Introduction and Economic Landscape

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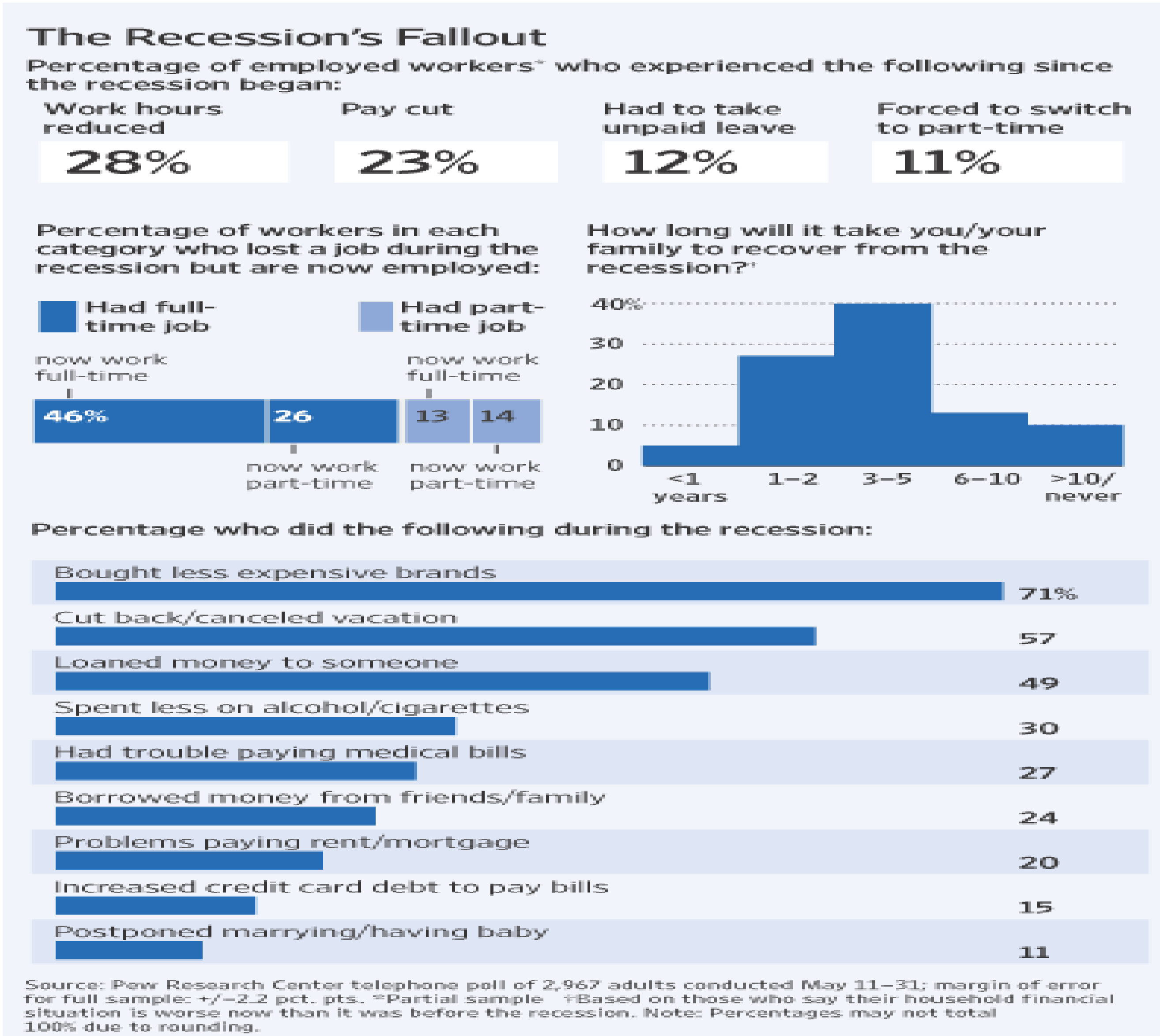
Spring 2013

Introduction

- CV
  - (underlined words typically are links or videos)
- Syllabus
- We will use Blackboard, which is where you will find the syllabus, important information, quizzes, and all of your grades posted. You will need to check this site **regularly** for class emails and updates.
- You will find my website (www.vanceginn.weebly.com) helpful throughout this course.

Why Should We Study Economics?



Macro vs. Micro

- Economics – the study of using ____________________ efficiently and effectively

- Macro- studies the economy as a __________: business cycles (recessions, trough, expansion, peak), inflation, unemployment, fiscal and monetary policy (Used to understand the news, Self-interest, civic responsibility for voting)

- Micro- studies individual and firm behavior (utility, production maximization, marginal costs and marginal benefits, budget constraints, etc)

Macro Economic Landscape

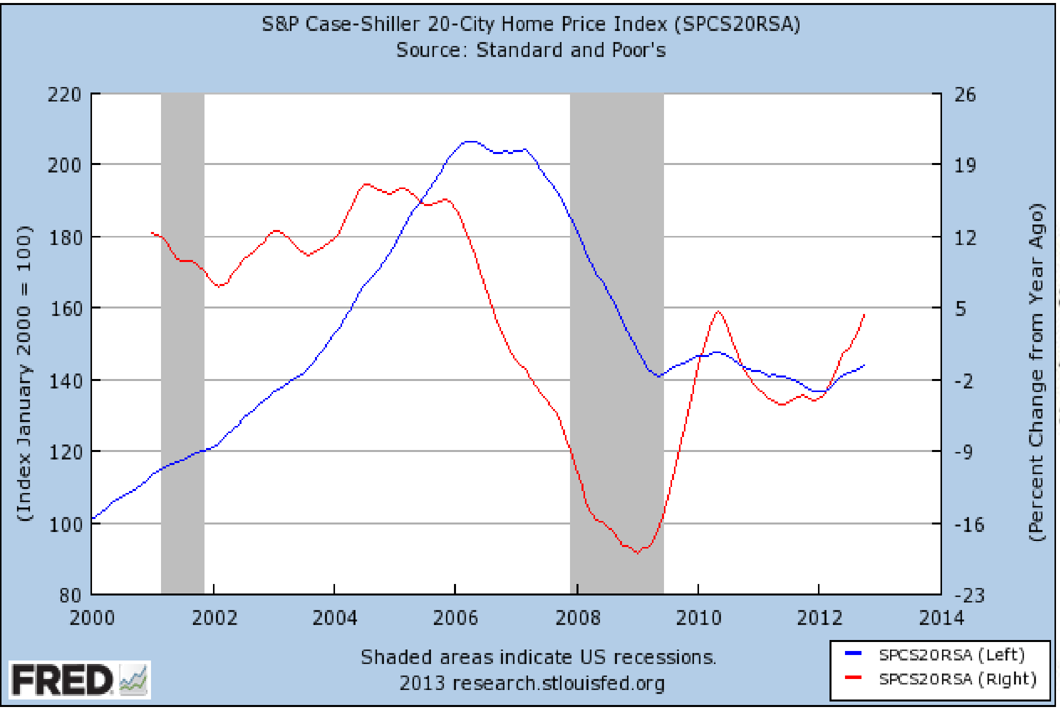
- Economic expansion occurred from 1991-2001
  - Dot com bubble –read-collapsed in 2000 after IT boom

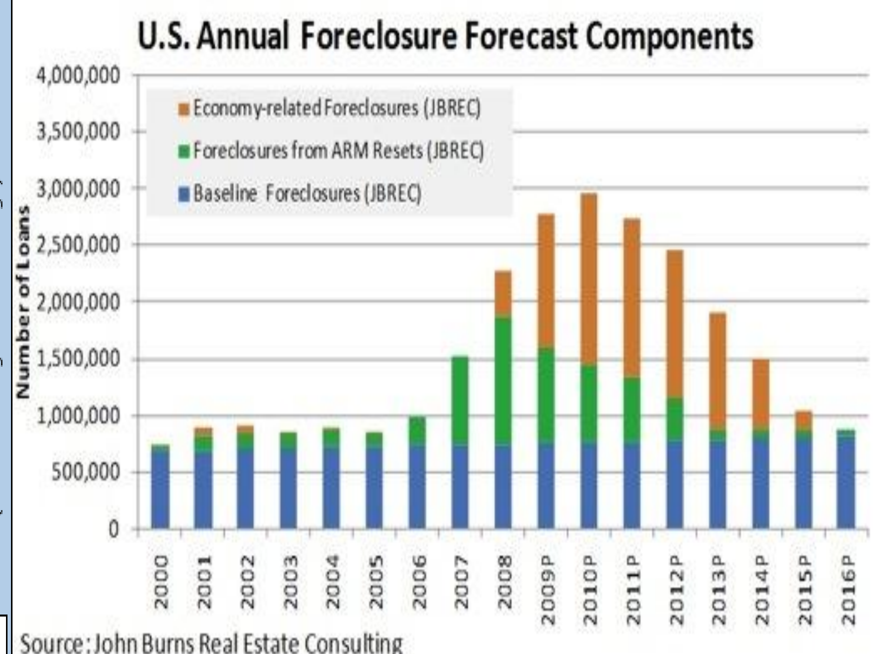
- Recession from March 2001-November 2001
  - _______________ with UR topping out at 6.5%
  - President Bush implemented $1.4 trillion in tax cuts and other stimulus measures to expand the economy in 2001, and these tax cuts were fully implemented in 2003 (all 6 marginal tax rates were reduced)
  - The highest tax bracket was lowered from 39.6% to 35% and the lowest tax bracket was reduced from 15% to 10%, where all of these were extended through 2012 in Dec '10.

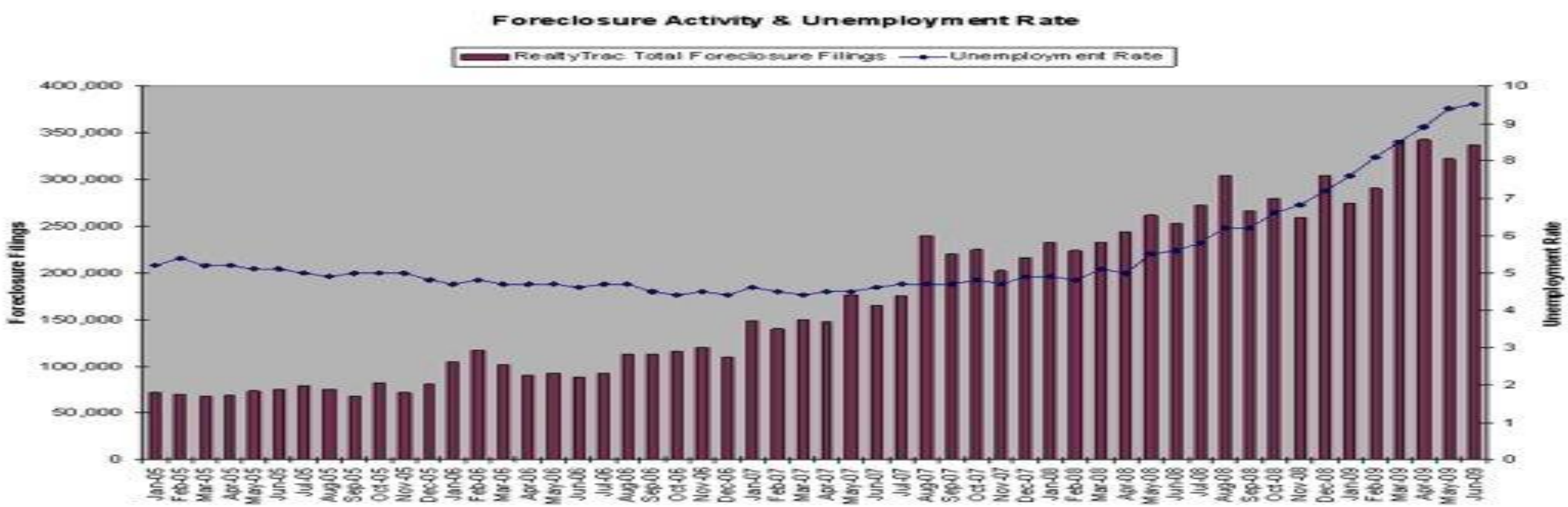
- Economic expansion occurred from November 2001-December 2007

- Recession from **_____________________ (Great Recession- graphs)**
  - Severe recession: UR increased to a high of 10% in October 2009

Causes of the 2007-09 Recession







Causes of 07-09 Recession: 1.Housing Market

- The following are a few reasons for what contributed to the housing market boom and bust (“bubble”) (video):

a. ________________: Low federal funds rate (rate that banks borrow and lend at overnight)of 1% by Federal Reserve (central bank) from 2003-04 led to historical lows for interest rates on mortgage loans.

b. Affordable Housing: the change in 1993 to the Community Reinvestment Act (CRA) of 1977 that mandated that close to half of all mortgages made by Fannie Mae and Freddie Mac (Government Sponsored Enterprises (GSE)) must be to low and moderate income individuals (subprime lending).

c. Ownership Society: the movement that everyone should own their own home that was pushed by President Clinton and President Bush. The American Dream?

1. Housing Market Cont.

d. Excessive risk taking: Implicit backing from the government of the loans that banks made from the CRA; whereby, the government implicitly, then explicitly, backed FM and FM to purchase loans from commercial banks (around 6,000). This process reduced marginal costs to banks to lend and increased risk taking beyond the market processes (moral hazard).

- From ‘03-’07 the average increase in home prices was around 12% per year with 3-5% being the “normal” average over the past 100 years; leading to the ________________________________. (Reversion to mean)

- The housing bubble eventually burst. The national house price index remains down about 30% from where it was in 2006.

- Key indicators for the housing market: housing starts, Case-Shiller Index for housing prices, demand for mortgage loans, LIBOR rates and 10 year note yield (interest rate)

2. Credit Market Freeze

a. Credit began drying up in 2007 from default on debts related to mortgages and this caused significant write downs and losses by banks.

b. Many banks slowed lending to one another and very little lending to the public took place. There are two explanations for this:

1. ________________________– readily convertible asset into money disappeared
2. ________________________– one party's concern for another party's reliability

-*Getting Off Track* by John Taylor

c. In Sept 2007, the Federal Reserve started lowering the Fed funds rate (lending rate between commercial banks) from 5.25% to today's range of 0-.25%.

- Stock market high during the economic expansion from Nov. 2001-Dec. 2007 was on 10/9/07, where the Dow reached 14,164 and the S&P 500 was at 1,565.

3. Bank Failures

a. On 9/14/08 the Fed lent $35 b to JP Morgan to purchase _________________ due to "systemic risk" (precedence, moral hazard)

b. In Sept. 2008, the Fed and Treasury brought private sector banks together to work out a deal for ___________________________; but none would budge due to the bad assets on LB balance sheets. *LB filed for bankruptcy.*

c. In Sept. 2008, the Fed lent $85 billion to AIG (largest US insurance company), government then had 80% stake in AIG and still has a significant share of the company.

d. In September 2008, the Treasury nationalized Fannie Mae and Freddie Mac (GSEs) into what is called a conservatorship. (Effectively the government took them over)

3. Bank Failures Cont.

f. In Sept. 2008, ______________________________ became bank holding companies, which allowed them to be able to get credit from the Fed and take deposits.

g. In Sept. 2008, Bank of America purchased ____________________.

h. On Sept. 2008, JP Morgan purchased Washington Mutual.

i. In Sept. 2008, Wells Fargo purchased Wachovia.

j. Therefore, the five major investment banks no longer exist as investment banks.

k. 25 commercial banks failed in 2008, 140 banks failed in 2009, 157 in 2010, 92 in 2011, 51 in 2012 = Total of 365

>4,000 banks are estimated to have failed in 1933

In Fed We Trust by David Wessel

Government Policies

a. Fiscal Policy (FP): Economic Stimulus Act of 2008 (Bush Administration) (2/08):

>A $152 billion tax rebate, where taxpayers could get a $300 check.

- Deemed to be not very effective as the extra income increased savings and not consumption.

b. FP: Troubled Asset Relief Program (TARP) (Bush Administration): In 10/08, the amount of $700 billion was allocated to inject capital in financial markets by the Treasury buying preferred shares of commercial banks.

-The Bush Administration was allocated $350 billion and the Obama Administration $350 billion.

-690 banks received funds

-TARP was also used to fund auto bailouts and for home mortgage restructuring

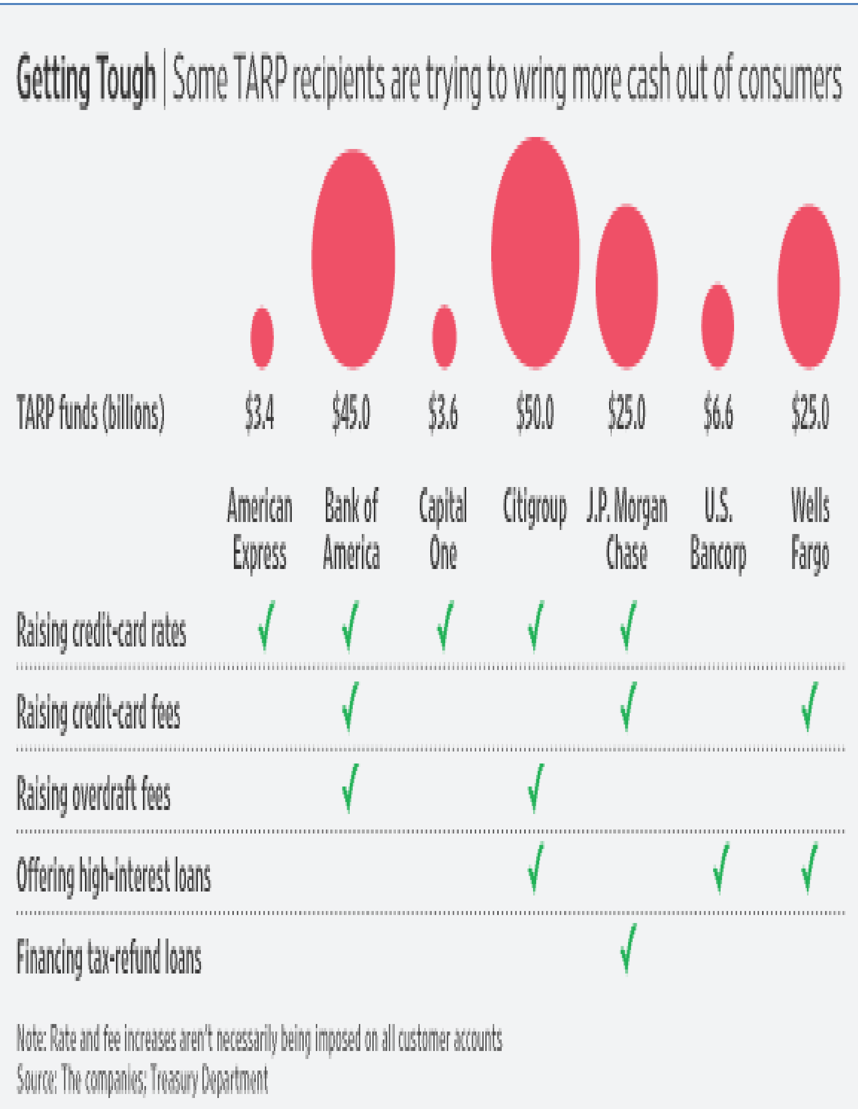
--OCCUPY WALL STREET-video

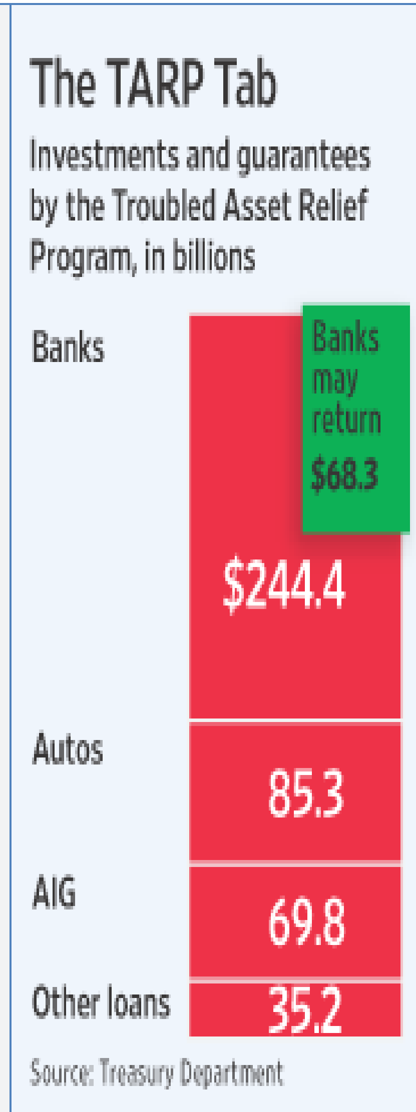
c. Monetary Policy (MP): In 12/08 the Fed lowered the Fed funds rate to where it is today to a range of 0-.25% to increase liquidity and stimulate economy.

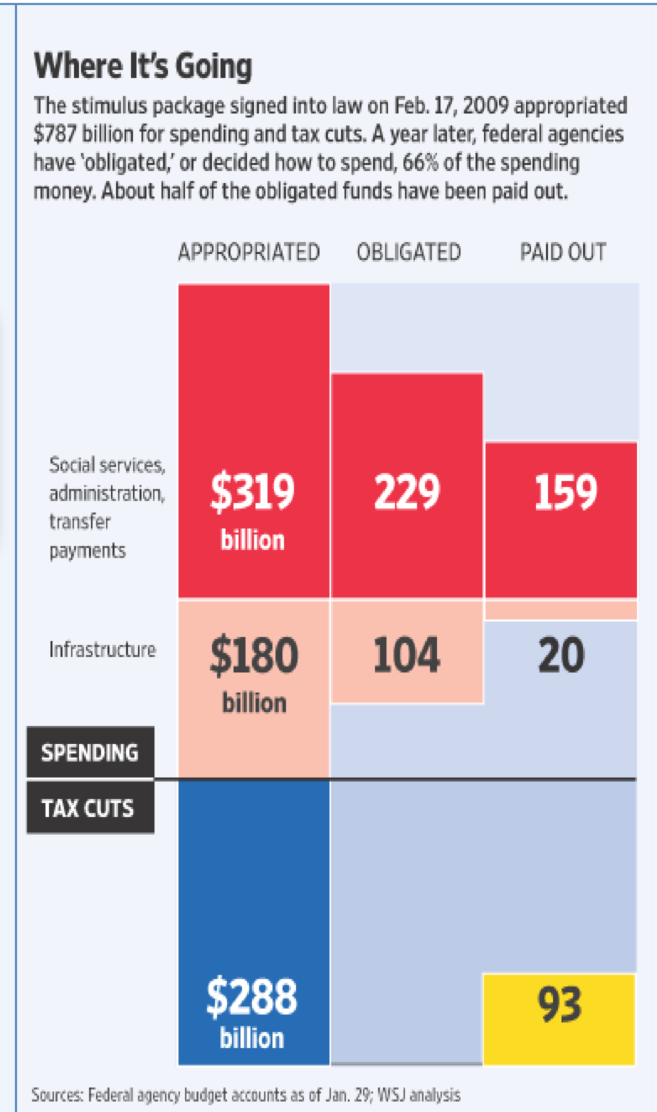
d. FP: American Recovery and Reinvestment Act –read-(ARRA) (Obama Administration) (2/09): A $787 billion stimulus program that was estimated to add $787 billion to the national debt over the next ten years.

-Other funds have been added to increase the amount to $831 billion since it was passed

TARP and ARRA Data







Gov't Policies Cont.

f. MP: On 3/18/09, the Fed implemented **Quantitative Easing (QE1),** which includes Long Term Securities Purchases ($300b), Agency debt ($200b), and Mortgage Backed Securities ($1.25 tr)

g. FP: Two other programs during 2009: Cash for Clunkers ($4 b) and $8,000 tax credit for first time home buyers

h. FP: Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (Tax Relief and Job Creation Act of 2010) (Obama Administration) (12/10):

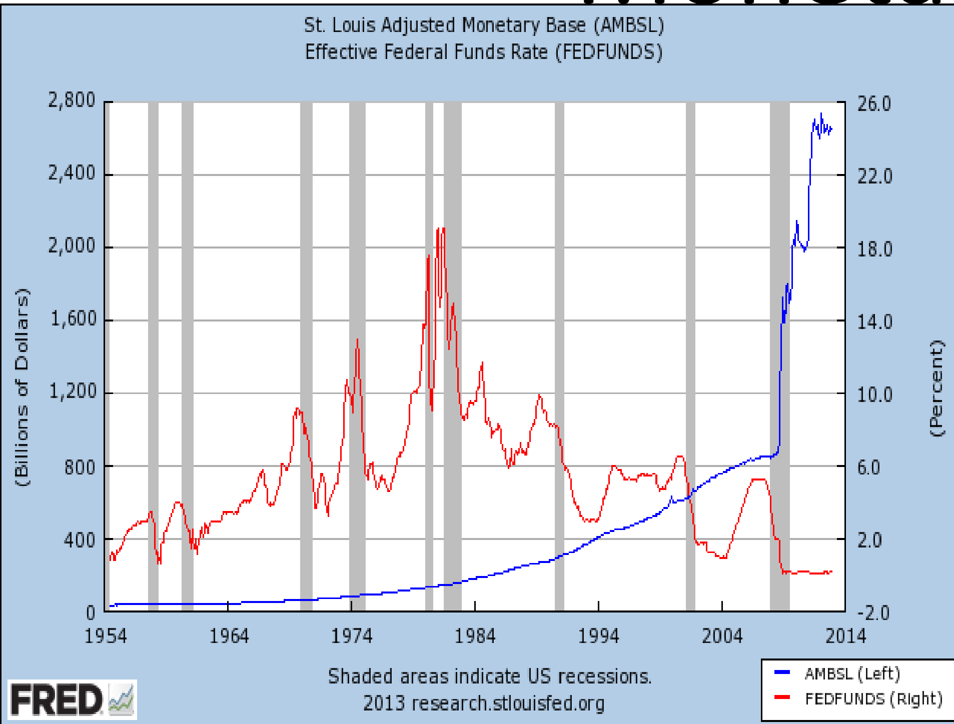
-$858 billion bill that will add this amount to the national debt by 2020.

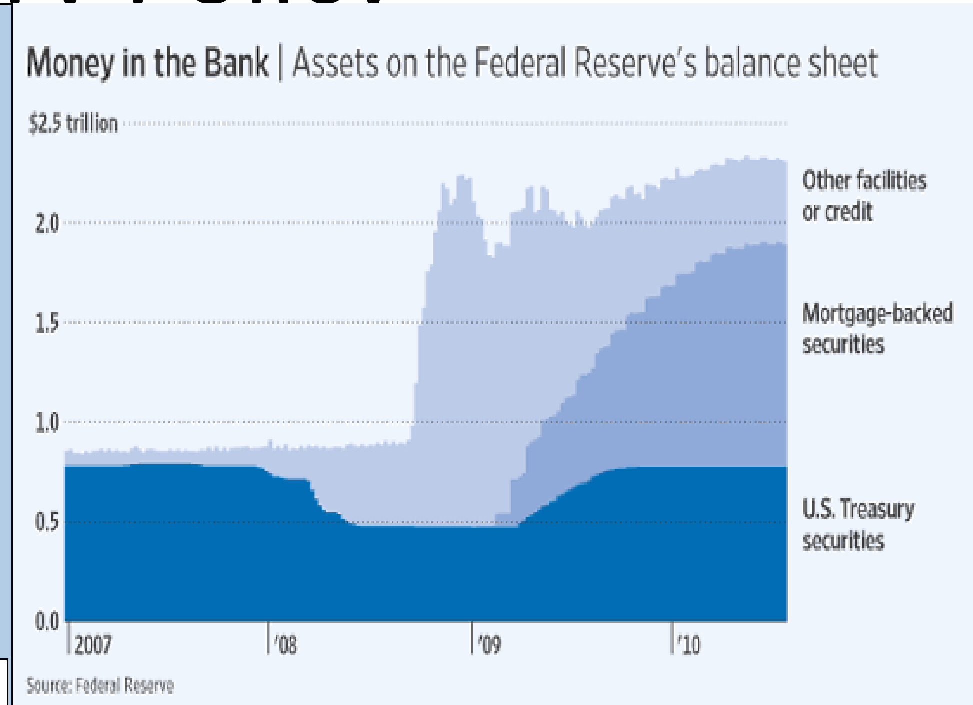
-Main components include: Extend Bush Tax Cuts, 2% payroll tax cut, extends UI for 13 months (then 99 weeks), and 100% write-offs of new investments by firms in 2010

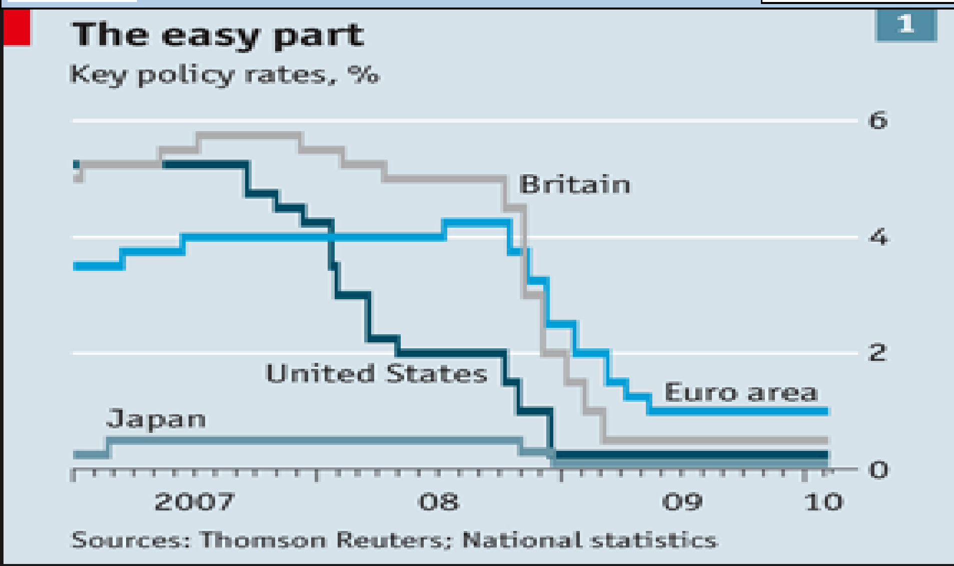
i. MP: On 11/3/2010 the Federal Reserve (graph) implemented QE2, where they announced that they will purchase an additional $600 b in Long Term Treasury Securities and another $300 from maturing MBSs—WHY NOT PRINT MORE MONEY??-video (QE 3 & QE 4 after)

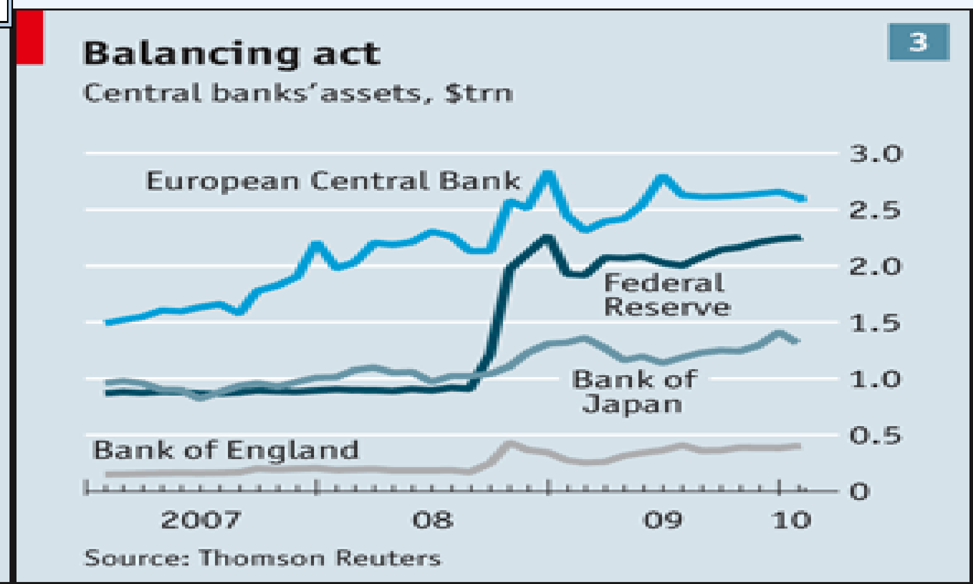
- 3/9/09: Dow low was 6,547 (down 55%) and S&P low was 676 (down 57%)

Monetary Policy









Data

a. UR:

Dec 07: 4.9%, May 09: 9.4%, Aug 09: 9.7%; Oct. 2009: 10.1% (highest in recession), July 2010: 9.5% ; **Dec 2012: _______**

b. GDP –read-growth:

2007: 1.9%; 2008: -0.3%; 2009: -3.1%; 2010: 2.4%; 2011: 1.8%

2012: [1st Q: 2%; 2nd Q: 1.3%; 3rd Q: 3.1%]

GDP growth was **-4.7%** during the 07-09 recession.

>From 1929-32, GDP growth was -27%; broken down into quarters, that is -1.7% per Q. If we were on same pace to match the -27% through 10 quarters, GDP would have "grown" -17%.

c. Federal Budget Deficits:

- $1.4 tr (10% of GDP) in fiscal year 2009.
- $1.3 tr (8.9% of GDP) in fiscal year 2010.
- $1.3 tr (8.7% of GDP) in fiscal year 2011.
- $1.1 trillion (7% of GDP) in fiscal year 2012.

-Total of $5.1 trillion increase in government debt to $16.3 trillion. Expected to increase by $7 tr. over the next 10 years.

Data Cont.

d. Jan 2013 Jobs Report for Dec. 2012:

1. Net number of jobs created was ____________.

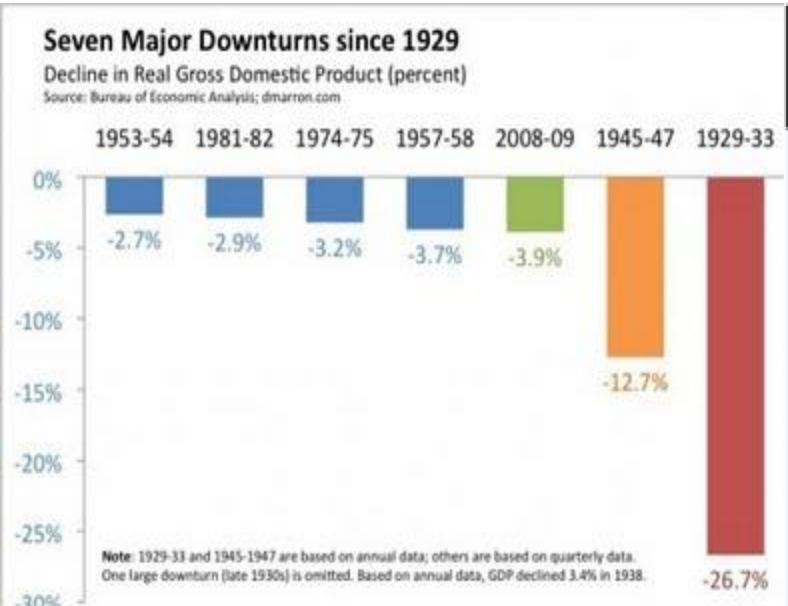
2. The unemployment rate is ___________

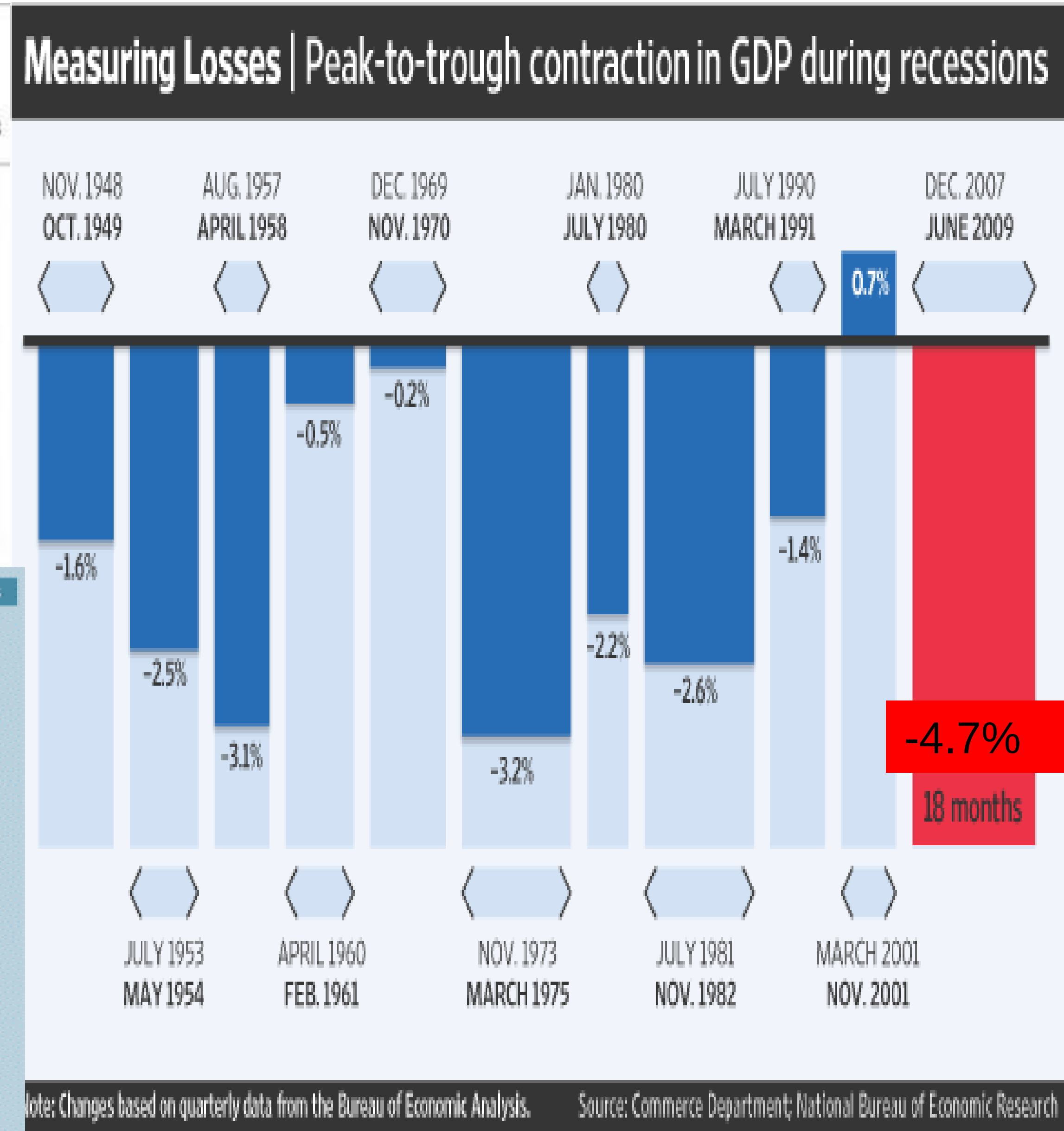
3. Average hourly earnings increased by 2.1% over the last year, which helps labor costs for businesses to stay low and provides a real earnings increase of .3%.

-12.2 million people are unemployed.

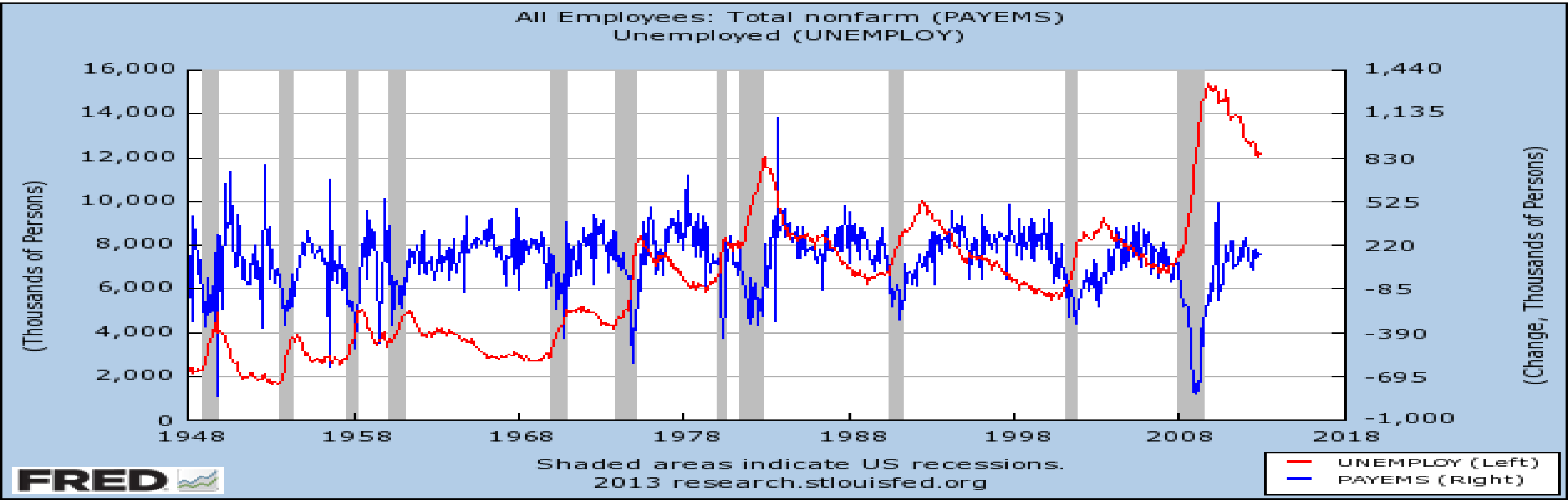
-If you include all of those who are looking and do not have a job (unemployed) and those not looking (discouraged workers) for a job, the U-6 rate (U6)14.4%. >Employment-to-pop ratio is 58.6%.

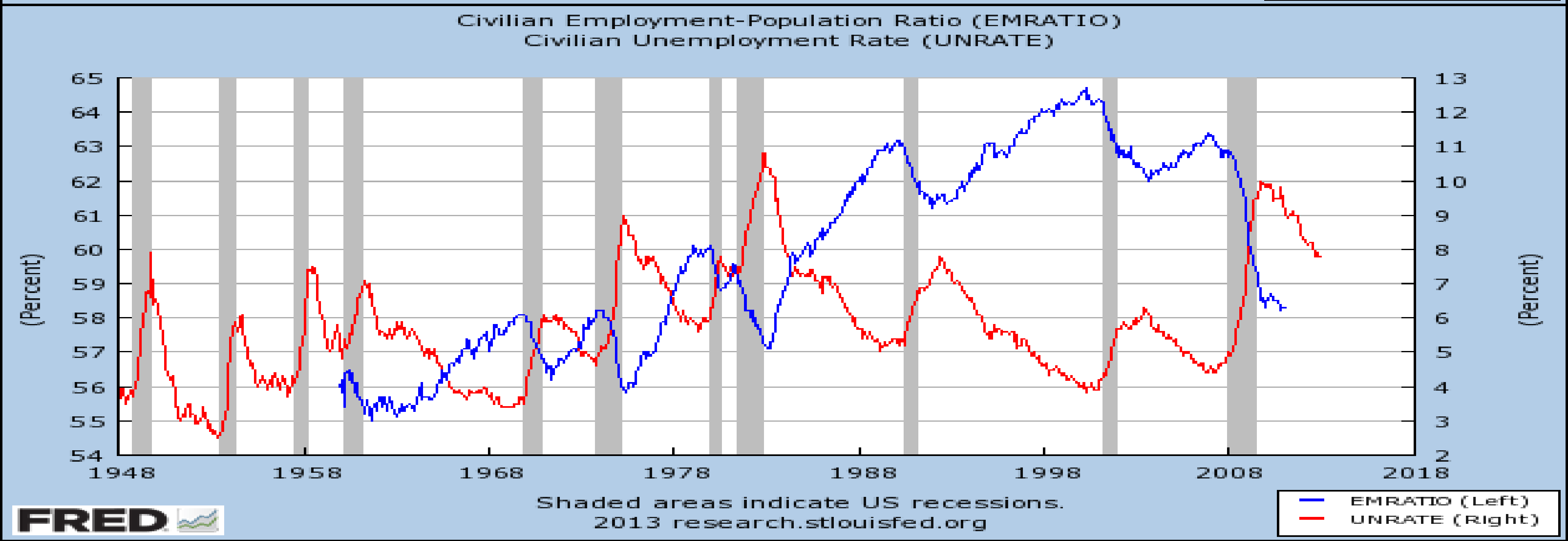
Comparing Recessions



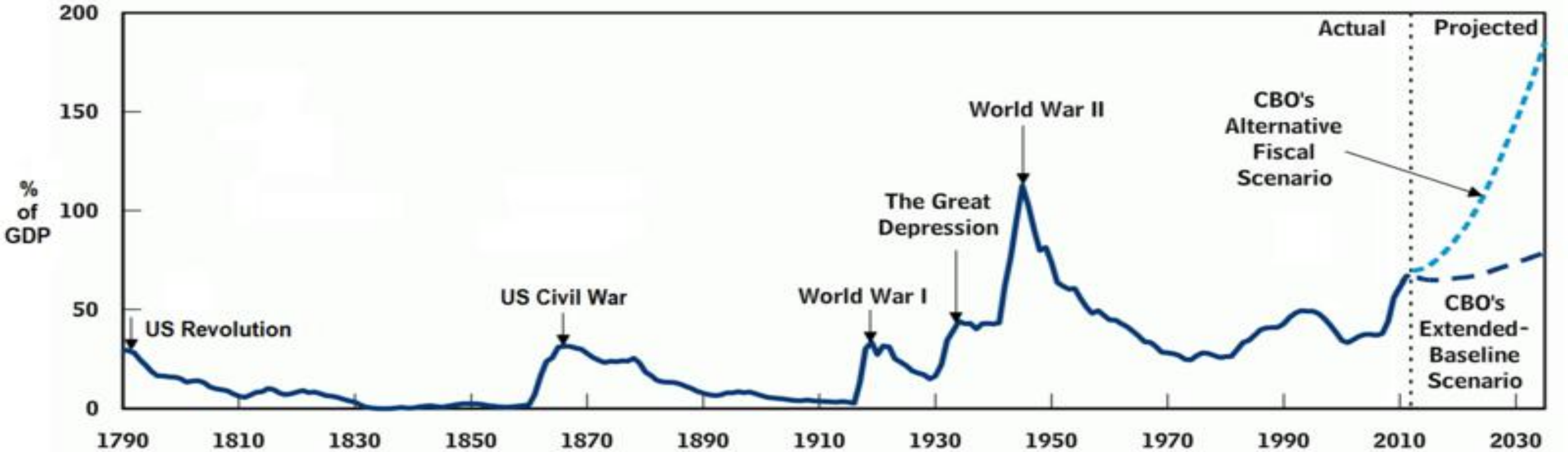


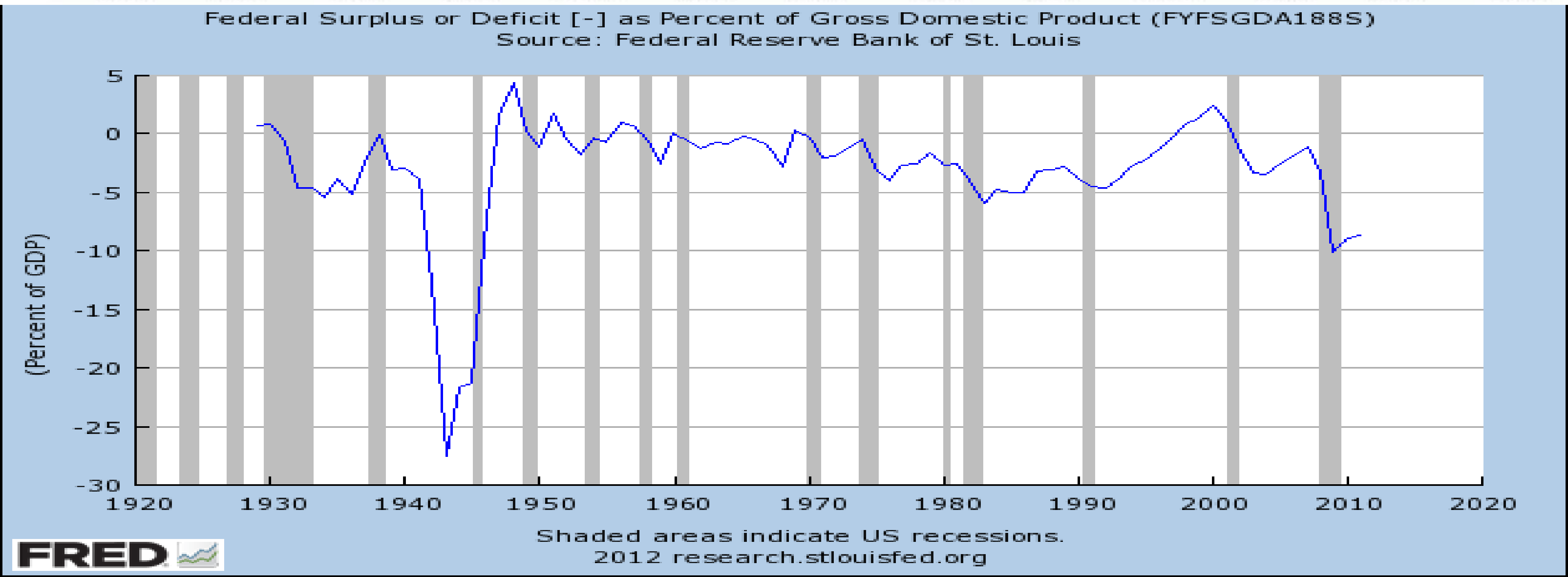
Labor Market Data





Gov't Debt & Deficits as a % of GDP





Policies Working? CUT SPENDING?- Read & Video