The Two Pillars of Economics

Rational Behavior of the Participants

Interaction of Participants in Markets

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LEARNING TOOLS

Required Textbook:


2. Professor's Web Site. http://www.econ.washington.edu/user/mhadjimi/ This site contains resources for the course, including NARRATED PRESENTATIONS that are coordinated with the textbook, and previous exams. Also, access to the Economic Commentary.

Following Money, Banking, and Financial Markets in the Financial Press and on the World Wide Web:

- The Wall Street Journal. The "Credit Markets" column, a daily column appearing in Section C of The WSJ, is relevant for this course. For other pertinent articles, check the daily summary, "What's News -- Business and Finance" that appears on page A1. The url for the online edition is http://online.wsj.com/home/us
- http://www.economist.com/ The Economist, the business news weekly published in Great Britain that covers the globe, is of a high quality, and is widely read.
- World Wide Web. This class incorporates reports and data from the Federal Reserve's web sites (as well as other sites) www.federalreserve.gov. The web site of the Board of Governors of the Federal Reserve System contains an introduction to the Federal Reserve System, speeches and testimony of the chairman and other governors, the semiannual monetary policy reports to Congress, other policy statements, and the Fed's statistical releases. It also has links to the web sites of the 12 district Federal Reserve Banks, such as the Federal Reserve Bank of San Francisco (http://www.frbsf.org/), and to foreign central banks, such as the Bank of Japan (http://www.boj.go.jp/en/)
- Additional Recommended Web Sites. See the recommended list accessed from my home page at http://www.econ.washington.edu/user/mhadjimi/
Exam Schedule and Grading:

1. Midterm Exam: Tuesday, February 11, 2014, Weight = 40%.
2. Final Exam: Friday, March 21, 2014, 2:30-4:20. Weight = 50-60%
3. Discretionary Factor: Class participation may count for up to 10% of your grade.
INTRODUCTION

1. Overview of Course

   Read:

   1. a. Chapter 1

         http://www.federalreserve.gov/newsevents/speech/bernanke20140103a.htm

         http://www.federalreserve.gov/newsevents/speech/bernanke20130710a.htm


      e. Fed’s Most Recent Assessment: December 18, 2013 Press Release,

         http://www.federalreserve.gov/newsevents/speech/bernanke20110826a.htm

      g. Ben Bernanke, “The Effects of the Great Recession on Central Bank Doctrine and Practice,” October 18, 2011,
         http://www.federalreserve.gov/newsevents/speech/bernanke20111018a.htm


Questions and Problems: pp.17-18: 1, 2, 4, 6, 7, 9, 13.
THE FINANCIAL SYSTEM: THE PARTICIPANTS, THE INSTRUMENTS, AND THE (FINANCIAL) ENVIRONMENT

2. Introducing the Participants and the Economy

Read:
2. Chapter 18, Banking and Information, pp. 386-89.

Questions and Problems: p. 41: 1, 2, 5, 6, and 13.

3. A Framework for Understanding Financial Instruments

Read:
1. Chapter 3

Questions and Problems: Try-It-Out 3.1; pp. 65-66: 3, 4, 6, 7, 11, 13

4. a. The Basic Financial Instruments

Read:
1. Chapter 4, pp.67-83
Also, Suzanne Kapner, “A Market to Prop Up—Mortgages,” (Fannie Mae and Freddie Mac,) Financial Times, March 23, 2010

Questions and Problems: Try-It-Out 4.1, p. 90: 1-4

b. The Balance Sheets of the Six Participants

Read:
1. Chapter 4, pp. 84-90.
2. Ben Bernanke, “The Federal Reserve’s Balance Sheet: An Update,” At the Federal Reserve Board Conference on Key Developments in Monetary Policy, October 8, 2009
3. “Credit and Liquidity Programs and the Balance Sheet,” September 2011,
   http://www.federalreserve.gov/monetarypolicy/bst.htm
   (The Fed’s Exit Strategy: Fed Introduces Tool to Drain Extra Reserves.)

Questions and Problems: p.90: 5-7, 13, 15-17

5. The Evolution to the New Financial Environment

a. Part 1: Deregulation in the 1980s

Read:
Chapter 5

b. Part 2: The Shadow Banking System and the Current Crisis

1. “Borrowing Short and Lending Long,” Econbrowser
   http://www.ft.com/cms/s/0/4560d050-e74f-11dd-aef2-0000779fd2ac.html
2. Ben Bernanke, Fed Chairman, “Monetary Policy and the Housing Bubble,” At the Annual Meeting of the American Economic Association Atlanta, Georgia, January 3, 2010
Questions and Problems: pp.115-16: 1, 2, 4 - 6, 8-12

6. The Structure, Regulation, and Supervision of U.S. Financial Firms
   Read:
   1. Chapter 17 and Ch.19
      http://www.federalreserve.gov/newsevents/speech/bernanke20091023a.htm
      http://www.federalreserve.gov/newsevents/testimony/bernanke20100317a.htm
   5. Governor Daniel Tarullo, “Comments on Regulating the ‘Shadow Banking System’,” September 17, 2010
      http://www.federalreserve.gov/newsevents/speech/tarullo20100917a.htm
      http://banking.senate.gov/public_files/070110_Dodd_Frank_Wall_Street_Reform_comprehensive_summary_Final.pdf
   7. Governor Daniel Tarullo, “Regulatory Reform”
   8. Governor Daniel Tarullo “The Volcker Rule,” January 18, 2012,

   8. Tim Braithwaite, “Dodd-Frank Bill is no Glass Steagall,” June 28, 2010

MONEY, INTEREST, AND PRICES

7. The Theory of Portfolio Choice: The Basic Laws of Asset Demand
   Read:
   Chapter 6
   Questions and Problems: Try-It-Out 6.1; p.130: 3-5, 7, and 8

8. The Deposit-Rate Setting Behavior of Banks and Money Demand
   Read: Chapter 7 and Chapter 21

9. The Money Supply Process
   a. Traditional Policies
      Read:
      1. Chapter 8
      2. Chapter 15, pp. 310-19
   b. Non-traditional Policies


10. Two Tales of Determining the Interest Rate
Read:


Read:
1. Chapter 10, pp. 191-208
2. Chapters 24, 25, 26
3. For Econ 301 or 401 background, listen to NARRATED PRESENTATIONS: Introduction to the IS-LM Model, Monetary Policy in the IS-LM Model, Fiscal Policy in the IS-LM Model, The AD-AS Model, A First Look.

End-of-Chapter Questions for Chapters, 24-26.

12. Money, Interest, and Prices: The Liquidity Effect, the Real Income Effect, the Price Level Effect, and the Expected Inflation Effect
Read:
Chapter 10, pp. 208-19
Questions and Problems: pp. 219-20: 2-14

THE FEDERAL RESERVE AND ITS BEHAVIOR

13. a. The Federal Reserve System: Form and Function
Read:
1. Chapter 11

Questions and Problems: pp. 246-47: 1-12

b. Functions of Federal Reserve Banks: The Details
Read:
1. Chapter 12
2. “The Evolving Role of the Federal Reserve Banks,” former Vice Chairman Donald L. Kohn, November 3, 2006,
   http://www.federalreserve.gov/newsevents/speech/kohn20061103a.htm
14. **Instruments, Targets, and Goals of Monetary Policy**  
*Read:*  
1. Chapter 13  
2. “Policy Tools,” Board of Governors of the Federal Reserve System, (List of traditional and non-traditional tools, with links that briefly explain each of the tools)  
http://www.federalreserve.gov/monetarypolicy/default.htm  
Part 1: How is the Fed structured and what are its policy tools?  
Part 2: What are the goals of U.S. monetary policy?  
Part 3: How does monetary policy affect the U.S. economy?  
Part 4: How does the Fed decide the appropriate setting for the policy instrument?  

**Questions and Problems:** p. 266: 1, 2, 5, 9, and 10

15. **Understanding Open Market Operations and Movements in Reserves**  
*Read:*  
1. Chapter 14  
2. Federal Reserve Press Release, January 19, 2000, (announcement of change in disclosure procedures),  
3. Update 2009. “The Federal Reserve’s Balance Sheet: Table 1. Factors Affecting Reserve Balances of Depository Institutions” (See Table 1 description and current release)  
http://www.federalreserve.gov/monetarypolicy/bst_fedsbalancesheet.htm

**Questions and Problems:** pp. 308-9: 1-3, 7, and 10

16. **The Money Supply in More Detail**  
*Read:* Chapter 15  
**Questions and Problems:** pp. 327-28: 4 - 6, 8 – 13

17. **The Conduct of Monetary Policy: The Experience**  
*Read:*  
1. “Success and Failures of Money Policy since the 1950s,” former Vice Chairman Donald Kohn, September 21, 2007,  
http://www.federalreserve.gov/newsevents/speech/kohn20070921a.htm  
The Wall Street Journal, September 14, 2009,  
http://online.wsj.com/article/SB125288495316307191.html

   http://www.federalreserve.gov/newsevents/speech/bernanke20090821a.htm

   http://www.federalreserve.gov/newsevents/testimony/bernanke20100210a.htm

FINANCIAL INSTITUTIONS AND THEIR BEHAVIOR

18. The Profit-Maximizing Banking Firm

   a. The Theory
   Read:
   Chapter 18
   Questions and Problems: pp. 408-9: 4 – 16

   b. Application: Recent Events
   Read:
   1. Edward Gramlich, “Booms and Busts: The Case of Subprime Mortgages,”
      August 31, 2007

   2. “Rescue Plan Comes Around to Views of the Academics,” The Wall Street
      Journal, October 11, 2008
      http://online.wsj.com/article/SB122368180323324909.html


   1. The Theory, Class Lectures.
      Reserve System, February 10, 2010,
      http://www.federalreserve.gov/newsevents/testimony/bernanke20100210a.htm
      http://www.federalreserve.gov/newsevents/speech/bernanke20070615a.htm
   4. Ben S. Bernanke, “Federal Reserve Programs to Strengthen Credit Markets and the
      Economy,” Federal Reserve Board, February 10, 2009
      http://www.federalreserve.gov/newsevents/testimony/bernanke20090210a.htm
   5. Ben S. Bernanke and Vincent R. Reinhart, “Conducting Monetary Policy at Very Low

20. Nondepository Institutions—“Shadow Banks”
   Read:
   1. Chapter 19

21. A Summing Up
   Class Lecture