

Applied International Economics – an analysis of current issues

International macroeconomics ten years after the great recession – a bubble of historic proportions or an astute exercise in financial repression?

This series of seminars focuses on an analysis of recent developments in the global economy. By its nature, the topics for consideration and the accompanying readings are decided on a real-time basis. Perhaps this is best illustrated by a look at this month's focus of the seminar.

The major new development was the abrupt financial market drop, especially equities in the US, at the very beginning of February. The tentative moves towards monetary policy normalization have revived long-standing concerns about asset valuations. Market commentary has increasingly focused on the degree of asset price inflation that unconventional monetary policies may have instilled in different asset classes. Stock market valuations have come under particularly close scrutiny. At the root of these uncertainties are questions about how the compression of term premia in major sovereign bond markets may affect other asset valuations. There is also significant uncertainty about the levels those yields will reach once monetary policies are normalized in the core jurisdictions.

So the seminar has been analyzing the possible resurgence of inflationary pressures, the sudden concerns with fiscal policy imbalances in the US, the repricing of debt and debt sustainability. Students need to demonstrate that they understand how to apply their education in economic theory to these actual developments. Specific country and sector cases are followed as well as the most recent material from the IMF and the BIS.

Purpose and summary

This mini-course presents a challenge to HSE students in economics to apply their theoretical training to one of the most difficult, practical set of issues facing the economics profession today. It may come as some relief to know that nobody seems to know the answer to the question. In a series of four thematic sessions, the class will explore theoretical, historical, and empirical aspects of the issues.

There is a significant probability that the world economy is about to stumble into a period of financial dislocation. The unwillingness and/or inability of the major economic powers to confront the imbalances that led to the financial crisis of 2007-8 have laid the basis for a historical repetition. It is

probably only a question of time. The danger is that the confluence of slow real growth, low productivity increases, inflated asset prices (notably real estate) and higher public debt in some of the major G20 economies cannot be sustained much longer. So despite efforts to strengthen global governance over these past ten years, the economic foundation has little resilience. Ironically, Russia is one of the few exceptions. The Bank for International Settlements, among others, has been expressing its concerns that collectively we have been unable to constrain the build-up of financial imbalances, leading to a progressive narrowing of policy options.

Not only are financial imbalances now even worse than in 2008 but the concentration and power of large banks is more entrenched, shadow banking is more pervasive, and there has been a massive misallocation of capital owing to mispricing, which has exacerbated income inequality via financial repression and productivity-sapping bailouts to crippled firms. These seem to have the side effect of perpetuating unsustainable asset bubbles. It hardly seems surprising that that de-globalization has become a factor in the internal politics of too many countries.

Reading and resources

(the readings for the course will be finalized and prioritized about a week prior to the first session):

<https://www.hse.ru/data/2017/02/20/1167635815/4.%20Minsky.%20%20Financial%20Instability%20Hypothesis.%20LEI.%201992.pdf>

<https://www.hse.ru/data/2017/02/20/1167636363/1.%20Bernanke.%20Great%20moderation.%20EEA.%202004.pdf>

[https://www.hse.ru/data/2017/02/20/1167638293/5.%20Reinhart,%20Rogoff.%20This%20Time%20Is%20Different%20\(SHORT\).%20NBER.%202008.pdf](https://www.hse.ru/data/2017/02/20/1167638293/5.%20Reinhart,%20Rogoff.%20This%20Time%20Is%20Different%20(SHORT).%20NBER.%202008.pdf)

<https://www.hse.ru/data/2017/02/20/1167637125/Financial%20Repression%20Redux.pdf>

<https://www.hse.ru/data/2017/02/20/1167637690/9.%20White.%20Unintended%20Consequences.%20Dallas%20Fed.%202012.pdf>

[https://www.hse.ru/data/2017/02/20/1167640714/3.%20Gordon.%20Secular%20Stagnation%20\(ADAPTED\).%20DEJ.%202015.pdf](https://www.hse.ru/data/2017/02/20/1167640714/3.%20Gordon.%20Secular%20Stagnation%20(ADAPTED).%20DEJ.%202015.pdf)

<https://www.hse.ru/data/2017/02/20/1167641235/6.%20Summer.%20Secular%20Stagnation.%20Harvard.%202014.pdf>

<https://www.hse.ru/data/2017/02/20/1167635768/The%20Trouble%20With%20Macroeconomics.pdf>

Also, check www.bis.org for the annual and quarterly reports, as well as www.imf.org for the latest WEO (world economic outlook) and global financial stability report – both available for free twice a year.

Outline of the sessions (preliminary)

I. Systemic issues

- International monetary system – more than 7 decades after Bretton Woods
- Revisiting the Triffin trilemma
- Advanced and emerging market economies
- The limitations of traditional macroeconomic policy
- Financial repression – a historical overview

II. Crisis prevention

- What happened in 2007-8? What did we do?
- The elusive goal of financial stability, masking real instability
- Balance sheet risks in the global economy
- Financial mania and panics – Minsky et al
- Is the debt bubble sustainable?

III. Growth dilemma

- 10 years after the beginning of the Great Recession
- Real and nominal values: example of the determinants of GDP growth
- The productivity paradox – a worldwide phenomenon
- Growing inequality and the political economy dimension
- The problem with debt
- De-globalization as a reversion to the mean