

**Econ 104-002**

**Principles of Macroeconomics**

**Spring 2017**

Tue and Thur: 10:30 – 11:50 AM  
Enterprise Hall 80

Instructor: James Caton

Office Hours: Tue and Thur 12:00 – 1:00 PM Mason Hall, Econ Dept.

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**Grading:**

Participation: 20%

Midterm 1: 15%

Midterm 2: 25%

Final: 40%

Final Exam: Tuesday 5/16, 10:30 AM - 1:10 PM

**Required Texts:**

Rustici, T., Caton, J., Shamoun, D., Shamoun, T. (2015) *Macroeconomics: Monetary Foundations of the Macroeconomy*. San Diego, CA: Cognella.

Rustici, T., Caton, J., Shamoun, D., Shamoun, T. (2015) *Macroeconomics: Past and Present*. San Diego, CA: Cognella.

**Course Prerequisites:**

Principles of Microeconomics (Econ 103) or equivalent:

**Grades Scored Between Grade**

97% and Higher	A+
93% and Less Than 97%	A
90% and Less Than 93%	A-
87% and Less Than 90%	B+
83% and Less Than 87%	B
80% and Less Than 83%	B-
77% and Less Than 80%	C+
73% and Less Than 77%	C
70% and Less Than 73%	C-
60% and Less Than 70%	D
Less Than 60%	F

**Exams:**

Students will complete two midterms and a final exam. These exams must be taken at the scheduled time. Exceptions may be made in the case of an emergency – for example, a medical emergency or death in the family – and will be dealt with on a case by case basis.

**Participation:**

Students are called upon at random. If a student called is unable to sufficiently answer a question or is not present, that student's participation grade will fall by 10%. If you will be absent you must make an arrangement with me. If you are unable to attend lecture due to illness, you can arrange to complete a substitute for attendance.

**Course Objective and Overview:**

This course is intended to aid each student in growing his or her knowledge and familiarity with the language and logic of economics and support a fundamental understanding of macroeconomics. Students will learn to employ tools that will help them to both understand monetary and macroeconomic issues in the news and history, as well as apply them to understand the likely outcomes of a variety of monetary and macroeconomic policies. During this course, students will be exposed to conflicting perspective. It is the student's job to evaluate and work through these conflicts both outside and inside of the classroom.

**Attendance**

It is expected that each student will attend class regularly. Part of the student grade will be dependent upon their regular contribution to discourse in the classroom.

**Communication**

Whenever necessary, I will email the class with announcements via blackboard. This requires that each student regularly check his or her Mason email account. It is the student's responsibility to activate the Mason email account and employ it in communicating with their department and university administration whenever necessary.

**Honor Code:**

Students are expected to understand and comply with George Mason University's Honor Code. Students may neither give nor receive help from other students or from sources not specifically condoned by the instructor during the exam. Students are obligated to report any violations observed.

**Students with Disabilities:**

If you are a student with a disability and you need academic accommodations, please see me and contact the [Office of Disability Services](http://ods.gmu.edu) at 703-993-2474 or <http://ods.gmu.edu>. All academic accommodations must be arranged through that office.

## **Week 1: Complexity and Auto-poetic Order**

**Tuesday 1/24:**

### **Human Perception, Action, and Interaction**

I Pencil

What Can a Pencil Teach Us about Economic Theory?:

<http://moneymarketsandmisperceptions.blogspot.com/2017/01/what-can-pencil-teach-us-about-economic.html>

I Pencil (video): <https://www.youtube.com/watch?v=IYO3tOqDISE>

**Breakout:** Using the information from the video, can you chart a network identifying the processes by which a pencil is created?

**Thursday 1/26**

### **Human Action**

“A First Analysis of the Category of Human Action” by Ludwig von Mises

“Economic Action: Subjectivity, Value, and the Price System”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/01/economic-action-subjectivity-value-and.html>

“A Theory of Social Economy I: What is Theory?:

<http://moneymarketsandmisperceptions.blogspot.com/2017/01/a-theory-of-social-economy-i-what-is.html>

**Breakout:** What does your theory of your world look like? Create a list of the objects and persons that are significant to your life. Include attributes of these features. Once you feel that your list is complete, use it explain aspects of your life that you enjoy or think are important with your neighbor.

## **Week 2: The Objects of Economic Analysis (I)**

**Tuesday 1/31:**

### **Economic Goods and Scarcity**

“The General Theory of the Good” in *Principles of Economics*, by Carl Menger

[http://mises.org/sites/default/files/Principles%20of%20Economics\\_5.pdf](http://mises.org/sites/default/files/Principles%20of%20Economics_5.pdf)

“A Theory of Social Economy II: Reformulating a Framework for Economic Analysis”:

<http://moneymarketsandmisperceptions.blogspot.com/2017/01/a-theory-of-social-economy-ii.html>

**Breakout:**

Last class you constructed an outline of the objects and persons significant to your life. Can use some of the terms that we have learned to inform the story that you told your neighbor last week?

### **Thursday 2/2:**

#### **Prices and Information**

“The Use of Knowledge in Society” by F. A. Hayek

“Prices, Information, and Coordination of Disparate Agents”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/01/prices-information-and-coordination-of.html>

**Breakout:** Describe a time in your life that the price of a good you like fell or increased unexpectedly. Why do you think the price of the good changed? How did you respond to this price change?

### **Week 3: The Objects of Economic Analysis (II)**

#### **Tuesday 2/7:**

##### **The Entrepreneur and the Economy**

“The Entrepreneur” by Gustav Cassel

“Competition as a Discovery Procedure” by F. A. Hayek:

[https://mises.org/sites/default/files/qjae5\\_3\\_3.pdf](https://mises.org/sites/default/files/qjae5_3_3.pdf)

“The Role of the Entrepreneur: Coordination and Innovation”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/02/the-role-of-entrepreneur-coordination.html>

**Breakout:** Have you ever had to compete for a scarce resource? How did your willingness to compete reflect your valuation of that resource? How did uncertainty of the result of your action affect your willingness to pursue the resource? Were you more or less emboldened?

#### **Thursday 2/9:**

##### **Entrepreneur**

“Uncertainty, Evolution, and Economic Theory” by Armen Alchian:

<http://institutoamagi.org/download/Alchain-Armen-Uncertainty-Evolution-and-Economic-Theory.pdf>

“Types of Entrepreneurial Action and Overcoming Difficulty: Trade Facilitation, Innovation, and Political Entrepreneurship”: <http://moneymarketsandmisperceptions.blogspot.com/2015/02/types-of-entrepreneurial-action-and.html>

**Breakout:** Have you ever had to organize other people for a project or a gathering? What were some challenges that arose in the course of organization? Were their benefits that you received because you were the one organizing the activity?

## **Week 4: Organizing Society**

### **Tuesday 2/14: Cooperation, Comparative Advantage, and the Law of Association**

“Comparative Advantage”: <http://www.econlib.org/library/Topics/Details/comparativeadvantage.html>

“Action Within the Framework of Society” in *Human Action* by Ludwig von Mises: [http://lf-oll.s3.amazonaws.com/titles/1893/3843.01\\_LFeBk.pdf](http://lf-oll.s3.amazonaws.com/titles/1893/3843.01_LFeBk.pdf): 157-166.

#### **Breakout:**

What is the division of labor? Why would someone choose to specialize in a particular activity? Why does Mises refer to this insight from Ricardo as the Law of Association? Have you ever worked on a team or a company where you were able to specialize in a task? If so, how did it help? If not, do you think specialization would have helped your goal?

### **Thursday 2/16:**

#### **Out From Anarchy:**

“Constitutional Contract: The Theory of Law” in *Between Anarchy and Leviathan* by James Buchanan [http://lf-oll.s3.amazonaws.com/titles/1827/0102-07\\_LFeBk.pdf](http://lf-oll.s3.amazonaws.com/titles/1827/0102-07_LFeBk.pdf): 69-95

“So Close and Yet So Different: The Economics of the Rio Grande” by Daron Acemoglu and James A. Robinson

#### **Breakout:**

Have you ever had any experience with bullying in school? How did you resolve this conflict? Did you appeal to an authority? What did you do if you were unable to appeal to an authority? Were able to establish common understanding with the bully? Did friends get involved to help you? How can does this situation inform our understanding of anarchy?

## **Week 5: Money**

### **Tuesday 2/21:**

#### **The Origins and Evolution of Money**

“The Island of Stone Money” by Milton Friedman

“The Theory of Money” by Carl Menger\*

#### **Breakout:**

Do you find Carl Menger’s theory of the evolution of money believable? Which part seemed the most surprising to you? If not, which parts do you disagree with? Is there anything that you would add or take away from the story?

### **Thursday 2/23:**

#### **Money and the State**

“An Evolutionary Theory of the State Monopoly over Money” by David Glasner\*

**Breakout:**

Is the state required for creation and use of money? Why does the state desire to establish a monopoly over money? What might money look like in a world without this intervention?

**Week 6: The Equation of Exchange**

**Tuesday 2/28:**

\*\*\*\*\* Midterm 1 \*\*\*\*\*

**Thursday 3/2:**

**The Equation of Exchange (or The Quantity Theory of Money)**

“The Quantity Theory: Its Versions and Variables” by Thomas Rustici

“The Determinates of the Objective Exchange-Value, or Purchasing Power, of Money” by Ludwig Von Mises

“The Equation of Exchange, Its Versions, and Its Elements”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/02/the-equation-of-exchange-its-versions.html>

**Breakout:**

Rearrange the equation of exchange to figure out what is the relationship between prices and each of the other 3 variables. What is the relationship between the quantity of money in circulation and each of the other variables? How would you explain these relationships in terms of causality?

**Week 7: Aggregate Demand and Supply**

**Tuesday 3/7:**

**Money and Inflation**

“Fiat Money in France” by Andrew White

“Cross Country Data on Inflation and Monetary Growth” by Robert Barro

“Intuitive Sums: Making the Equation of Exchange Easy to Interpret”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/02/intuitive-sums-making-equation-of.html>

**Aggregate Demand and Aggregate Supply**

“Appendix 3: Price Level, National Income Accounting, and Aggregate Supply and Aggregate Demand”

“Dynamics of Aggregate Demand”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/02/dynamics-of-aggregate-demand-and-prices.html>

**Breakout 1:**

Have prices, on average, changed since you were a child? If you believe they have changed, how have they changed? What do you believe is the cause of this change?

**Breakout 2:**

Explain to your neighbor what aggregate demand is and its relationship to the equation of exchange. What happens to aggregate demand if the supply of money increases? If the velocity of money increases? In the long run, do changes in the left hand side variables have any effect on the right hand side variables?

**Thursday 3/9:**

**Short-run Aggregate Supply**

“The Money Illusion” by Irving Fisher

Short-run Aggregate Supply: <https://www.youtube.com/watch?v=3nbalsyibKU>

“Upward-Sloping Short-run Aggregate Supply”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/02/upward-sloping-short-run-aggregate.html>

**Breakout:**

What is the “money illusion”? How does it relate to the equation of exchange? What effects might the “money illusion” have on our interpretation of the equation of exchange? Use the concept of the long and short run to explain. In your own life, have you ever observed anything like Fisher describes?

**Week 8: Say’s Identity**

**Tuesday 3/21:**

**Say’s Identity**

“Classical Economics Reconsidered” by Thomas Sowell

“Of the Demand or Market for Products” by Jean Baptiste Say

“Say’s Principle: What it Means and Doesn’t” by Axel Leijonhufvud and Robert Clower

Say’s Principle and Macroeconomic Analysis:

<http://moneymarketsandmisperceptions.blogspot.com/2015/03/says-principle-and-macroeconomic.html>

**Breakout 1:**

What do we mean in Say's Identity by planned expenditures? How does the plan relate to income? Do plans to spend money that you don't have matter in respect to market activity? Do they have any significance at all?

#### **Breakout 2:**

How does Say's Identity inform your understanding of economics. What economic concepts does Say's Identity connect together? How can you use it to tell a story about economic activity? How does Say's Identity help us to justify and explain the relationship between aggregate demand curve and equation of exchange.

#### **Thursday 3/23:**

##### **Savings and the Interest Rate**

"Interest" by Ludwig von Mises

Interest Rates in Austrian Theory: <https://www.youtube.com/watch?v=17MJzNUj-gY>

"The Nature and Role of the Interest Rate":

<http://moneymarketsandmisperceptions.blogspot.com/2015/03/the-nature-and-role-of-interest-rates.html>

#### **Breakout:**

Have you ever saved money at a bank? Have you ever considered where that money goes once you deposit it? If the bank paid you a higher interest rate, would you be willing to save more?

#### **Week 9: Banking**

##### **Tuesday 3/28:**

##### **Banking**

"The Theory of Banking" by Ralph Hawtrey

"Paper Money and the Quantity Theory" by Ralph Hawtrey

Money Supply – M0, M1, and M2: <https://www.youtube.com/watch?v=LPh72gx6GE>

"Money and Credit: Origins, Instruments, and Dynamics":

<http://moneymarketsandmisperceptions.blogspot.com/>

#### **Breakout 1:**

When you save money at a bank, how quickly can you access it? Does this change depending on the type of account you have? How quickly can you access money that you have invested in stocks or bonds? When you access that money, what is happening to your ownership of these assets?

#### **Breakout 2:**

How do you define money? Do you think of your atm card as being the equivalent of money? Checks? Other investments? What criteria would you use for deciding whether or not something qualifies as money? How do you decide whether to hold your money as cash, in a bank account, or in an investment?

#### **Thursday 3/30:**

##### **Alternative Monetary Arrangements: Theory and History**

“The Central Bank Role of Clearing Houses” by Richard Timberlake

“The Evolution of a Freebanking System” by Lawrence H. White and George Selgin

What is Free Banking and Why Should I Care?: <https://www.youtube.com/watch?v=IVK-kgSQMPs>

“The Emergence of the Clearinghouse”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/04/the-emergence-of-clearinghouse.html>

##### **Breakout:**

You have been assigned to teach a ten-year old about money and banking. How would you describe the following concepts to the child:

- Money
- Credit
- Banking
- Clearinghouse

#### **Week 10: Banking and Trade Fluctuations**

##### **Tuesday 4/4:**

##### **Monetary Policy**

“Appendix 2: Central Banking and Money Creation”

“Monetary Policy” by James Tobin:

<http://www.econlib.org/library/Enc/MonetaryPolicy.html>

“Monopoly Money and Inflation” by Geoffrey Brennan and James Buchanan

“Central Banking: The Basics”: <http://moneymarketsandmisperceptions.blogspot.com/2015/03/central-banking-basics.html>

##### **Breakout:**

What part of the money stock does the Federal Reserve directly control? Which part does it not directly control? If you were the chairman at the Federal Reserve, how would you approach setting policy? How would the theory that you have learned help inform your decisions? What are some complications that might arise that our theory will be unable to help us with?

##### **Thursday 4/6:**

## **Business Cycle Theories**

“Business Cycle Theory” by Thomas Cate, et al.

“The Trade Cycle” by Ralph G. Hawtrey

“The Fundamental Causes of Business Fluctuations” by F. A. Hayek

Business Cycles Explained: Austrian Theory: [https://www.youtube.com/watch?v=Log\\_dcRj7HI](https://www.youtube.com/watch?v=Log_dcRj7HI)

“How The Credit Cycle Forms the Basis of the Business Cycle”:

<http://moneymarketsandmisperceptions.blogspot.com/2015/04/how-credit-cycle-forms-basis-of.html>

### **Breakout:**

The market is in crisis as a massive wave of defaults on government treasuries around the world, including in the U.S., have led to the tightening of credit markets. Officials at the Federal Reserve must choose whether to facilitate lending in these markets so as to avert total collapse. However, they face the problem that if they facilitate, the investors will expect higher inflation and demand even higher interest rates on government bonds. What policies should the Federal Reserve and the Treasury adopt? What are some possible outcomes from such a scenario? Think about expectations in your response.

## **Week 11: Modern Business Cycle Theory**

**Tuesday 4/11:**

### **Modern Business Cycle Theories**

“Business Cycle Theory” by David W. Findlay

“A Cash Balance Interpretation of Depression” by Leland Yeager

Business Cycles Explained: Monetarist Theory: <https://www.youtube.com/watch?v=SgweT-7i1hU>

### **Breakout:**

Why are there so many theories of the business cycle? Do they all seem to fit together? Which is most appealing? Which is least? Why?

**Thursday 4/13:**

\*\*\*\*\*Midterm 2\*\*\*\*\*

## **Week 12: History of the Gold Standard**

**Tuesday 4/18:**

### **World War I and the Roaring Twenties**

“The Yellow Brick Road to Ruin” by James Caton

“The Post World War I Monetary and Trade Setting” by Thomas Rustici

History of Economic Booms and Busts: <https://www.youtube.com/watch?v=83sX8Ent4vo>

“Mises Unwitting Affirmation of the Hawtrey-Cassel Explanation of the Great Depression”:  
<http://uneasymoney.com/2015/07/03/misess-unwitting-affirmation-of-the-hawtrey-cassel-explanation-of-the-great-depression/>

#### **Breakout:**

What is *the* gold standard?

#### **Thursday 4/20:**

##### **The Great Depression**

“Herbert Hoover: Father of the New Deal” by Steven Horwitz

“Rethinking the Great Depression” by Gene Smiley

“Fear the Boom and Bust”: <https://www.youtube.com/watch?v=d0nERTFo-Sk>

“Keynes vs. Hawtrey (Final Round): Gold Demand and Gold Prices”:  
<http://moneymarketsandmisperceptions.blogspot.com/2014/02/keynes-vs-hawtrey-final-round-gold.html>

#### **Breakout:**

Imagine that you are a business owner in the Great Depression. When you see that the market has crashed in October, how does this affect your plans for the future? Do you think you would understand why the depression was occurring? Would you expect that it would last for four years? Why?

### **Week 13: The New Deal and Keynesian Economics**

#### **Tuesday 4/25:**

##### **The New Deal**

“New Deal Policies and the Persistence of the Great Depression” by Harold L. Cole and Lee E. Ohanian

“Fight of the Century: Keynes vs Hayek, Round 2”: <https://www.youtube.com/watch?v=GTQnarzmTOc>

##### **Keynes**

“The General Theory of Employment, Interest and Money” by John Maynard Keynes

“Keynes’ Not-So-General Theory” by James Caton

Business Cycles Explained: Keynesian Theory: [https://www.youtube.com/watch?v=g\\_647R\\_vUVc](https://www.youtube.com/watch?v=g_647R_vUVc)

#### **Thursday 4/27:**

##### **Rational Expectations and Efficient Markets**

“The Role of Monetary Policy” by Milton Friedman

“Rational Expectations” by Thomas Sargent

“A Random Walk Down Wall Street” by Burton Malkiel

“Eugene F. Fama, Efficient Markets, and the Nobel Prize” by John H. Cochrane

**Breakout:**

How does rational expectations posit that agents form expectations? Does this seem realistic? In what ways do you think rational expectations is correct? Relate this to the challenge of an investor “beating the market”.

**Week 14 Past and Future**

**Tuesday 5/2:**

“The Unacknowledged Success of Neoliberalism” by Scott Sumner

“The Pretence of Knowledge” By F. A. Hayek

**Breakout:**

Why do markets make efficient use of resources? How do regulations and taxes (tariffs) affect this efficiency? How do these interventions affect the ability of entrepreneurs to act in light of their contextual knowledge?

**Thursday 5/4:**

Review