public savings
 Savings and growth as a consistency check
 Foreign savings and the trade deficit

B. Readings:

Goldman-Sachs, "The Long Term Outlook for the BRICs," 2009, in <http://www.goldmansachs.com/our-thinking/archive/brics-at-8/brics-the-long-term-outlook.pdf>

Paul Romer "Economic growth" in <http://www.econlib.org/library/Enc1/EconomicGrowth.html>

"The Unpleasant Arithmetic of Budget and Trade Deficits", Gary H. Stern, President, Federal Reserve Bank of Minneapolis in <http://minneapolisfed.org/pubs/ar/ar1986.cfm>