

**University College London
Department of Economics**

ECON0016 Macroeconomic Theory and Policy

Term 1: The closed economy

The course is structured around a number of questions:

- what causes business cycles?
- what should policy do to smooth the business cycle, and what can it do?
- what determines the natural (equilibrium) rate of unemployment, and what can policy do to change it?

Term 2: The open economy

The second term extends the core 3-equation model laid out in Term 1 to the open economy addressing questions about business cycles and macroeconomic policy for flexible and fixed exchange rate regimes.

- how does monetary policy affect the nominal and real exchange rate and how does this affect the central bank's behaviour?
 - how does an oil shock affect the macroeconomy and what should the policy response be?
 - what difference to the nature of shocks and policy options does it make if an economy has its own central bank?
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The course equips students with the theoretical models they need to understand contemporary debates about economic performance and policy.

Reading:

The **textbook** for the course is:

- Wendy Carlin and David Soskice, *Macroeconomics: Institutions, Instability and the Financial System* (Oxford University Press,

2014/2015). **Note: There is free access to the ebook version via UCL Library.**

Quizzes, tutorials and typical graded homework assignments:

- There are 9-10 quizzes per term
 - There are five tutorials for each term
 - There are two substantial homework assignments per term
 - In each tutorial class, the focus will be on problem solving and communication skills in explaining your reasoning.
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Macroeconomic simulator (allows you to play with the models and check your reasoning) In Term 2, you will use this for many exercises and for the module as a whole, you can be expected to use the simulator / simulation output in the Summer Assessment.

Typical Assessment:

The overall mark in this module comprises the following assessments:

- 25% coursework to be submitted at the beginning of Term 2.
 - 75% coursework to be submitted in Term 3.
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Provisional Course Outline:

Term 1

Week	Lecture topic
6	Introduction <ul style="list-style-type: none"> • What is the macro about • Why should we study macro Demand side part 1: A microfounded model of consumption: the permanent income hypothesis.
7	Demand Side Credit constraints. A microfounded model of investment: Tobin's q. The IS curve.
8 T	Supply Side An imperfectly competitive model of the labour market: price setting, wage setting and the Phillips curve.
9 H	Macroeconomic Dynamics A microfounded model of monetary policy: the MR curve. Using the 3 equation model.
10 P T	Expectations and the effectiveness of policy Different ways of forming expectations and their implications for policy. An empirical test of policy effectiveness,
11 RW	READING WEEK
12 P	Monetary Policy Controlling inflation: the Thatcher disinflation. The modern monetary framework: independent central banks and Taylor rules. The future of monetary policy.
13 T	Fiscal Policy Automatic stabilisers; active stabilisation; debt dynamics and sustainability.
14	Finance and the macroeconomy Banking, the financial sector, bubbles, and the link between finance and the macroeconomy.
15 T H	The global financial crisis The zero-lower bound on nominal rates. A narrative of the "crisis"; understanding events via the three equation model.
16 T P	Final lecture - the consequences of the crisis / course overview Balance sheet recessions; government debt crises.

P: stands for practical lectures

T: stands for tutorials

H: stands for homework (due Friday in the corresponding week)

Term 2

(T = week with tutorials; H = week with homework due at the end of the week)

Week	Lecture topic
20	Introduction <ul style="list-style-type: none">• Globalization in trade and capital markets• Macro policy making in the open economy• Open economy elements of crises Model-building: financial markets, exchange rates and the UIP condition
21	Supply-side, demand-side and real exchange rates Model-building: The medium-run model in the open economy (AD-ERU model)
22 T	Inflation-targeting in the open economy Model-building: Extending the inflation-targeting model to include the foreign exchange market (3-equation model)
23 H	Inflation-targeting, exchange rate overshooting & volatility Model-building: Using the 3-equation model
24 T	The real exchange rate, external balance and the demand side Model-building: Competitiveness, multipliers, Marshall-Lerner condition, terms of trade
25	Reading Week
26	The real exchange rate, inflation and the supply side (the AD-BT-ERU model) Model-building: AD-BT-ERU model and policy analysis
27 T	All about oil: macro analysis of oil shocks and natural resource windfalls Model-building: Oil shocks in the AD-BT-ERU model; Applying the PIH to the open economy
28 H	External imbalances Model-building: 2-bloc model with inflation targeting central banks
29 T	Economics of a Common Currency Area – the Eurozone’s first decade, the sovereign debt crisis and COVID-19 Model-building: Fixed exchange rates, stabilization, governance
	Final lecture - the financial crisis, the great recession, secular stagnation, climate change COVID-19.