

Economics 662 – Fall 2008
International Macroeconomics
Course website: <http://www2.hawaii.edu/~noy/662.html>

Tuesday-Thursday 12:00-1:15 (GRG 214)

Ilan Noy - pronounced *ee-lan*

Saunders Hall 516

noy@hawaii.edu

Tel: (808) 956-7749

Fax: (808) 956-4347

Office hours: Tuesday & Thursday 10:30-11:30, or by appointment on Fridays.

Email is by far the best way to contact me for appointments, emergencies, questions or clarifications. In case the UH mail system is down, you can email me at: ilannoy@yahoo.com

Course Description

The study of international economics is usually divided into two parts: trade (micro-analysis) and finance (monetary/open macroeconomics). This course studies the latter. We first define the field and introduce the major concepts of macroeconomics as they relate to open economies (output, exchange rates, etc.). We then develop intertemporal models that help us evaluate policies that affect the determination of output, unemployment, price levels, and exchange rates. We continue with a number of selected topics in international finance based on the class and the instructor's interests and preferences. Throughout, we also analyze the current state of the empirical literature.

Lectures should only be considered a supplement to the readings. The lectures are designed to cover the most fundamental issues and provide a foundation for the readings. The exam may include topics covered by the required readings that were not dealt with in class (required readings are indicated by an asterisk).

Readings

Required Textbook

[OR] Obstfeld, Maurice, and Kenneth Rogoff. *Foundations of International Macroeconomics* (Cambridge, Mass.: MIT Press, 1996).

[Available on reserve at Sinclair library.]

Optional Textbook

[BS] Barro, R. and X. Sala-i-Martin. *Economic Growth* (2nd edition).

Class Requirements

A. Presentations

Each student will present at least two papers chosen by the instructor (from the reading list). The presentation should include both the main arguments and ideas of the paper, the methodology used, a technical description of results and your own critique. This information should also be included in a handout provided to the class before the lecture. A presentation should last about 30-45 minutes. If you want, your presentation can be posted online ahead of time.

B. Exam

A take-home exam will cover the first part of the course. You will have 24 hours to do the exam (date: TBA)

C. Final paper

The final paper will discuss a topic of your choice (out of the topics we choose in the latter half of the course). It will describe the major contributions on the topic, the current state of the literature, and will propose in detail at least one possible extension/addition to that literature.

Grading

Presentations	30% (15% each)
Exam	25%
Final Paper	25%
Attendance & participation	20%

Grades awarded will include +/- notation

Disability Needs

If you feel you need reasonable accommodations because of the impact of a disability, please, (1) contact the KOKUA program at 956-7511 or 956-7612 (rm. 013 at QLCSS) and (2) discuss with me any specific needs related to your documented disability.

THIS IS NOT A FINAL READING LIST!

1. THE INTERTEMPORAL APPROACH TO THE CURRENT ACCOUNT

*OR, sections 1.1-1.5, 2.1-2.3, 2.5.

*Bergin, P. and Sheffrin, S., 2000. Interest rates, exchange rates and present value models of the current account. *Economic Journal*, 110, 535-558.

*Nason, James M. and John H. Rogers, 2006. The present-value model of the current account has been rejected: Round up the usual suspects. *Journal of International Economics* 68, 159–187.

Svensson, L., and A. Razin, 1983. The Terms of Trade and the Current Account: The Harberger-Laursen-Metzler Effect. *Journal of Political Economy*, 91, 97-125.

*Tornell, Aaron, and Philip Lane (1998). Are windfalls a curse? A Non-Representative Agent Model of the Current Account. *Journal of International Economics*, 44, 83-112.

2. FISCAL POLICY IN THE OPEN ECONOMY

*OR, sections 3.1-3.5.

Asdrubali, Pierfederico, Bent Sorensen and Oved Yosha (1996). "Channels of Interstate Risk Sharing: United States 1963-90." *Quarterly Journal of Economics*, 111, 1081-110.

*Frenkel, J. and A. Razin (1986). "Fiscal Policies in the World Economy." *Journal of Political Economy*, 94, 564-594.

3. EXCHANGE RATES

*OR, sections 4.2, 4.5, 5.1, 5.2, 5.3.

*Bacchetta, P. and van Wincoop, E., 2006. Can Information Heterogeneity Explain the Exchange Rate Determination Puzzle? *American Economic Review*, 96(3).

Bayoumi, Tamim, Jaewoo Lee, and Sarma Jayanthi, 2006. New Rates from New Weights. *IMF Staff Papers* 53(2).

*Cheung, Yin-Wong, Menzie Chinn, and Antonio Garcia Pascual (2003). Empirical Exchange Rate Models of the Nineties: Are Any Fit to Survive? *Journal of International Money and Finance*.

Chinn, M.D. and R.A. Meese, 1995, "Banking on Currency Forecasts: How Predictable is Change in Money," *Journal of International Economics* 38, 161–178.

Chinn, Menzie D. (2006). The (partial) rehabilitation of interest rate parity in the floating rate era: Longer horizons, alternative expectations, and emerging markets. *Journal of International Money and Finance* 25(1), 7-21.

*Crucini, Mario J., Chris I. Telmer, and Marios Zachariadis (2005), Understanding European Real Exchange Rates. *American Economic Review* 95(3).

Engels, C. and J. Hamilton, 1990, "Long Swings in the Exchange Rate: Are They in the Data and Do Markets Know It?" *American Economic Review* 80, 689–713.

Engels, Charles (1999). "Accounting for US Real Exchange Rate Changes," *Journal of Political Economy* 107, 507-538.

*Engels Charles and K. West (2005). "Exchange Rates and Fundamentals." *Journal of Political Economy* 113(3), 485-517.

Goldberg, Penny K. and Michael Knetter (1997). "Goods Prices and Exchange Rates: What have we Learned?" *Journal of Economic Literature* 35, 1243-72.

*Imbs, J., H. Mumtaz, M. Ravn and H Rey (2005). "PPP Strikes Back: Aggregation and the Real Exchange Rate." *Quarterly Journal of Economics* 120(1), 1-43.

Kilian, L. and M.P. Taylor (2003). "Why is it so Difficult to beat the Random Walk Forecast of Exchange Rates." *Journal of International Economics* 60, 85–108.

Hanno Lustig and Adrien Verdelhan, 2007. The Cross Section of Foreign Currency Risk Premia and Consumption Growth Risk. *American Economic Review* 97(1).

Mark, N., (1995). "Exchange Rates and Fundamentals: Evidence on Long Horizon Predictability," *American Economic Review* 85, 201–218.

Parsley, David C. and Shang-Jin Wei, 2007. A prism into the PPP puzzles: The micro-foundations of big mac real exchange rates. *Economic Journal*, 117, 1336–1356.

Rogoff, Kenneth (1996). "The Purchasing Power Parity Puzzle." *Journal of Economic Literature*.

Taylor, M.P. (1995). "The Economics of Exchange Rates." *Journal of Economic Literature* 33(1), 13-47.

Taylor, Alan M. and Mark P. Taylor (2004). The Purchasing Power Parity Debate. *Journal of Economic Perspectives* 18(4).

4. MONEY AND THE NEW OPEN ECONOMY

*OR, sections 8.2, 9.2-9.3, 10.1-10.2.

*Corsetti, Giancarlo and Paolo Pesenti (2001). "Welfare and Macroeconomic Interdependence," *Quarterly Journal of Economics*, 421-445.

*Dornbusch, Rudiger (1976). "Expectations and Exchange Rate Dynamics." *Journal of Political Economy*, 24, 1161-1176.

Obstfeld, Maurice (2002). "Exchange Rates and Adjustment: Perspectives from the New Open Economy Macroeconomics." NBER WP 9118.

Obstfeld, Maurice and Ken Rogoff (1995). "Exchange Rate Dynamics Redux." *Journal of Political Economy*, 102.

*Obstfeld, Maurice and Kenneth Rogoff (2000). "New Directions in Stochastic Open Economy Models." *Journal of International Economics*, 48, 117-153

*Philip Lane (2001). "The New Open Economy Macroeconomics: A Survey." *Journal of International Economics*, 54, 235-266.

5. BALANCE OF PAYMENTS CRISES - THEORY

OR, pp. 558-67, 576-78, 648-653.

Aghion, Philippe, Philippe Bacchetta, Abhijit Banerjee. (2001). "Currency Crises and Monetary Policy in an Economy with Credit Constraints." *European Economic Review* (45)7, 1121-1150.

*Allen, Franklin, and Douglas Gale. (1998). Optimal Financial Crises. *Journal of Finance* 53, 1245-1284.

Allen, Franklin, and Douglas Gale (2000). Bubbles and Crises. *Economic Journal* 110, 236-255.

Arellano, Cristina and Enrique Mendoza (2002). Credit Frictions and 'Sudden Stops' in Small Open Economies: An Equilibrium Business Cycle Framework for Emerging Markets Crises. NBER WP 8880.

*Burnside, Craig, Martin Eichenbaum and Sergio Rebelo (2001). Prospective Deficits and the Asian Currency Crisis. *Journal of Political Economy* 109(6).

Caballero, Ricardo and Arvind Krishnamurthy (2004). Smoothing Sudden Stops. *Journal of Economic Theory* 119(1), 104-127.

*Calvo, Guillermo (1987) "Balance of Payments Crises in a Cash-in-Advance Economy." *Journal of Money, Credit and Banking*, 19, 19-32.

Calvo, Guillermo. (1998). "Capital Flows and Capital-Market Crises: The Simple Economics of Sudden Stops." *Journal of Applied Economics* 1, 35-54.

*Chang, Roberto and Andres Velasco (2001). "A Model of Financial Crises in Emerging Markets." *Quarterly Journal of Economics*, 489-518.

Corsetti, Giancarlo, Paolo Pesenti, and Nouriel Roubini. (1999). "Paper Tigers? A Model of the Asian Crisis." *European Economic Review*, 43, 1211-1236.

Dooley, Michael (2000). "A Model of Crises in Emerging Markets." *Economic Journal* 110, 256-272.

*Diamond, Douglas and Phillip Dybvig, 1983. "Bank Runs, Deposit Insurance, and Liquidity." *Journal of Political Economy*, 91(3), 401-419.

*Drazen, Allen and Paul Masson (1994). "Credibility of Policies versus Credibility of Policymakers." *Quarterly Journal of Economics* 109(3), 735-754.

Flood, Robert P., and Peter M. Garber, 1991, "The Linkage between Speculative Attacks and Target Zone Models of Exchange Rates." *Quarterly Journal of Economics*, 106, 1367-72.

*Gopinath, Gita (2004). "Lending Booms, Sharp Reversals and Real Exchange Rate Dynamics". *Journal of International Economics* 62, 1-23.

*Hellwig, C., 2006. Self-Fulfilling Currency Crises: The Role of Interest Rates. *American Economic Review*, 96(5).

*Krugman, Paul (1979). "A Model of Balance of Payment Crisis." *Journal of Money, Credit and Banking*, 11, 311-325.

Mendoza, Enrique G. 2006. Lessons from the Debt-Deflation Theory of Sudden Stops. *American Economic Review* 96(2), 411-416.

Morris, Stephen and Hyun Song Shin (1998). "Unique Equilibrium in a Model of Self-Fulfilling Currency Attacks." *American Economic Review* 88, 587-97.

*Obstfeld, Maurice (1994). "The Logic of Currency Crises." *Cahiers économiques et monétaires* 43, 189-213.

Schneider, Martin and Aaron Tornell (2004). "Balance Sheet Effects, Bailout Guarantees and Financial Crises". *Review of Economic Studies* 71, 883-913.

6. MISCELLENOUS

*Obstfeld, Maurice and Kenneth Rogoff (2000). "The Six Major Puzzles in International Macroeconomics: Is there a Common Cause?" in Ben Bernanke and

Kenneth Rogoff (eds.), *NBER Macroeconomics Annual 2000*. Also NBER WP 7777.

7. ELECTIVE TOPICS

A. Currency Unions

Alesina, Alberto, and Robert Barro, "Currency Unions," mimeo, Harvard University.

Corsetti, Giancarlo, and Paolo Pesenti. (2002). "Self-Validating Optimum Currency Areas." NBER WP 8783.

Dixit, Avinash (2001). Games of monetary and fiscal interactions in the EMU, *European Economic Review*, 45(4), 589-613

Glick, Reuven and Andrew K. Rose (2002). "Does a currency union affect trade? The time-series evidence." *European Economic Review*, 46(6), 1125-1151.

Klein, Michael W. (2005). Dollarization and Trade. *Journal of International Money and Finance* 24, 935-943.

Mundell, Robert (1961). "A Theory of Optimum Currency Areas." *American Economic Review* 51(4), 657-665.

B. Exchange Rate Regimes

Calvo, Guillermo and F. Mishkin (2003). "The Mirage of Exchange Rate Regimes for Emerging Market Countries." *Journal of Economic Perspectives* 17(4).

Calvo, Guillermo and Carmen M. Reinhart, 2002, "Fear of Floating," *Quarterly Journal of Economics*, 117(2), 379-408.

Luis Felipe Céspedes, Roberto Chang, and Andrés Velasco (2004). Balance Sheets and Exchange Rate Policy. *American Economic Review* 94(4).

Chang, Roberto, and Andres Velasco. (2000). "Financial Fragility and the Exchange Rate Regime." *Journal of Economic Theory* 92, 1-34.

Fischer, Stanley (2001). "Exchange Rate Regimes: Is the Bipolar View Correct?" *Journal of Economic Perspectives* 15(2), 3–24.

Jeanne O. and A. K. Rose (1999). "Noise Trading and Exchange Rate Regimes," NBER WP # 7104.

Levy-Yeyati, Eduardo and Federico Sturzenegger (2003). "To Float or to Fix: Evidence on the Impact of Exchange Rate Regimes on Growth." *American Economic Review*, 93(4). 1173-1193.

Krugman, Paul (1991). "Target Zones and Exchange Rate Dynamics." *Quarterly Journal of Economics*, 106, 669–82.

Amartya Lahiri, Rajesh Singh, and Carlos Végh, 2007. Segmented asset markets and optimal exchange rate regimes. *Journal of International Economics* 72, 1–21.

Reinhart, Carmen M., and Kenneth S. Rogoff, 2004, “The Modern History of Exchange Rate Arrangements: A Reinterpretation,” *Quarterly Journal of Economics*, 119(1), 1–48.

C. Balance Of Payments and Banking Crises - Empirics

Arteta, Carlos, and Barry Eichengreen (2002). "Banking Crises in Emerging Markets: Presumptions and Evidence." In: M. Blejer and M. Skreb (eds.) *Exchange Rate and Financial Vulnerability in Emerging Markets*.

Ashcraft, A., 2005. Are Banks Really Special? New Evidence from the FDIC-Induced Failure of Healthy Banks. *American Economic Review*, 95(5).

Demirgüç-Kunt, Asli, and Enrica Detragiache. (1998). “The Determinants of Banking Crises in Developing and Developed Countries.” *IMF Staff Papers*, 45, 81-109.

Demirgüç-Kunt, Asli, Enrica Detragiache and Poonam Gupta, 2006. Inside the crisis: An empirical analysis of banking systems in distress. *Journal of International Money and Finance* 25, 702-718.

Frankel, Jeffrey, and Andrew Rose. (1996). “Currency Crashes in Emerging Markets. An Empirical Treatment.” *Journal of International Economics* 41, 351-366.

Forbes, Kristin (2002). “Cheap Labor Meets Costly Capital: The Impact of devaluations on Commodity Firms”. *Journal of Development Economics* 69(2), 335-365.

Glick, Reuven and Michael Hutchison (forthcoming). “Capital Controls and Exchange Rate Instability in Developing Economies,” *Journal of International Money and Finance*.

Hutchison, Michael and Ilan Noy (2005). “How Bad are Twins? Output Costs of Currency and Banking Crises”. *Journal of Money, Credit and Banking* 37(4).

Hutchison, Michael and Ilan Noy (2006). “Sudden Stops and the Mexican Wave: Currency Crises, Capital Flow Reversals and Output Loss in Emerging Markets.” *Journal of Development Economics* 79(1), 225-248.

Kaminsky, Graciela and Carmen M. Reinhart (1999). "The Twin Crises: The Causes of Banking and Balance of Payments Problems." *American Economic Review*, 89, 473-500.

Randall S. Kroszner, Luc Laeven and Daniela Klingebiel, 2007. Banking crises, financial dependence, and growth. *Journal of Financial Economics* 84, 187–228.

Milesi-Ferretti, Gian Maria, and Assaf Razin. (2000). "Current Account Reversals and Currency Crises: Empirical Regularities." In *Currency Crises*, edited by P. Krugman.

Noy, Ilan (2004). "Financial Liberalization, Prudential Supervision and the Onset of Banking Crises - Empirical Findings" *Emerging Markets Review* 5(3), 341-359.

Jeanne, Olivier (2000). "Foreign Currency Debt and the Global Financial Architecture." *European Economic Review* 44(4), 719-727.

D. Sovereign risk

OR page 349-388, 407-17, 419-22

Bulow, J. and K. Rogoff (1989). "A Constant Recontracting Model of Sovereign Debt." *Journal of Political Economy* 97, 155-78.

Bulow, J. and K. Rogoff (1989). "Sovereign Debt: Is to Forgive to Forget?" *American Economic Review* 79, 43-50.

Eaton and Gersovitz (1981). *Review of Economic Studies* 48, 289-309.

Kletzer, K. (1984). "Asymmetric Information and the LDC Borrowing with Sovereign Risk." *Economic Journal*, 287-307.

Kletzer, Kenneth and Brian Wright (2000). "Sovereign Debt as Intertemporal Barter." *American Economic Review* 90, 621-639.

E. Dollarization

Berg, Andrew and Eduardo Borensztein, 2000, "The Pros and Cons of Full Dollarization." IMF WP/00/50.

Edwards, Sebastian (2001). "Dollarization: Myths and Realities," *Journal of Policy Modeling*, 23.

Jeanne, O. (2003). "Why do Emerging Market Economies Borrow in Foreign Currency." IMF WP/03/177.

Reinhart, Carmen M., Kenneth S. Rogoff and Miguel A. Savastano (2003). "Addicted to Dollars." NBER WP 10015.

Uribe, Martin (1997). "Hysteresis in a Simple Model of Currency Substitution," *Journal of Monetary Economics*, 40(1), 185-202.

F. History of the International Financial System

Boughton, James M. (2004). "The IMF and the Force of History: Ten Events and Ten Ideas That Have Shaped the Institution." IMF WP/04/75.

Dooley, M., Folkerts-Landau, D and P. Garber (2004). "The Revived Bretton Woods System." NBER WP 10332.

Eichengreen, Barry J., (1996). *Globalizing Capital: A History of the International Monetary System* (Princeton: Princeton University Press).

Eichengreen, Barry J., (2004). "Global Imbalances and the Lessons of Bretton Woods." NBER WP 10497.

Lothian, James R. and Mark P. Taylor (1996) "Real Exchange Rate Behavior: The Recent Float from the Perspective of the Past Two Centuries." *Journal of Political Economy* 104, 488-509.

Obstfeld, Maurice, Jay C. Shambaugh and Alan M. Taylor (2004). "Monetary Sovereignty, Exchange Rates, and Capital Controls: The Trilemma in the Interwar Period." NBER WP 10393.

G. Capital Flows, Capital Controls and International Financial Integration

Gourinchas, Pierre-Olivier and Olivier Jeanne (2006). The Elusive Gains from International Financial Integration. *Review of Economic Studies* 73, 715–741.

Kose, M. Ayhan, Eswar S. Prasad, Marco E. Terrones, 2006. How do trade and financial integration affect the relationship between growth and volatility? *Journal of International Economics* 69, 176– 202.

Martin, Philippe and Hélène Rey (2006). Globalization and Emerging Markets: With or Without Crash? *American Economic Review*, forthcoming.

Ashoka Mody and Antu Panini Murshid, 2005. Growing up with capital flows. *Journal of International Economics* 65, 249– 266.

Shang-Jin Wei and Zhiwei Zhang, 2007. Collateral damage: Exchange controls and international trade. *Journal of International Money and Finance* 26, 841-863.

Wright, Mark L.J. (2006). Private capital flows, capital controls, and default risk. *Journal of International Economics* 69, 120–149.

van Wincoop, Eric and Cedric Tille, 2007. International Capital Flows. NBER Working Paper 12856.