

Economics 232C — Spring 2003

International Macroeconomics

April 2, 2003

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Class Time:	TuTh 12:30pm - 1:50pm
Class Web Page:	econ.ucsd.edu/muendler/teach/03s/232c

1 Course Objectives

This course examines open-economy macroeconomics and international finance. Topics include theories of the exchange rate, foreign exchange regimes, current account adjustments, and international portfolio investments. The course investigates real and monetary explanations, and implications of international capital market integration.

2 Prerequisites

Instructor's consent.

3 Readings

Textbook: Obstfeld and Rogoff (1996)

Additional readings: Sarno and Taylor (2002), Obstfeld (1995), Obstfeld and Rogoff (2000b), Neely and Sarno (2002), Froot and Obstfeld (1991), Driffill and Sola (1998), Caballero and Krishnamurthy (2000), Diamond and Dybvig (1983), Obstfeld (1996), Morris and Shin (1998), Dornbusch (1976), Obstfeld and Rogoff (1995), Obstfeld and Rogoff (2000a)

The additional readings are available through the class web page (see link above) and the UCSD electronic library. They are also available as printed custom materials from AS Soft Reserves (copyright fees apply).

4 Problem Sets

There will be three problem sets, due on scheduled dates throughout the quarter. You are encouraged to work on the problems with your classmates. Your solutions to the problem sets will be checked (check/no check) but your performance on them does not become a formal part of the final grade.

5 Research Paper Proposal

You may choose to submit a research paper proposal as part of your course work. I strongly encourage this.

The detailed proposal should be 5 to 10 pages in length. A proposal includes a thorough review of the related literature, and a detailed outline of a theoretical model along with its conjectured implications *or* a detailed discussion of a data set and an estimation procedure along with its identifying assumptions. A draft of the paper proposal is due on May 23, 5:00pm and the final proposal is due on June 6, 5:00pm.

6 Assessment

There will be a final exam during finals week, but no midterm exam. The final exam will take 120 minutes (120 points). You have two options for your assessment.

1. You can take the final exam only (120 points; score multiplied by 5/3.)
2. You can choose to submit a detailed research paper proposal. (A draft of the paper proposal is due on May 23, 5:00pm and the final proposal is due on June 6, 5:00pm.) Under this option, the final paper proposal counts for 40 percent of your grade (80 points) and the final exam for 60 percent (120 points).

7 Class Schedule

I. Microfoundations of International Macroeconomics

1. **Tue, April 1:** Intertemporal Trade in a Small Open Economy
(Obstfeld and Rogoff 1996/Ch. 1)
2. **Thu, April 3:** Intertemporal Trade in a Two-Region World
(Obstfeld and Rogoff 1996/Ch. 1)
PROBLEM SET 1 OUT
3. **Tue, April 8:** Current Account Dynamics
(Obstfeld and Rogoff 1996/Ch. 2)

4. **Thu, April 10:** Firms, Investment and the Current Account
(Obstfeld and Rogoff 1996/Ch. 2)
5. **Tue, April 15:** The Real Exchange Rate, Nontraded Goods and Productivity
(Obstfeld and Rogoff 1996/Ch. 4; Sarno and Taylor 2002)
6. **Thu, April 17:** The Terms of Trade and International Specialization
(Obstfeld and Rogoff 1996/Ch. 4)
7. **Tue, April 22:** International Risk Sharing in a Small Open Economy
(Obstfeld and Rogoff 1996/Ch. 5)
PROBLEM SET 1 DUE
8. **Thu, April 24:** International Risk Sharing in a World Economy
(Obstfeld and Rogoff 1996/Ch. 5)
PROBLEM SET 2 OUT
9. **Tue, April 29:** Sovereign Risk and Incentive-Compatible Borrowing
(Obstfeld and Rogoff 1996/Ch. 6)
10. **Thu, May 1:** Sovereign Risk and Investment under Sanctions or Commitments
(Obstfeld and Rogoff 1996/Ch. 6)
11. **Tue, May 6:** International Macroeconomic Puzzles and Trade Frictions
(Obstfeld 1995, Obstfeld and Rogoff 2000b)

II. Monetary Foundations of International Macroeconomics

12. **Thu, May 8:** Exchange Rates under Flexible Prices
(Obstfeld and Rogoff 1996/Ch. 8; Neely and Sarno 2002)
13. **Tue, May 13:** Exchange Rates, Inflation and Bubbles
(Obstfeld and Rogoff 1996/Ch. 8; Froot and Obstfeld 1991, Driffill and Sola 1998)
PROBLEM SET 2 DUE
14. **Thu, May 15:** Dollarization, Currency Mismatch and “Original Sin”
(Obstfeld and Rogoff 1996/Ch. 8; Caballero and Krishnamurthy 2000)
PROBLEM SET 3 OUT
15. **Tue, May 20:** Exchange Rate Interventions and Currency Attacks
(Obstfeld and Rogoff 1996/Ch. 8; Diamond and Dybvig 1983)
16. **Thu, May 22:** Second- and Third-Generation Currency Attack Models
(Obstfeld 1996, Morris and Shin 1998)
- Fri, May 23:** DRAFT OF PAPER PROPOSAL DUE
17. **Tue, May 27:** Price Rigidities and Exchange Rate Overshooting
(Dornbusch 1976; Obstfeld and Rogoff 1996/Ch. 9)

18. Thu, May 29: Price Rigidities and World-Economy Redux
(Obstfeld and Rogoff 1996/Ch. 10; Obstfeld and Rogoff 1995)

19. Tue, June 3: Price Rigidities and Monetary Policy Transmission
(Obstfeld and Rogoff 1996/Ch. 10; Obstfeld and Rogoff 2000a)

Thu, June 5: Review session
PROBLEM SET 3 DUE

Fri, June 6: FINAL PAPER PROPOSAL DUE

Mon, June 9 (Finals Week), 12:00n to 2:50pm: FINAL EXAM. Room: Econ 300

References

- CABALLERO, R. J., AND A. KRISHNAMURTHY (2000): "Dollarization of Liabilities: Underinsurance and Domestic Financial Underdevelopment," *MIT Department of Economics Working Paper*, 00/14, forthcoming *Journal of Finance*.
- DIAMOND, D. W., AND P. H. DYBVIK (1983): "Bank Runs, Deposit Insurance, and Liquidity," *Journal of Political Economy*, 91(3), 401–19.
- DORNBUSCH, R. (1976): "Expectations and Exchange Rate Dynamics," *Journal of Political Economy*, 84(6), 1161–76.
- DRIFILL, J., AND M. SOLA (1998): "Intrinsic Bubbles and Regime-Switching," *Journal of Monetary Economics*, 42(2), 357–73.
- FROOT, K. A., AND M. OBSTFELD (1991): "Intrinsic Bubbles: The Case of Stock Prices," *American Economic Review*, 81(5), 1189–214.
- MORRIS, S., AND H. S. SHIN (1998): "Unique Equilibrium in a Model of Self-Fulfilling Currency Attacks," *American Economic Review*, 88(3), 587–97.
- NEELY, C. J., AND L. SARNO (2002): "How Well Do Monetary Fundamentals Forecast Exchange Rates?," *Federal Reserve Bank of St. Louis Review*, 84(5), 51–74.
- OBSTFELD, M. (1995): "International Capital Mobility in the 1990s," in *Understanding interdependence: The macroeconomics of the open economy*, ed. by P. B. Kenen, pp. 201–61. Princeton University Press, Princeton.
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- (1996): *Foundations of international macroeconomics*. MIT Press, Cambridge, MA and London.
- (2000a): "New Directions for Stochastic Open Economy Models," *Journal of International Economics*, 50(1), 117–53.
- (2000b): "The Six Major Puzzles in International Macroeconomics: Is There a Common Cause?," *NBER Working Paper*, 7777.
- SARNO, L., AND M. P. TAYLOR (2002): "Purchasing Power Parity and the Real Exchange Rate," *IMF Staff Papers*, 49(1), 65–105.