

Macroeconomic Theory and Policy

Lecture 22 Overall Review

Overall Review

What did we do?

List of Lecture topics

1. What is macroeconomics?	13. Human capital and economic growth
2. Keynesian theory of aggregate demand	14. Technology and economic growth
3. IS-LM Models: short run	15. Role of expectation
4. New Keynesian theory of aggregate supply	16. Theories of inflation
5. Macroeconomic equilibrium: medium run	17. Structure of labour market
6. Fiscal policy	18. Theories of unemployment
7. Monetary policy	19. Theories of consumption
8. Output, inflation and unemployment	20. Theories of investment
9. Open economy macro model	21. International monetary system
10. Exchange rate policy	22. Mid-term
11. Trade and balance of payment	23. Presentation
12. Economic growth: long run	24. Overall Review

And Tutorials 1-12.

Are economic models capable of forecasting the future economic events?

- Short run fluctuations
- Long run growth

Yes, to some extent.

What do we know about the macroeconomy?

- Capacity to produce determines the standard of living in the long run.
- Aggregate demand influences amount of goods available in the short run.
- Inflation is proportional to growth rate of money in the long run.
- Trade-off between inflation and unemployment in the short run.
- Monetary policy can be used to stabilise the economy in the short run.
- Fiscal policy can be used to steer the economy in the long run.
- Good policies (rules) better than discretionary policies.
- Doing nothing better than bad policies.
- Policy have different effects if people already know what the government is doing rather than in a case when they do not know about the future policy actions.

What we know and what we do not know?

What we do not know about the macroeconomy?

- Can policy makers raise the natural level of output?
- Should they try to stabilise the economy?
- How costly is inflation and how costly is reducing inflation?
- Is government deficit a real problem?
- Effect of a policy in the economy

» Past, present and future of macroeconomics

- Econometric models useful for forecasting short run activities but may not be able to give realistic description of the economy in the long run.
- Full employment models seem unrealistic in the short run but useful tool to approximate the long run path of the economy.

Further issues than covered in this module

Outcome of policy game under uncertainty

Overlapping generation model and intergenerational accounting

Recursive dynamic system

Burn-Mitchel business cycle propagation mechanism

Structural and forecasting models for an economy, for a region and for a global economy

A stylised view of Macroeconomic theories and Policy

	New Classical	Gradualist monetarist	Moderate Keynesian	Extreme Keynesian
Market clearing	Very fast	Quite fast	Quite slow	Very slow
Expectations	Rational – adjust quickly	Adjust more slowly	Could be fast or slow to adjust	Adjust slowly
Long run/ short run	Not much difference	Long run more important	Don't neglect short run	Short run v. important
Full employment	Always close	Never too far away	Could be far away	Could stay away
Hysteresis	No problem	No problem	Might be big problem	Not a big problem
Policy conclusion	Demand management useless; need supply-side	Supply-side more important; avoid wild swings in demand	Demand management important too	Demand management is what counts