Economics 137  
Macroeconomic Policy

Course Description: This course will study the theory of macroeconomic policy. First we will examine some issues in the conduct of fiscal policy and then turn our attention to the theory and practice of modern monetary policy. The focus of the course will be on relatively recent developments; in several cases, the economists associated with these ideas were awarded the Nobel prize in Economics for their scientific contributions. Recently proposed monetary policy rules will be the topic for the final part of the course.

Note: Several of the topics will be presented at an advanced undergraduate level – it will be assumed that you have had (and remember) the necessary prerequisites. Moreover, calculus and probability will be used in developing the theory. The reason for this emphasis on rigor is to bridge the gap between undergraduate economic education and what economists actually do.

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Office Hours:  
Professor Salyer: SSH 1120, Monday 3:30-5:30pm or by appointment.  
Paul Gaggl: TBA

Grading: There will be one midterm exam (worth 35%) and a cumulative final exam (55%). The remaining 10% will be determined by performance on homework assignments and class participation.

Note the dates of the midterm and final – there will be no alternate exams given!!

Readings: All articles (see below) are available from the class web site:

http://www.econ.ucdavis.edu/faculty/kdsalyer/LECTURES/ecn137.html
Schedule of Topics

1. Review Material (to be covered in Section)
   Reading: Math Handout, Stats Handout, Bond Pricing, Term Structure of Interest Rates

   We will first examine the fiscal implications of the current Social Security and Medicare policies. Then, we will begin our study of optimal policy within dynamic economies. Our focus will be on the optimal path of taxes and the effects of deficits on interest rates.
   
   Readings:
   - Doepke, M., A. Lehnert, A. Sellgren, Macroeconomics, Chapter 14.

3. Time Inconsistency – The case of the benevolent, dissembling government (4/19 – 4/26)
   The 2004 Nobel Prize was awarded to Ed Prescott and Finn Kydland in large part for their 1977 article on time inconsistency. We explore this concept within the context of optimal taxation of capital and labor.
   
   Readings:

   
   Readings:

Robert Lucas won the 1995 Economic Nobel Prize in part because of his critique of policy evaluation. We look at this in detail.

**Reading:**


Robert Lucas forcefully demonstrated that the Phillips curve does not necessarily imply a policy trade-off between inflation and output. This contribution was another reason for his winning the Nobel prize.

**Reading:**
Romer, D, *Advanced Macroeconomics, Chapter 6 excerpt.*


We examine the modern formulation of monetary policy in a stochastic general equilibrium model with rational expectations. We also discuss inflation targeting and Taylor rules.

**Readings:**

**FINAL, SATURDAY JUNE 5, 8AM**