



Macroeconomics 1

(A European Perspective)

Week 7

Utrecht School of Economics

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Group Discussion

Blanchard, O., Amighini, A., Giavazzi, F. (2021). Macroeconomics: A European Perspective, 4th edition. Pearson: New York.

Group discussion: Set A

1. Technical change and inequality. See Figures 16.9a and 16.9b, the log-run and short-run effects of technical change on the labour market.
 - (a) Explain the difference between the Blanchard WS curve and the CORE WS curve.
 - (b) Explain the differences between the short-run effects and the long-run effects.
 - (c) How is the dynamics for short-run to medium-run equilibrium?
 - (d) Add figure 16.11 and explain the effects of technical change on inequality.
 - (e) Remember this is the consequence according to the WS-PS model: do you agree with the conclusions, is the model a reasonable predictor?

2. The Phillips curve and the policymakers preference.
 - (a) Study Figure 15.5, make sure that you understand the structure of the graph.
 - (b) Answer exercise 15.3.
 - (c) What would the policymakers indifference curve look like if (s)he would care about inequality?

3. The golden age, the era of stagflation and the great moderation.
(For all figures: be aware of the differences between the Blanchard WS curve and the CORE WS curve!)
- (a) See figure 17.12: explain the presentation of the golden age of capitalism in the WS-PS model. What would be the adaptations in the IS-LM-PC model?
 - (b) See figure 17.15: explain the presentation of the era of stagflation in the WS-PS model.
 - (c) What is exactly the path of stagflation in the IS-LM-PC model?
(Hint: check week 3 Thursday question 1.f)
 - (d) The following great moderation has been described as supply side reforms. Explain the shifts in WS-PS and IS-LM-PC during the great moderation.

Problem Set

Problem set

1. The global financial crisis.
 - (a) See figure 17.19 in section 17.8. Explain the strong correlation between the increase in house prices and the increase in household debt-to-income ratio with the terms financial accelerator and leverage.
 - (b) See figure 17.20 in section 17.8. Which of the two households has the highest leverage ratio? What will happen if the house value drops by 10%.
 - (c) See figure 17.27 in section 17.10. Explain why the provision of subprime mortgages were essential in the housing boom and bust. Explain as well why the part expected future earnings from employment changes during the boom and bust.

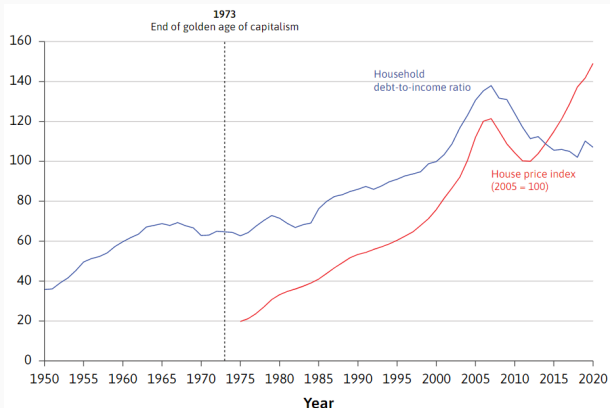


Figure 17.19 of CORE.

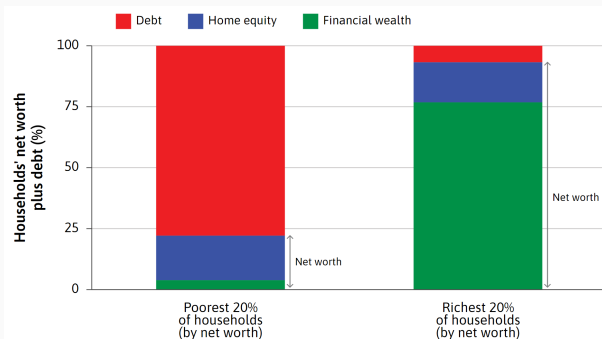


Figure 17.20 of CORE.

Problem set

- (d) Hyman Minsky developed a theory of the business cycle. Explain what is meant with this phrase: Stability even of an expansion is destabilizing in that more adventurous financing of investment pays off to the leaders, and others follow.
- (e) Section 17.11 presents the role of banks in the crisis. Remember the typical balance sheet of the representative commercial bank that we discussed in week 3 and the complex financial products as discussed in section 17.8; explain the fire sale of financial products during the crisis.

2. Bubbles.

- (a) Use the Price dynamics curve in figures 11.17 and 11.18 (section 11.8) to explain the difference between stable and unstable equilibrium points.
- (b) Eugene Fama and Robert Shiller are influential economists, with opposing views on markets, prices and bubbles. Fama is famous for his efficient market hypothesis. Search for the exact meaning of the term efficient market hypothesis and the consequences of this theory for markets, prices and bubbles. Shiller strongly opposes this hypothesis; what is his view on markets, prices and bubbles?

Questions?