SYLLABUS

University of Chicago Harris School of Public Policy Studies
PPHA 39530 Macroeconomic Policymaking

Monday and Wednesday: 9:00 to 10:20 am
March 20 – May 19, 2023

INSTRUCTOR:
Carlos Fernandez Valdovinos
cfv@uchicago.edu

TAs: Maria Soledad Hurtado and Gabriel Angarita

Course Description

This course is about economic policymaking, with a focus on fiscal and monetary policies. It is structured around six topics. For each session, we will begin with a review of some materials that give the student a broad perspective on the state-of-the-art knowledge in the particular topic, before turning to the specific and practical policy issues. The course aims to give students two things:

1. A good understanding on what policymakers should do in each policy area covered (the normative aspects)
2. A sound explanation on why policies are not always optimal and, many times, deviate from the desirable course of action, emphasizing the obstacles for achieving optimality (for example, political).

Course Structure

The course is organized in different topics. I have compiled a list of readings for each topic, some of which we will cover in class and others which are for your own reference. Before the lecture for each topic, in order to help your participation in class, you may want to:

1. Read the paper with the recommended reading marker (*).
2. Skim the other papers if you are interested.

Given that the instructor is not based in the US, some lecture sessions will be remote, and others will take place on Fridays at 10:00am. All sessions will be recorded and available on the Canvas Zoom Main Account. Please refer to the Canvas main page for calendar details.

Evaluations

There is a team take-home monetary policy exercise that will be explained by the end of week 3, and an in-person mid-term exam that will cover the main concepts reviewed until week 5. The final is an individual take-home project that involves a practical case of financial programming. For the final, collaboration between 2-3 people will be allowed, with the requirement that each student must include the names of the people they collaborated with.
Attendance, Participation, and Discussion

Attendance is highly important to your success in class. Students will be graded for the quality and quantity of their participation while attending class.

Participation will also be evaluated discussion-based through reading checks. Students will have the option to post questions related to the weekly readings, or answers to the other students’ questions (50 words max. for both the questions and answers). Points will be discounted if the content is not related to the corresponding week’s readings or if exceeds the word limit. Canvas Discussions links will be provided by TAs before the reading check deadlines.

Note: there are 5 reading checks in total, but only 2 good questions and 2 answers from different reading checks will be required. This means that if one week your question or answer is not sufficiently good, or if you miss one discussion, you will still be able to get 100% points in this section. You can post as many questions and answers as you want. The objective of this evaluation is to encourage discussion among students and bring more pre-meditated content to the lecture sessions to continue discussing it in class.

Grade Distribution

10% In-Class Participation
10% Reading Checks Canvas Discussion (2 questions and 2 answers in total)
10% Monetary Policy Exercise
30% Midterm Exam
40% Final Project

Grade Ranges

A …..96-100
A-……..90-95.9
B+……87-89.9
B……84-86.9
B-……80-83.9
C+……77-79.9
C……74-76.9
C-……70-73.9

Professor

C. Fernández Valdovinos is a part-time lecturer at the University of Chicago with vast experience as a policymaker. He earned his degree in economics from Universidad Federal de Paranaé, Brazil (1990). He received his M.Sc. in economics from the University of Illinois at Urbana–Champaign (1994) and his Ph.D. in economics from University of Chicago (1999). He was Governor of the Central Bank of Paraguay between 2013 and 2018, having received several awards and recognitions for his work. Previously he served as an economist at the World Bank and the IMF, where he was appointed as the IMF Resident Representative for Bolivia and Brazil.
Required Texts

Selected articles and reports will be assigned, as indicated below. These will be posted to Canvas. Additional articles and reports may be assigned and discussed based on timely topics.

Guest Speakers

There will also be one or two lecture sessions with guest speakers that have deep experience in policy implementation.

Content Schedule:

Week 1 and 2: Frameworks for implementing monetary policy: the case of inflation targeting.

Inflation targeting involves the public announcement of medium-term numerical targets for inflation with an institutional commitment by the monetary authority to achieve these targets. In recent years, several central banks, both in industrialized and emerging markets countries, have adopted this strategy for monetary policy. The framework allows a central bank "constrained discretion," rather than as an ironclad policy rule in the Friedman sense. Still, the adoption of a numerical target for inflation poses many operational questions (challenges) that policymakers must address. In this session we will discuss the potential of the inflation-targeting approach for making monetary policy more coherent and transparent, and for increasing monetary policy discipline. Other topics covered in the lectures will be the role of the exchange rate in an IT regime and the crucial importance of an independent central bank to control inflation. We will also review one case study of successful IT Implementation in an emerging market economy.

Week 2: A primer on capital flows

Open economies are always subject to shocks. The novel coronavirus, which has taken a huge toll across the world, is just the latest example. Other examples include changing global financial conditions, large drops in commodity prices and severe recessions in major trade partners. These global factors are usually associated with cyclical movements of capital flows. Under certain conditions, foreign financing available to borrower countries could unexpectedly dry up (“sudden stop”). What are the main drivers of capital flows? Are these flows mainly driven by global (“push”) factors or rather by country specific (“pull”) factors? How should policy react to these events? What are the implications of monetary policy normalization in advanced economies after the pandemic for emerging markets?


Week 3: Fiscal budget restrictions at work

In this part, we will develop a conceptual framework for analyzing the interactions between aggregate fiscal policy and monetary policy. The framework draws on existing models that analyze sovereign debt crises and balance-of-payments crises. This framework will serve as a guide for analyzing the monetary and fiscal history of a set of major Latin American countries from the 1960s until now.

Week 3 and 4: Fiscal adjustment. Challenges when implementing fiscal austerity.

When is it necessary to reduce the fiscal deficit and when should governments increase it? This is a perennial theme in the economic policymaking debate with very little consensus. Standard textbooks say that deficits are desirable when the economy needs an expansion, but advocates of austerity claim that under some circumstances fiscal contractions can be expansionary if they generate credibility. A lot depends on initial conditions—especially the level of public debt—a topic that we will discuss.

5. Chapter 4 of the IMF’s Regional Economic Outlook, April 2014 (pp. 49-62) also discusses fiscal adjustment in Latin America in response to the commodity shock.

Special Topic: Fiscal Policy after the Pandemic.

Week 6 to 8: The importance of fiscal rules

The convenience of rules versus discretion, of commitment versus flexibility, is a central issue of today’s fiscal policy debate. Why might governments want to surrender discretion? Which are different ways to tie their hands for the sake of fiscal responsibility? Fiscal rules have emerged as
the favorite mechanism to ensure macroeconomic stability and to enhance the ability to access international financial markets at favorable rates. However, revenue volatility (associated with commodity dependence), expenditure pressures and rigidities, make fiscal adjustments (and compliance with fiscal rules) very hard. We will study fiscal rules and their effectiveness in a number of countries.


Optional (Week 8): Sovereign debt management and sustainability

This session will discuss sovereign borrowing and debt management issues, medium-term debt sustainability analysis, and debt crises and restructurings. It will discuss the policies that support sustainable debt; the keys to a successful restructuring; the particular challenges faced when dealing with domestic and external creditors. It will also look at the recent update of the IMF- WB Debt Sustainability Framework.

Week 9: Assessing the economy: An introduction to financial programming

Policymakers continuously need to evaluate the current state of the economy, forecast where it is heading, and identify economic policies that can change the course of the economy. The IMF uses its well-known "financial programming model" (FPM) for economic surveillance purposes. The institution also uses FPM to derive monetary and fiscal programs to achieve desired macroeconomic targets in countries undergoing crises and having an IMF-supported economic program. Financial programming is based on monetary, balance of payments, and fiscal accounting identities. In this part, the students will learn the basic skills required to conduct financial programming.