Macro-Modelling
Economics 244, Spring 2013
University of Pennsylvania

Instructor: Guillermo Ordonez

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General Information

Lecture Times: Mondays and Wednesdays, 10:30am - 12:00pm

Lecture Location: MUSB 101

Office Hours and Availability: Tuesdays 9:30am-11:30am (in my office), or by appointment.

Teaching Assistant: The TA for the course is Vesa-Heikki Soini. His e-mail address is soini@sas.upenn.edu. His office hours are on Thursdays 2:00pm-4:00pm in 417 McNeil.

Course Website: Course information is available through Blackboard. You are encouraged to check Blackboard regularly. From time to time I will post relevant papers for you to read. Some of these papers will be more difficult than the material we cover in class.

Attendance: Students are expected and strongly encouraged to attend every lecture.

Pre-requisites

• Econ 101 and Econ 102. Intermediate Micro and Intermediate Macro.
• Math 104. Calculus 1
• Math 114 or Math 115. Calculus 2

Course Policies: The Department of Economics maintains a common set of policies that apply to all classes. By taking this class you agree to abide by these policies. You are encouraged to read these policies carefully. Full details can be found here:

http://economics.sas.upenn.edu/undergraduate-program/resources/policies.
Course Description

The recent global financial crisis exposed some of the most important open questions in macroeconomics. What is the role of financial markets and financial intermediaries for the aggregate economy? Do financial markets spur growth and development? Do they trigger and spread painful crises? Which policies can improve the positive effects of financial markets, and reduce their negative ones?

Given the renewed interest in these questions and the clear importance of coming up with answers, this course focuses on a very particular type of macro modeling; the modeling of macroeconomics in which financial markets play a role.

To answer these questions by constructing sensible macroeconomic models, however, we should first understand why there is financial intermediation in the first place, why the financial market is so different than other markets and what is so special about financial organizations. To model seriously financial markets in a macroeconomic environment, we have to delve first into their micro-foundations, so that then we can seriously understand their macroeconomic impact.

Structure of the Course

The course will be divided into four sections.

First Section (8 lectures): We will cover theoretical explanations (micro foundations) about why financial intermediation exists and what makes financial institutions and financial markets so special. We will also study the growth and decline of the so-called “shadow banking”, critical, for example, in the understanding of the recent financial crisis.

Second Section (6 lectures): We will review the role of financial markets in macroeconomic models, the theoretical arguments about why financial markets are important to spur economic growth, why they are so fragile and why financial crises can both generate economic recessions and amplify real activity problems.

Third Section (6 lectures): We will cover empirical studies that test quantitatively the effects of financial development on economic development and growth and the channels through which financial crises spread over real activity.

Fourth Section (4 lectures): At the start of each class, I will provide an overview of the questions, empirical techniques and the relevant literature. This will then be followed by students presenting short summaries of a particular reading from the syllabus and the class discussing the paper together. Topics will include:

- Financial Development, Financial Liberalization and Economic Growth,
- Bubbles, Panics and Crashes,
- History of Financial Crises,
- Policy Responses to Financial Crises,
- The Recent Financial Crisis.
Grading and Course Dynamics

Your success in this course is important to me. Therefore I want to be available for your questions as much as possible. It is best to ask your questions during class because it is highly likely that if you are either confused by something, or interested to know more about something, then others are too. So, please, interrupt me a lot.

You can e-mail me to arrange an appointment if my office hours are not convenient. I am also happy to try and answer questions directly over e-mail. However, I encourage you to first meet with the TA, before meeting with me. His contact details and office hours can be found above. For most questions that you have about the course content, he will be able to help you out.

Your feedback during the course is key. If there is something in the course that you think can be improved, please let me know. We are in this together. The higher the quality of the class, the better for all of us.

Finally, I’m planning this class to be very flexible, particularly during the second part. We will be discovering new common interests along the way, so I will try to accommodate them. Hence, the reading list is not exhaustive and may change during the semester.

Your grade will be based on three midterms, a long homework and a short presentation, which are worth 25 points each. Note this adds up to 125 points. Thus, I will drop your worst 25 points. If you are absent from one of the midterms or you do not hand in the homework, I can drop those points from consideration. This does not count for presentations though. If you do not present I will not drop those points from the total grade. The rationale for this policy is presentations run for two weeks, so we can always reschedule if needed.

The first midterm (Wednesday, February 13th) will cover the material of the first section, the second midterm (Monday, March 18th) will cover the material of the second section and the last midterm (Monday, April 22nd) will focus mostly on the last two sections, but will be more comprehensive, potentially exploiting material of the first two sections as well.

The homework will require you work with data and will also require a short essay in which you are expected to relate media discussions about financial markets (that I will determine when time comes) with the theoretical background introduced in class.

Finally, the presentation will be about one of the papers listed below under “Students Presentations”. We will talk more about this when time comes.

A textbook that I’ll refer frequently during the semester is Knoop, Todd (2008). “Modern Financial Macroeconomics: Panics, Crashes and Crises”. During the first section I will also use Freixas, Xavier and Rochet, Jean-Charles (2008) “Microeconomic of Banking” (there are copies available at the library). The most important material for the midterms, however, are my classes and my slides. I will post those slides as we advance, before going through them in class.
Reading List
An asterisk (*) means alternative, but recommended, reading.

Lectures 1-8 - Foundations of Financial Intermediation.


*Lectures 15-20 – Evidence on financial liberalization and economic growth.*


**Lectures 21-24 – Students Presentations.**

**Financial Crises Experiences and Policy Responses.**

- **19th Century Crises**


- **Great Depression**


- **Chile and Mexico (80s)**


- **Japan (90s)**


**The Recent Crisis and Policy Responses.**


* Carey, M., R. Correa, and J. Kotter (2009), "Revenge of the Steamroller: ABCP as a Window on Risk Choices” mimeo, Federal Reserve System.

