

MACROECONOMICS – I

- A. **COURSE DESCRIPTION:** This is a basic macroeconomics course. It exposes the students to the major issues concerning the central questions of macroeconomics. The course builds upon the knowledge of undergraduate macroeconomics and provides an advanced treatment of the subject.

B. COURSE OUTLINE

1. Introduction

Schools in Macroeconomics: Classical to New Keynesian.

Consumption: Consumption under certainty: Permanent Income Hypothesis; Consumption under uncertainty: Random Walk Hypothesis; Interest Rate and Saving; Consumption and Risky Asset: Consumption CAPM; Beyond the Permanent Income Hypothesis: Liquidity Constraints, Relative Consumption, Time Inconsistency and Precautionary Saving.

Investment: Investment and the Cost of Capital; Investment with Adjustment Costs; Tobin's q ; Effects of Uncertainty; Kinked and Fixed Adjustment Costs; Investment in the Housing Market

Readings:

- i) David Romer: *Advanced Macroeconomics*, McGraw Hill, Fourth edition (chapters 8 and 9)
- ii) Ola Olsson: *Essentials of Advanced Macroeconomic Theory*, Routledge (chapters 8 and 9)

2. Long-Run Economic Performance

The Malthusian World; Classical Growth Theories: Adam Smith, Ricardo, Marx; Harrod-Domar Model

Solow-Swan Model: Basic Model, Concepts of Absolute and Conditional Convergence, Speed of Convergence, Solow Model with Human Capital and Speed of Convergence; Golden Rule of Capital Accumulation, Solow Model with Natural Resource and Land, Empirical Issues, Objections to the Neoclassical Growth Model

Endogenous Growth Theory: AK model; Endogenous Technological Change; Learning by Doing; Romer's Product Variety Model; Schumpeterian Growth Models; Innovation versus Imitation; Cross Country Income Differences: Social Infrastructure, Geography, Colonialism and Institutions.

Readings:

- i) Ola Olsson: *Essentials of Advanced Macroeconomic Theory*, Routledge (chapter 1)
- ii) David Romer: *Advanced Macroeconomics*, McGraw Hill, Fourth edition (chapters 1, 2, 3 and 4).
- iii) Robert J. Barro and Xavier Sala-i-Martin (2004): *Economic Growth*, MIT Press. (chapter 1)
- iv) Debraj Ray: *Development Economics*, OUP. (Section 3.3 in chapter 3 and chapter 4)
- v) Journal articles to be used as supplements to the core textbook(s)

3. Short-Run Fluctuations and Policy

Exogenous Nominal Rigidity: A Baseline Case: Fixed Prices; Price and Wage Rigidity; Departures from Perfect Competition in the Goods and Labor Markets; Toward a Usable Model with Exogenous Nominal Rigidity

Microeconomic Foundations of Incomplete Nominal Adjustment: Model of Imperfect Competition and Price Setting; Are Small Frictions Enough?; Real Rigidity; Coordination Failure Models and Real Non-Walrasian Theories; Lucas Imperfect Information Model.

Inflation and Monetary Policy: Inflation, Money Growth and Interest Rate; Monetary Policy and the Term Structure of Interest Rate; The Microeconomic Foundations of Stabilization Policy; Optimal Monetary Policy in a Simple Backward-Looking Model; Optimal Monetary Policy in a Simple Forward-Looking Model (divine coincidence); Additional Issues in the Conduct of Monetary Policy; Dynamic Inconsistency Theory of Low Inflation Monetary Policy; Seignorage and Inflation Problems

Budget Deficit and Fiscal Policy: The Government Budget Constraint; Ricardian Equivalence Debate; Tax-Smoothing; Political Economy Theories of Budget Deficit; Strategic Debt Accumulation; The Cost of Deficits; A Model of Debt Crisis

Readings:

- i) David Romer: *Advanced Macroeconomics*, McGraw Hill, Fourth edition (chapters 6, 11 and 12)
- ii) Journal articles to be used as supplements to the core textbook.