Course Overview: This course will examine the American policy response to the recent financial crisis and associated Great Recession. The objective is to illuminate (i) the changes in macroeconomic thinking necessitated by recent events (ii) the relationship between analytical macroeconomics, finance and policymaking in a political context (iii) lessons of recent experience for public policies directed at preventing crises in the future and responding to them when they come. The lectures will draw on the professional economic literature to the minimum extent necessary to facilitate understanding of the issues involved. The primary focus will be on the process of policy choice and the factors entering into actual policy decisions. Each lecture after the first introductory lecture will cover a different aspect of the policy response to the crisis. Sections will take up relevant analytical economic aspects.

Requirements: Students taking the course for credit will be required to write a 20 page paper addressing some policy question involved with the response to the crisis. Papers can either (i) consider one of the arguments made against a policy choice that was made and evaluating its merit in light of subsequent events or (ii) argue that on the basis of the information available at the time a different policy choice in some area should have been made and then evaluate their argument with the benefit of hindsight. Topics should be selected to focus on something specific—a paper on the merits of a wage subsidy as a component of the fiscal stimulus is more appropriate than one asking whether fiscal stimulus was a good idea. Students are free to write a paper applying the arguments of the paper in a non-American context with permission from the instructor or one of the Teaching Fellows. The paper is
due on the last day of the reading period, May 5th, at midnight.

Lectures:

March 21   I. The Obama Inheritance: How and Why the Crisis Developed; Initial Responses and Choices Presented

March 28   II. The Crisis and the Real Economy: The Role of Fiscal and Monetary Policy

April 4    III. The Financial Crisis: The Breakdown of Intermediation; Banking and Shadow Banking; Bailouts, Bail Ins, and Stress Tests; Government as a Liquidity Provider of Last Resort

April 11   IV. Key Sectors in Crisis: Housing, Automobiles and Manufacturing; Commerical Real Estate; Small Business

April 18   V. Crisis Prevention: Risk Management; Regulation; Supervision; Resolution; Scope and Scale Restriction; Monetary Policy

April 25   VI. The Global Dimension: International Experiences; Global Policy Coordination and Imbalances; Resisting Protectionism; Looking Forward

Reading List

The objective of this reading list is to provide a compendium of crisis related materials and to provide jumping off points for student papers. Starred papers are required and will be referenced in the lectures.

Overview


I. Background to the Crisis

Context


Galbraith, John Kenneth – A Short History of Financial Euphoria


Early Accounts


* Swagel, Phillip, “The Financial Crisis: An Inside View,” Brookings Papers on Economic Activity,
Spring 2009.


A Problem of Free Markets?


Cassidy, John, "Chicago Interviews," Rational Irrationality, 21 January, 2010:

Central Bank Policy and Monetary Conditions


Fischer, Stanley, “Comments on Charles Goodhart's paper ``The Changing Role of Central Banks.'”, 9th BIS Annual Conference.


**TARP**


**II. Financial Crisis and the Real Economy**

**Banking and the Real Economy**


Robert Hall: "Why Does the Economy Fall to Pieces after a Financial Crisis". JEP (2010)

The Liquidity Trap and Depression Economics


Fiscal Policy: Prospective


Summers, Lawrence, “Why America Must Have a Fiscal Stimulus,” Finacial Times, January 6, 2008:


Early Analysis of Policy


III. Financial Institutions, Shadow Banking and Crisis Response


Brunnermeier, "Deciphering the Liquidity and Credit Crunch,” Journal of Economic Perspectives.


Nationalizing the Banks


Zingales, Luigi, “Yes We Can, Mr Geithner,” VoxEU Debate on the Global Crisis, January 19, 2009.

Jones, Garett, “An Alternative to TARP II: Just Doing the Normal Thing,”


**Stress Tests**


**TALF**


Anusha Shrivastava, “The Verdict on TALF: It Worked; Program Increased Demand and Credit Flow; Even a Profit?” Wall Street Journal Online, March 5, 2010.


IV. The Sectoral Dimension

Housing Markets

* Edward L. Glaeser, with Joshua Gottleb and Joseph Gyourko, “Can Cheap Credit Explain the Housing Boom,” (July 2010).


Bernanke, Ben. – Monetary Policy and the Housing Bubble. Speech at the annual meeting of the American economic association.


Cowen, Tyler, “Mortgage Modification,” Marginalrevolution.com, March 5, 2009:


Summers, Lawrence, “The Way Forward for Fannie and Freddie” July 28 2008:

Summers, Lawrence, “What We Can Do in This Dangerous Moment” June 29 2008.


Newberry, Sterling, “Elizabeth Warren is with Us, Who is Going to be with Her?”, FDL blog.

Automotive Industry


Congressional Oversight Panel, September Oversight Report, September 9, 2009:


V. Regulation


Macroprudential


Kashyap, Rajan and Stein – “Rethinking Capital Regulation”, working paper August 2008

Size and scope


Johnson, Simon, “Should Megabanks Be Broken Apart?”


**Consumer Financial Protection**


**Derivatives**


Viral Acharya and Robert Engle "A Case for (Even) More Transparency in the OTC Markets", Vox, 29 August 2009:

Lynn A. Stout "Why We Need Derivatives Regulation" Dealbook, October 7, 2009:


Skin in the game


Capital and leverage constraints


Executive Compensation


**Comparison of British and American Approaches**


Andrew Haldane, “The $100 Billion Question,” Speech at the Institute of Regulation & Risk, North Asia (IRRNA), in Hong Kong on 30 March 2010.


**Too Big to Fail**

Baker, Dean, “This Isn't Canada: Krugman on Too Big to Fail,” The Guardian Unlimited, April 7, 2010.


**Contingent capital**

* Squam Lake Report, chapter 7

* Dudley, William C. “Some Lessons from the crisis,” Remarks at the Institute of International
Bankers Membership Luncheon, New York City.


Shiller, Robert J. “Engineering Financial Stability,” www.project-syndicate.org blog, January 18th 2010,

McDonald, Robert L., “Contingent Capital With a Dual Price Trigger” (541).

VI. Looking Forward and Globally

Timothy F. Geithner, “Global Recovery: Remarks at the Brookings Institution,” transcript reprinted in Financial Times, October, 6, 2010

The US Deficit

Johnson, Simon and James Kwak, “Four Steps to US Fiscal Health,” Project syndicate blog, August 17th 2010,

Johnson, Simon “Does the U.S. Really Have a Fiscal Crisis?”, Economix blog.

The future of the dollar and the US trade deficit


Simon Hall, “China’s Thirst for Oil at All-Time High,” Wall Street Journal, January 18, 2011.


Two speed recovery and the new role of the G-20

Inman, Phillip, "IMF warns of two-speed recovery", The Guardian, February 23, 2011:


Lanman, Scott, "Bernanke Takes Defense of Monetary Stimulus Abroad, Turns Tables on China", Blomberg.com, November 19th 2010

Andrew F. Cooper, “Keynote Address: The G20: A Work in Progress for Global Governance?,” 8th FES-SWP North-South Dialogue, June 17, 2009:

Barry Eichengreen, “The G20 and the Crisis,” VOX, March 2, 2009,


Simon Kennedy, “G-7 Take ‘Back Seat’ as Crisis Pushes G-20 to Fore (Update 2)” Bloomberg Online,
February 13, 2009, 9:12 AM.


European Sovereign crises

Eurostat (2010), “Information Note on Greek Fiscal Data”, November 2010


Eurostat, Greek Primary Surplus and Deficit.


Hugh, Edward, “Standard & Poor's Puts Spanish Sovereign Debt on Ratings Watch Negative”, A fist full of dollars, January 2009


Johnson, Simon “Greece and the fatal flaw in an IMF rescue”, The Huffington Post.