

**BGP-266M: Crisis Economics:**  
**History and Evaluation of the Policy Response to the Great Recession**  
**Spring 2011**  
**Starr Auditorium, Mondays 4:00-6:00pm**

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Course Overview: This course will examine the American policy response to the recent financial crisis and associated Great Recession. The objective is to illuminate (i) the changes in macroeconomic thinking necessitated by recent events (ii) the relationship between analytical macroeconomics, finance and policymaking in a political context (iii) lessons of recent experience for public policies directed at preventing crises in the future and responding to them when they come. The lectures will draw on the professional economic literature to the minimum extent necessary to facilitate understanding of the issues involved. The primary focus will be on the process of policy choice and the factors entering into actual policy decisions. Each lecture after the first introductory lecture will cover a different aspect of the policy response to the crisis. Sections will take up relevant analytical economic aspects.

Requirements: Students taking the course for credit will be required to write a 20 page paper addressing some policy question involved with the response to the crisis. Papers can either (i) consider one of the arguments made against a policy choice that was made and evaluating its merit in light of subsequent events or (ii) argue that on the basis of the information available at the time a different policy choice in some area should have been made and then evaluate their argument with the benefit of hindsight. Topics should be selected to focus on something specific—a paper on the merits of a wage subsidy as a component of the fiscal stimulus is more appropriate than one asking whether fiscal stimulus was a good idea. Students are free to write a paper applying the arguments of the paper in a non-American context with permission from the instructor or one of the Teaching Fellows. The paper is

due on the last day of the reading period, May 5<sup>th</sup>, at midnight.

Lectures:

- March 21 I. The Obama Inheritance: How and Why the Crisis Developed;  
Initial Responses and Choices Presented
- March 28 II. The Crisis and the Real Economy: The Role of Fiscal and Monetary Policy
- April 4 III. The Financial Crisis: The Breakdown of Intermediation;  
Banking and Shadow Banking; Bailouts, Bail Ins, and Stress Tests;  
Government as a Liquidity Provider of Last Resort
- April 11 IV. Key Sectors in Crisis: Housing, Automobiles and Manufacturing;  
Commerical Real Estate; Small Business
- April 18 V. Crisis Prevention: Risk Management; Regulation; Supervision; Resolution;  
Scope and Scale Restriction; Monetary Policy
- April 25 VI. The Global Dimension: International Experiences; Global Policy Coordination  
and Imbalances; Resisting Protectionism; Looking Forward

**Reading List**

The objective of this reading list is to provide a compendium of crisis related materials and to provide jumping off points for student papers. Starred papers are required and will be referenced in the lectures.

**Overview**

Federal Reserve Bank of St. Louis, (2009) "[The Financial Crisis: A Timeline of Events and Policy Actions,](#)"

Wessel, David (2009), In Fed We Trust: Ben Bernanke's War on the Great Panic, published by Crown Business.

Sorkin, Andrew Ross (2009), Too Big to Fail: The Inside Story of How Wall Street and Washington Fought to Save the Financial System—and Themselves, published by Viking press.

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*Financial System*, New York : Business Plus, 2010.

Wolf, Martin, *Fixing Global Finance*, The Johns Hopkins University Press, 2010.

## **I. Background to the Crisis**

### **Context**

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Bernanke, Ben S. "[The Great Moderation](#)," Remarks at the Meetings of the Eastern Economic Association, 20 February, 2004.

Rajan, Raghuram G., "[Has Financial Development Made the World Riskier?](#)" Federal Reserve Bank of Kansas City, Jackson Hole, Wyoming. August 27, 2005.

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Charles Kindleberger, *Manias, Panics and Crashes: A History of the Financial Crisis*, Wiley, 4th ed., 2000, Chapter 2, pp. 21-32.

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Mark Whitehouse, "[Q&A: Ken Rogoff Says Crises Are Like Heart Attacks, Predicting Timing Is Tough](#)," Wall Street Journal Blogs, February 10, 2011, 2:05 AM.

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### **Early Accounts**

\* Financial Crisis Inquiry Commission Report: <http://www.fcic.gov/report>, 'Conclusions of the FCIC', Part III, dissenting views by Hennessey, Holtz-Eakin and Thomas, and Dissenting views by Wallison.

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\* Swagel, Phillip, "[The Financial Crisis: An Inside View](#)," Brookings Papers on Economic Activity,

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\* Summers, Lawrence H. "[Responding to an Historic Economic Crisis: The Obama Program.](#)" Remarks at The Brookings Institution, March 13, 2009.

French, Kenneth et al. - The Squam Lake Report (2010), Chapter 1.

Vincent Reinhart "[A Year of Living Dangerously: The Management of the Financial Crisis in 2008](#)" JEP (2011)

The United States Government Printing Office, [Economic Report of the President](#), July 7, 2010, Chapters 1-3.

John Cassidy, "[No Credit](#)," *The New Yorker*, March 15, 2010.

Laura Alfaro and Renee Kim, "[U.S. Subprime Mortgage Crisis: Policy Reactions \(B\)](#)," Harvard Business School, 9-709-045, June 3, 2010.

Gorton, Gary B. "" [Kansas City Fed](#) (2008).

### **A Problem of Free Markets?**

\* Bernanke, Ben, "[Monetary Policy and the Housing Bubble](#)," Remarks at the Annual Meeting of the American Economic Association, January 4, 2010.

Posner, Richard A., *A Failure of Capitalism*, Harvard University Press, 2009.

Cassidy, John, "[After the Blowup](#)," *The New Yorker*, 11 January, 2010.

Cassidy, John, "[Chicago Interviews](#)," *Rational Irrationality*, 21 January, 2010:

### **Central Bank Policy and Monetary Conditions**

\* Bill White, [Is price stability enough?](#) BIS Working Paper No 205 (2006).

Bill White, Bank for International Settlements [78th Annual Report](#).

Goodheart, C.A.E., "[The Changing Role of Central Banks](#)," 9th BIS Annual Conference.

Fischer, Stanley, "[Comments on Charles Goodhart's paper 'The Changing Role of Central Banks'](#)", 9th BIS Annual Conference.

Krosner, Randall, "[What Should Central Banks Do? Comments on Charles Goodhart's 'The Changing Role of Central Banks'](#)," 9th BIS Annual Conference.

## **TARP**

Congressional Oversight Panel, [April Oversight Report: Assessing Treasury's Strategy: Six Months of TARP](#), April 7, 2009.

United States Department of the Treasury, Office of Financial Stability (2010) "[Troubled Asset Relief Program: Two Year Retrospective](#)"

Congressional Oversight Panel, [September Oversight Report: Assessing the TARP on the Eve of Its Expiration](#), September 16, 2010.

"[Rolling up the Tarp](#)," *Wall Street Journal*, October 27, 2009: A20.

Steven M. Davidoff, "[As TARP Fades, a Look at Its Flaws and Its Success](#)," *New York Times Online*, September 17, 2010, 3:26 PM.

Ben Smith, "[TARP: A success none dare mention](#)," *Politico*, September 14, 2010, 2:01 PM.

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## **II. Financial Crisis and the Real Economy**

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Bernanke, Ben S. (1983) "[Nonmonetary Effects of the Financial Crisis in the Propagation of the Great Depression](#)," American Economic Review 73: 257-76.

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Robert Hall: "[Why Does the Economy Fall to Pieces after a Financial Crisis](#)". JEP (2010)

### **The Liquidity Trap and Depression Economics**

\* Krugman, Paul, "[How Much of the World is in a Liquidity Trap?](#)", The Conscience of a Liberal, March 17, 2010.

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### **Fiscal Policy: Prospective**

\* Barro, Robert, "[Government Spending is No Free Lunch](#)", The Wall Street Journal, January 22, 2009.

\* Krugman, Paul, "[Stimulus Arithmetic \(Wonkish but Important\)](#)" The Conscience of a Liberal.

\* Stiglitz, Joseph E., "[The \\$1 Trillion Answer](#)," The New York Times, November 29, 2008.

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Stiglitz, Joseph E., "[Obama's Ersatz Capitalism](#)," The New York Times, March 31, 2009.

### **Early Analysis of Policy**

\* Cogan, John F., Taylor, John B., Wieland, Volker, "[The Stimulus Didn't Work](#)," The Wall Street Journal, September 17, 2009.

Congressional Budget Office, "[Estimated Impact of the American Recovery and Reinvestment Act on Employment and Economic Output from April 2010 Through June 2010](#)," August 2010.

Taylor, John, "[The Obama Stimulus Impact: Zero](#)." WSJ, December 9, 2010.

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Barro, Robert, "[The Stimulus Evidence One Year On](#)," The Wall Street Journal, February 23, 2010.

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Becker, Gary S., "[Fiscal Stimulus Packages: What Are Their effects?](#)" *Becker-Posner Blog*, March 1, 2010.

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Becker, Gary S. "[The Treasury's Plan to Buy Bank Assets](#)," *The Becker-Posner Blog*, March 29, 2009:

#### **IV. The Sectoral Dimension**

##### **Housing Markets**

\* Edward L. Glaeser, with Joshua Gottlieb and Joseph Gyourko, "[Can Cheap Credit Explain the Housing Boom](#)," (July 2010) .

\* Martin Feldstein, "[How to Stop the Mortgage Crisis](#)" *Wall Street Journal (Eastern edition)*. New York, N.Y.: Mar 7, 2008. p. A.15

\* Warren, Elizabeth, "[Testimony Submitted to the Senate Finance Committee](#)", March 31, 2009.

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\* Zywicki, Todd J., "[Chrysler and the Rule of Law](#)," *Wall Street Journal*, May 13, 2009: A19.

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Steven Rattner, *Overhaul: An Insider's Account of the Obama Administration's*

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\* Timothy F. Geithner, "[Geithner's Speech to the American Enterprise Institute](#)," *transcript reprinted at RealClearPolitics.com*, March 25, 2010.

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