

ECON 163: INTERNATIONAL MACROECONOMIC POLICY AND MONETARY INSTITUTIONS
FALL 2009, POMONA COLLEGE
[HTTP://WWW.ECONOMICS.POMONA.EDU/SLAVOV/ECON163](http://www.economics.pomona.edu/slavov/econ163)

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Office hours: Tuesday 2-3 pm, Wednesday 3-4 pm, Thursday 3-4 pm

Prerequisites:

Econ 101, Econ 102, and Econ 107 (or 167)

Class meetings:

We will meet Mondays and Wednesdays at 1:15 pm in Hahn 107.

Required book:

Blustein, Paul. The Chastening: Inside the Crisis that Rocked the Global Financial System and Humbled the IMF. PublicAffairs, 2003.

Recommended books:

Obstfeld, Maurice, and Kenneth Rogoff. Foundations of International Macroeconomics. MIT Press, 1996. (*Available at the Bookstore. We'll cover 50-80 pages from this graduate-level text.*)

Krugman, Paul, and Maurice Obstfeld. International Economics: Theory and Policy. 8th edition. Addison-Wesley, 2009. (*A good background reference for those who have not taken Econ 123.*)

Yarbrough, Beth, and Robert Yarbrough. The World Economy: Trade and Finance. 6th edition. South-Western, 2003. (*Ditto.*)

What is this course about?

This course will explore the field of international finance, sometimes also called “open-economy macroeconomics.” We are going to cover a mix of theoretical models, empirical evidence, and policy debates. Our primary focus will be on how well global financial markets help us deal with time and uncertainty. We will zoom in on the incompleteness, imperfections, failures, and crises which plague those markets, with particular focus on the ongoing global financial crisis. We will learn about the international monetary system and its main institutions. In terms of technique, we will emphasize dynamic models with explicit micro-foundations – those have become the staple of modern macroeconomics.

The course will be divided into three parts. In the first part, roughly September 2 till October 14, we will cover sections from the Obstfeld and Rogoff (OR) textbook, and the class will be based primarily on lectures and homeworks. OR is a graduate-level text, so we will cherry-pick those segments which are accessible. For the most part, OR will paint an idealized picture of how international asset markets are *supposed* to work. We are also going to read Paul Blustein's book on the spate of emerging market crises in 1997-99 because the book is fun ("a riveting thriller about the IMF"), because it provides non-technical background to the course, and because quite a few characters and events from that book will sound eerily familiar in the midst of the ongoing global financial crisis.

In the second part, approximately October 21 till November 11, we are going to discuss a subset of the papers listed at the end of this syllabus. Students will take the center stage and will take turns presenting papers and leading the discussion. I will sit in the back of the room and (hopefully) keep very quiet.

In the final part of Econ 163, roughly November 16 till December 9, you are going to write your own research paper based on everything you have learned in this class.

<u>Grading:</u>	Homeworks (best 3 out of 4)	10%
	Writing assignments (best 10 out of 12)	10%
	Presentation	10%
	2 midterms	30%
	Research paper (proposal, first draft, presentation, final draft)	30%
	Class attendance and participation	10%

So far, so good, but always make sure you read the small print:

The due dates for the homeworks are as follows: September 18, October 2, October 30, November 13 (all Fridays). Late homework will not be accepted. It is your responsibility to plan accordingly and submit your homework on or before the due date.

The writing assignments will be based on the chapters from Paul Blustein's books and on the papers you will present and discuss during the second segment of the class. Assignments should be typed, 1-2 pages long, and will be due in class only. I will not accept them before or after class, or over e-mail. In your writing assignment, you should suggest topics for classroom discussion. Do you have any disagreements with the author(s)? Anything that puzzles you? Any limitations, omissions, or loose ends? Any questions you would like to bring up in class – and perhaps possible answers to these questions?

You can skip 1 homework and 2 writing assignments without penalty. Use these freebies wisely – save them for illness, travel, job interviews, crunch in other classes, religious observances, or any other unanticipated emergency.

Together with a classmate, you will be responsible for presenting a paper and leading the discussion once during the second segment of the class. More detailed guidelines on the structure of the presentations will be provided later.

The two midterms will take place on October 7 and November 18 (both Wednesdays), during regular class time. There will be no alternate midterm dates. Both tests will be closed-book, closed-notes.

For the research paper, you will turn in a short proposal in class on November 2. You will present a first draft of your paper in class some time between November 16 and December 9. The first draft of your paper will be due by noon on the day before your class presentation. The final draft of your research paper will be due on Friday, December 18. More detailed guidelines on the research paper will be provided later.

Take a careful look at all dates listed above. Please enroll in this class only if you can reconcile them with your travel plans and other commitments.

This is a small discussion-based class, so class attendance is mandatory. I expect you to come to class on time at 1:15 pm sharp. I also expect you to demonstrate your command of the assigned readings, and to contribute questions as well as answers and ideas to the discussion. Your attendance and participation record will be reflected in your final grade for Econ 163.

Both the structure and the substance of this course are flexible. The syllabus is deliberately vague in order to deal with two sources of uncertainty – ultimate student enrollment and your preferences.

Finally, if you have a documented disability and wish to discuss academic accommodations, please contact me as soon as possible. To request academic accommodations due to a disability, please contact Dean Marcelle Holmes if you are a Pomona student. She can be contacted via e-mail at mdc04747@pomona.edu or at 909-607-2147. If you attend another one of the Claremont Colleges, please contact your home college's disability officer: Rochelle Brown (Pitzer), Jill Hawthorne (Scripps), Maggie Browning (Harvey Mudd), or Julia Strong (CMC).

Communication:

The course has a web page where I will post lots of good stuff. The address is:

<http://www.economics.pomona.edu/slavov/econ163>

Schedule of readings from Blustein's book:

Monday, September 7: Chapters 1-2 in The Chastening

Monday, September 14: Chapters 3-4 in The Chastening

Monday, September 21: Chapters 5-6-7 in The Chastening

Monday, September 28: Chapters 8-9 in The Chastening

Monday, October 5: Chapters 10-11 in The Chastening

Monday, October 12: Chapters 12-13 in The Chastening

TOPICS AND PAPERS

I. Financial fragility (“original sin” and “conflicted virtue”), balance sheet effects, fear of floating

Calvo, Guillermo, and Carmen Reinhart. Fixing for Your Life. NBER Working Paper 8006, November 2000.

Calvo, Guillermo, and Carmen Reinhart. “Fear of Floating.” Quarterly Journal of Economics 117 (2002): 379-408.

Eichengreen, Barry, and Ricardo Hausmann. Exchange Rates and Financial Fragility. NBER Working Paper 7418, November 1999.

Eichengreen, Barry, Ricardo Hausmann, and Ugo Panizza. Currency Mismatches, Debt Intolerance and Original Sin: Why They Are Not the Same and Why It Matters. NBER Working Paper 10036, October 2003.

Hausmann, Ricardo, Ugo Panizza, and Ernesto Stein. “Why Do Countries Float the Way They Float?” Journal of Development Economics 66 (2001): 387-414.

Krugman, Paul. “Analytical Afterthoughts on the Asian Crisis.” Available online at <http://web.mit.edu/krugman/www/MINICRIS.htm>, September 1999.

McKinnon, Ronald, and Gunther Schnabl. “The East Asian Dollar Standard, Fear of Floating, and Original Sin.” Review of Development Economics 8 (2004): 331-60.

McKinnon, Ronald, and Gunther Schnabl. “The Return to Soft Dollar Pegging in East Asia: Mitigating Conflicted Virtue.” International Finance 7 (2004): 169-201.

Reinhart, Carmen. “The Mirage of Floating Exchange Rates.” American Economic Review 90 (May 2000): 65-70.

II. Global imbalances, “the global saving glut” and “the revived Bretton Woods system” hypotheses

Blanchard, Olivier, and Francesco Giavazzi. “Current Account Deficits in the Euro Area: The End of the Feldstein-Horioka Puzzle?” Brookings Papers on Economic Activity 2002 (2002): 147-186.

Chinn, Menzie, and Hiro Ito. “What Matters for Financial Development? Capital Controls, Institutions, and Interactions.” Journal of Development Economics 81 (2006): 163-192.

Chinn, Menzie, and Hiro Ito. “Current Account Balances, Financial Development and Institutions: Assaying the World ‘Saving Glut.’” Journal of International Money and Finance 26 (2007): 546-569.

Chinn, Menzie, and Eswar Prasad. “Medium-Term Determinants of Current Accounts in Industrial and Developing Countries: An Empirical Exploration.” Journal of International Economics 59 (2003): 47-76.

Dominguez, Kathryn. International Reserves and Underdeveloped Capital Markets. Mimeo, September 2008.

Dooley, Michael, David Folkerts-Landau, and Peter Garber. “The Revived Bretton Woods System.” International Journal of Finance and Economics 9 (2004): 307-313.

Dooley, Michael, David Folkerts-Landau, and Peter Garber. Direct Investment, Rising Real Wages and the Absorption of Excess Labor in the Periphery. NBER Working Paper 10626, July 2004.

Dooley, Michael, David Folkerts-Landau, and Peter Garber. Savings Gluts and Interest Rates: the Missing Link to Europe. NBER Working Paper 11520, July 2005.

Edwards, Sebastian. “The U.S. Current Account Deficit: Gradual Correction or Abrupt Adjustment?” NBER Working Paper 12154, April 2006.

Eichengreen, Barry. Global Imbalances and the Lessons of Bretton Woods. NBER Working Paper 10497, May 2004.

Faruqee, Hamid, and Jaewoo Lee. Global Dispersion of Current Accounts: Is the Universe Expanding? Mimeo, April 2008.

Forbes, Kristen. “Why do Foreigners Invest in the United States?” Working Paper 2008-27, Federal Reserve Bank of San Francisco, October 2008.

Gruber, Joseph, and Steven Kamin. Explaining the Global Pattern of Current Account Imbalances. International Finance Discussion Paper 846, Board of Governors of the Federal Reserve System, November 2005.

Obstfeld, Maurice, and Kenneth Rogoff. The Unsustainable US Current Account Position Revisited. NBER Working Paper 10869, November 2004.

Roubini, Nouriel, and Brad Setser. Will the Bretton Woods 2 Regime Unravel Soon? The Risk of a Hard Landing in 2005-2006. Manuscript, New York University, February 2005.

Schnabl, Gunther, and Stephan Freitag. An Asymmetry Matrix in Global Current Accounts. Mimeo, January 2009.

III. Debates on purchasing power parity and exchange rate dynamics, empirical exchange rate models, exchange rate pass-through

Choudhri, Ehsan, and Dalia Hakura. Exchange Rate Pass-Through to Domestic Prices: Does the Inflationary Environment Matter? IMF Working Paper WP/01/194, December 2001.

Engel, Charles. "Accounting for U.S. real exchange rate changes." Journal of Political Economy 107 (1999): 507-538.

Evans, Martin, and Richard Lyons. "Order Flow and Exchange Rate Dynamics." Journal of Political Economy 110 (February 2002): 170-180.

Froot, Kenneth, and Kenneth Rogoff. Perspectives on PPP and Long-Run Real Exchange Rates. NBER Working Paper 4952, December 1994.

Gagnon, Joseph, and Jane Ihrig. "Monetary Policy and Exchange Rate Pass-Through." International Journal of Finance and Economics 9 (2004): 315-338.

Goldfajn, Ilan, and Sergio Werlang. The Pass-Through from Depreciation to Inflation: A Panel Study. Discussion Paper 243, Department of Economics, PUC-Rio (Pontificia Universidade Catolica do Rio de Janeiro), April 2000.

McCarthy, Jonathan. Pass-Through of Exchange Rates and Import Prices to Domestic Inflation in Some Industrialized Economies. Staff Report 111, Federal Reserve Bank of New York, September 2000.

Rogoff, Kenneth. "The Purchasing Power Parity Puzzle." Journal of Economic Literature 34 (1996): 647-668.

Rogoff, Kenneth. "Dornbusch's Overshooting Model After 25 years." IMF Staff Papers 49 (2002): 1-35.

Slavov, Slavi. "Does Monetary Integration Reduce Exchange Rate Pass-through?" The World Economy 31:12 (December 2008): 1599-1624.

Taylor, John. "Low Inflation, Pass-Through, and the Pricing Power of Firms." European Economic Review 44 (2000): 1389-1408.

IV. The role of the dollar in the international monetary system

Chinn, Menzie, and Jeffrey Frankel. Will the Euro Eventually Surpass the Dollar as Leading International Reserve Currency? NBER Working Paper 11510, August 2005.

Eichengreen, Barry. Sterling's Past, Dollar's Future: Historical Perspectives on Reserve Currency Competition. NBER Working Paper 11336, May 2005.

Goldberg, Linda, and Cedric Tille. Vehicle Currency Use in International Trade. NBER Working Paper 11127, February 2005.

V. International capital mobility, “sudden stops”

Alfaro, Laura, Sebnem Kalemli-Ozcan, and Vadym Volosovych. “Why Doesn’t Capital Flow from Rich to Poor Countries? An Empirical Investigation” The Review of Economics and Statistics 90:2 (May 2008): 347–368.

Calvo, Guillermo, Alejandro Izquierdo, and Ernesto Talvi. Sudden Stops, the Real Exchange Rate, and Fiscal Sustainability: Argentina’s Lessons. NBER Working Paper 9828, July 2003.

Feldstein, Martin, and Charles Horioka. “Domestic Saving and International Capital Flows.” The Economic Journal 90 (1980): 314-329.

Henry, Peter, and Diego Sasson. Capital Account Liberalization, Real Wages, and Productivity. NBER Working Paper 13880, March 2008.

Kaminsky, Graciela, Carmen Reinhart, and Carlos Vegh. When It Rains, It Pours: Procyclical Capital Flows and Macroeconomic Policies. NBER Working Paper 10780, September 2004.

Kose, Ayhan, Eswar Prasad, and Marco Terrones. “Does Openness to International Financial Flows Raise Productivity Growth?” Journal of International Money and Finance 28 (2009): 554-80.

Lucas, Robert. “Why Doesn’t Capital Flow from Rich to Poor Countries?” The American Economic Review 80 (May 1990): 92-96.

Prasad, Eswar, Raghuram Rajan, and Arvind Subramanian. Foreign Capital and Economic Growth. NBER Working Paper 13619, November 2007.

Prasad, Eswar, Raghuram Rajan, and Arvind Subramanian. “Patterns of International Capital Flows and Their Implications for Economic Development.” In Global Demographic Change: Economic Impacts and Policy Challenges, pp. 119-158.

Prasad, Eswar, Kenneth Rogoff, Shang-Jin Wei, and Ayhan Kose. Financial Globalization, Growth and Volatility in Developing Countries. NBER Working Paper 10942, December 2004.

Quinn, Dennis, and Hans-Joachim Voth. Free Flows, Limited Diversification: Explaining the Fall and Rise of Stock Market Correlations, 1890-2001. CEPR Discussion Papers 7013, October 2008.

Ranciere, Romain, Aaron Tornell, and Frank Westermann. “Decomposing the Effects of Financial Liberalization: Crises vs. Growth.” Journal of Banking & Finance 30 (2006): 3331–3348.

Reinhart, Carmen, and Kenneth Rogoff. “Serial Default and the ‘Paradox’ of Rich-to-Poor Capital Flows.” The American Economic Review 94 (May 2004): 53-58.

Rodrik, Dani, and Arvind Subramanian. “Why Did Financial Globalization Disappoint?”

VI. Garden-variety business cycles, currency and financial crises

Coffey, Niall, Warren Hrung, Hoai-Luu Nguyen, and Asani Sarkar. Capital Constraints, Counterparty Risk and Deviations from Covered Interest Rate Parity. Mimeo, July 2009.

Krugman, Paul. "What Happened to Asia?" Available online at <http://web.mit.edu/krugman/www/DISINTER.html>, January 1998.

Krugman, Paul. "Fire-sale FDI." Available online at <http://web.mit.edu/krugman/www/FIRESALE.htm>, February 1998.

Mauro, Paolo, Nathan Sussman, and Yishay Yafeh. "Emerging Market Spreads: Then versus Now." Quarterly Journal of Economics 117 (2002): 695-733.

McKinnon, Ronald, and Gunther Schnabl. "Synchronized Business Cycles in East Asia and Fluctuations in the Yen/Dollar Exchange Rate." World Economy 26 (2003): 1067-88.

Rodrik, Dani. Growth After the Crisis. Mimeo, May 2009.

Rogoff, Kenneth. "Oil and the Global Economy."

Slavov, Slavi. "Measuring and Modeling the Effects of G-3 Exchange Rate Fluctuations on Small Open Economies: A Natural Experiment." Economic Systems 32:3 (September 2008): 253-273.

Spilimbergo, Antonio, Steve Symansky, Olivier Blanchard, and Carlo Cottarelli. "Fiscal Policy for the Crisis." IMF Staff Position Note SPN/08/01, December 2008.

VII. Exchange rate regimes: anchor, float, or jump ship?

Bordo, Michael, and Hugh Rockoff. "The Gold Standard as a 'Good Housekeeping Seal of Approval.'" Journal of Economic History 56 (1996): 389-428.

Eichengreen, Barry, and Douglas Irwin. The Slide to Protectionism in the Great Depression: Who Succumbed and Why? NBER Working Paper 15142, July 2009.

Frankel, Jeffrey. The Estimated Effects of the Euro on Trade: Why Are They Below Historical Effects of Monetary Unions Among Smaller Countries? NBER Working Paper 14542, December 2008.

Frankel, Jeffrey, and Andrew Rose. "An Estimate of the Effect of Common Currencies on Trade and Income." Quarterly Journal of Economics 117 (2002): 437-466.

Ghosh, Atish, Marco Terrones, and Jeromin Zettelmeyer. Exchange Rate Regimes and External Adjustment: New Answers to an Old Debate. Mimeo, May 2008.

Husain, Aasim, Ashoka Mody, and Kenneth Rogoff. "Exchange Rate Regime Durability and Performance in Developing Versus Advanced Economies." Journal of Monetary Economics 52 (2005): 35–64.

Klein, Michael, and Jay Shambaugh. "Fixed Exchange Rates and Trade." Journal of International Economics 70 (2006): 359-83.

Rose, Andrew. "One Money, One Market: The Effect of Common Currencies on Trade." Economic Policy 30 (April 2000): 8-45.

Rose, Andrew. "A Stable International Monetary System Emerges: Inflation Targeting Is Bretton Woods, Reversed." Journal of International Money and Finance 26 (2007): 663-681.

Slavov, Slavi. "Do Common Currencies Facilitate the Net Flow of Capital among Countries?" Forthcoming in The North American Journal of Economics and Finance.

VIII. Stuff that simply would not fit anywhere

Engel, Charles, and John Rogers. "How Wide Is the Border?" American Economic Review 86 (1996): 1112-1125.

Obstfeld, Maurice, and Kenneth Rogoff. The Six Major Puzzles in International Macroeconomics: Is There a Common Cause? NBER Working Paper 7777, July 2000.

Stock, James, and Mark Watson. "Vector Autoregressions." Journal of Economic Perspectives 15:4 (Fall 2001): 101–115.