

Princeton University: Department of Economics  
**ECO 342: Money and Banking (fall 2010)**  
(September 14, 2010)

Instructor:	Ana Babus <a href="mailto:ababus@princeton.edu">ababus@princeton.edu</a> BCF 305, 258-0126	Lecture: T-Th 10:00 – 10:50 am Guyot 10
Office Hours:	W 4:30pm – 5:30pm	Precepts: T 11:00 – 11:50 am T 1:30 – 2:20 pm W 7:30 – 8:20 pm
Preceptor:	Constantinos Kalfarentzos <a href="mailto:kkalfare@Princeton.EDU">kkalfare@Princeton.EDU</a> Fisher Hall, B08	
Office Hours:	T 2:20pm – 3:20pm location TBD	

This course studies the role that financial markets, institutions and money play in resource allocation. We explore these questions analytically, using tools of economic theory. We begin with an overview of the main concepts and ideas. Then we analyze prices and allocations in a frictionless environment. The main goal is to be able to evaluate state-contingent goods at different future dates. In the first half, we follow relatively closely the textbook.

In the later half of the course, we introduce the frictions of private information, limited enforcement, sticky nominal wages and product prices in order to examine financial institutions, money and government policy. Here, the students are expected to read assigned articles in addition to the textbook.

There will be three weekly precepts. Precepts will have three main functions. First, they will review background necessary to understand the lectures; second, they will occasionally cover new material, including illustrative cases; third, they will answer questions about lectures and assignments.

## 1. Prerequisites

Econ 300 or 310, and Econ 301 or 311. Those who have background of only 100 level micro and macro economics can take this course on their own responsibility.

## 2. Grading

Midterm 30% (closed book), Final Examination 50% (closed book), Homework 20%.

### **3. Textbook**

The required textbook for the course is 'Money and Banking' by Robert Wright and Vincenzo Quadrini, 2008, Flatworldknowledge.com. The students can read the textbook at <http://www.flatworldknowledge.com>. The book will NOT be available for purchase through Labyrinth Books. Students who wish to buy the hard copy need to order it themselves at Flatworldknowledge.

In addition to the textbook, the second half of the course uses research articles. The references provided below are indicative and may change in due course. The articles will be available electronically at the blackboard of this course and/or E-Journals of Princeton Library.

### **4. Course Outline**

- I. An Overview, Flow-of-funds and System of National Accounts
- II. Time and Resource Allocation in a Frictionless Economy
  2. Households' Choice of Consumption and Saving
  3. Firms' Investment Choice
  4. A General Equilibrium Model of a Two-Period Economy under Certainty
- III. Valuation Models
  5. Valuation of Bonds
  6. Valuation of Common Stocks
- IV. Financial Institutions and Monetary System
  7. The Role of Money
  8. The Role of Financial Intermediaries
- V. Monetary Policy and Financial Crisis
  9. Monetary Policy
  10. Financial Crisis and Policy Reaction

## 5. References

- T. Adrian and H. Shin. "Money, Liquidity and Monetary Policy," *American Economic Review* (May 2009): 600-605.
- B. Bernanke. "The Macroeconomics of the Great Depression: A Comparative Approach," *Journal of Money, Credit, and Banking* (1995): 257-276.
- B. Bernanke and M. Gertler. "Inside the Black Box: the Credit Channel of the Monetary Policy," *Journal of Economic Perspectives* (Fall 1995): 27-48.
- M. Brunnermeier. "Deciphering the 2007-08 Liquidity and Credit Crunch," in *Journal of Economic Perspective* (2008): 77-100.
- N. Kiyotaki and R. Wright. "Acceptability, Means of Payments and Media of Exchange," *Quarterly Review*, Federal Reserve Bank of Minneapolis (Summer 1992). Available at <http://www.minneapolisfed.org/research/qr/>.
- D. Diamond and P. Dybvig. "Bank runs, Deposit Insurance and Liquidity," *Journal of Political Economy* (1983): 401-419. Available at E-Journal of Princeton Library.
- G. Gorton. "Slapped in the Face by the Invisible Hand: Banking and the Panic of 2007," mimeo, Yale University (2009).
- G. Gorton and A. Metrick. "Securitized Banking and the Run on Repo," Yale ICF Working Paper 09-14 (2009). Available at the author's webpage.
- N. Kiyotaki and J. Moore. "Credit Cycles," *Journal of Political Economy* (1997): 211-248.
- N. Kiyotaki and J. Moore. "Balance-Sheet Contagion," *American Economic Review* (May 2002): 46-50.
- N. Kiyotaki and J. Moore. "Evil is the Root of All Money," *American Economic Review* (May 2002): 62-66.
- T. Sargent and Neil Wallace. "Some Unpleasant Monetarist Arithmetic," *Quarterly Review*, Federal Reserve Bank of Minneapolis (Fall 1981)
- S. Williamson. "Recent Development of Modeling Financial Intermediation," *Quarterly Review*, Federal Reserve Bank of Minneapolis (Summer 1987).