Monetary and Financial Policy, autumn 2014  
Economics 320  
Professor: Thomas Bishop

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Office hours: Monday, Wednesday 2:30-5:00, or by appointment

Class time, location: Wednesday 18:00-20:50, Broome Library 2490

Midterm exam: October 8  
Final exam: December 10

Course website: Blackboard (This site has lecture notes, assigned readings, and answers to homework assignments and exams.)


Grading system

Your grade for the course is based on homework and exams in the following way:

<table>
<thead>
<tr>
<th>Task</th>
<th>Percent of grade</th>
</tr>
</thead>
<tbody>
<tr>
<td>Homework assignments</td>
<td>25</td>
</tr>
<tr>
<td>Midterm exam</td>
<td>35</td>
</tr>
<tr>
<td>Final exam</td>
<td>40</td>
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</table>

Grades for total points from the homework and exams will be assigned according to the following distribution:

- 90%-100%: A+, A  
- 80%-89%: B+, B  
- 70%-79%: C+, C  
- 60%-69%: D+, D

I may also adjust the scores to account for the difficulty of the course in English. For example, if few people get a final score above 90%, then I will give out more As to account for difficulty of the English instruction or exams. In this case, I can allocate up to 30%-50% As and up to 65%-90% As and Bs.
Exams

There will be no make-up exams, so if you can not attend class on the day of the exams or you can not
attend the final exam, please do not enroll in this course for a grade. You are welcome to take the course
for a pass-fail grade. You may not have a job interview during an exam and take a make-up exam later!

The midterm exam will cover all material up to its date. The final exam will have questions based on
definitions and concepts from earlier material, so you should not forget the earlier material when studying
for the final exam. Both exams will include multiple choice questions taken primarily from the lecture
notes but can include questions based on the assigned reading.

Homework assignments

Late homework will not be accepted. If you can not finish in time, hand in what you have completed for
partial credit. I do this out of fairness for your fellow students. If you know that you will be out of town
or otherwise unavailable when the assignment is due, you must submit it early. Please turn in your
assignments at class time by the end of class time on the due date.

Homework assignments are generally from the end of each assigned chapter, and they are completed in
teams. I will initially assign teams, but you are free to switch teams before the first homework
assignment is due. Each team should have 3-5 students, and work should be allocated equally. A team
 submits only one copy of answers, and all team members receive the same grade for the assignment.
When you turn in your homework assignment, write the names of each team member in the upper right
corner of the first page, so that credit can be given to each member.

Answers to the homework problems will be posted on the website after the due date. You are expected to
read the answers to the homework assignments by yourself, since I will not generally cover homework
assignments in lecture.

Class participation

Regular class participation can help your grade if you are on the borderline between two grades. For
example, if you are at the cutoff between a B+/A, regular class participation would boost your grade to an
A.

Course overview

We will study money, non-monetary assets, financial institutions and monetary policy with a little
emphasis on Korean financial institutions and monetary policy and a little emphasis on US financial
institutions and monetary policy (since I studied in Korea too). We will consider the role of money,
interest rates and bonds in the economy. We will also study how banks operate and how and why they
are regulated. Finally, we will study central banks, monetary policy and their effects on production,
employment and inflation.

The course is a mix of theory and applications of theory to real policies and issues. The theory is
intended to give you a methodical way to think about important issues in economics (and in real life) and
to simplify them so that they are more comprehensible.
Program Learning Goals: Skills that I aim to convey and to teach in the course include

- critical thinking and analysis of monetary and financial issues
- oral communication through questions and answers in class
- written communication through written homework assignments
- collaboration through homework assignments
- ethical conduct: no cheating on exams, but cooperation/collaboration for homework is encouraged.
- competency in monetary and financial economics to prepare you for a job at a financial institution and to prepare you to understand personal finances (see course learning outcomes)

Course Learning Outcomes: At the end of this course, good students will be able

- to understand how the financial system basically operates
- to define money and to understand its use
- to calculate yield rates on bonds and return rates on assets in general
- to explain the traditional activities of banks and how they are recorded on a balance sheet
- to understand various non-traditional financial activities that modern banks sometimes use
- to understand the types of risks that banks and other financial institutions face
- to explain important banking regulations
- to explain how central banks function
- to predict how monetary policy influences inflation, production and employment

Advice on studying

Create your own notebook: print the lecture notes before lecture and write on them during lecture.

You will get more value out of your tuition dollars if you read the assigned material before it is covered in class. Treat academics as you might athletics: pace yourself throughout the semester, rather than cram before exams. Try to stay healthy and maintain a healthy sleep regimen: the course will be much more enjoyable and you will probably learn more.
<table>
<thead>
<tr>
<th>Date</th>
<th>Lecture topic</th>
<th>Assigned reading</th>
<th>Homework assignment</th>
</tr>
</thead>
<tbody>
<tr>
<td>8.27</td>
<td>Introduction, an overview of the financial system</td>
<td>Overview of the Financial System</td>
<td></td>
</tr>
<tr>
<td>9.3</td>
<td>The concept of money, measures of money, velocity and the money market</td>
<td>Money and the Money Market</td>
<td></td>
</tr>
<tr>
<td>9.10</td>
<td>Calculating interest, yield and return rates on non-monetary assets</td>
<td>Interest, Yield and Return and Non-Monetary Assets</td>
<td>Problems due from Money and the Money Market</td>
</tr>
<tr>
<td>9.17</td>
<td>Traditional borrowing, lending and depositing; assets, liabilities and capital</td>
<td>Traditional Role of Banks</td>
<td>Problems due from Interest, Yield and Return and Non-Monetary Assets</td>
</tr>
<tr>
<td>9.24</td>
<td>Forward and futures contracts, options and swap contracts</td>
<td>Innovative Banking Activities</td>
<td></td>
</tr>
<tr>
<td>10.1</td>
<td>Credit default swaps and securitization</td>
<td>Innovative Banking Activities</td>
<td>Problems due from Traditional Role of Banks</td>
</tr>
<tr>
<td>10.8</td>
<td>Midterm exam</td>
<td></td>
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<tr>
<td>10.15</td>
<td>Representations of uncertainty, liquidity risk, credit risk, market risk, capital risk</td>
<td>Risk Management</td>
<td></td>
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<tr>
<td>10.22</td>
<td>Insurance, derivative assets, diversification</td>
<td>Risk Management</td>
<td></td>
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<tr>
<td>10.29</td>
<td>Problems of asymmetric information, regulations intended to address problems of asymmetric information</td>
<td>Bank Regulation</td>
<td>Problems due from Risk Management</td>
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<tr>
<td>11.5</td>
<td>When bankruptcy occurs, causes of financial crises</td>
<td>Bank Regulation</td>
<td></td>
</tr>
<tr>
<td>11.12</td>
<td>Central bank functions, central bank balance sheet, central bank independence</td>
<td>Purpose and Role of Central Banks</td>
<td>Problems due from Bank Regulation</td>
</tr>
<tr>
<td>11.19</td>
<td>Creation of credit and money</td>
<td>Creation of Credit and Money</td>
<td>Problems due from Purpose and Role of Central Banks</td>
</tr>
<tr>
<td>11.26</td>
<td>Goals of monetary policy</td>
<td>Goals of Monetary Policy</td>
<td></td>
</tr>
<tr>
<td>12.3</td>
<td>Targets of monetary policy</td>
<td>Targets of Monetary Policy</td>
<td>Problems due from Goals of Monetary Policy</td>
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<tr>
<td>12.10</td>
<td>Final exam</td>
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