This course examines the global macroeconomic and financial setting of business. It deals with flows of money, interest rates and exchange rates, reserves and debt, and problems of economic management and policy formation -- the so-called monetary aspects of the global economy. The course is paired with a first-half course taught by Prof. Wilbur Chung which considers global competitive advantage, trade flows and commercial policies, global direct investment patterns and the operation of multinational firms -- the so-called real sector issues in the global business environment.

The course builds logically toward an integrated open-economy macroeconomic structure which can be helpful in diagnosing what’s going on and how it may influence the management of business firms. Among the questions considered are the following:

$ What determines rates of economic growth, and why do growth rates differ so dramatically among countries?

$ How is the level of economic activity determined, and how do fiscal, monetary and trade policies influence it?

$ What drives exchange rates and how do they affect investors and business firms from a strategic and tactical perspectives?

$ How are exchange rates and interest rates linked through increasingly seamless global financial markets?

$ How are exchange rates and inflation rates related, and what happens when things get seriously out of line?

$ How do interest rates and inflation rates affect the real economy, and vice-versa?

$ What are policymakers trying to achieve, how do they go about it, and how does the “policy mix” affect business decisions?
What are today’s important macroeconomic issues, including the future of the global economic and financial “architecture?”

In general, the course is strategy and policy oriented, with plenty of practical examples. Theory and models are used only to the extent that they can be used in a practical way to understand what is going on. The objective is to provide students with a broad-gauge, user-friendly diagnostic tool for interpreting the macroeconomic environment of business.

Materials


Cases:

*Federal National Mortgage Association* (to be distributed in class).

*Acme de Mexico S.A. de C.V. - Recuerdos Tristes de un Pasado Alegre* (to be distributed in class).

Homepage

The homepage for this course can be found at [http://www.stern.nyu.edu/~iwalter/](http://www.stern.nyu.edu/~iwalter/). Copies of various materials and media reports will be posted from time to time. Students will be notified by e-mail about new postings, which should be read for the next class session.

Course Requirements and Grading

Students should read the assigned material *before* coming to each class. Some of the textbook reading is extensive, and should be started well ahead of time in order to keep up.

There is one case writeup -- *Acme de Mexico S.A. de C.V.* This is due at the beginning of the last class on December 12th, during which the case will be discussed. This writeup will represent 40% of the course grade.
There will be a final exam on all of the material covered in the course, which is scheduled from 6:00 to 8:00 pm on Thursday, December 19th. This will represent 60% of the course grade.

Class participation and discussion is important. Strong and consistent classroom performance can raise a student's assessment by up to one full letter-grade.

Instructor

Ingo Walter, Charles Simon Professor of Applied Financial Economics and Director, New York University Salomon Center. Phone: 998-0707. Fax: 995-4220. E-mail iwalter@stern.nyu.edu.

Course Outline and Assignments

Pre-reading:

Please be sure to read the following chapters in the textbook before the first class session: David Miles and Andrew Scott, *Macroeconomics*, Chapters 1-3.

Session 1  October 31  Introduction -- Macroeconomic Performance

About the Course
How the course is structured.
Course mechanics and evaluation.

Economic Growth: Basic Facts and Theory
Growth rates around the world.
Framework for understanding economic growth.
How useful are growth models and what do they explain?
The Solow neoclassical growth model.
Why growth rates differ through time -- current views on growth cycles.
Why growth differs among national economies.
What we don't know -- or can't yet measure -- about economic growth.

Economic Growth: The Role of Productivity
Using growth models.
What determines productivity and how do we measure it?
Productivity concepts and growth accounting.
Growth and problems of structural adjustment.
Getting it up and keeping it up -- policies for growth.
Productivity slowdown and the “New Economy.”

Assignment: David Miles and Andrew Scott, *Macroeconomics*, Chapters 4-7.
Session 2  November 7  Capacity Utilization and National Income

Aggregate demand.
Consumer spending, income and wealth.
Investment spending.
Government spending
Exports and imports.
The IS function.
The LM function
General equilibrium
Imbalances in the economy.


Session 3  November 14  Tools of Macroeconomic Policy

**Money, Finance and Monetary Policy**
How is the money supply defined and controlled?
Monetary policy, interest rates and asset prices.
What’s so bad about inflation?
How can monetary policy drive inflationary pressures?
Sticky and un-sticky prices in the real and financial economy.
Monetary policy and the exchange rate: Sterilized and unsterilized intervention.
Coping with financial innovation.
Financial intermediation dynamics and the importance of regulation.

**Monetary Conditions and the Real Economy**
How real-sector developments affect interest rates and inflation rates.
Whatever happened to the Phillips curve?
Monetary policy and economic activity.
What central banks try to achieve, and why?
Central bank signaling and business decisions -- watching their smoke.

**Economic Policy and the Public Purse**
The budget: Taxes and spending before and after the fact.
What’s fixed and what’s variable in national budgets.
Why the level and structure of taxes matter.
How fiscal policy affects the real and financial economy.

**The Politics of Economic Policy**
Whose ox is gored? The permanent battle over economic policy choices.
Paralysis in fiscal policy and one-armed policymakers.
Central bank independence -- does it matter?
What’s the evidence on central bank independence?
What does central bank independence really mean, and who cares?
Desperate problems and radical solutions: Currency boards.

**Assignment:** David Miles and Andrew Scott, *Macroeconomics*, Chapters 10-17.

**November 21**

**Global Linkages**

**Foreign Exchange**
Foreign exchange: Transaction volumes and market structure.
Where does forex demand come from?
Where does forex supply come from?
Forex market equilibrium.
The “effective” exchange rate
What makes exchange rates volatile?
Central banks, intervention and forex market disequilibrium -- a first-cut.

**The Balance of Payments, Exchange Rates and Interest Rates**
The balance of payments accounts and forex: Two sides of a coin.
Understanding and interpreting balance of payments data -- IMF version.
How are interest rates and exchange rate linked?
Interest arbitrage -- why it’s hard to make money in efficient markets.
How currency swaps link global markets.
Uncovered interest parity, covered interest parity -- and all that.
How country risk and counterparty risk can introduce market anomalies.
Transactions costs and market efficiency.

**Exchange Rates and Inflation Rates**
Why inflation rates ought to affect exchange rates.
From Big Macs to hard- and soft-anchor purchasing power parity relationships.
Using parity lines: What they do and don’t mean -- UBS Brinson client services.
Defining and interpreting exchange rate overshooting.
Real effective exchange rate relationships: What’s in JP Morgan’s data?
How to deal with exchange rate overshooting: BMW’s Rover cars vs. GE’s electric irons.

**Assignment:** David Miles and Andrew Scott, *Macroeconomics*, Chapters 18-20.

**Case:** *Federal National Mortgage Association*
December 5  Macroeconomic Adjustment in Open Systems
Macro-adjustment in Equilibrium Systems
Shock-adjustment under fixed exchange rates.
How things tend to get back into balance.
Shock-adjustment under flexible exchange rates.
Where the adjustments get made and why elasticities are important.
Elasticities and exchange rate volatility.

Macroe-adjustment in Disequilibrium Systems
Why do central banks intervene in foreign exchange markets?
Sterilized vs. unsterilized intervention.
External reserves and debt.
The IMF, World Bank, and the global financial “architecture.”
The use and misuse of exchange controls.
Country risk assessment

Assignment: David Miles and Andrew Scott, Macroeconomics, Chapters 21-24.

Session 6  December 12  Applications

Making the Euro Work
Monetary unification in Europe in history.
EMU from the Werner Plan to Maastricht.
What is lost?
What is gained?
What is needed?
The euro versus the dollar.

Managing in Financial Crises
Why things get out of line – political-economic policy scenarios.
Predicting crises.
Why financial crises get contagious.
How to lose your shirt if you don’t understand global macroeconomics.
Good projects in bad countries – winning in a tough environment.
Rumblings in Mexico and Asia – what were the similarities and differences?
What did we actually learn – and what will we remember when the next one comes?

Assignment: Acme de Mexico S.A. de C.V.

Session 7  December 19 (6:00-8:00 pm)  Final Examination