

DREW UNIVERSITY
Department of Economics
Econ 119 – MONEY, BANKING AND THE MACROECONOMY
Spring 2011

Dr. Bilge Erten

Office: HSC 338

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Class time and location: TTH 10:25am-11:40am, HSC 308

Course Description

This course is designed to introduce students to the role of money in the economy, the institutional characteristics of the banking system, and the functioning of international financial markets. Central topic of interest include the theory and evidence on demand for money, control of money supply and tools of monetary policy, interest rate determination and term structure of interest rates, bank management and operation of the banking system, financial innovation, bank regulation and deregulation, and the international financial system. Keeping a balance between theory and policy, the course will combine theoretical analyses with empirical investigations of the regularities underlying the monetary economy.

Learning Objectives

- (1) Understand the importance of financial markets for the overall functioning of the economy.
- (2) Understand the central dynamics of the recent financial crisis and the major policy responses to it.
- (3) Explain changes in interest rates using fundamental economic theories including present value calculations, behavior towards risk, and supply and demand models of money and bond markets.
- (4) Explore the structure of the Federal Reserve System and the mechanisms in which it controls the money supply.
- (5) Analyze macroeconomic problems and prescribe appropriate monetary policy solutions.

Course Materials

Required Texts

Frederic Mishkin, *The Economics of Money, Banking, and Financial Markets*, 9th Edition, Addison Wesley, 2010.

Real World Banking and Finance: Readings in Economics, Business, and Social Policy, From Dollars & Sense Real World Economics, Edited by Doug Err, Chris Sturr, Marty Wolfson, 6th Edition, 2010.

Mishkin is the textbook, and the Real World Banking and Finance is a reader on critical perspectives about money, banking, and finance. Class handouts and contributions from the secondary literature (placed on Moodle) will be assigned from time to time during the semester.

Work Requirements and Grading

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|--|---------------|
| Forum Questions and Quizzes ⁽¹⁾ | 15% (150 pts) |
| Assignments ⁽²⁾ | 15% (150 pts) |
| Group Project ⁽³⁾ | 15% (150 pts) |
| Midterms ⁽⁴⁾ | 40% (400 pts) |
| Project Presentation ⁽⁵⁾ | 10% (100 pts) |
| Classroom Participation ⁽⁶⁾ | 5% (50 pts) |

- (1) There will be a number of forum questions, which will be posted on Moodle. These questions will ask you to engage with critical readings from the reader or outside sources of readings which will be posted on Moodle. It will be our objective to critically examine crucial policy choices from a historical and institutional perspective after learning their central aspects from the textbook. In addition, there will be many announced and unannounced (pop) quizzes given throughout the semester. Adequate preparation for these requires reading ahead for class and completing homework assignments on time. Classes will begin with your questions so that you can resolve any problems with assigned work before the quiz begins.
- (2) There will be three assignments due in this class. To complete each of them you will have at least one week. You may submit your work as a group write-up with two other people, in which case you would turn in only one assignment per group, indicating all members of your group on the front page.
- (3) The group project will be a semester-long research project that will be due April 21. Each group will be composed of three students. The project topics will be

distributed in class. Each project report should be not exceed 10 pages of single-spaced, excluding tables, charts and references. All sources should be properly referenced. All direct quotations (including quotes from documents or web-based materials) should appear within quotation marks, with the source attributed. Please comply with the academic integrity standards of the University that are listed below. The deadline for the submission of final papers is April 26.

- (4) The two midterm exams will consist of short essay questions and problems from lecture presentations, discussions, and assignments. They will be closed-book exams on March 1 and April 12.
- (5) The project presentation will take place on April 26. Each presentation is anticipated to last 12-15 minutes. The use of Powerpoint is highly recommended.
- (6) Attendance in class is required and is considered in your participation grade, which counts for 5% of your final grade. Questions, comments, and discussion are strongly encouraged, as is seeking assistance from the instructor outside the classroom (during office hours, or by appointment).

Additional Considerations

- (1) Required readings are absolutely required readings, including class handouts and materials posted on Moodle.
- (2) Late assignments will be devalued by 10% per class session.
- (3) Cell phones and beepers are not allowed in the classroom, they must be turned off. If you need to have such devices with you for work-related or medical reasons you need to have the instructor's permission in advance.
- (4) Laptops are not allowed in the classroom, unless we have an exercise that requires the use of laptops. An exception is provided with documentation from the Office of Educational Services.
- (5) Students are required to check their Drew email account on a regular basis. Students will receive email reminders for readings, exams, handouts, and other course-related information. The instructor will send an email when new material is posted on Moodle. Reading course related emails also counts in class participation grade.

Your grade will be determined based on the percentage of points earned, and the following scale will be used to determine your grade for the course:

| <u>Grade</u> | <u>Percentage</u> | <u>Points</u> |
|---------------------|--------------------------|----------------------|
| A | 94-100 | 940-1000 |
| A- | 90-93 | 900-930 |
| B+ | 87-89 | 870-890 |
| B | 84-86 | 840-860 |
| B- | 80-83 | 800-830 |
| C+ | 77-79 | 770-790 |
| C | 74-76 | 740-760 |
| C- | 70-73 | 700-730 |
| D+ | 67-69 | 670-690 |
| D | 64-66 | 640-660 |
| F | 0-63 | 0-630 |

Special Accommodations

Should any student require academic accommodations, request(s) must be formally processed with the Office of Educational Affairs (BC 114, extension 3327). Students are responsible for providing the instructor with the appropriate written documentation at least one week prior to any request for specific course accommodations. Completing and complying with this procedure is the student's responsibility. There are no retroactive accommodations.

Academic Integrity

Drew University regards academic honesty and scholarly integrity as indispensable to genuine learning and true scholarship. Cheating on examinations, papers or computer assignments, offering work done by others as one's own, using the words and ideas of others without proper acknowledgment, improperly providing information, papers, or projects to others, or falsifying the nature or results of one's research are inimical to learning and scholarship, and infringe on the mutual faith and trust essential to the academic enterprise. Students should be familiar with the Drew University Standards of Academic Integrity. Violations will be taken to the Dean of the College of Liberal Arts.

Course Outline

I. Introduction, Central Concepts, and Empirical Overview

** Mishkin: Chapter 1 ("Why Study Money, Banking, and Financial Markets?")

II. Overview of the Financial System and the Evolution of the Payments System

** Mishkin: Chapter 2 ("An Overview of the Financial System")

** Mishkin: Chapter 3 ("What is Money?")

** Real World Banking and Finance: Chapter 1, Article 1.2 and Chapter 2, Articles 2.1 – 2.4 (“The Banking and Finance Industry”)

III. Understanding the Behavior of Interest Rates

** Mishkin: Chapter 4 (“Understanding Interest Rates”)
** Mishkin: Chapter 5 (“The Behavior of Interest Rates”)
** Mishkin: Chapter 6 (“The Risk and Term Structure of Interest Rates”)
** Handout on “Interest Rates and the Price of Bonds”

IV. The Stock Market, the Efficient Market Hypothesis, and the Wealth Distribution

** Mishkin: Chapter 7 (“The Stock Market, the Theory of Rational Expectations and the Efficient Market Hypothesis”)
** Real World Banking and Finance: Chapter 5 (“The Stock Market”)

V. Financial Structure

** Mishkin: Chapter 8 (“An Economic Analysis of Financial Structure”)
** Real World Banking and Finance: Chapter 2, Articles 2.5 – 2.9 (“The Banking and Finance Industry”)

VI. Financial Instability and the Financial Crises

** Mishkin: Chapter 9 (“Financial Crises and the Subprime Meltdown”)
** Minsky, Hyman. 1983. “A Restatement of the Financial Instability Hypothesis”
** Crotty, James. 2009. “Structural causes of the global financial crisis: a critical assessment of the ‘new financial architecture’”
** Real World Banking and Finance: Chapter 3 (“Mortgages, Consumer Credit, and Predatory Lending”)

VII. Banking, the Management of Financial Institutions, and Credit Flows

** Mishkin: Chapter 10 (“Banking and the Management of Financial Institutions”)
** Gary Dymski and John Veitch. 1994. "Credit Flows to Cities: Introducing Cindy Mae." In *Reclaiming Prosperity*.

VII. Financial Regulation

** Mishkin: Chapter 11 (“Economic Analysis of Financial Regulation”)
** Mishkin: Chapter 12 (“Banking Industry: Structure and Competition”)
** Real World Banking and Finance: Chapter 4 (“The Financial Crisis”)
Crotty, James and Gerald Epstein, "A Financial Precautionary Principle: New Rules for Financial Product Safety," *Wall Street Watch* (July, 2009), available at:
http://www.peri.umass.edu/fileadmin/pdf/conference_papers/SAFER/Crotty_Epstein_Financial.pdf

VIII. Central Banking

- ** Mishkin: Chapter 13 ("Central Banks and the Federal Reserve System")
- ** Mishkin: Chapter 14 ("The Money Supply Process")
- ** Real World Banking and Finance: Chapter 1, Articles 1.1, 1.3 - 1.9 ("Money, the Federal Reserve, and the Economy")

IX. Monetary Policy

- ** Mishkin: Chapter 15 ("Tools of Monetary Policy")
- ** Mishkin: Chapter 16 ("The Conduct of Monetary Policy: Strategy and Tactics")
- ** Epstein, Gerald, "Financialization and Federal Reserve Policy in the Crisis: Central Bank Accountability for Financial Stability and Economic Reconstruction" (May, 2009), available at:
http://www.peri.umass.edu/fileadmin/pdf/conference_papers/SAFER/Epstein_Federal_Reserve_Policy.pdf

X. International Finance and Monetary Policy

- ** Mishkin: Chapter 17 ("The Foreign Exchange Market")
- ** Mishkin: Chapter 18 ("The International Financial System")
- ** Real World Banking and Finance: Chapter 7 ("The International Financial System")
- ** Ha-Joon Chang and Ilene Grabel. 2002. *Reclaiming Development: An Alternative Economic Policy Manual* pp. 150-1199.

XI. Retirement Finance

- ** Real World Banking and Finance: Chapter 6 ("Retirement Finance")