Management 321
Business in the World Economy

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Overview

We use a mixture of examples, cases, and readings to expose the underlying economic structure behind the major macroeconomic forces affecting business. Many of these forces are shaped by globalization. Through lectures, assignments, Q&A, and class discussion, we systematically develop the tools to understand the forces that govern aggregate economic activity; we also explore the implications for business. Examples are drawn from the United States, Europe, South America, and Asia. Since the economy is complex and the relationships approximate, your goals in this course should be to learn (and apply) the tools and methods emphasized. Every class session will also provide opportunities for you to articulate your thoughts and communicate them to others.

Course Requirements

Group questions: (20% of course grade). For two of the three Group assignments (your choice), printed copies of your answers are due at the start of class on the day indicated.

Quizzes: (20% of course grade). There are 6 electronic quizzes (see Blackboard) covering the material in the book (Moss) and my Module outlines. Quizzes are true/false and multiple choice. You are given 60 minutes to take the quiz, which must be before 9pm Sunday night of each week. We will drop the lowest quiz grade.

Debates: (15% of course grade). Each group will ‘compete’ in a debate during the mod. Groups will be assigned by the Dean’s office. On debate day, I will tell you which side of the argument you must defend. Groups need to work together to prepare their best winning arguments and communication strategies. Debate grades and procedures are explained below.

Involvement: (15% of course grade). There are 4 “P”s of student involvement: (1) Preparation – you need to be prepared; (2) Presence – you need to be in class (with your name tag displayed and with all electronic devices turned off); (3) Promptness – late arrivals disrupt the class and demonstrate disrespect for everyone else; and (4) Participation – learning is facilitated by participation and I will try and manage this process. I will rotate individual participation via a daily “call list” of class members. Each person’s name will recur on more than one of the 14 daily lists.

Final exam: (30% of course grade). The final exam will be held during the regular exam period and will be comprehensive, with a mixture of easy (20%), intermediate (40%), and challenging questions (40%). The exam will contain multiple-choice, short answer, and true/false questions.

Course Materials

There is one HBS Case available at the bookstore. All other reading materials will be on BlackBoard.

Honor Code Policy: Collaboration Policies are specified on each assignment. Additionally, use of previous years’ (and other non-expressly sanctioned) materials is prohibited. See Blackboard for more policies.
Corresponding to each day I list a set of questions and the reading materials that you should be prepared to discuss on the day indicated. These are your guide to marking your progress in the class.

**Day 1: Introduction & Measuring an economy**

*Required Readings: Moss, Chapter 1; Module 1a notes*

- How is measuring an economy different (or similar) than measuring a company?
- Is it meaningless to compare (say) Hong Kong (or India) to the U.S.? That is, given the obvious differences in these economies, how can one compare them?
- What legitimate comparisons might one make? What comparisons make little sense?
- Some comparisons of economic data across countries are trivially obvious & we don’t learn anything. List some ways to compare (summarize data from) two very different economies (e.g., Hong Kong & the U.S.) that might be informative.
- What conclusions could one hope to make?

**Day 2: National Income Accounting (NIA)**

*Required Readings: Moss, Chapter 5; Module 1b notes*

- Why would an increase in GDP be good?
- All increases in GDP are good (T/F – and why)
- Suppose we (as a nation) wanted to encourage bio-medical research, and decided to subsidize it. Discuss the macroeconomic implications and pros/cons.
- What is significant about the statement that the macro economy is a closed system?
- How can the Federal Government run a Deficit?
- Imports lower our GDP and therefore enter the NIA accounts as a negative (T/F & why)

*Required Readings: Moss, Chapter 6; Module 1c notes*

- Is the US Current Account deficit sustainable? What are the alternatives?
- Why is it impossible for a country to simultaneously run a CA surplus and a FA surplus?
- What would an Investment boom normally imply about the CA?

**Part 2: Money & Inflation**

*Required Readings: Moss, Chapters 2-3; Module 2a notes*

- Why does an economy have money?
- How can a government collect Seigniorage – that is, why would people let themselves be taxed this way?
- What’s real about a real interest rate? Is there a ‘fake’ rate?
- Define the Long Run and the Short Run

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**U.S. Inflation**

![Graph of U.S. Inflation](source: http://data.bls.gov/cgi-bin/surveymost?cu)

- The above figure plots annual % changes in the U.S. Consumer Price Index data (the 1st item at [http://data.bls.gov/cgi-bin/surveymost?cu](http://data.bls.gov/cgi-bin/surveymost?cu)). Comment on any trends in inflation over the period.
- What does the quantity theory predict about the causes of inflation?
- What are the costs of inflation at a macroeconomic level?
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Daily topics for class discussion

Day 4:  Case: The German Hyperinflation
Required Readings: HBS Case: German Hyperinflation

- Speculate on why German real government revenues fell after 1921? (Exhibit 5)
- War reparations imposed on Germany by the allies at the close of the war were ‘only’ ~ 100% of GDP. Why was this “staggering”?
- Why did the Reichsbank increase its holdings of Treasury bills? Of Commercial paper?
- Why was there inflation? Who was responsible?
- What advice would you have given the German government on reducing inflation?

Group Assignment #1: Use the data in the excel spreadsheet “OECD CPI & Money.xls”, and for any country in the table. The source of this data is the OECD (Organization for Economic Cooperation and Development). Prepare your answers on one sheet of paper using a minimum font size of 18 pts. I may project your answers on the screen in class. Address the following questions:

1. Pick a country and graph the relationship between money growth and inflation over at least 25 years. Note, you will need to decide: (a) what measure of inflation to use, (b) what measure of ‘money’ to use, and (c) how ‘growth rate’ is defined (e.g., month-to-month, year-to-year, 5-year averages, etc.). Label your vertical axis “Percent” and your horizontal axis “time”.
2. Run a regression of inflation on money growth and be prepared to interpret the results.

Day 5:  Part 1: (Debate): China will be richer than the U.S. by 2025
Part 2: The Federal Reserve
Required Readings: Moss, Chapters 2-4; Module 2a notes

- What is the relationship between inflation and interest rates? Do you expect this relationship to hold all the time? Why or why not?
- How is a nation’s money supply increased?
- What are the short-run and long-run effects of increasing the money supply?
- Why is inflation bad (give several reasons).
- If inflation is bad, can you point to concrete macroeconomic consequences of inflation? For each of your reasons, consider why the predicted ‘cost’ of inflation may be overstated.
- What are the benefits of inflation?
- How would you expect the Fed to respond to a major oil shock? How could this benefit your diversified multinational company?
Day 6: Floating Exchange Rates

*Required Readings: Moss, Chapter 2, 4, & 7; Module 2b notes*

- What is the relationship between inflation and exchange rates? (Hint: PPP). Do you expect this relationship to hold all the time? Why or why not?

- Warren Buffet has made public statements that he believes the U.S. dollar will depreciate, which has led him to look for other currencies to invest in. Answer the questions below:

**Group Assignment #2:**

1. If you were Warren Buffet and could only buy a **developed** country’s currency, (a) which one would you choose, and briefly state why; and (b) what is your forecast for this country’s exchange rate six-months from now? Briefly, what are the reasons behind this forecast?

2. Similarly, if you were Warren Buffet and could only buy a **developing** country’s currency, (a) which one would you choose, and briefly state why; and (b) what is your forecast for this country’s exchange rate six-months from now? Briefly, what are the reasons behind this forecast?

Data and other useful information for this assignment may be found on the Walker Library electronic data bases below, or the University of British Columbia web site listed first.

- Exchange rate data is easy to get at: [http://fx.sauder.ubc.ca/data.html](http://fx.sauder.ubc.ca/data.html) (choose monthly)

Day 7: *(Debate): The $/euro exchange rate will reach 1.60 within 18 months.*
Day 8:  Fixed exchange rates

*Required Readings: Moss, Chapters 4, 6, 7; Module 2c notes*

- Describe how inflation is determined (the process) in an economy with fixed exchange rates. How is this different in an economy with floating exchange rates?
- Suppose you work in asset management for a large multinational. How could you use your knowledge of how fixed exchange rates work to save your company some money?
- List 4 business-relevant applications of PPP
- Provide an explicit numerical example of how to compute/estimate the effects of a shock in one country on business conditions in another?

**In class exchange rate simulation: East Owen/West Owen**

- The vital role of exchange rates
- Linkages between the exchange rate regime and the real economy
- Why do some countries choose fixed exchange rates?

Day 9:  Debate: Hong Kong should adopt a different exchange rate peg.

*Required Readings: Moss, Chapter 5-7; Module 2c notes*
Day 10: The Current Global Crash
Required Readings: *** “The complexities of the Financial Turmoil of 2007 and 2008” ***
This is a difficult reading – you need to devote ample time to reading it!

- What factors fueled the boom?
- How did the housing boom spill-over to the real economy?
- What role did securitization play in the ‘shadow banking system’?
- What factors contributed to the liquidity crisis?
- What were the key Fiscal and Monetary policy responses?

Day 11: (Debate): Historians will place Monetary (or) Fiscal Policy as the deciding factor in the resolution of the 2007-09 U.S. financial and economic mess.

Day 12: The Return of Depression Economics
Required Readings: Moss, Chapter 3, Krugman Ch. 1-10.

The book the Return of Depression Economics is a concise tour of global economic crises since about 1990. While the book’s author, Paul Krugman, is an outspoken liberal economist, and writes two columns per week for the New York Times, his descriptions of events in Mexico, Argentina, Brazil, Japan, Russia, Thailand, Malaysia, ...., are basically on track. At any rate, there is probably no other place to get a broad overview in so short a book, or in such clear writing. Each person should have read the entire book by now, but today the discussion will be ‘led’ primarily by specific groups. I will (of course) call on those individual names on my “list” to solicit clarification and/or amplification points.

Group Assignment #3: Each group is responsible for reading (and reporting on) two chapters of Krugman’s “The Return of Depression Economics and the Crisis of 2008”. Each group should prepare two chapter summaries (one chapter per page). These should be turned in at the start of class. Chapter summaries may be a short paragraph, or a bullet point list.

Group 1 – Ch. 2 & 9  
Group 2 – Ch. 3 & 8  
Group 3 – Ch. 4 & 7  
Group 4 – Ch. 5 & 6  
Group 5 – Ch. 6 & 5  
Group 6 – Ch. 7 & 4  
Group 7 – Ch. 8 & 3  
Group 8 – Ch. 9 & 2
Day 13  Economic Growth and Business Cycles

Required Readings: Module 3a notes

- Why is economic growth so important?
- What does total factor productivity measure and how is it measured?
- Why is total factor productivity so important?
- What is the best way for a country to raise its standard of living?
- What happens in a recession? (what makes a recession a recession)?
- Based on the data presented, is the business cycle related to the exchange rate?

![Graph showing U.S. Business Cycles versus Exchange Rate: 1975-2007 (Grey bars indicate economic slowdown of at least 1 month)]

Notes: The index of ‘coincident’ indicators is an indicator of where the country is, in terms of its business cycle; the coincident indicator should go up when business is booming and decline when business conditions slow; the bars indicate a 1-month downturn in economic activity. The exchange rate index is a weighted-average of its bilateral exchange rates versus its major trading partners. The average is weighted by the relative amount of trade (i.e., how much) each trading partner conducts with the specified country. Since it is an average of different exchange rates, the result is converted into index form (i.e., in the base period the weighted-average is arbitrarily set to 100).

Day 14: Ten Important Conclusions

- List the 10 most important concepts, or tools in this course. Concepts or tools should be useful for analyzing or understanding economic events or policy proposals. These could be specific theories or specific explanations for economic events. You should be prepared to share items from your list in class.
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Format for Debates

Each group will participate in one debate.
The debates: teams of ~5 students are formed by the Dean’s office.

- Each team prepares a presentation (or an outline of the major arguments covered; with the plan for defeating the other argument included) that has to be sent to Shad.Thomas.2009@owen.vanderbilt.edu by 8:00 am the morning of the debate (the top line of the outline should include the names of all group members and the topic of the debate). There has to be two well labeled presentations in Power Point or Adobe, one that supports the YES and the other that supports the NO. In other words, each team knows which topic they will be debating but you do not know if you will be debating in favor or against. So, you have to prepare both arguments.

- At the start of the class, I will take a poll of the students in the class. If a student is not there at the time the poll is being taken, we will consider the student absent from class (members of the teams debating will not participate in the polls). Significant others are allowed in the class. They will also fill the survey but their votes will not be counted.

- After the poll is taken, I decide which team will debate which position: in favor or against, and in which order (in a very dictatorial fashion, perhaps by flipping a coin).

- Each team has 5 minutes to present opening remarks.

- Then, each team has 8 minutes for questions for the other team. (Be sure to prepare these in advance).

- Finally, I will allow 2 more minutes for each team to rebut back (if they want to). I might follow up with additional questions of my own – again in a very dictatorial fashion.

- Timing: EACH GROUP IS RESPONSIBLE FOR ENFORCING TIME LIMITS ON ITSELF; going over time reduces your total possible points.

- Immediately after this period I take the poll again. The team that moves public opinion in their direction wins the debate. It does not matter by how much. Thus, it is possible to move one vote to your side and win the debate. If the public opinion did not change (which has never happened), I may cast the deciding vote.

- After this time, we open for general discussion.

- Grading of the debates: 20 points for quality of the outline & of the actual delivery + 5 points to the winner (0 to the loser); in the case of a tie 2.5 points to each.
Useful web links

1. [http://fx.sauder.ubc.ca/data.html](http://fx.sauder.ubc.ca/data.html); Time series of (daily, weekly, monthly...) exchange rates.

2. [http://www.helsinki.fi/WebEc/framec8d.html](http://www.helsinki.fi/WebEc/framec8d.html); Resources for economists are available as well as U.S. macro and regional data.

3. [http://hadm.sph.sc.edu/courses/econ/Tutorials.html](http://hadm.sph.sc.edu/courses/econ/Tutorials.html); Economic interactive lectures and exercises. Topics include demand, elasticity, supply-demand equilibrium, total cost, variable cost, and marginal cost.

4. [http://www.bls.gov/home.htm](http://www.bls.gov/home.htm); Bureau of Labor Statistics provides recent and historical data on labor productivity, labor force, unemployment, earnings, CPI, and PPI.


6. [http://www.federalreserve.gov](http://www.federalreserve.gov); Federal Reserve Chairman of the Board of Governors provides monetary policy testimony and reports to Congress.

7. [http://www.census.gov/hhes/www/income.html](http://www.census.gov/hhes/www/income.html); The U.S. Census Bureau provides information on businesses that includes: agriculture, government, international trade, manufacturing, mining, services, and wholesale goods. Economic related information on people that includes: income, poverty, labor force, and households. Additional data on GDP, wages, prices, and jobs is provided.


9. [http://www.frbsf.org/education/index.html](http://www.frbsf.org/education/index.html); The San Francisco Federal Reserve Bank provides an overview of the major economic schools of thought.

10. [http://www.homefair.com/homefair/cmr/salcalc.html](http://www.homefair.com/homefair/cmr/salcalc.html); The salary calculator provides a quick comparison of the cost of living in different cities.


14. [http://www.usatoday.com/money/mfront.htm](http://www.usatoday.com/money/mfront.htm); The economy tract provides explanations and data on construction, consumer confidence, employee costs, factory orders, Federal Reserve, GDP, housing, income, leading economic index, prices, productivity, retail sales, related leads (FED) trade, and unemployment.

Long-Term Perspectives on the Current Boom in Home Prices, by Robert Shiller

Contrary to Robert Shiller's Predictions, Stock Market Investors Made Much Money in the Past Decade: What Does This Tell Us?, by Brad DeLong and Constantin Magin
http://www.bepress.com/ev/vol3/iss7/art2/

Divergent Views on the Coming Dollar Crisis, by Brad DeLong
http://www.bepress.com/ev/vol2/iss5/art1/

Progressive Consumption Taxation as a Remedy for the U.S. Savings Shortfall, by Robert H. Frank
http://www.bepress.com/ev/vol2/iss3/art2

Foreign Exchange Market in the United States - NY Fed
http://www.ny.frb.org/education/addpub/usfxm/

US Monetary Policy - An Introduction - SF Fed

What we know and don't know about the Term Premium

The U.S. Productivity Acceleration and the Current Account Deficit

Post-Apartheid South Africa: the First Ten Years, IMF 2006

An editorial by me in the San Francisco Chronicle
The effect of an undervalued yuan on the U.S. current account (op ed by D. Parsley & H. Popper)
http://www2.owen.vanderbilt.edu/david.parsley/Non-technical/SF%20Chronicle%208-8-08.pdf

Excellent Readable Books and articles about important subjects:

The Economics of Aid

Economics without graphs or equations
- Charles Wheelan, Naked Economics, 2002, W.W. Norton

A compendium of information about the ease (or difficulty) of doing business around the world

Financial crisis:
http://www.vanityfair.com/politics/features/2008/12/banks200812
http://online.wsj.com/video-center/the-end-of-wall-street.html