



ST. FRANCIS XAVIER UNIVERSITY

Department of Economics
Faculty of Arts

ECON 335 & 336: Money and Financial Markets I & II

Fall 2021 & Winter 2022

Description:

This two-course sequence focuses on the inter-relationship between asset price movements and macroeconomic developments, with a special emphasis on monetary and financial policy tools and objectives

In 335 we deal with the various forms of financing that can be available to firms, governments and households (bank credit, bonds and equity issues). We derive and study models that explain asset price movements with a specific focus on factors that can be influenced by policy-makers. We examine the consequences of severe asset price corrections, with the financial crisis of 2008-09 being given special consideration. We also study how policy-makers can prevent, or mitigate, the impact of crises via macro-prudential regulations.

In 336 we examine how asset price movements can influence output and inflation. We also examine how the central bank can, via monetary policy actions, influence the path of asset prices, output and inflation. Special attention will be given to current policy issues, including the impact of Covid-19 on the economy and the extraordinary monetary policy actions taken since March 2020, and through 2021 and 2022, to mitigate the impact of the pandemic on the economy.

Lectures:

Wednesday 9:45 – 11:00

Friday 8:15 – 9:30

Lecture Locations:

335 (Fall 2021): Mulroney Hall 2070

336 (Winter 2022): Schwartz 256

Instructor:

Greg Tkacz, Ph.D.

Instructor's Office:

Mulroney Hall 3075

Office Hours:

Wednesday 11:00 to 12:30

Thursday 10:00 to 12:30

Friday 9:30 to 11:00

or by appointment

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Profile Page:

www.mystfx.ca/economics/greg-tkacz

Evaluation:

ECON 335: Fall 2021

Assignment #1 (due Friday October 1): 10%
Mid-Term Exam (Wednesday October 13, in-class): 30%
Assignment #2 (due Friday November 19): 10%
Final Exam (to be scheduled by Examinations Office in December): 50%

ECON 336: Winter 2022

Assignment (due Friday February 4): 10%
Mid-Term Exam (Wednesday February 16, in-class): 30%
Monetary Policy Report group presentation & participation (March 23, 25, 30 or April 1): 20%
Monetary Policy Report, final draft (March 23): 40%

Key Dates:

ECON 335: Fall 2021

Wednesday September 8: First ECON 335 class
Friday October 1: Assignment #1 is due
Wednesday October 13, 9:45 to 11:00: MID-TERM EXAM
Monday November 8 to Friday November 12: Fall Study Break (No Classes)
Friday November 19: Assignment #2 is due
Friday December 3: Last ECON 335 class
December 9 to 18: EXAMINATION PERIOD

ECON 336: Winter 2022

Wednesday January 5: First ECON 336 class
Friday February 4: Assignment is due
Wednesday February 16, 9:45 to 11:00: MID-TERM EXAM
Monday February 21 to Friday February 25: Winter Study Break (No Classes)
Wednesday March 23: Monetary Policy Reports are due
March 23, 25, 30, April 1: Group Monetary Policy Report presentations
Friday April 1: Last ECON 336 class.

Drop Dates

Students may drop ECON 335 on Banner by **WEDNESDAY NOVEMBER 3.**

Students may drop ECON 336 on Banner by **FRIDAY MARCH 11.**

Learning Objectives:

1. To expand students' knowledge of monetary theory by introducing them to different measures of the money supply and how changes in these can impact the economy and financial markets;
2. To show students how monetary policy is conducted in practice, including the range of issues that confront policy-makers, and the types of data they monitor; and
3. To allow students to make informed contributions to monetary policy and financial stability policy debates and discussions.

Pre-Requisites and Math Requirements:

Pre-requisites: ECON 101 and ECON 102

Math Requirements: You'll be expected to know high-school-level algebra (e.g. the quadratic equation, cubic functions, exponents, etc.) We'll freely use algebra in 335 to derive some key results in Finance that, up until now, you may only have learned using a business calculator.

Calculator: For the assignments and exams, I recommend you find a simple calculator that can at least handle exponents and square roots. You should be able to find one for no more than \$10. If you have a fancy Business or Scientific calculator, you can feel free to use it.

Textbook and Readings:

These courses are designed around a FREE open-source textbook. This has the advantage of lowering costs for students, but the disadvantage is that the book is U.S.-based, so we need to "Canadianize" the content. For this reason, we will also rely upon some FREE Canadian resources.

1. Wright, Robert E. (2012) *Money and Banking*. Saylor Foundation: Open Textbook Library, ISBN: 978098204308. FREE textbook that can be downloaded from <https://open.umn.edu/opentextbooks/textbooks/29>
2. Bank of Canada *Financial System Review* and *Monetary Policy Report*.
3. We will monitor current economic and financial developments in the media. Links to relevant stories will be provided on Moodle.

Course Outline

ECON 335: Fall 2021

Weeks 1-2: Introduction

We explain the fundamentals of finance, and define the concept of money. We'll cover both conventional money, and explain how Cryptocurrencies fit into the monetary framework. We will also explain the roles and structures of central banks in Canada and the United States. Finally, we will look at recent financial and macroeconomic data to gauge the current health of the economy and financial markets.

→ Chapter 2: The Financial System

→ Chapter 3: What is Money?

Weeks 3-6: Bond Financing and Interest Rate Movements

Bonds are the most popular form of finance, and so we need to understand how they are determined and why their prices move. We'll cover some standard bond pricing models, and see how bond prices and interest rates are inversely-related. Importantly, we'll understand why some interest rates movements tend to be highly correlated with one another, and others less so.

→ Chapter 4: The Meaning of Interest Rates

→ Chapter 5: The Economics of Interest Rate Fluctuations

→ Chapter 6: The Economics of Interest Rate Spreads and the Yield Curve.

Weeks 7-8: Equity Financing and Stock Price Movements

Stock prices are widely reported in the financial press, and yet they are not the most important form of financing – nor the largest component of financial wealth. Nevertheless, it is important to understand their movements, as extreme stock price movements can spillover into other financial sectors or the economy. We can extend one of our bond-pricing models to obtain a simple model of stock prices.

→ Chapter 7: The Stock Market, the Theory of Rational Expectations and the Efficient Market Hypothesis

Weeks 9-11: Bank Financing: Real Estate Prices & Financial Crises

Banks play a large role in the financial system, especially as it pertains to personal loans, with real estate loans being the largest category. We will discuss how banks can promote financial efficiency, but also explain how, if left unregulated or under-regulated, improper bank lending can lead to very detrimental outcomes. We will discuss how bank lending impacts real estate prices and how these could lead to a full-blown financial crisis.

→ Bank of Canada 2021 *Financial System Review*

→ Chapter 8: Financial Structure, Transaction Costs and Asymmetric Information

→ Chapter 13: Financial Crises

Weeks 12: Preventing Financial Crises: Banks and Banking Regulations (Time Permitting)

→ Chapter 11: The Economics of Financial Regulation

Course Outline

ECON 336: Winter 2022

Weeks 1-3: Monetary Policy Tools and Targets

We'll explain how the Bank of Canada can implement policy by influencing the money supply and overnight interest rate. This is currently extremely relevant as the Bank has been conducting "Quantitative Easing" since March 2020. How does it work? What are the implications? We'll also explain how monetary policy goals are set every five years in Canada, with the latest update occurring in October 2021.

- Chapter 15: The Money Supply Process and the Money Multipliers
- Chapter 16: Monetary Policy Tools
- Chapter 17: Monetary Policy Targets and Goals

Weeks 4-7: Monetary Theory

We'll develop a simple model that allows us to track the impact of monetary policy actions on interest rates, output and inflation.

- Chapter 20: Money Demand
- Chapter 21: IS-LM
- Chapter 22: IS-LM Analysis
- Chapter 23: Aggregate Supply and Demand

Weeks 8-10: Current Macroeconomic and Financial Developments

*Using the tools we've developed, we will analyze current financial and economic developments and determine what policy-makers **should** do. This will help students think about the issues that should enter their **Monetary Policy Reports**.*

Weeks 11-12: Student Presentations

*Groups of four students will draft a **Monetary Policy Report**, a (maximum 20-page) document that:*

- *Analyzes Canadian and international economic developments*
 - *Analyzes Canadian and international financial developments*
 - *Based on all available information, predicts what will happen to the economy and financial markets over the next 24 months;*
 - *Identify potential RISKS (economic, financial, political, social, environmental, etc.) that could impact your prediction above; and*
 - *Provides specific advice to the Governor of the Bank of Canada (i.e. ME) regarding monetary policy actions (e.g. should the overnight rate increase, decrease, or stay the same? When should it change? Should Quantitative Easing be wound-down or expanded? Etc.)*
- *All groups will have 20 minutes to present the above to the whole class, with five minutes available for Q&A.*