UNIVERSITY OF CALIFORNIA
DEPARTMENT OF ECONOMICS

Economics 202A
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Lecture Outline, 10/4 & 10/6

MACROECONOMIC CRISES

I. THE MACROECONOMIC AND FINANCIAL CRISIS OF 2007 AND BEYOND

A. Background: The Great Moderation
- 1. Macroeconomic performance form the mid-1980s to roughly 2006
- 2. Candidate explanations

B. The Run-Up and Bust in House Prices
- 1. The explosion of house prices
  - a. Some basic facts
  - b. Some issues that this raises
- 2. The fall

C. The Real Economy
- 1. Macroeconomic performance from 2006 to mid-2008
- 2. Macroeconomic performance in late 2008 and early 2009
- 3. Two nitty-gritty data issues

D. Why Were the Real Effects of the Financial Stress So Large?
- 1. Candidate explanations
- 2. A few facts

E. The Failure of Our Models to Predict or Explain the Crisis
- 1. The severity of the downturn
- 2. The sluggishness of the recovery
- 3. The behavior of inflation

F. Financial Regulation and Unconventional Monetary Policy
- 1. Interventions in financial markets
- 2. What are the grounds for government intervention?
  - a. Economists' usual view of government intervention
  - b. Analyses of intervention in financial markets
  - c. Some examples of difficult policy issues

G. The Importance of the Zero Lower Bound on Nominal Interest Rates
- 1. The zero lower bound
- 2. Its importance in the episode
- 3. Possible ways of dealing with the zero lower bound

H. A Few Thoughts about Fiscal Stimulus
- 1. The gap between frontier academic models and models used in practice
- 2. The political economy of fiscal stimulus

(OVER)

I. Some Other Issues Raised by the Crisis Thus Far
   1. The costs of macroeconomic fluctuations
   2. How much of current high unemployment is structural?
   3. The political economy of monetary policy

J. Some Other Issues Raised by the Crisis Going Forward
   1. Background: Standard forecasts
   2. What, if anything, can be done to prevent those forecasts from becoming reality?
   3. Are large macroeconomic costs of financial crises inevitable?
   4. Do large, long downturns leave permanent scars?
   5. Possible long-run threats from the monetary and fiscal responses to the crisis, and how to address them.

K. Kocherlakota's and Bernanke's Speeches

L. How Will the Crisis Change Macroeconomics?

II. THE LOOMING FISCAL CRISIS

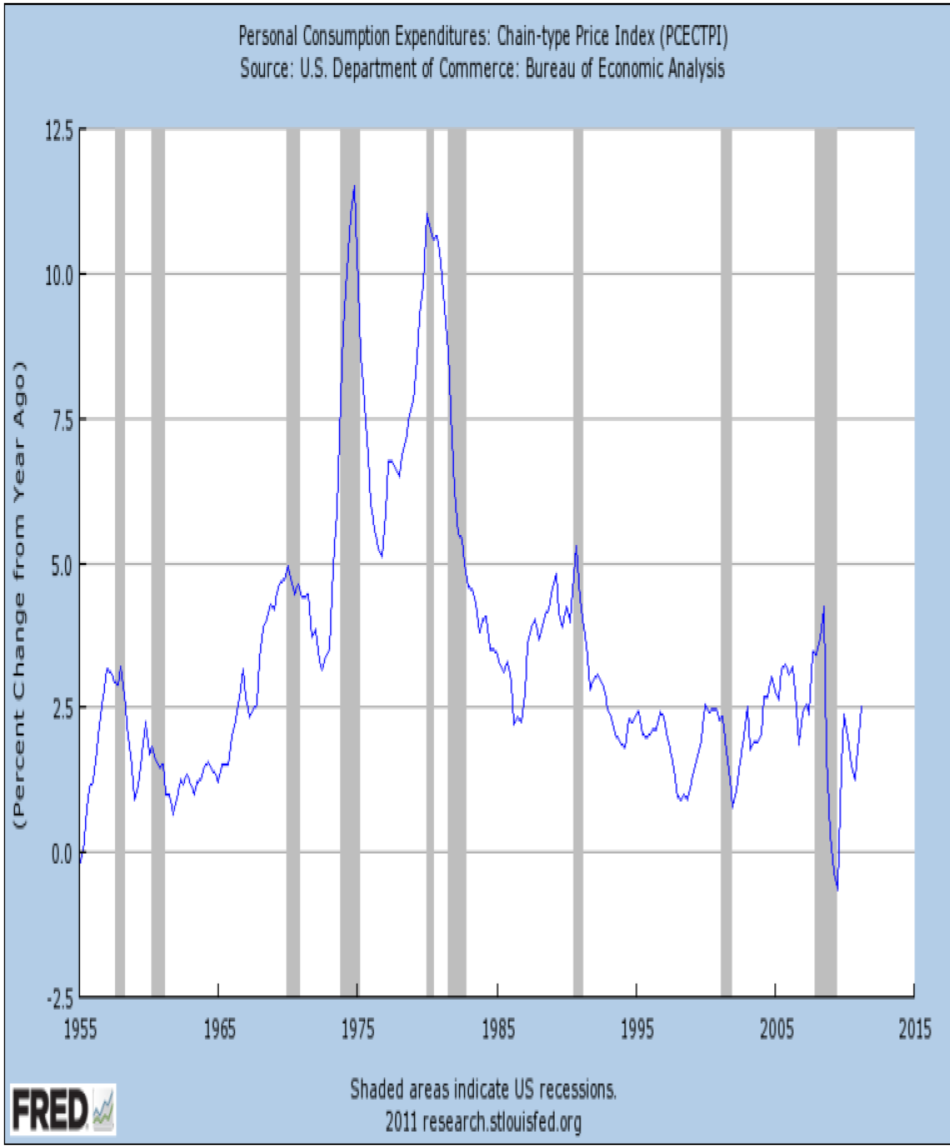
A. Introduction

B. The Auerbach Framework
   1. The government budget constraint
   2. Auerbach's calculation
   3. One immediate implication

C. Implementing the Framework for the United States Today
   1. Characterizing current policy
   2. Results

D. Discussion
   1. What's driving the results?
      a. Demography
      b. Growth in medical spending
      c. Policy decisions made over the period 2001-2008
   2. Uncertainty
      a. How uncertain are these estimates?
      b. How does uncertainty affect optimal policy?

E. Where Do We Go from Here?
   1. What would a social planner do?
      a. Save more
      b. Work more
      c. Not use all the available medical technology?
      d. Market complications
      e. The bottom line
   2. What would happen if we tried to stay on our current path?
      a. Lower national saving
      b. Some type of crisis or meltdown
      c. Disruptions at the individual level
   3. What is likely to happen? A prediction


Personal Consumption Expenditures: Chain-type Price Index (PCECTPI)
Source: U.S. Department of Commerce: Bureau of Economic Analysis
(Percent Change from Year Ago)
12.5
10.0
7.5
5.0
2.5
0.0
-2.5
1955
1965
1975
1985
1995
2005
2015
FRED
Shaded areas indicate US recessions.
2011 research.stlouisfed.org

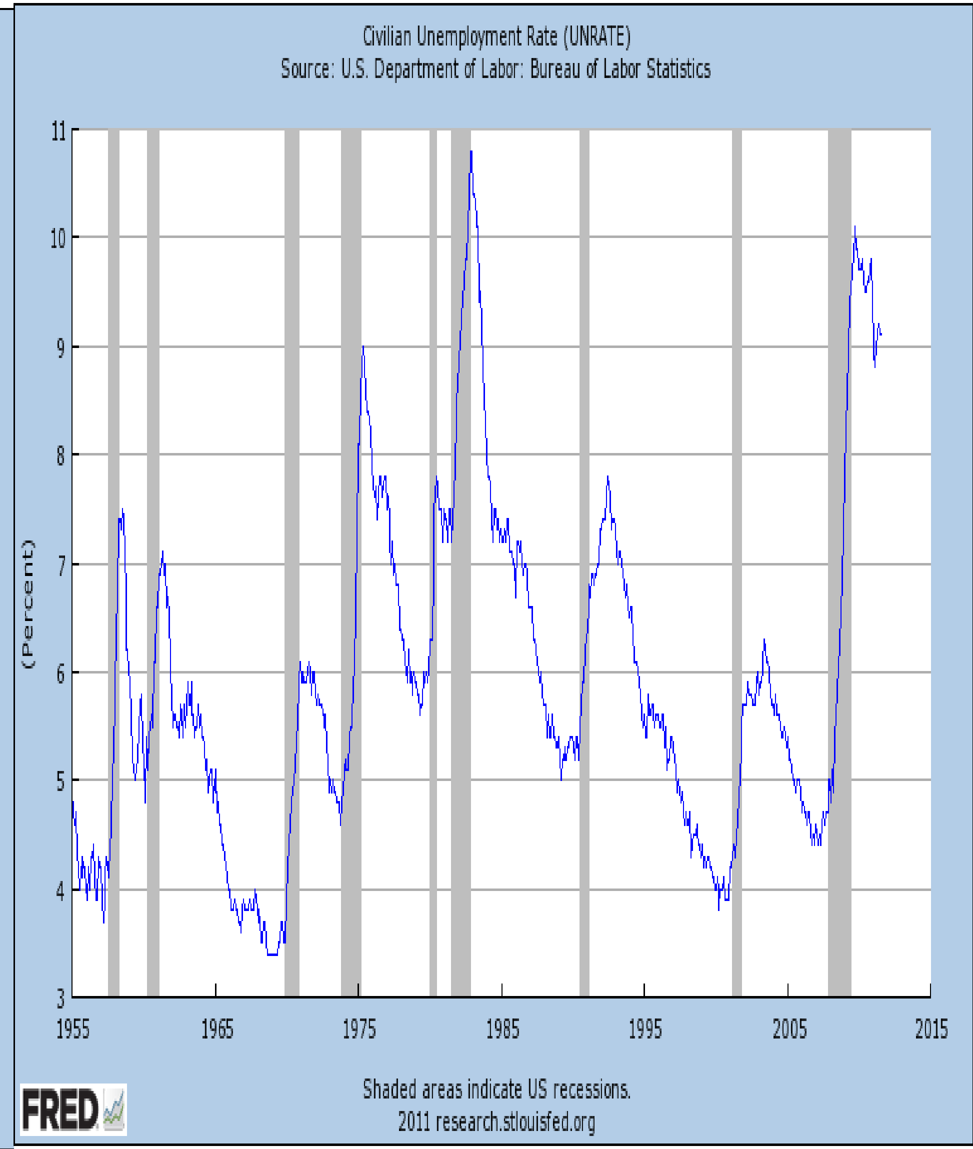
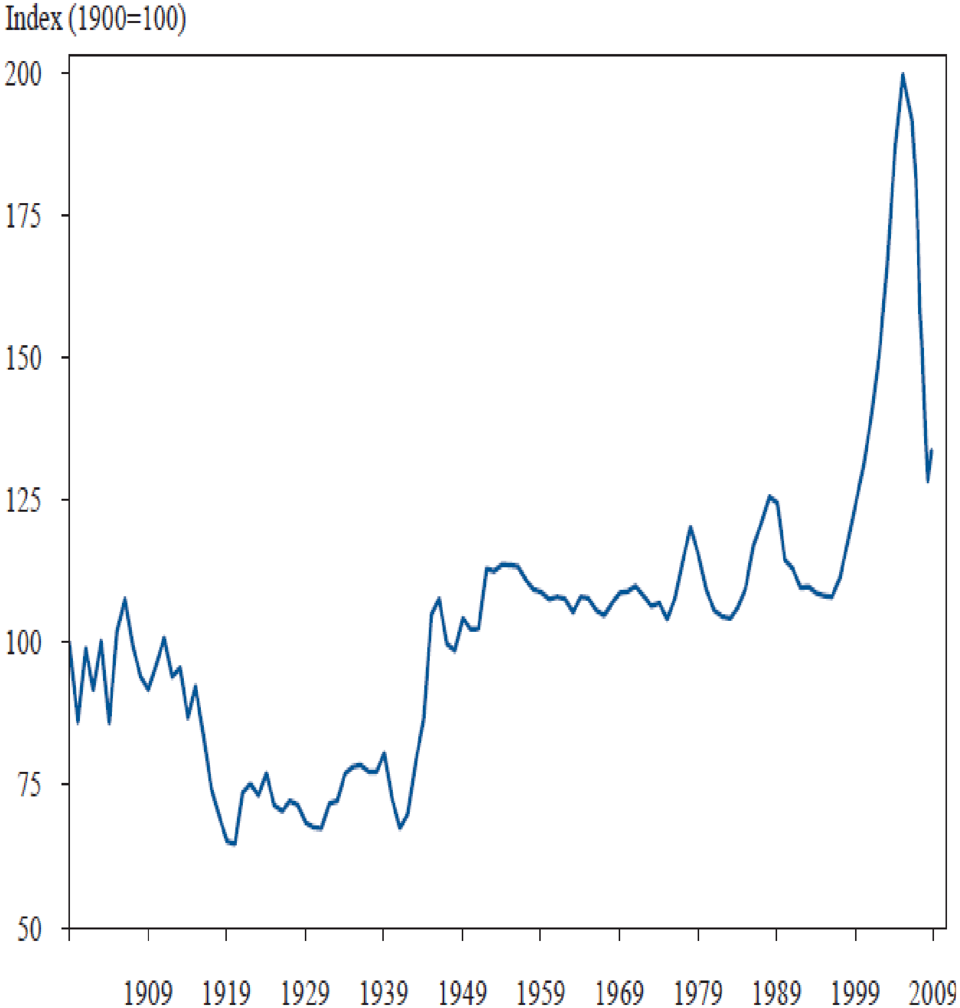

Civilian Unemployment Rate (UNRATE)
Source: U.S. Department of Labor: Bureau of Labor Statistics
(Percent)
11
10
9
8
7
6
5
4
3
1955
1965
1975
1985
1995
2005
2015
FRED
Shaded areas indicate US recessions.
2011 research.stlouisfed.org

Figure 2-1
House Prices Adjusted for Inflation

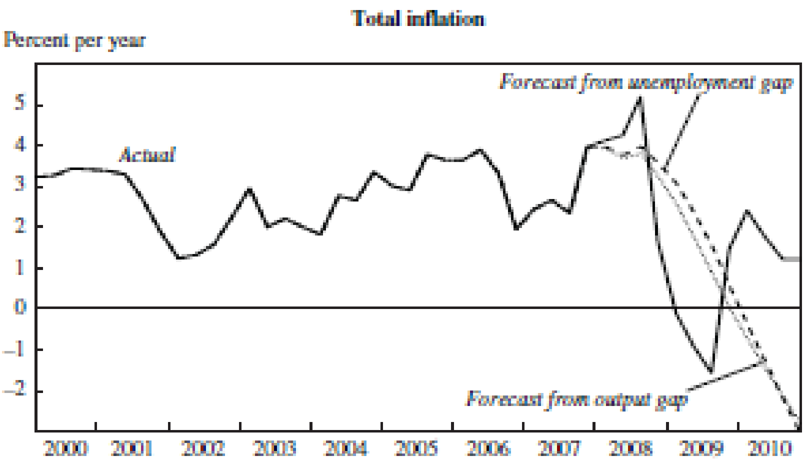


Sources: Shiller (2005); recent data from http://www.econ.yale.edu/~shiller/data/Fig2-1.xls.

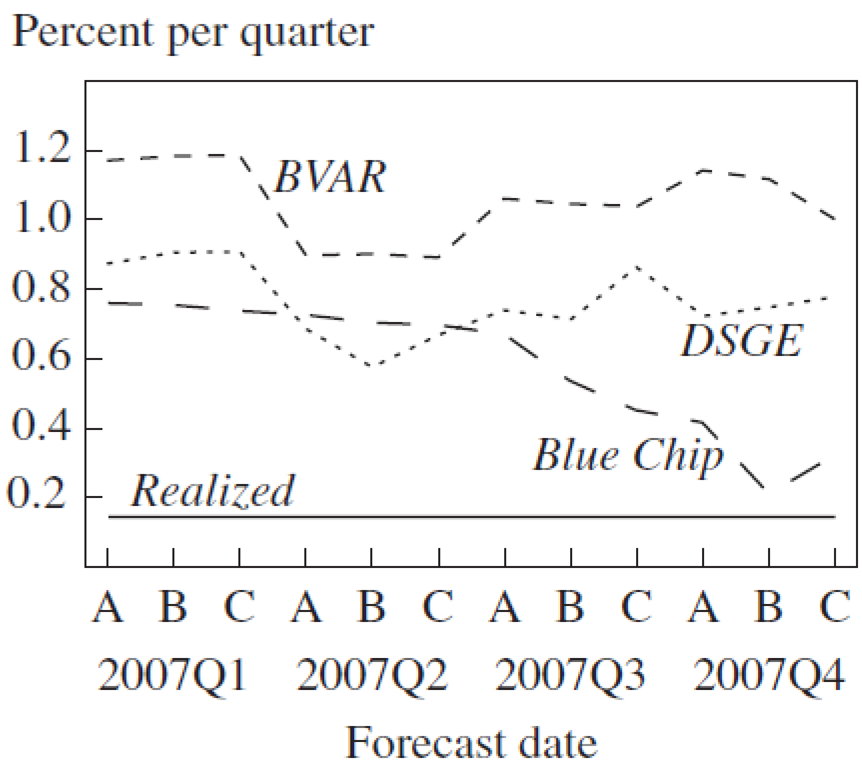
Figure 2-3
TED Spread and Moody's BAA-AAA Spread Through December 2008

Notes: The TED spread is defined as the three-month London Interbank Offered Rate (Libor) less the yield on the three-month U.S. Treasury security. Moody's BAA-AAA spread is the difference between Moody's indexes of yields on AAA and BAA rated corporate bonds.
Source: Bloomberg.

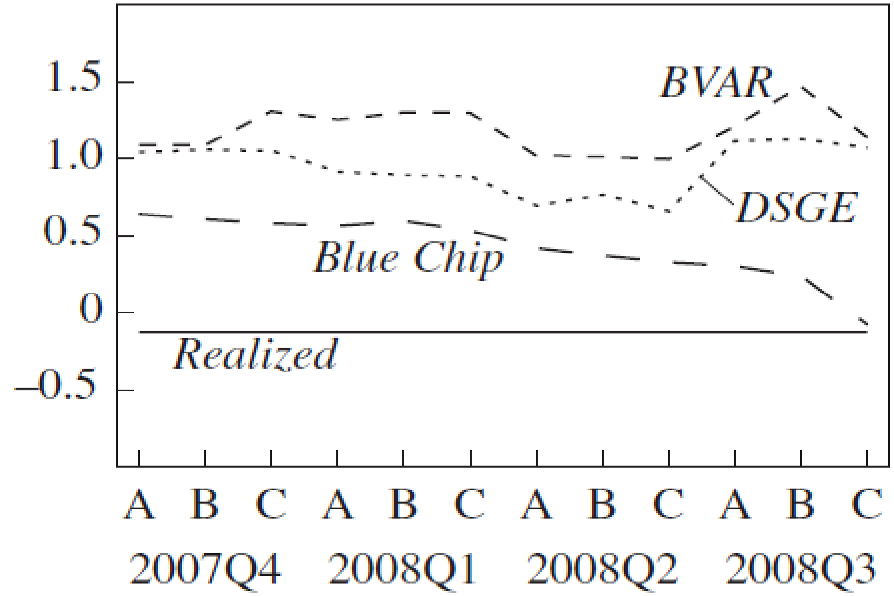
Figure 1. Dynamic Forecasts of Consumer Price Inflation, 2008–10[a]



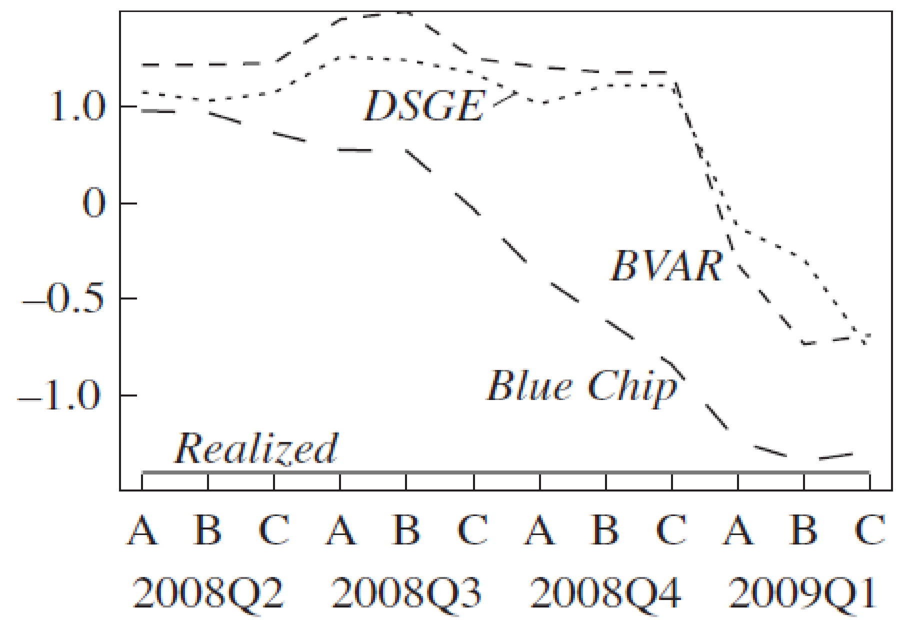
2007Q4 forecasts



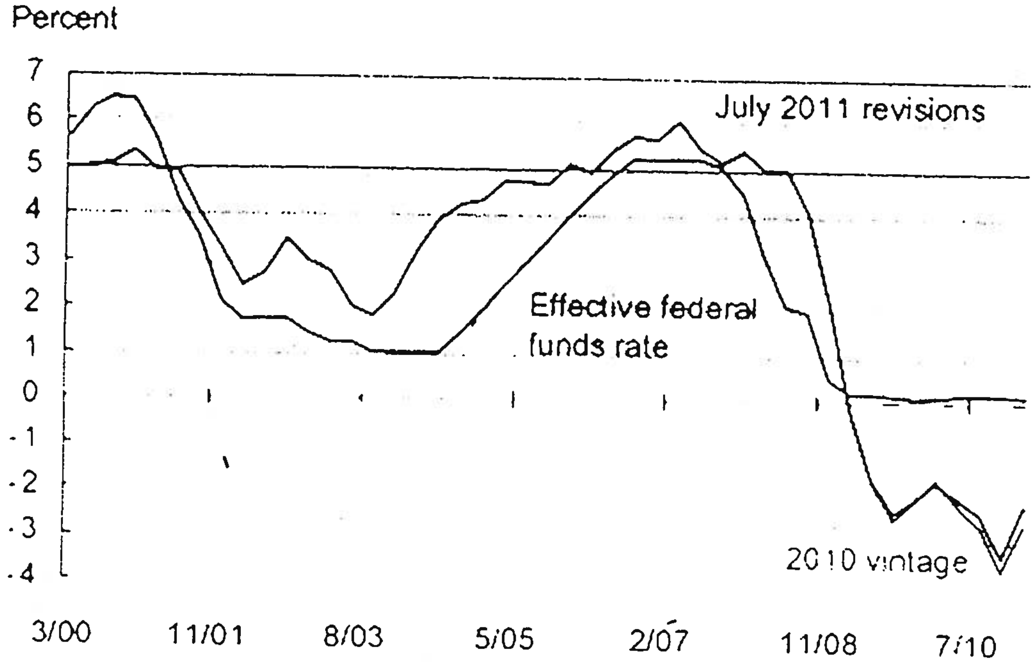
2008Q3 forecasts



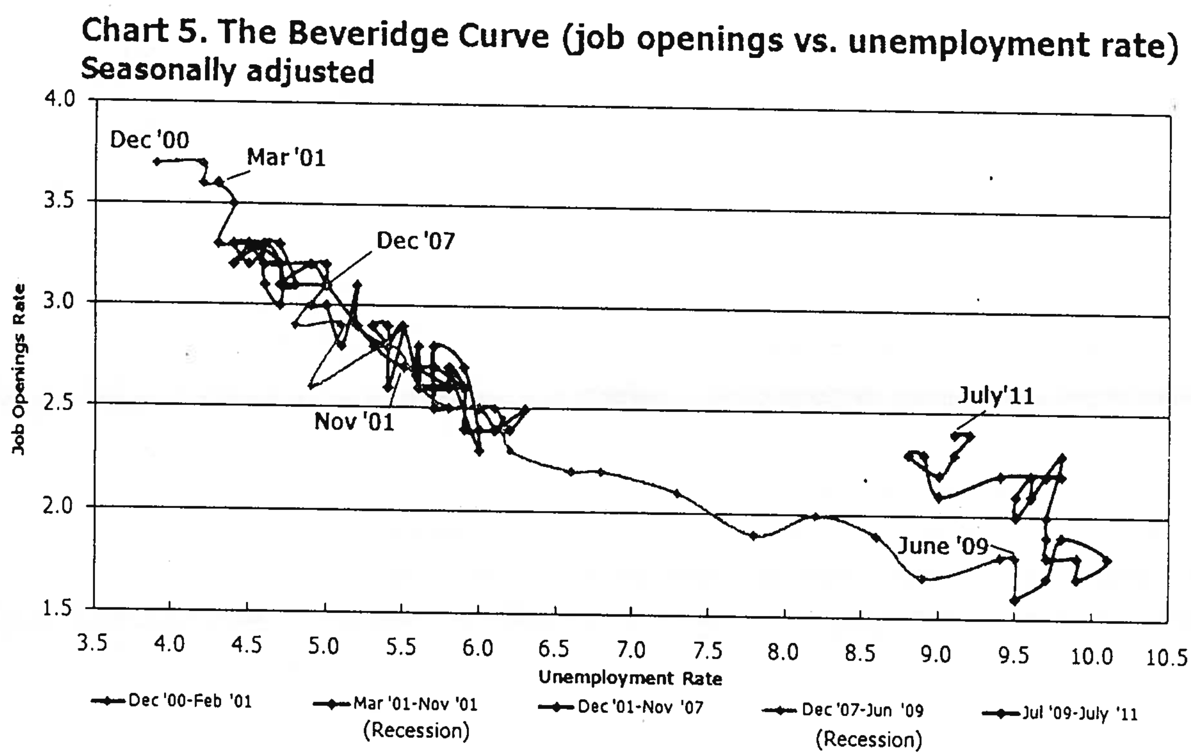
2009Q1 forecasts



Estimated Taylor-Type Rule Using Unemployment



Sources: Bureau of Economic Analysis, Bureau of Labor Statistics, Federal Reserve Board.



Source: Bureau of Labor Statistics, Current Population Survey and Job Openings and Labor Turnover Survey, September 7, 2011.

SUMMARY TABLE
SURVEY OF PROFESSIONAL FORECASTERS
MAJOR MACROECONOMIC INDICATORS

	2011 Q3	2011 Q4	2012 Q1	2012 Q2	2012 Q3	2011	2012 (YEAR-OVER-YEAR)	2013	2014
PERCENT GROWTH AT ANNUAL RATES									
1. REAL GDP (BILLIONS, CHAIN WEIGHTED)	2.2	2.6	2.2	2.9	3.2	1.7	2.6	2.9	3.1
VARIABLES IN LEVELS									
5. UNEMPLOYMENT RATE (PERCENT)	9.1	9.0	8.8	8.7	8.6	9.0	8.6	8.1	7.6