

# Macro-2

Module 2, 2020/21

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## Course information

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## Course description

Macroeconomics is the study of aggregate behavior in an economy? Although this behavior is a result of choices and actions taken by millions of individuals, macroeconomists would look at the average behavior in the economy. Nevertheless, there are issues that are unique for the economy as a whole such as unemployment or the value of the local currency.

Modern macroeconomics builds on the foundations of microeconomics, the study of individual firms and households. Students have been exposed to these foundations in Macro-1 and different Micro-modules. Macro-2 then builds on the fact that the overall macroeconomic outcomes in the economy are the result of an aggregations of many firms and households.

What determines the output level? What are the factors for high unemployment? Why are there business cycles? What is the role of government in spurring output levels, stabilizing inflation and reducing unemployment? How these issues evolve in the short and long-run? What different policies should governments

adopt in the short and long-run. We will answer these questions, which are important not only from a macroeconomic point of view but also from the microeconomic point of view as it helps individuals in deciding how much to save and borrow or spend.

This course answers these questions mostly using the New-Keynesian model, still the New-Classical model will be at the background. Students will be exposed to the standard IS-LM apparatus and its open economy extensions, as well as analyzing the aggregate demand and supply and the Phillips curve.

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## **Course requirements, grading, and attendance policies**

The final grade will be based upon:

1. PS - 20%
2. A final exam - 80%
3. Class participation is obligatory.

“Class Participation” centers on two major components; attendance and preparedness. First, you need to attend class in order to reap the full benefits of the course. Second, you should be prepared for each class, having completed the required readings and being prepared to participate actively in the class.

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## **General Reading**

N. Gregory Mankiw. *Macroeconomics*. Worth Publishers, New York, eighth edition, 2012.

Jeffrey D. Sachs and Felipe Larrain B. *Macroeconomics in the Global Economy*. Prentice-Hall, Inc., 1993.

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## **Course contents**

### **Aggregate supply and aggregate demand**

Different theories of aggregate supply: New Classical versus New Keynesian approach. Long run versus short run.

Mankiw (2012), chapter 10.

Sachs and Larrain (1993), chapter 3.

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### **Output determination in a closed economy**

The IS-LM framework in a closed economy and the effect of fiscal and monetary policies.

Mankiw (2012), chapters 11, 12.

Sachs and Larrain (1993), chapter 12.

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### **Output determination in an open economy**

The IS-LM framework in an open economy with fixed or flexible exchange rate and the effect of fiscal and monetary policies.

Mankiw (2012), chapter 13.

Sachs and Larrain (1993), chapters 13,14.

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### **Inflation, inflation tax and Seigniorage**

The government budget, money growth and inflation and government's deficit.

Sachs and Larrain (1993), chapters 9, 11.

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## **Inflation and unemployment**

Economic policy and the Philips curve.

Mankiw (2012), chapter 14.

Sachs and Larrain (1993), chapter 15.

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## **Sample tasks for course evaluation**

1. Assume that because of better training, workers become more productive.
    - (a) What would happen to the demand for labor?
    - (b) What would happen to the equilibrium real wage?
    - (c) Is involuntary unemployment changed? How does your answer depend on whether the real wage is flexible or not?
  
  2. Discuss what happens to aggregate supply curve under the classical, basic Keynesian, and extreme Keynesian cases when
    - (a) There is a technological improvement.
    - (b) An earthquake destroys half the capital stock of the economy.
    - (c) Workers' preferences change, and they want to work more at any wage rate.
    - (d) New, more productive machines are invented, but only a third of the labor force knows how to operate them.
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## **Academic integrity policy**

Cheating, plagiarism, and any other violations of academic ethics at NES are not tolerated.