



ST. FRANCIS XAVIER UNIVERSITY

Department of Economics
Faculty of Arts

ECON 335: Money and Financial Markets I

Fall 2023

Description:

This course focuses on the inter-relationship between asset price movements and macroeconomic developments, with a special emphasis on monetary and financial policy tools and objectives

We deal with the various forms of financing that can be available to firms, governments and households (bank credit, bonds and equity issues). We derive and study models that explain asset price movements with a specific focus on factors that can be influenced by policy-makers. We examine the consequences of severe asset price corrections, with the financial crisis of 2008-09 being given special consideration. We also study how policy-makers can prevent, or mitigate, the impact of crises via macro-prudential regulations.

We also examine how asset price movements can influence output and inflation. We study how the central bank can, via monetary policy actions, influence the path of asset prices, output and inflation. Special attention will be given to current policy issues, including the impact of Covid-19 on the economy and the extraordinary monetary policy actions taken since March 2020 to mitigate the impact of the pandemic on the economy – as well as their long-term repercussions.

Lectures:

Monday 1:00 – 2:15
Wednesday 11:30 – 12:45

Lecture Locations:

Mulroney Hall 4034

Instructor:

Greg Tkacz, Ph.D.

Instructor's Office:

Mulroney Hall 3075

Office Hours:

Monday 11:15 to 1:00
Wednesday 9:45 to 11:30
Friday 9:00 to 11:00
or by appointment

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Profile Page:

<https://www.stfx.ca/faculty-staff/greg-tkacz>

Evaluation:

Assignment #1: 15%
Mid-Term Exam: 30%
Assignment #2: 15%
Final Exam: 40%

Key Dates:

Wednesday September 6: First ECON 335 class
Wednesday October 4: Assignment #1 is due
Monday October 9: Thanksgiving Day (NO CLASSES)
Monday October 16, 11:15 to 1:00: MID-TERM EXAM
Monday November 6 to Friday November 10: Fall Study Break (NO CLASSES)
Wednesday November 22: Assignment #2 is due
TUESDAY December 5: Last ECON 335 class (Monday class will be held)
December 9 to 19: EXAMINATION PERIOD

Drop Date

Students may drop ECON 335 on Banner by **WEDNESDAY NOVEMBER 1.**

Learning Objectives:

The Bank of Canada is concerned with both price stability and the soundness of the financial system. To fully appreciate the challenges the central bank faces in meeting its goals, a good knowledge of macroeconomics and financial markets is required. ECON 335 will focus on financial markets and financial system policy, while 336 will focus on macroeconomics and monetary policy.

The learning objectives of ECON 335 are:

1. To introduce students to various financial assets, and to understand the factors that influence their prices;
2. To show students how financial market and banking disturbances can lead to financial crises, and the severe negative impacts these can have on society; and
3. To allow students to make informed contributions to financial system stability policy debates and discussions.

Pre-Requisites and Math Requirements:

Pre-requisites: ECON 101 and ECON 102

Math Requirements: You will be expected to know high-school-level algebra (e.g. the quadratic equation, cubic functions, exponents, etc.) We'll freely use algebra in 335 to derive some key results in Finance that, up until now, you may have only learned using a business calculator.

Calculator: For the assignments and exams, I recommend you find a simple calculator that can at least handle exponents and square roots. You should be able to find one for no more than \$10. If you have a fancy Business or Scientific calculator, you can feel free to use it.

Textbook and Readings:

This course is designed around a FREE open-source textbook. This has the advantage of lowering costs for students, but the disadvantage is that the book is U.S.-based, so we need to "Canadianize" the content. For this reason, we will also rely upon some FREE Canadian resources.

1. Wright, Robert E. (2012) *Money and Banking*. Saylor Foundation: Open Textbook Library, ISBN: 978098204308. FREE textbook that can be downloaded from <https://open.umn.edu/opentextbooks/textbooks/29>
2. Bank of Canada *Financial System Review* and *Monetary Policy Report*.
3. We will monitor current economic and financial developments in the media. Links to relevant stories will be provided on Moodle.

Course Outline

Weeks 1-2: Introduction

We explain the fundamentals of finance, and define the concept of money. We'll cover both conventional money, and explain how Cryptocurrencies fit into the monetary framework. We will also explain the roles and structures of central banks in Canada and the United States. Finally, we will look at recent financial and macroeconomic data to gauge the current health of the economy and financial markets.

→ Chapter 2: The Financial System

→ Chapter 3: What is Money?

Weeks 3-6: Bond Financing and Interest Rate Movements

Bonds are the most popular form of finance, and so we need to understand how they are determined and why their prices move. We'll cover some standard bond pricing models, and see how bond prices and interest rates are inversely-related. Importantly, we'll understand why some interest rates movements tend to be highly correlated with one another, and others less so.

→ Chapter 4: The Meaning of Interest Rates

→ Chapter 5: The Economics of Interest Rate Fluctuations

→ Chapter 6: The Economics of Interest Rate Spreads and the Yield Curve.

Weeks 7-8: Equity Financing and Stock Price Movements

Stock prices are widely reported in the financial press, and yet they are not the most important form of financing – nor the largest component of financial wealth. Nevertheless, it is important to understand their movements, as extreme stock price movements can spillover into other financial sectors or the economy. We will extend one of our bond-pricing models to develop a simple model of stock prices.

→ Chapter 7: The Stock Market, the Theory of Rational Expectations and the Efficient Market Hypothesis

Weeks 9-10: Bank Financing: Real Estate Prices & Financial Crises

Banks play a large role in the financial system, especially as it pertains to personal loans, with real estate loans being the largest category. We will discuss how banks can promote financial efficiency, but also explain how, if left unregulated or under-regulated, improper bank lending can lead to very detrimental outcomes. We will discuss how bank lending impacts real estate prices and how these could lead to a full-blown financial crisis.

→ Bank of Canada 2023 *Financial System Review*

→ Chapter 8: Financial Structure, Transaction Costs and Asymmetric Information

→ Chapter 13: Financial Crises

Weeks 11-12: Monetary Policy Tools and Targets (Time Permitting)

We'll explain how the Bank of Canada can implement policy by influencing the money supply and overnight interest rate. This is currently extremely relevant as the Bank conducted "Quantitative Easing" from March 2020 to 2022. How does it work? What are the implications? We'll also explain how monetary policy goals are set every five years in Canada, with the latest update occurring in December 2021. An overview of what we will cover in ECON 336.

→ Chapter 15: The Money Supply Process and the Money Multipliers

→ Chapter 16: Monetary Policy Tools

→ Chapter 17: Monetary Policy Targets and Goals