

Spring 2007
Revised March 19, 2007

New York University
Stern School of Business

B30.2333
Monetary Policy, Banks and Central Banks

Paul Wachtel

The structure of the financial system and the role of central banks are often in the news as countries cope with banking crises and macroeconomic problems. *Monetary Policy, Banks and Central Banks* is an MBA elective course that examines the structure of financial systems from both perspectives. Several broad questions are addressed over the course of the semester:

- Why is monetary policy important?
- How is monetary policy conducted?
- How does monetary policy affect the macro economy?
- Why and how do countries regulate the financial sector?
- How does monetary policy, financial sector regulation and exchange rate management differ around the world?
- How is globalization of the financial sector affecting the conduct and efficacy of monetary policy?

These questions, among others, are discussed with a combination of lecture, discussion, case analysis and student presentations.

Course info. B30.2333 meets on Thursday at 6:00 from February 8 – May 3 (with a Spring break on March 15). The instructor is Prof. Paul Wachtel whose office is KMEC 7-69. He can be reached at 212 998 4030 and pwachtel@stern.nyu.edu. There are no fixed office hours but appointments with Prof. Wachtel can be arranged (by email) almost any day and many evenings.

Course materials. There is no assigned textbook because none exists. However, there is a wealth of publicly available material, which will be available through BLACKBOARD. Files or links for the course readings are on Blackboard.

Powerpoint lecture notes will be distributed in class.

Specific articles and questions for class discussions will be posted and distributed by email. Students are expected to be prepared when a class discussions is announced.

Students are expected to keep abreast of Monetary Policy developments around the world. To do so, become a regular reader of the *Financial Times*, the *Wall Street Journal* or *The Economist*.

Course Requirements and Grades. The course grades will be based on the following with percentages indicated in parentheses:

- Assignments and cases (See below for specific assignments) (30%)
 - (i) Class discussions of FOMC meetings
 - (ii) Fed decision making in 1992
 - (iii) Brazil 2003 case
 - (iv) Central bank comparison
- Group presentation and paper (35%)
- Final QUIZ (25%) – May 8
- Class participation (10%)

Course Outline (REVISED March 19, 2007)

Session 1 – February 8

(1) Money and financial institutions

- Definition and role of money
- Banking business and intermediation
- Origins and Roles of Central Bank

Discussion of Jan. 30-31 FOMC meeting

Session 2 – February 15

(2) Monetary Policy and Macroeconomics

- Money in macro theory
- Keynesian and Classical (Quantity theory) approaches
- Monetary transmission mechanism

Session 3 – February 22

(3) Central banks and monetary policy

- Tools of monetary policy
- What can a central bank do?
- Monetary policy institutions in US
- Comparison of Fed and ECB

Case on Fed decision making in 1992

Session 4 – March 1

Session 5 – March 8

SPRING BREAK

Session 6 – March 22

(4) Monetary policy operations in the US

- Policy operations in the US

- Day to day activities

Discussion of FOMC meeting on March 20-21.

GROUP PRESENTATIONS BEGIN

Presentation - S & L crisis

Session 7 – March 29

(5) Conducting monetary policy

- Instruments, targets, objectives
- Credibility and reputation
- Central bank independence

Presentation – Argentina currency board

Session 8 – April 5

(6) Exchange rate regimes and international financial institutions

- Gold standard and Bretton Woods
- Fixed exchange rates, dollarization, currency boards
- Capital controls
- Currency unions and the Euro
- IMF and financial crises of the 90s
- International financial architecture of the future

Assignment due – Central bank comparison

Presentation – Yield curve

Session 9 – April 12

(7) Financial stability and bank regulation

- Why regulate
- Trends in banking
- US financial regulation and deregulation
- Regulatory issues - deposit insurance, capital adequacy and lender of last resort
- Basle II and international financial regulatory policy
- Deposit insurance

Presentation - China

Session 10 – April 19

Presentation – IMF

Session 11 – April 26

Case discussion and assignment – Japan

Session 12 – May 3

Final Quiz – 90 minutes

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COURSE READINGS

** indicates more important items*

If link is not provided document is available on Blackboard – Course Readings

0. Background and general information

The RGE Monitor – the renowned Roubini Global Economics data and information source maintained by Stern’s Prof. Nouriel Roubini – is available to all Stern students. To register for it, you need to use a campus computer; the registration screen will allow free registration as long as a valid NYU email address is used for registration. After registration, RGE can be accessed from any computer with your username and password.

<http://www.rgemonitor.com/>

[*Fedpoints*](#) is a reference series explaining the structure and functions of the Federal Reserve System and the economic concepts relevant to its work.

[*Understanding Open Market Operations*](#), M.A. Akhtar, Federal Reserve Bank of New York.

[*The Federal Reserve System: Purposes and Functions*](#), Board of Governors of the Federal Reserve.

[*U.S. Monetary Policy and Financial Markets*](#). A. Meulendyke, Federal Reserve Bank of New York, 1998 (dated but still useful).

1. Money and financial institutions

* [*Money Matters: The American Experience with Money*](#). FRB of Chicago.
Michael Bryan, [*Island Money*](#), *Economic Commentary*, FRB of Cleveland, Feb. 2004.

* Sandra Pianalto, [*A Perspective on Monetary Policy*](#), *Economic Commentary*, FRB of Cleveland, May 2004.

*Economic Focus, *The Economist*, [“Who Needs Money?”](#) Jan. 22, 2000 and [“E-Money Revisited.”](#) June 22, 2000.

*S. Cecchetti, [“The Future of Financial Intermediation and Regulation,”](#) FRBNY Current Issues, May 1999.

2. Monetary Policy and Macroeconomics

Charles Morris and Gordon Sellon, Jr., [Bank Lending and Monetary Policy: Evidence on a Credit Channel](#), FRB of Kansas City *Economic Review*, 1995 I

*Bank of England Monetary Policy Committee, [The Transmission of Monetary Policy](#), May 1999.

*Simon Hall, [Credit channel effects in the monetary transmission mechanism](#), Bank of England, 2001.

*David Altig, [“When is Fed Rate Hike Not Tighter Policy?”](#) *Economic Commentary*, FRB of Cleveland, August 2004.

R.W. Hafer, [What Remains of Monetarism?](#) FRB of Atlanta *Economic Review*, 2001 IV. (* particularly pp.1-8)

*Ben Bernanke, [Balance Sheets and the Recovery, February 21, 2003](#)

*Ben Bernanke, [The Benefits of Price Stability](#), February 24, 2006.

Ben Bernanke and Mark Gertler, “Inside the Black Box: The Credit Channel of Monetary Policy Transmission”, *Journal of Economic Perspectives*, Autumn 1995.

*Milton Friedman, “The Fed’s Thermostat”, *Wall Street Journal*, August 19, 2003.

3. Central banks and monetary policy

A Note on Monetary Policy and Institutions, Paul Wachtel.

*Pollard, [“A Look Inside Two Central Banks: The European Central Bank and the Federal Reserve](#), FRB of St. Louis Review, Jan./Feb. 2003.

*[Five Years of the Euro: Successes and New Challenges](#), *Southwest Economy*, FRB of Dallas, July/August 2004.

Ed Stevens, [“The Euro”](#), FRB of Cleveland *Economic Commentary*, Jan. 1, 1999.

*Ed Stevens, [“The New Discount Window,”](#) FRB of Cleveland, *Economic Commentary*, May 15, 2003.

*Gordon Sellon and Stuart Weiner, [Monetary Policy Without Reserve Requirements: Analytical Issues](#), *Economic Review* FRB of Kansas City, 4th Quarter 1996 and...:[Case Studies and Options for the U.S.](#), *Economic Review* FRB of Kansas City, 2nd Quarter 1997.

4. Monetary policy operations in the US

*Lawrence Meyer, [Come With Me to FOMC](#), Federal Reserve Board, 1998.

*Betty Joyce Nash, [The Federal Open Market Committee: Data and Intuition Meet](#), FRB of Richmond, *Region Focus*, Summer 2002

*P. Davies, [Right on Target: A Behind the Scenes look at open market operations](#), *The Region*, FRB of Minneapolis, December 2004.

[“Domestic Open Market Operations during 2005”](#), Federal Reserve Bank of New York.

[“Open Market Operations in the 1990s”](#), Federal Reserve Bulletin, November 1997.

Paul Bennett and Spence Hilton, [Falling Reserve Balances and the Federal Funds Rate](#), *Current Issues in Economics and Finance*, FRB of New York, April 1997.

[The Evolution of the Federal Reserve's Intraday Credit Policies](#), *Federal Reserve Bulletin*, Feb. 2002.

*Christopher Neely, [“The Federal Reserve Responds to Crises: Sept. 11 Was Not the First”](#), *Review*, FRB of St. Louis, March/April 2004.

5. Conducting monetary policy

*William Poole, [Monetary Policy Rules?](#) *Review* FRB of St. Louis, Mar/Apr 1999.

* Ben Bernanke, [‘Constrained Discretion’ and Monetary Policy](#), FR Board, February 3, 2003.

*S. Piantato, [“Expectations, communications and monetary policy,”](#) Economic Commentary FRB of Cleveland, April 2005.

*William Poole, [FOMC Transparency](#), *Review* FRB of St. Louis, Jan/Feb 2005.

J. Haubrich, [Waiting for Policy Rules](#), *Economic Commentary*, FRB of Cleveland, Jan 2000.

George Kahn and Klara Parrish, [Conducting Monetary Policy With Inflation Targets](#), *Economic Review*, FRB of Kansas City, 3rd Quarter 1998.

* William Poole, [Inflation Targeting](#), *Review* FRB of St. Louis, May/June 2006.

*Lawrence Meyer, [Inflation Targets and Inflation Targeting](#), FRB of St. Louis *Review*, Nov./Dec. 2001.

*Frederic Mishkin and Adam Posen, [Inflation Targeting: Lessons from Four Countries](#), *Economic Policy Review*, August 1997. (Read Parts I-II (pp. 9-17); VII-VIII (pp. 87-96) and take a look at one of the case studies).

*P. Gomme, [Why policy makers might care about stock market bubbles](#), Economic Commentary FRB of Cleveland, May 2005.

Roger Ferguson, [“Recessions and recoveries associated with asset price movements,”](#) Federal Reserve Board, January 12, 2005.

*Adam S. Posen, [“Why Central Banks should not burst bubbles.”](#) Institute for International Economics, January 2006.

* Evan F. Koenig, [“Monetary Policy Prospects”](#), *Southwest Economy*, FRB of Dallas, May/June 2004.

*William Poole, [The Fed’s Monetary Policy Rule](#), *Review* FRB of St. Louis, January/February 2006.

* [Taylor’s rule](#), St. Louis Fed

Interest rates and Taylor Rule, HSBC May 1997

* Ben Bernanke, [“Deflation: Making Sure “it” doesn’t happen here”](#), Federal Reserve Board, Nov. 2002

E. Stevens, [“Beyond Zero: Transparency in the Bank of Japan’s Monetary Policy”](#) FRB of Cleveland *Economic Commentary*, March. 2001.

*C. Carlstrom and T. Fuerst, [Central Bank Independence: The Key to Price Stability](#), FRB of Cleveland *Economic Commentary*, September 1, 2006.

*Paul Gomme, [Central Bank Credibility](#), FRB of Cleveland *Economic Commentary*, August 1, 2006

6. Exchange rate arrangements and international financial architecture

Charles Enoch and Anne-Marie Gulde, ["Are Currency Boards a Cure for All Monetary Problems?"](#), *Finance & Development*, Dec.1998.

*Carlos Zarragoza, ["Can Currency Boards Prevent Devaluations and Financial Meltdowns?"](#), FRB of Dallas, *The Southwest Economy*, 1995.

*Christopher J. Neely, [An Introduction to Capital Controls](#), *Review*, FRB of St.Louis, 81(6), November/December 1999.

*Roberto Chang, ["Dollarization: A Scorecard"](#), FRB of Atlanta *Economic Review*, 2000 III.

* [Moving to a Flexible Exchange Rate: How, When, and How Fast?](#) *Economic Issues*, IMF, Sept. 2006.

*Robert Mundell, ["A Theory of Optimum Currency Areas"](#), 1968.

Robert Mundell, "Threat to Prosperity", *Wall Street Journal*, March 30, 2000

Richard W. Kopcke, ["Currency Boards: Once and Future Monetary Regimes?"](#), *New England Economic Review*, FRB of Boston, May/June 1999.

G. Antinolfi and T. Keister, ["Dollarization as a Monetary Arrangement for Emerging Market Economies"](#), FRB of St. Louis *Review*, 2001.

*[Is Official Foreign Exchanger Intervention Effective?](#) FRB of San Francisco, *Economic Letter*, July 2003.

Owen Humpage, [On the Rotation of the Earth...And Exchange Rate Policy](#), *Economic Commentary*, FRB of Cleveland, Feb. 2004.

Anne Krueger, ["International Financial Architecture for 2002: A new approach to sovereign debt restructuring.](#): IMF, November 2001.

* Timothy Lane and Steven Phillips, [Moral Hazard](#), *IMF Economic Issues* #28, 2002.

* Mervyn King, [Reform of the IMF](#), Bank of England, Feb. 2006.

7. Financial stability and bank regulation

*[Capital Standards for Banks: The Evolving Basle Accord](#), *Federal Reserve Bulletin*, Sept. 2003.

* L. Randall Wray, [CAN BASEL II ENHANCE FINANCIAL STABILITY?](#), Levy Institute Public Policy Brief, 2006.

Ed Stephens, ["Evolution In Banking supervision."](#) FRB of Cleveland *Economic Commentary*, March 2000.

M. Quintyn and M. Taylor, ["Should Financial Sector Regulators be Independent?"](#) *IMF Economic Issues*, 2004.

*T. Latter, [The Causes and Management of Banking Crises](#), Bank Of England, 1997.

*G. Shinasi, ["Preserving Financial Stability,"](#) *IMF Economic Issues*, 2005.

Claudia Dziobek, [“Lessons from Systemic Bank Structuring,”](#) IMF Economic Issues #14, 1998.

*Gillian Garcia, [“Protecting Bank Deposits,”](#) IMF Economic Issues, 1997.

Mark D. Vaughan and David C. Wheelock [“Deposit Insurance Reform: Is It Déjà Vu All Over Again?”](#) FRB St. Louis, Regional Economist, Oct. 2002.

Adam M. Zaretsky, [“A New Universe in Banking,”](#) FRB St. Louis, Regional Economist, April 2000.

*Alan Greenspan, [“The Role of Capital in Optimal Banking Supervision and Regulation”](#), FRB of NY Economic Policy Review, Oct. 1998.