

THE COLLEGE OF NEW JERSEY
SCHOOL OF BUSINESS: ECONOMICS PROGRAM

Economics 102: Principles of Macroeconomics

Instructor: Dr. Bozena Leven
Business Building, Room 217, Ph. # 771-3140
Office Hours: T, F 8:00-8:30am and 11:30-12:00pm
Tues 1:30-2:00pm
Wed. by appt.

Course Text:

McConnell, C. And Brue, S.L. Economics, the latest edition
Study Guide is optional
Additional readings provided during the semester

Recommended Readings: Wall Street Journal, New York Times, Economist.

Course Description:

An introduction to economic concepts and their application to problems of increasingly global economy. Contemporary problems of unemployment, inflation, economic growth are analyzed. Government fiscal and monetary policies are also considered along with international aspects.

Course Major Objective:

After successful completion of the course student should be able to identify, understand and analyze major macroeconomic issues discussed in quality newspapers.

Learning Activities

Preliminary course plan and schedule:

Week 1:	Introduction, Production Possibility Frontier
Week 2:	Supply and Demand
Week 3	Unemployment, Inflation, Circular Flow, GDP, test 1
Week 4	Consumption and Investment
Week 5	Aggregate Expenditure,
Week 6	Keynes vs. the Classics, multiplier
Week 7-8	Fiscal Policy, test 2
Week 9	Supply of Money, Federal Reserve System
Week 10	Demand for Money, 3-sector, test

Week 11	Monetary Policy Debates, Government Debt & Crowding Out
Week 12	Exchange-Rate Determination
Week 13	Neoclassical Synthesis of Keynesians and Classical: Aggregate Supply, Aggregate Demand, Policy debates
Week 14	Final exam

Grading Policy

Test I	25 percent
Test II	25 percent
Final exam	25 percent
Paper	15 percent
Class participation	10 percent

Paper topic: Describe four major problems faced by the US economy currently

Help: Besides regular office hours, I will make individual appointments with students requesting assistance. Additionally, hours of economics tutors will be announced in class.

Every student is expected to participate in each of his/her courses through regular attendance at lecture and laboratory sessions. It is further expected that every student will be present, on time, and prepared to participate when scheduled class sessions begin.

The College of New Jersey is a community of scholars and learners who respect and believe in academic integrity. *Academic dishonesty* is any attempt by the student to gain academic advantage through dishonest means, to submit, as his/her own, work which has not been done by him/her or to give improper aid to another student in the completion of an assignment. Such dishonesty would include, but is not limited to: submitting as his/her own a project, paper, report, test, or speech copied from, partially copied, or paraphrased from the work of another (whether the source is printed, under copyright, or in manuscript form). Credit must be given for words quoted or paraphrased. The rules apply to any academic dishonesty, whether the work is graded or ungraded, group or individual, written or oral.

ECO 102: Principles of Macroeconomics

Basic information on course

- A. **Purpose:** In a market economy, personal well-being or hardship are often linked to macroeconomic performance. This course's ultimate goal is economic literacy, for those who participate in policy formation directly or as citizens assessing electoral candidates, and for those who will work for a living or participate in running a business. By the end of the course, most discussions of macroeconomic topics that appear in national newspapers and business magazines should be clear to students.
- B. **Course Description:** Macroeconomics is the study of the economy as a whole. It introduces economic aggregates (e.g., GDP, inflation, unemployment, the exchange rate) and explores how they are determined, both over the business cycle, and over the long run. It provides theoretical and institutional information on government demand-management capabilities (fiscal and monetary policies) and their limitations, and the analytical basis of policy debates on appropriate intervention.
- C. **Course Prerequisites:** None.

Learning goals

Content goals

- 1. **Core concepts:** GDP, investment and investment schedule, unemployment, inflation, production possibilities frontier, Keynes vs. the Classics, saving, consumption, income, money, wealth, Keynesian-Cross model of GDP determination, Fiscal policy, Money and the Banking System, Supply of Money, interest rate, Demand for Money, Federal Reserve System and Policy, Exchange-rate determination, Aggregate Demand, Aggregate Supply, Phillips Curve-
- 2. **Deep Understandings**
 - A. **GDP:** real vs. nominal, measure of extent of the market vs. measure of social welfare, component parts (consumption, investment, government spending, net exports), equivalence to GDI (its components: wages, distributed profits, rent, interest, undistributed profits, capital consumption allowance, indirect business taxes), value-added approach to GDP accounting, growth, income distribution.
 - B. **Investment:** real vs. financial investment and capital, depreciation and replacement investment, net investment as addition to capital stock, components (equipment, plant, inventories), the inclusion of housing construction as investment, the weak/strong effect of interest rate on corporate investment/housing construction, **investment schedule**,

determinants (expected profit, interest rate, confidence), and slope (rank-ordered investment projects).

- C. **Unemployment:** definition, vs. labor force participation, product of duration and incidence, descriptive categories (seasonal, recession, depression), business-cycle patterns (including leading indicators), and 20th century stylized history; analytical categories (frictional, structural, cyclical, long-wave), full employment/natural rate of unemployment/NAIRU.
- D. **Inflation:** Price-level construction, limitations, real vs. nominal variables, inherent unevenness of inflation, real-income effects of inflation for borrowers vs. lenders, real interest rate, inverse relationship of bond price and bond interest rate.
- E. **Production Possibilities Frontier:** role of natural resources, capital stock, labor force size and quality, technology and production techniques, institutional context (culture, laws), fully utilized resources assumed, explanation of slope, opportunity cost on the frontier. **Productivity** and contribution of investment to shifts in frontier/potential GDP.
- F. **Keynes vs. the Classics:** Saving out of income vs. savings as accumulated wealth, life-cycle hypothesis (need to save) vs. interest rate as incentive to save given preference for current consumption, investment under uncertainty and the role of expectations and confidence vs. investment dependent on diminishing marginal physical product of capital under perfect information. Excess capacity, job shortage, work to stay alive vs. fully utilized resources, diminishing returns (crowded factories), labor-leisure trade-off.
- G. **Keynesian-Cross model** of GDP determination--aggregate expenditure and passive supply: marginal propensities to consume, to save, and to import; expenditure multiplier as inverse of induced leakage ratios, actual vs. planned investment and unplanned accumulation of inventories, equilibrium as no tendency to move.
- H. **Fiscal Policy:** direct effects of government expenditure, taxes, transfer benefits; automatic stabilizers; discretionary vs. non-discretionary fiscal policies.
- I. **Supply and Demand:** microeconomic partial-equilibrium mechanics of supply and demand curves.
- J. **Money and the Banking System:** money supply vs. currency unit, functions of money (medium of exchange, means of payment, store of value; unit of account, unit of account denominating debts), narrow/broad definition of money supply and monetary base, money (wealth) vs. income (flow); fractional-reserve banking under commodity-money system and potential for financial crisis; bank loan creation and money expansion, money multiplier as inverse of induced leakages out of lending, **Supply of money**, **interest rate** (prime rate vs. cost of funds).

- K. **The Federal Reserve System:** history and policy tools (open market operations, reserve requirements, discount rate), emergence of federal funds market and discovery of Fed role, changing structure of the Fed, of deposit insurance, 1980s S&L failures, 1989-90 bank failures and FDIC liquidity crisis, and 1989 FIRREA.
- L. **Demand for money:** money as medium of exchange or means of payment vs. money as an asset;; interest rate as return to not hoarding or as cost of loan; Fed accommodation, Fed intervention, and asymmetric influence of contractionary vs. expansionary monetary policy, historical conditions that have changed power of Fed policy. Monetarist-Keynesian debates about de/stabilizing monetary policy; crowding out.
- M. **Foreign-exchange markets:** exchange rate definition (price of the dollar in terms of other currencies), exchange-rate regimes (floating, fixed), balance of payments definitions, role of central bank, exchange-rate determination (demand for dollars: exports, capital inflows; supply of dollars: imports, capital outflows), conflict of interest between finance and industry over exchange-rate level, commonality of interest over stability, Fed intervention to currency markets to maintain exchange-rate target.
- N. **Aggregate Supply:** reinterpret 45° line as set of possible equilibrium points. Change Keynes's inventory-adjustment story to perfect-competition price-response to excess demand. Reinterpret Aggregate-expenditure diagram as theory of demand. Horizontal segment of aggregate supply:, Keynesian depression; vertical segment, Classical full employment; upward-sloping segment, general business-cycle Neoclassical synthesis. Short-run upward slope explanations: diminishing returns, bottlenecks, input price contracts, money illusion, labor contracts; long-run alternatives revert to Classical macro-model. Supply shifts: like Production possibility frontier shifts, or anything changing profitability.
- O. **Aggregate Demand:** Downward slope: transactions demand for money under non-accommodating Fed, fixed nominal exchange rate and relative price-level changes, real wealth effect focusing on money holdings, not debt.
- P. **Phillips Curve:** Phillips' empirical study of wage growth and unemployment, Alternative approaches: Phillips curve as alternative version of aggregate supply, horizontal mirror of aggregate supply in short run and long run, aggregate demand shifts along aggregate supply and in/voluntary unemployment. Demand shifts as cyclical, supply shifts as shocks, stagflation. Alternative interpretations: wage-price mark-up equations and Keynesian-Cross model.

3. Anticipated Misunderstandings

- A. **Real vs. financial investment:** capital formation vs. claims on wealth.
- B. **Stock vs. flows:** stock of capital/wealth vs. flow of investment or depreciation or capital consumption allowance/saving out of current income.
- C. **Saving out of income vs. savings accounts** (form in which hold wealth).

- D. **Income vs. money**, money as one among many forms of wealth, income as potentially adding to wealth but potentially consumed today. Fully financed changes in transfers do not change aggregate expenditure, but changes in only transfer benefits or only the taxes to finance them will change autonomous expenditure.
- E. **Fiscal issues**: Changes in taxes do not necessarily change government expenditure, nor vice versa, ditto for transfer benefits (e.g., entitlements).
- F. **Monetary issues**: The Fed (central bank) is not the feds (FBI or government). Gold is not the basis of the banking system in any operational sense, but can be the means of payment during world wars. The Fed does not create money when it prints currency to give to banks so they can give it to those they have lent money to, the Fed creates money when it injects reserves into the banking system.
- G. **Money vs. quantity of currency in foreign-exchange market**: money supply is stock, flow of currency trading hands does not change the stock of money
- H. **Higher price level vs. higher inflation**: one-time price increase vs. sustained, continuous increases.
- I. **Supply of money and aggregate supply of output**: money market events affect demand for output, but supply.
- J. **Supply and demand in micro, vs. aggregate supply and aggregate demand in macro**: individual market, individual price and real relative price, vs. aggregate output and price-level, which includes wage level. Higher price level means higher wages in general.
- K. **Inflation is not bad for everyone**: inflation is a distributional issue rather than a uniform negative, inflation benefits borrowers and hurts lenders.

B. Performance

1. Complex Tasks, Core Performances

- a. Systematically analyze the consequence of given economic events for GDP, the interest rate, the exchange rate, unemployment, price level, and inflation, in the short run and the long run.
- b. Systematically analyze the consequence of given fiscal and monetary policies for GDP, the interest rate, the exchange rate, unemployment, price level, and inflation, in the short run and the long run.
- c. Link policy conclusions to their analytical frameworks, and show how different assumptions lead to different implications for the effectiveness and consequences of monetary and fiscal policy (e.g., New Classical vs. Keynesian; Monetarist vs. Post Keynesian). Evaluate the economics content of news articles and interpret the logic or adhoquery of the economic reasoning provided.

2. Technical Knowledge and Procedures

- A. Production Possibilities Frontier: shifts, movements along, movements underneath
- B. Real value calculations, value added calculations
- C. Business cycle stylized facts (trough, peak)
- D. Investment schedule (graph)
- E. Classical Capital market (graph)

- F. Saving function (algebra and graph)
- G. Consumption function (algebra and graph)
- H. Aggregate expenditure function (algebra and graph), shifts
- I. Passive supply, 45° line and equilibrium GDP determination (algebra and graph), expenditure multiplier (rounds of spending)
- J. Fiscal policies, multiplier effects, shifts in aggregate expenditure
- K. Rounds of lending (T-accounts), money multiplier
- L. Money market: demand for and supply of money, theory of slope, shifts in both
- M. Crowding out: implications of slope of supply of money
- N. 3-sector model, shifts in investment schedule
- O. Foreign exchange market: shifts in demand for and supply of dollars
- P. Aggregate supply: slope in short run, long run, and shifts
- Q. Aggregate demand: slope and shifts