Macroeconomics, Finance and Monetary Economics

Xavier Ragot

xavier.ragot@gmail.com

General Motivation

Necessary?

- Finance is about transferring wealth in the future, lending or borrowing.
  Financial factors affect the macroeconomy : Stock market, the yield curve, short nominal interest rate (monetary policy), housing market, etc.
- The macroeconomy affects asset returns : Effect of average growth, inflation, exchange rate, etc.

What macroeconomists should know about finance?
What financial economists should know about the macroeconomy?

- Monetary economics is about a special assets: Money
- Money is created by open market operations : real effects?

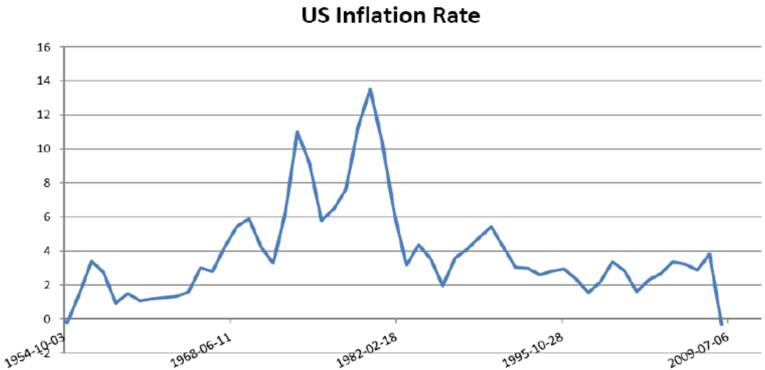
Class is divided in three main parts:

- From macro to finance. Assets prices: Stock market, yield curve. (CAPM, and so on...)
- Finance and Macro. Financial imperfections : Credit constraints, uninsurable risks, risk-shifting
- Monetary economics

Roadmap

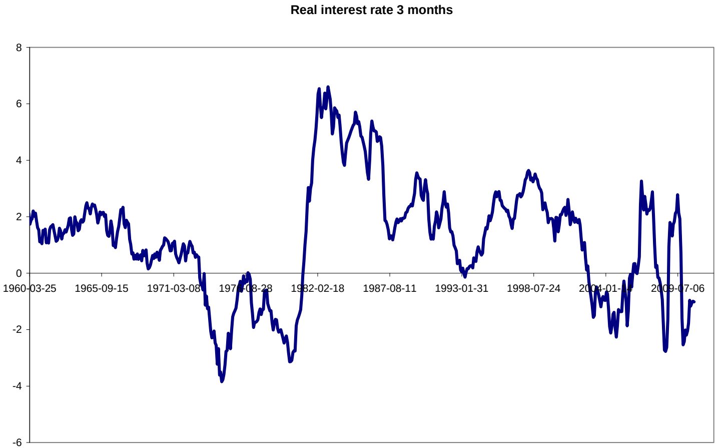
1. Introduction:
   - Facts in finance, Back to basics
2. The prices of assets
   - Pricing Kernels, CAPM, Equity premium puzzle
   - "Solutions": - Habit Formation, Incomplete markets, Epstein-Zin, Disaster events, Long-run risks, expectations dynamics.
3. Fixed Income: The yield curve
4. Debt and credit constraints. The Financial multiplier. Holmstrom and Tirole, Advances in DSGE Bernanke Gertler Gilchrist, Kiyotaki and Moore, Iacovello, Banking sector
5. Uninsurable risks
   - Heterogenous agents macroeconomy
   - A simple case, Applications
6. Monetary economics
   - what is money
   - Money and transaction?
   - Money and finance

Inflation

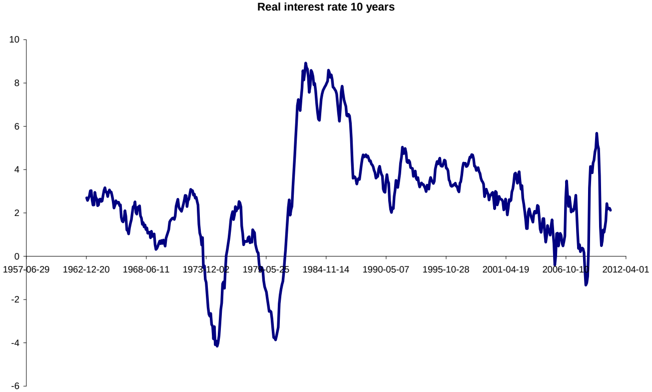


US Inflation Rate
16
14
12
10
8
6
4
2
0
-2
1954-10-03
1968-06-11
1982-02-18
1995-10-28
2009-07-06

Interest rate



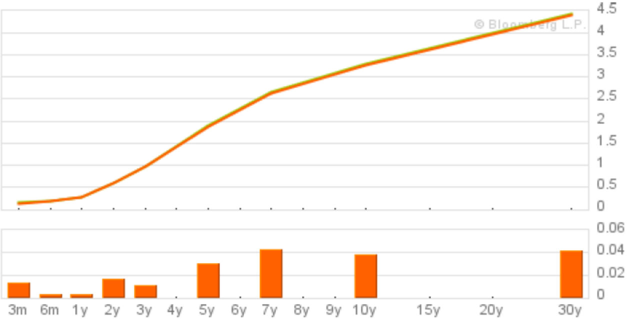
Real Interest rate



(1960-2009 monthly, annualized)

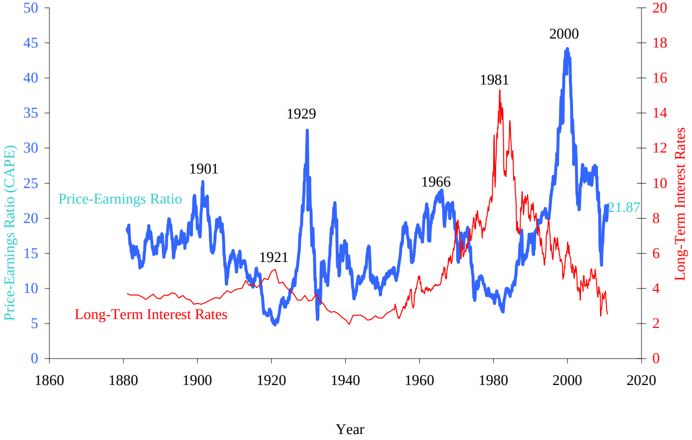
Mean 3 months	Mean 10 years
1.0%	2.6%

Yield Curve



Nominal Interest for various maturities in month (December 13, 201

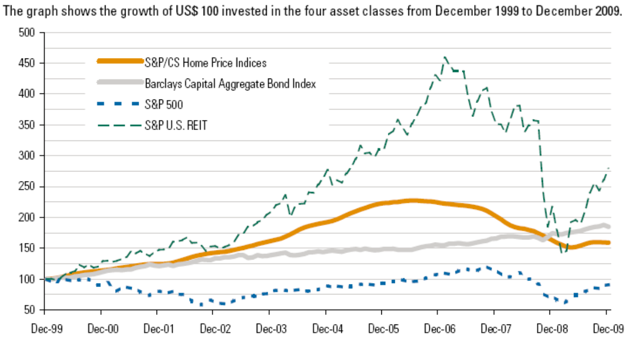
Stock Price SP500



From Shiller Web'page.

	Real return
$1950's$	16.6%
$1960's$	5.2%
$1970's$	-1.5%
$1980's$	11.5%
$1990's$	14.7%
$2000's$	3.5%
$1950-2009$	7.0%

House Price



From Standard and Poor's Fact Sheets

We should look at asset prices and asset quantities. Credit bubbles.