

January 21, 2008

New York University
Stern School of Business

C30.0221 Monetary Policy and Banking
Spring 2008
Monday and Wednesday from 11:00-12:15

Prof. Paul Wachtel

Monetary policy in the U.S. and around the world is frequently in the news as policymakers work hard to control inflation, bring about balanced growth and maintain the stability of the financial system. *Monetary Policy and Banking* is a Stern Economics elective course that examines the institutions that run macroeconomic and banking policy and explains how they are supposed to work.

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 is banking and financial sector regulation important?
- How does monetary policy relate to exchange rate management?
- How is globalization of the financial sector affecting the conduct and efficacy of monetary policy?

Monetary policy is the most important macro policy tool because it is used to attain three essential goals: a) to keep an economy out of recession, b) to keep inflation under control and c) to preserve the stability of the banking environment. The course examines the structure of the central bank, the Federal Reserve in the U.S., and explains how policy makers try to attain these three goals. The role of money, interest rates and exchange rates are studied as well as the way in which monetary policy affects each. In addition, the regulation of the financial sector and efforts to maintain stability are examined. The ways in which policy makers respond to financial crises and chronic inflation are also examined.

The course emphasizes current problems such as how the Fed should respond to the possibility of a recession and to fragility of mortgage markets. In addition, monetary policy developments around the world are discussed such as the expansion of the Euro area, chronic deflation in Japan and exchange rate and banking crises in emerging

markets. We will carefully follow all of the Federal Reserve Open Market Committee meetings during the semester.

Course staff. 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.

Course materials.

- F. Mishkin, *The Economics of Money Banking and Financial Markets*, 8th ed.
- Additional materials on monetary policy coming from central banks, the IMF, etc. All additional materials will be available through BLACKBOARD
- 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*.
- The RGE Monitor – the renowned Roubini Global Economics data and information source maintained by Stern’s Prof. Nouriel Roubini – is a useful resource for finding information for the presentations and following current events. Stern students may register for it from a campus computer. The initial registration screen will allow free registration as long as a valid NYU email address is used. After registration is completed, RGE can be accessed from any computer with your username and password.

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

Course Requirements. (further information to follow)

- Midterm quiz – March 3
- Assignments and cases
 - The upcoming FOMC meeting – March 14
 - TBA
- Presentations and papers – after Spring break
- Final exam

Course Grading (subject to revision).

The course grades will be based on the following with percentages indicated in parentheses:

- Assignments and cases – 20%
- Midterm – 20%
- Presentation and paper – 20%
- Final – 25%
- Class participation – 15%

Course Outline

1. Monetary Policy and Banking: An Introduction
 - Financial intermediation
 - Investment, savings and financial structure
 - What is money?
 - READING: Mishkin chapters 1-3

2. Banking
 - Economics of financial structure
 - What is a bank and why is it special?
 - Banking industry, structure, competition and regulation
 - Why do we regulate banks?
 - READING: Mishkin chapters 8-11

3. Central banking and the money supply
 - Why do we have central banks?
 - Structure of the Federal Reserve System
 - The European Central Bank and others central banks
 - Money creation
 - READING: Mishkin chapters 12-14

4. Conduct of monetary policy
 - Tools of monetary policy – open market operations, discounting, reserves
 - Goals and targets of a central bank
 - Inflation targeting
 - Operating procedures and communication
 - READING: Mishkin chapter 15-16

5. Monetary policy and the macro economy
 - How monetary policy affects the macro economy - Transmission mechanism
 - Keynesian and Monetarist channels
 - Expectations and credibility
 - Money and inflation
 - READING: Mishkin chapter 23-25

6. Topics in monetary policy and banking

- Foreign exchange crises
- Banking crises
- Exchange rate systems
- Capital controls
- The world's central bank – the IMF
- New advances in regulation – Basle II
- Deposit insurance
- And more....

7. Topics in monetary policy history

- The Fed and the Great Depression
- The Fed and inflation – 1970s and 80s
- Deflation in Japan in the 1990s – monetary policy that failed
- The US Savings and Loan crisis
- Banking and exchange rate crises in Asia in 1998
- Argentina, Brazil and Mexico in the 1990s
- The mortgage meltdown and the recession of 2009
- And more...