Master Degree in Business Administration - Cdl MBA

- Interpreting macroeconomic scenarios

Interpreting macroeconomic scenarios
A.Y. 2017/2018
Introduction

1. This lecture is an introduction to the course which will begin at the end of November

2. In the meantime you are advised to read:
   - your textbooks
   - articles in newspapers and magazines

3. Such articles will be a crucial source for our course
1. Readings for this lecture

- Alex Marshall’s article ‘A New Normal’ (2017)

- Roger’s Farmer (2010): preface and introduction
2. Why do we start from reading an article?

1. To learn about OBJECT of analysis: i.e. WHAT do we study?

2. To define METHOD of analysis: HOW we study it
3. Object of analysis

1. Focus on the scenario called ‘NEW NORMAL’ (NN)

2. In the article there is a distinction between
   - DRIVERS
   - OUTCOMES
4. Drivers

KEY TRENDS OR STYLIZED FACTS

1. Globalisation

2. Technological change

3. Financialization

4. Econ theory: e.g. Efficient Markets Hyp. Farmer p.xiii

5. Economic Policy (e.g. neo-liberalism, policies to avoid Depression, Farmer p. xvi)
5. Outcomes

1. Low growth
2. Unemployment
3. Few good jobs
4. Inequality
5. Low inflation
6. Booming stock markets

These outcomes differ across areas: OECD, Europe, Italy (partially different scenarios)
6. Method of analysis

- INDUCTIVE approach:

1. Start from real world stylized facts

2. Interpret them using
   - Macroeconomic THEORIES (various economists’ opinions)
   - HISTORY: to understand the NN, need to look at the past, at the ‘old’ normal, the world before crisis of 2007
7. Why interpretation of scenarios is difficult

1. Main trends are INTERCONNECTED

2. Economists DISAGREEE

3. Economics is a PECULIAR science
8. Interconnectedness

1. We live in a world which is highly interconnected, more interconnected than past

2. For this reason, we can talk about New Capitalism vs Modern Capitalism

3. 2 types of Interconnectedness are most relevant:
   - between institutions and the economy, e.g. bail outs
   - between economic trends, e.g. between globalisation and technological change: they can be self-reinforcing
9. Economists Disagreee

1. Using theory is necessary, facts do not speak for themselves

2. But what theory? You have learned economics by reading textbooks which apparently talk about ‘THE’ theory

3. As article shows, in reality economists disagree

4. For example, for some globalisation is good, an OPPORTUNITY

5. For others it is bad, a PROBLEM
10. Economics is a peculiar science

1. In principle it is a science (e.g. Farmer quote, p.xi-xii)

2. Like other sciences, it isolates DRIVERS or CAUSAL FACTORS that generate outcomes

3. However, it cannot make laboratory experiments,

4. For this reason,
   • it needs history as its laboratory
   • There is ineliminable controversy among economists
11. How to overcome difficulties

1. Our method tries to overcome these difficulties

2. This means going beyond simple textbook analysis

3. Textbooks are useful but do not lead to a balanced interpretation of scenarios

4. They are bound to generate flawed or blind interpretations as lamented by Queen Elizabeth.
It's awful - Why did nobody see it coming?':
The Queen gives her verdict on global credit crunch

The Queen spoke for the nation when she asked how the credit crunch could have taken so many economics experts by surprise.
12. What is wrong with textbooks

1. They assume STABILITY (this means that the ‘opportunity’ side is supposed to prevail)

2. Focus on MODELS that rely on ceteris paribus (consider one effect alone, taking everything else as given)

3. Focus on LONG-RUN effects, but often allow for different SHORT-RUN effects

4. This distinction corresponds to that between two main macroeconomic theories: i.e. standard or CLASSICAL THEORY and KEYNESIAN THEORY (Farmer, p.3-4)
CLASSICAL THEORY:

• the system is internally stable, free markets are inherently self-stabilizing, government intervention does more harm than good

• After crisis, the system, if left to itself, would quickly go back to full employment, thanks to price flexibility
■ KEYNESIAN THEORY:

- The Great Depression shows that the economy is not a self-regulated system

- Theoretical explanation: a lack of aggregate demand

- Remedy: expansionary fiscal policy (more public expenditure) and monetary policy (low interest rates)

- Successful for three decades until 1970s

- Stagflation in the 1970s: high inflation and high unemployment

- End of success in academia, not of Keynesian policies
13. Our approach

1. WE DO NOT ASSUME STABILITY, both opportunities and problems must be accounted for

2. No focus on single models (ceteris paribus effects) but on INTERCONNECTEDNESS of phenomena

3. we build BALANCED SCENARIOS using theories

4. Two main THEORIES ARE TREATED ON A PAR: they single out different DRIVERS both in short and long run

5. RED and BLUE scenarios; Which one prevails is a matter of assessment, probability
Our agenda for the next 10 lectures

1. Provide an account of the two main theories singling out the key drivers (lectures 1-2)

2. Discuss the main trends of the NN in the light of theories (lectures 3-7)

3. Build two alternative scenarios putting together the various trends (lectures 8-9)

4. Assess the likelihood of the two alternative scenarios (lecture 10)
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Thank you for your attention!