

Policy Responses to the Great Recession

(provisional, subject to revision)

1. INTRODUCTION

This course will examine the hypotheses underlying the origins and propagation of the Great Recession of 2007, and the policy responses that have occurred along a variety of dimensions. The candidate causes include lax monetary policy, the “saving glut”, deregulation, securitization and the widespread use of derivatives, the activities of the Government Sponsored Enterprises (“Fannie Mae” and “Freddie Mac”), among others.

The discussion of responses will include the conduct of monetary policy and fiscal policy, the appropriateness of financial regulatory policy, the harmonization of international financial policy and trade policy. Other policies not typically thought to be related to the workings of the macro economy (housing, energy, sectoral/industrial policy, e.g., automobiles) will also be examined.

Prerequisites: Macroeconomics (either Econ 302 or Public Affairs 854), or consent of instructor. Economics 330 (“Money and Banking”) will be useful.

2. OFFICE HOURS

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Updated information will be posted on the course website,
http://www.ssc.wisc.edu/~mchinn/web974_f09.html.

3. SCHEDULE AND READINGS

There is no textbook. However, for background, one can refer to Caves, Frankel and Jones, *World Trade and Payments*, 10th Edition (Addison-Wesley Longman, 2006), Hall and Papell, *Macroeconomics: Economic growth, fluctuations, and policy*, 6th Edition (Norton, 2005) or any other standard intermediate level macroeconomics textbook. Required readings will be assigned during the semester from the Web, as well as a book manuscript written by myself and Jeffrey Frieden. You will also be expected to refer to the following weblog for current macroeconomic commentary: <http://www.econbrowser.com> .

1. Review

[Notes on IS-LM](#)

[Notes on Transactions and Portfolio Crowding Out](#)

2. Background

[IMF, *World Economic Outlook*, April 2009, Chapter 1.](#)

3. Causes

[M. Jickling, *Causes of the Financial Crisis*, \(Congressional Research Service, January 29, 2009\).](#)

[Council of Economic Advisers, *Economic Report of the President, 2009* \(U.S. GPO, 2009\), Chapter 2.](#)

[John B. Taylor, "The Financial Crisis and the Policy Responses: An Empirical Analysis of What Went Wrong," \(November 2008\).](#)

~~Chinn and Frieden, *The Lost Decade*, Chapters 2 and 3.~~

4. Financial complications

Chinn and Frieden, Chapter 4.

[M. Brunnermeier, "Deciphering the Liquidity and Credit Crunch, 2007-2008," *Journal of Economic Perspectives* 23\(1\) \(Winter 2009\).](#)

[P. Mizen, "The Credit Crunch of 2007-2008: A Discussion of the Background, Market Reactions, and Policy Responses," *Federal Reserve Bank of St. Louis Review* 90\(5\) \(September/October 2008\).](#)

[J.D. Coval, J. Jurek, E. Stafford, "The Economics of Structured Finance," *Harvard Business School Working Paper* 09-060. Published *Journal of Economic Perspectives* 23\(1\) \(Winter 2009\).](#)

[David Greenlaw, Jan Hatzius, Anil K Kashyap, Hyun Song Shin, "Leveraged Losses: Lessons from the Mortgage Market Meltdown," paper presented at US Monetary Policy Forum Conference, February 29, 2008.](#)

[IMF, *World Economic Outlook*, April 2009, Chapter 4.](#)

[IMF, *Global Financial Stability Report* \(October 2009\), Chapter 1.](#)

5. Recession

[NBER, Business Cycle Expansions and Contractions.](#)

[The Financial and Economic Crisis Interpreted in a CC-LM Model](#)

[IMF, *World Economic Outlook*, April 2009, Chapter 3.](#)

6. Macro policy responses

6.1 Fiscal Policy

[CBO, *Options for Responding to Short-Term Economic Weakness* \(January 2008\).](#)

[Douglas W. Elmendorf, “The State of the Economy and Issues in Developing an Effective Policy Response,” testimony before the Committee on the Budget, U.S. House of Representatives \(January 27, 2009\).](#)

[CEA, *Estimates of Job Creation from the American Recovery and Reinvestment Act of 2009* \(Executive Office of the President, May 2009\)](#)

[CBO, *Estimated Macroeconomic Impacts of the American Recovery and Reinvestment Act of 2009* \(March 2, 2009\)](#)

[C. Freedman, M. Kumhof, D. Laxton, and J. Lee, “The Case for Global Fiscal Stimulus,” *IMF Staff Position Note* No. 09/03 \(March 6, 2009\).](#)

[D. Leigh and S.J. Stehn, “Fiscal and Monetary Policy During Downturns: Evidence from the G7,” *IMF Working Paper* No.09/50 \(March 2009\).](#)

[D. Elmendorf, “Implementation Lags of Fiscal Policy,” presentation at IMF Fiscal Affairs and Research Departments Conference on Fiscal Policy \(June 2, 2009\).](#)

6.2 Monetary Policy

[BIS, “Chapter VI. Policy responses to the crisis,” *BIS Annual Report* \(June 29, 2009\).](#)

[Glenn Rudebusch, “The Fed’s Monetary Policy Response to the Current Crisis,” *FRBSF Economic Letter* 2009-17, May 22, 2009.](#)

[James Hamilton, “Concerns about the Fed's New Balance Sheet, in *The Road Ahead for the Fed*,” edited by John D. Ciorciari and John B. Taylor, Stanford: Hoover Institution Press, 2009.](#)

7. Financial Regulation

[BIS, “Chapter VII. Risks and opportunities: towards a fail-safe financial system, BIS Annual Report \(June 29, 2009\).](#)

[Mathias Dewatripont, Xavier Freixas, and Richard Portes, editors, *Macroeconomic Stability and Financial Regulation: Key Issues for the G20* \(CEPR, 2 March 2009\), pp. 91- .](#)

6. Trade Policy and Industrial Policy

[Richard Baldwin, and Simon J Evenett, editors, *The collapse of global trade, murky protectionism, and the crisis: Recommendations for the G20* \(CEPR, 5 March 2009\).](#)

8. Long term prospects

[OECD, “Chapter 4: Beyond the Crisis: Medium-term Challenges Relating to Potential Output, Unemployment and Fiscal Positions,” *OECD Economic Outlook* No 85 \(2009\).](#)

Chinn and Frieden, *The Lost Decade*, Chapter 8.

4. GRADING

Letter grading is determined as follows:

20%	Problem sets (×2)
80%	Term paper

Late assignments will not be accepted for credit. Although the problem sets do not constitute a large portion of the grade, I strongly encourage you to do the assignments in a timely and serious fashion. The problem sets provide valuable information regarding your grasp of the concepts.

5. THE TERM PAPER

A 20 page term paper will be due at the end of the semester. You will have latitude in terms of the choice of topic. However, I will be able to give you more guidance on certain topics than others. Additional details regarding this assignment, along with suggested readings, will be provided later in the term.