Eighth Edition

MACROECONOMICS

Olivier Blanchard

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To Noelle
Macroeconomics, eighth edition is organized around two central parts: A core and a set of two major extensions. The text’s **flexible organization** emphasizes an integrated view of macroeconomics, while enabling professors to focus on the theories, models, and applications that they deem central to their particular course.

The flowchart below quickly illustrates how the chapters are organized and fit within the book’s overall structure. For a more detailed explanation of the **Flexible Organization**, and for an extensive list of **Alternative Course Outlines**, see pages xiii–xiv in the preface.
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Preface

I had two main goals in writing this book:

■ To make close contact with current macroeconomic events. What makes macroeconomics exciting is the light it sheds on what is happening around the world, from the major economic crisis which engulfed the world in the late 2000s, to monetary policy in the United States, to the problems of the Euro area, to growth in China. These events—and many more—are described in the book, not in footnotes, but in the text or in detailed boxes. Each box shows how you can use what you have learned to get an understanding of these events. My belief is that these boxes not only convey the life of macroeconomics, but also reinforce the lessons from the models, making them more concrete and easier to grasp.

■ To provide an integrated view of macroeconomics. The book is built on one underlying model, a model that draws the implications of equilibrium conditions in three sets of markets: the goods market, the financial markets, and the labor market. Depending on the issue at hand, the parts of the model relevant to the issue are developed in more detail while the other parts are simplified or lurk in the background. But the underlying model is always the same. This way, you will see macroeconomics as a coherent whole, not a collection of models. And you will be able to make sense not only of past macroeconomic events but also of those that unfold in the future.

Solving Learning and Teaching Challenges

Flexible Organization

The book is organized around two central parts: a core, and a set of two major extensions. An introduction precedes the core. The two extensions are followed by a review of the role of policy. The book ends with an epilogue. The flowchart at the beginning of this book makes it easy to see how the chapters are organized and fit within the book’s overall structure.

■ Chapters 1 and 2 introduce the basic facts and issues of macroeconomics. Chapter 1 takes you on an economic tour of the world, from the United States, to the Euro area, and to China. Some instructors will prefer to cover Chapter 1 later, perhaps after Chapter 2, which introduces basic concepts, articulates the notions of short run, medium run, and long run, and gives the reader a quick tour of the book.

While Chapter 2 gives the basics of national income accounting, I have put a detailed treatment of national income accounts in Appendix 1 at the end of the book. This decreases the burden on the beginning reader and allows for a more thorough treatment in the appendix.

■ Chapters 3 through 13 constitute the core. Chapters 3 through 6 focus on the short run. Chapters 3 to 5 characterize equilibrium in the goods market and in the financial markets, and derive the basic model used to study short-run movements in output, the IS-LM model. Chapter 6 extends the basic IS-LM model to reflect the role of the financial system. It then uses it to describe what happened during the initial phase of the financial crisis.

Chapters 7 through 9 focus on the medium run. Chapter 7 focuses on equilibrium in the labor market and introduces the notion of the natural rate of unemployment. Chapter 8 derives and discusses the relation between unemployment and inflation, known as the Phillips curve. Chapter 9 develops the IS-LM-PC (PC for Phillips curve) model which takes into account equilibrium in the goods market, in the financial markets, and in the labor market. It shows how this model can be used to understand movements in activity and movements in inflation, both in the short and in the medium run.

Chapters 10 through 13 focus on the long run. Chapter 10 describes the facts, showing the evolution of output across countries and over long periods of time. Chapters 11 and 12 develop a model of growth and describe how capital accumulation and technological progress determine growth. Chapter 13, which is new, focuses on the challenges to growth, from inequality to climate change.

■ Chapters 14 through 20 cover the two major extensions. Chapters 14 through 16 focus on the role of expectations in the short run and in the medium run. Expectations play
a major role in most economic decisions and, by implication, play a major role in the determination of output.

Chapters 17 through 20 examine the implications of openness of modern economies. Chapter 20 looks at the implications of different exchange rate regimes, from flexible exchange rates, to fixed exchange rates, currency boards, and dollarization.

Chapters 21 through 23 return to macroeconomic policy. Although most of the first 20 chapters constantly discuss macroeconomic policy in one form or another, the purpose of Chapters 21 through 23 is to tie the threads together. Chapter 21 looks at the role and the limits of macroeconomic policy in general. Chapters 22 and 23 review fiscal and monetary policy. Some instructors may want to use parts of these chapters earlier. For example, it is easy to move forward the discussion of the government budget constraint in Chapter 22 or the discussion of inflation targeting in Chapter 23.

Chapter 24 serves as an epilogue: it puts macroeconomics in historical perspective by showing the evolution of macroeconomics over the last 80 years, discussing current directions of research, and the lessons of the crisis for macroeconomics.

Alternative Course Outlines

Within the book’s broad organization, there is plenty of opportunity for alternative course organizations. I have made the chapters shorter than is standard in textbooks, and, in my experience, most chapters can be covered in an hour and a half. A few (Chapters 5 and 9 for example) might require two lectures to sink in.

Short courses (15 lectures or less)

A short course can be organized around the two introductory chapters and the core (Chapter 13 can be excluded at no cost in continuity). Informal presentations of one or two of the extensions, based, for example, on Chapter 16 for expectations (which can be taught as a standalone) and on Chapter 17 for the open economy, can then follow, for a total of 14 lectures.

A short course might leave out the study of growth (the long run). In this case, the course can be organized around the introductory chapters and Chapters 3 through 9 in the core; this gives a total of 9 lectures, leaving enough time to cover, for example, Chapter 16 on expectations and Chapters 17 through 19 on the open economy, for a total of 13 lectures.

Longer courses (20 to 25 lectures)

A full semester course gives more than enough time to cover the core, plus one or both of the two extensions, and the review of policy. The extensions assume knowledge of the core, but are otherwise mostly self-contained. Given the choice, the order in which they are best taught is probably the order in which they are presented in the book. Having studied the role of expectations first helps students to understand the interest parity condition and the nature of exchange rate crises.

Innovative Features

I have made sure never to present a theoretical result without relating it to the real world. In addition to discussions of facts in the text itself, I have written many Focus boxes, which discuss particular macroeconomic events or facts from the United States or from around the world. Many of those are new to this edition.

I have tried to re-create some of the student–teacher interactions that take place in the classroom by the use of margin notes, which run parallel to the text. The margin notes create a dialogue with the reader and, in so doing, smooth the more difficult passages and give a deeper understanding of the concepts and the results derived along the way.

For students who want to explore macroeconomics further, I have introduced the following two features:

Short appendices to some chapters, which expand on points made within the chapter.

A ‘Further Readings’ section at the end of most chapters, indicating where to find more information, including key Internet addresses.

Each chapter starts with a one- or two-sentence summary at the end of the introduction, and ends with three ways of making sure that the material in the chapter has been digested:

A summary of the chapter’s main points.

A list of key terms.

A series of end-of-chapter exercises. “Quick Check” exercises are easy. “Dig Deeper” exercises are a bit harder, and “Explore Further” activities typically require either access to the Internet or use of a spreadsheet program.

A list of symbols at the end of the book makes it easy to recall the meaning of the symbols used in the text.
What’s New in This Edition

A new Chapter 13 on the challenges to growth. Topics include whether the introduction of robots will lead to mass unemployment, the relation between growth and inequality, and the challenges of climate change.

A revised Chapter 8 on the Phillips curve, reflecting a major change in the US economy. The Phillips curve is now a relation between inflation and unemployment rather than between the change in inflation and unemployment.

A revised Chapter 9 showing how the changes in the Phillips curve relation have led to changes in monetary policy.

A new appendix in Chapter 1, ‘What Do Macroeconomists Do?’, which will give you a sense of what careers you may pursue if you were to specialize in macroeconomics.

Updated Focus Boxes include:

- NEW! Will Bitcoins Replace Dollars? (Chapter 4)
- From Henry Ford to Jeff Bezos (Chapter 7)
- NEW! Nudging US Households to Save More (Chapter 11)
- What Lies Behind Chinese Growth? (Chapter 12)
- Uncertainty and Fluctuations (Chapter 16)
- NEW! US Trade Deficits and Trump Administration Tariffs (Chapter 19)

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Olivier Blanchard
Washington,
November 2019
A citizen of France, Olivier Blanchard has spent most of his professional life in Cambridge, U.S.A. After obtaining his Ph.D. in economics at the Massachusetts Institute of Technology in 1977, he taught at Harvard University, returning to MIT in 1982. He was chair of the economics department from 1998 to 2003. In 2008, he took a leave of absence to be the Economic Counsellor and Director of the Research Department of the International Monetary Fund. Since October 2015, he has been the Fred Bergsten Senior Fellow at the Peterson Institute for International Economics, in Washington. He also remains Robert M. Solow Professor of Economics emeritus at MIT.

He has worked on a wide set of macroeconomic issues, from the role of monetary policy, to the nature of speculative bubbles, to the nature of the labor market and the determinants of unemployment, to transition in former communist countries, and to forces behind the recent global crisis. In the process, he has worked with numerous countries and international organizations. He is the author of many books and articles, including a graduate level textbook with Stanley Fischer.

He is a past editor of the Quarterly Journal of Economics, of the NBER Macroeconomics Annual, and founding editor of the AEJ Macroeconomics. He is a fellow and past council member of the Econometric Society, a past president of the American Economic Association, and a member of the American Academy of Sciences.