

**THE UNIVERSITY OF ILLINOIS AT CHICAGO**  
**ECON 512: MACROECONOMICS II**  
**SPRING 2012**

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**Office Hours:**

Thu 1:00-2:00

or by appointment

**Required Text:** David Romer, *Advanced Macroeconomics*, 4<sup>th</sup> ed., McGraw-Hill, 2012.

**Other Recommended Texts:**

Benassy, Jean-Pascal, *Macroeconomic Theory*, Oxford, 2011. (Intermediate to advanced level, comprehensive coverage)

William H. Branson, *Macroeconomic Theory and Policy*, 3<sup>rd</sup> ed., Harper & Row, 1989. (Introductory level, comprehensive coverage)

Olivier Jean Blanchard and Stanley Fischer, *Lectures on Macroeconomics*, MIT, 1989. (Advanced level, comprehensive coverage)

John B. Taylor and Michael Woodford (eds.), *Handbook of Macroeconomics* (3 volumes), North-Holland, 1999. (Intermediate to advanced level, very thorough survey of macroeconomic topics)

Carl E. Walsh, *Monetary Theory and Policy*, 3<sup>rd</sup> ed., MIT, 2010. (Intermediate to advanced level, emphasis on monetary theory and stabilization)

Michael Wickens, *Macroeconomic Theory*, Princeton, 2008. (Intermediate to advanced level, comprehensive coverage)

Woodford, Michael, *Interest and Prices*, Princeton, 2003. (Advanced level, emphasis on monetary theory and policy)

**Overview:**

This is the second course of the graduate sequence in Macroeconomics. The purpose of this course is to provide a broad survey of the topics in Macroeconomic Theory. I will assume that you have mastered the models in Econ 511 and that you are familiar with the basic concepts of calculus, probability, and statistics.

Part I addresses the long-run issue of economic growth. Part II covers the modeling of the main components of GDP: private consumption, investment, government spending (and taxes), and net exports. Part III introduces money mainly from the long-run perspective. Part IV discusses theories of the business cycle, including all major schools of thought, and unemployment. Finally, Part V covers issues on the feasibility and desirability of stabilization policy, beginning with the debate between Keynesians and Monetarists, and concluding with a chapter on dynamic inconsistency.

**Evaluation:** Your grade will be based on a midterm (50%) and a final (50%) examination. In addition, there will be at least two practice problem sets.

**Course Outline:**

1. Introduction: a two-period model, an infinite-horizon model.

**PART I. CAPITAL ACCUMULATION AND ECONOMIC GROWTH**

2. Neoclassical Growth Models: Stylized Facts, the Solow Model, the Ramsey Model, a Malthusian model, Convergence.
3. New Growth Models: the Rebelo Model, Externalities, Endogenous Growth, Human Capital, Implications.
4. Other Growth Models: Overlapping Generations, the Aghion-Howitt model, Poverty Traps and Stagnation.

**PART II. NEOCLASSICAL MODELING**

5. Consumption: the Permanent Income Hypothesis, the Random Walk result, Liquidity Constraints, Precautionary Saving, Durables and Nondurables, Habit Formation.
6. Investment: the Jorgenson model, the Accelerator, Tobin's  $q$ , Taxes and Subsidies, the effects of Uncertainty.
7. Fiscal Policy: Taxes and Growth, Distortionary Taxes and Laffer Curves, Tax Smoothing, Ricardian Equivalence, the Optimal Government Size.
8. The Current Account: A simple model, a model with production, the Large Open Economy, an Infinite Horizon model.

**PART III. MONEY, GROWTH, AND INFLATION**

9. Demand for Money: Store of Value, Transactions Demand, Precautionary Demand.
10. Money and Growth: The Tobin Model, the Sidrauski Model, Superneutrality, Extensions, a Cash-in-Advance model.
11. Inflationary Finance: Welfare Costs of Inflation, Hyperinflations and Seignorage, Optimal Seignorage.

**PART IV. BUSINESS CYCLES**

12. The Standard Keynesian Model: Aggregate Demand, a Keynesian Aggregate Supply, the Friedman-Phelps Supply Function.
13. Rational Expectations: the Muth Model, the Sargent-Wallace Model, the Lucas Supply Function, Implications.
14. Real Business Cycles: Stochastic Solow and Ramsey Models, a Multi-Sector Model.
15. A New Keynesian Model: New Keynesian Phillips Curve, New Keynesian IS curve, Implications.
16. Unemployment: Indivisible Labor, the Efficiency Wage Model, Persistence of Unemployment, Insiders-Outsiders.

**PART V. STABILIZATION POLICY UNDER UNCERTAINTY**

17. Keynesians and Monetarists: Multiplier Uncertainty, Policy Errors and Lags, Asymmetric Effects, the Poole Model, Fixed vs Flexible Exchange Rates.
18. The Importance of Expectations: Adaptive vs Rational Expectations, Implications for Policy, a Complete Rational Expectations Model.
19. Dynamic Inconsistency: the General Problem, Output and Inflation, Reputation, Conservative Central Bankers and Indexation, Political Business Cycles.
20. Other Useful Models: Taylor Rules, Wage Indexation, Monetary Unification and Dollarization, a unified model of business cycles, the Barro model of Fiscal policy.