

ECON 714: Macroeconomic Theory II

3 credit course (2 lectures per week):

This 3 CR course has two 75 min lectures per week. Students are expected to work approximately 6 hours outside class to complete assignments and learn the relevant material.

Professor: Noah Williams

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Office hours: 2:30-3:30 Thursday, or by appointment.

TA: Anson Zhou, email: anson.zhou@wisc.edu

Course Schedule:

Lectures: Monday and Wednesday from 11:00-12:15, Birge B302

All course materials will be on the class web page: <http://www.ssc.wisc.edu/~nwilliam/Econ714>

Course Learning Outcomes:

Upon completing this course students will be able to:

- Explain how the economy works at aggregate level and how output, employment, prices, and interest rates are determined.
- Describe the factors underlying economic growth, business cycles, inflation, and unemployment.
- Assess rigorously the effects of various government policies and outside shocks on these features of the economy.

Requirements for this portion of the class include attendance at the lectures, problem sets (40% of grade), and a midterm (60%). No late homework will be accepted.

The midterm (final for this portion) will be in class on March 12.

Schedule of topics (subject to change, see web page):

1. Asset pricing
2. Economic fluctuations and incomplete markets
3. Search equilibrium
4. Fiscal policy
5. Monetary models: classical models and search
6. The New Keynesian model and monetary policy

There are no required textbooks for the course, but we'll use some of the following books:

- Ljungqvist, Lars and Thomas J. Sargent. (2004) *Recursive Macroeconomic Theory*. MIT Press, Cambridge. 2nd Edition. (LS)
- Stokey, Nancy and Robert E. Lucas, Jr. with Edward C. Prescott. (1989) *Recursive Methods in Economic Dynamics*, Harvard University Press, Cambridge. (SLP)
- Walsh, Carl E. (2003) *Monetary Theory and Policy*. MIT Press, Cambridge. 2nd Edition

Reading List

Subject to change, check the class web page for updates. More crucial readings are marked *.

Asset pricing and general equilibrium in complete and incomplete markets:

*SLP, Chapter 9, 10.6.

*LS, Chapters 8, 13.

*Cochrane, John H. (2001) *Asset Pricing*, Ch. 1, 2.

*Lucas, Robert E. (1978) "Asset Prices in an Exchange Economy," *Econometrica*, 46: 1426-1445.

Mehra, Rajnish and Edward C. Prescott (1985) "The Equity Premium: A Puzzle," *Journal of Monetary Economics*, 15: 145-162.

The real business cycle model:

*King and Rebelo (1999) "Resuscitating Real Business Cycles", Ch. 14 of *Handbook of Macroeconomics* (J. Taylor and M. Woodford, eds.), especially Sec. 3 and Appendix A.

Brock, William A. and Leonard J. Mirman (1972) "Optimal Economic Growth and Uncertainty: The Discounted Case," *Journal of Economic Theory* 4: 479-513.

Kydland, Finn and Edward C. Prescott (1982) "Time to Build and Aggregate Fluctuations," *Econometrica* 50: 1345-1370.

Incomplete markets models:

*LS, Chapter 17.

Ayagari, Rao (1994) "Uninsured Idiosyncratic Risk and Aggregate Saving," *Quarterly Journal of Economics*, 109: 659-84.

*Krusell, Per and Anthony A. Smith (1998) "Income and Wealth Heterogeneity in the Macroeconomy," *Journal of Political Economy*, 106: 867-896.

Search equilibrium:

*Pissarides, Christopher A. (2000) *Equilibrium Unemployment Theory*, 2nd edition. MIT Press, Cambridge. Chapters 1-2.

Dale T. Mortensen, Dale T. and Christopher A. Pissarides (1994), "Job Creation and Job Destruction in the Theory of Unemployment," *Review of Economic Studies*, 61: 397-415

Fiscal policy:

*LS, Chapter 11, 15.1-15.7.

*Chari and Kehoe (1999), “Optimal Fiscal and Monetary Policy,” Ch. 26 of *Handbook of Macroeconomics* (J. Taylor and M. Woodford, eds.), especially Sec. 2.1-2.3

Lucas, Robert E., Jr. and Nancy L. Stokey (1983), “Optimal Fiscal and Monetary policy in an Economy without Capital,” *Journal of Monetary Economics*, 12:55-93.

*Golosov, M., N. Kocherlakota, and A. Tsyvinski (2003) “Optimal Indirect and Capital Taxation,” *Review of Economic Studies*, 70: 569-587.

Albanesi, S. and C. Sleet (2006) “Dynamic Optimal Taxation with Private Information,” *Review of Economic Studies*, 73: 1-30.

Kocherlakota, N. (2005) “Zero Expected Wealth Taxes: A Mirrlees Approach to Dynamic Optimal Taxation,” *Econometrica*, 73:1587-1621

Monetary models:

Currency in the utility function:

*Walsh, Chapter 2

Shopping time and cash-in-advance models:

*Walsh, Chapter 3,

LS, Chapter 24

Search models:

*Walsh, Chapter 3.4.2

*LS, Chapter 26.8

*Wright, R. (2008) “Search-and-Matching Models of Monetary Exchange,” *The New Palgrave*, 2nd Edition.

The New Keynesian model and monetary policy

*Walsh, Chapter 5.4, 11

Woodford, *Interest and Prices*, Chapter 3.1-3.2, 4.1

*Clarida, R., J. Gali, and M. Gertler (1999) “The Science of Monetary Policy: A New Keynesian Perspective,” *Journal of Economic Literature*, 38: 1661-1707.

Misconduct Statement

Academic Integrity is critical to maintaining fair and knowledge based learning at UW Madison. Academic dishonesty is a serious violation: it undermines the bonds of trust and honesty between members of our academic community, degrades the value of your degree and defrauds those who may eventually depend upon your knowledge and integrity.

Examples of academic misconduct include, but are not limited to: cheating on an examination (copying from another student's paper, referring to materials on the exam other than those explicitly permitted, continuing to work on an exam after the time has expired, turning in an exam for regrading after making changes to the exam), copying the homework of someone else, submitting for credit work done by someone else, stealing examinations or course materials, tampering with the grade records or with another student's work, or knowingly and intentionally assisting another student in any of the above. Students are reminded that online sources, including anonymous or unattributed ones like Wikipedia, still need to be cited like any other source; and copying from any source without attribution is considered plagiarism.

The Dept. of Economics will deal with these offenses harshly following UWS14 procedures (<http://students.wisc.edu/saja/misconduct/UWS14.html>):

1. The penalty for misconduct in most cases will be removal from the course and a failing grade,
2. The department will inform the Dean of Students as required and additional sanctions may be applied.
3. The department will keep an internal record of misconduct incidents. This information will be made available to teaching faculty writing recommendation letters and to admission offices of the School of Business and Engineering.

If you think you see incidents of misconduct, you should tell your instructor about them, in which case they will take appropriate action and protect your identity. You could also choose to contact our administrator (Tammy Herbst-Koel, therbst@wisc.edu) and your identity will be kept confidential.

Grievance Procedure

The Department of Economics has developed a grievance procedure through which you may register comments or complaints about a course, an instructor, or a teaching assistant. The Department continues to provide a course evaluation each semester in every class. If you wish to make anonymous complaints to an instructor or teaching assistant, the appropriate vehicle is the course evaluation. If you have a disagreement with an instructor or a teaching assistant, we strongly encourage you to try to resolve the dispute with him or her directly. The grievance procedure is designed for situations where neither of these channels is appropriate.

If you wish to file a grievance, you should go to room 7238 Social Science and request a Course Comment Sheet. When completing the comment sheet, you will need to provide a detailed statement that describes what aspects of the course you find unsatisfactory. You will need to sign the sheet and provide your student identification number, your address, and a phone where you can be reached. The Department plans to investigate comments fully and will respond in writing to complaints.

Your name, address, phone number, and student ID number will not be revealed to the instructor or teaching assistant involved and will be treated as confidential. The Department needs this information, because it may become necessary for a commenting student to have a meeting with the department chair or a nominee to gather additional information. A name and address are necessary for providing a written response.