Economics 662. International Monetary Economics

Office Hours

- Tuesday 3:00-4:00; Wednesday 1:00-2:00, Saunders 513, 956-7285,
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Prerequisite

- Economics 607 Macroeconomic Theory I, or
- Economics 605 Macroeconomics and Policy Analysis.

Course Content

Economics 662 studies the macro side of international economics. Topics include balance of payments adjustment and macroeconomic stabilization policies under fixed and flexible exchange rates, empirical regularities of international prices, interest rates and exchange rates, models of exchange rate determination and exchange rate/current account dynamics, exchange rate policy for developed and developing economies, international capital flows and balance of payments crises.

Course Requirements

There will be a midterm exam and a comprehensive final exam, counting for 25% and 35% of your grade respectively, a term paper worth 25% of your grade, and article presentations worth 15% of your grade.

Exams:

You are responsible for all material covered in class and the associated articles or book chapters. For the most part, these will be the readings marked with an asterisk (*) in the reading list below. I may decide to skip some material in the list or assign other readings as the course progresses. Exam dates are firm. Except in the case of medical emergency, I will not schedule makeup exams.

Term Paper:

You will write a 15-20 page paper on a topic of your choice. For doctoral students, this paper should be a careful review of some aspect of the relevant academic literature. Masters students are encouraged to complete a study that applies theoretical or empirical results from the international monetary literature to a contemporary policy issue. For both groups of students, a one page description of your proposed topic (an abstract) will be due early in the term. I will then meet individually with each of you to discuss your research. The final draft of your paper will be due in November.

Article Presentations:

Class will be conducted in a seminar format that involves students in the presentation and discussion of the course material. With a classmate, you will be asked to lecture and lead discussion of one or more of the assigned readings. At the appropriate point during the term, you and your partner will present an overview of the reading, explaining its methodology, results, and importance in the literature. You may use the blackboard, overhead transparencies, or handouts in presenting the material. In short, you run the lecture on that topic.
Class Participation:

I expect you to attend class regularly, to read all assigned material, and to participate in class discussions.

Readings

Readings for the course will be taken from the journal literature and various texts. Primary readings (*) are indicated below. The other readings in the list are included because they give a useful alternative presentation of a topic, present related material, provide background information, or are historically important. Most articles and chapters that we will discuss will be placed on reserve in Sinclair Library; readings that should be available (not yet!) are marked with a section (§) symbol in the list below.

I have ordered the following volume as a recommended text for the course:


The book (FIM in reading list) provides thorough treatments of many course topics, and is particularly strong in its coverage of recent optimizing approaches. Other general texts, on reserve in Sinclair Library, are:


Some of the assigned readings are included in the following reserve volumes:


The following undergraduate texts may be useful references:


Course Schedule

The following is a plan for the course, showing exam dates and paper deadlines (firm) and beginning dates for each topic section (tentative)

<table>
<thead>
<tr>
<th>II</th>
<th>The Balance of Payments and Perspectives on the CA</th>
<th>Aug. 26</th>
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<tr>
<td>III</td>
<td>Traditional Open Economy Macro Models</td>
<td>Sep. 2</td>
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<td>IV.A-B</td>
<td>Devaluation: The Elasticity/Absorption Approach</td>
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<tr>
<td>IV.E</td>
<td>Devaluation: The Intertemporal Optimizing Approach</td>
<td>Sep. 16</td>
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<td><strong>Abstract Due</strong></td>
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<td>IV.F</td>
<td>Recent Balance of Payments Adjustment Experience</td>
<td>Sep. 23</td>
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**IF**, Chapter 1.
**IM**, Chapters 1-5.

II. The Balance of Payments and Perspectives on Current Account Imbalances.


**IF**, Chapter 2.


III. Traditional Models of International Macroeconomic Equilibrium and Policy.

A. The Income Determination Model.

*§Dornbusch, R. "Income Determination and the Trade Balance," Chapter 3 in *OEM*.


**IF**, Chapter 3, pp. 50-75.
B. The Mundell-Fleming Model and Extensions.

IF, Chapter 4.
IM, Chapters 6-7 (single country model), Chapters 8-11 (extensions), Chapter 13 (two-country model), Chapter 15 (evidence on international transmission), Chapter 38 (the assignment problem).

IV. Devaluation and Balance of Payments Adjustment.

A. The Classical Elasticity Approach.

*§IF, Chapter 3, pp. 57-65.
IM, Chapter 12, pp. 142-148.

B. The Keynesian Absorption Approach.

*§Dornbusch, R. "Relative Prices, Equilibrium Output, and the Trade Balance," Chapter 4 in OEM.
*§Alexander, S.S., "Effects of a Devaluation on a Trade Balance," IMF Staff Papers, 2, April 1952, reprinted as Chapter 22 in Caves and Johnson, RIE.
IF, Chapter 3, pp. 65-71.

C. The Monetary Approach.

IF, Chapter 5.
OEM, Ch. 7.
D. Developing Countries and Possible Contractionary Effects


F. The Role of Exchange Rates in Recent Balance of Payments Adjustment


A. Purchasing Power Parity.

IF, Chapter 6.
IM, Chapter 31, pp. 329-333.

B. Interest Parity and Foreign Exchange Market Efficiency.

International Asset Pricing.


VI. The Determination of Flexible Exchange Rates.

A. The Traditional Approach.


B. The Monetary Approach.


C. Monetary Models with Sticky Prices (Overshooting Models).


D. Portfolio-Balance Models and Current Account Dynamics.
E. Exchange Rate Modeling—Where do We Stand?


VII. Evaluating Exchange Rate Regimes

A. Real Exchange Rates and Misalignment

Sachs, J. and F. Larrain, Macroeconomics in the Global Economy, Ch. 21.

B. Fixing, Floating and Target Zones

IF, Chapters 10, 11.
IM, Chapters 36, 39.
FIM, Ch. 8, pp. 554-558, 569-579, and Ch. 9, pp. 631-634.

C. Exchange Rate Regimes and Stabilization in Developing Countries

*§Frankel, Jeffrey, "No Single Currency Regime is Right for All Countries or At All Times," NBER WP 7338, September 1999.
Eichengreen, Barry and T. Bayoumi, "Is East Asia an Optimum Currency Area? Can it Become One?" in S.
VIII. Contemporary Approaches to the Open Macroeconomy and Policy.


Marston, R. "Stabilization Policies in Open Economies" (Parts 5 and 6 only, pp. 892-911), Chapter 17 in Jones and Kenen, HIE.


IM, Ch. 24.

B. Fiscal Policy in Optimizing Models of the Open Real Economy


FIM, Chs. 1-3.

C. Optimizing Models with Nominal Rigidities: The New Open Economy Macroeconomics


Doyle, Brian, New Open Economy Macro home page.

*FIM, Ch. 10

IX. International Capital Flows

A. The Current Account in Intertemporal Optimizing Models


B. Capital Flows, Controls and Current Account Sustainability


C. Balance of Payments Crises

Roubini, Nouriel, Asia Crisis Homepage (on web).
FIM, Ch. 8, pp. 558-566.

D. Managing Debt

IF, Chapter 15.
FIM, Ch. 6.

X. Models of Economic Growth and International Convergence

FIM, Ch. 7.

XI. International Economic Policy Coordination.
*IF*, Chapter 13.
*IM*, Chapter 45.