

# **ECO353: International Monetary Economics**

## **Syllabus and Course Requirements**

**Fall 2018**

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**McCosh Hall, Room Number 46**

**Monday and Wednesday, 11:00 am-12:20 pm**

**Contact Information for Instructor:**

Iqbal Zaidi; JRRB, Room A26; izaidi@princeton.edu  
Office Hours: Wednesday, 1:30-3:00 pm

**Contact Information for Preceptors:**

Anna Belonog, abelonog@princeton.edu  
Jose Luis Cruz Alvarez, jlca@princeton.edu

**Precepts and AI Office Hours:**

Anna Belonog/Jose Luis Cruz Alvarez  
Precept 1: Tuesday 10:00 - 10:50 am; Room JRRB A26  
Precept 2: Tuesday 12:30 - 1:20 pm; Room JRRB A26  
Precept 3: Thursday 9:00-9:50 am; Room JRRB A26  
Precept 4: Thursday 11:00 -11:50 am; Room JRRB A26

Office Hours: TBA

Anna Belonog:  
Jose Luis Cruz Alvarez: Tue 2:30-3:30 and Th 1:30-2:30

**Course Overview and Objectives:** This course presents the theory of international monetary economics and applies it toward gaining an understanding of current policy issues in macroeconomics, including monetary and fiscal policies in an open economy, global financial imbalances, exchange rates, economic growth, international capital flows, portfolio diversification across countries, choice of the exchange rate regime, balance of payment crises, sovereign debt, and monetary unions. We will study various theoretical frameworks to examine currency, bond and equity markets in an open economy, and the roles of investors and speculators in spot and forward markets. The insights provided by these theoretical frameworks will enable us to discuss a broad range of policy issues, and the course readings will include several empirical and policy papers.

A few of the specific questions we will answer are: What links business cycles across countries? Why are price differentials across countries so large and persistent? What are the benefits and costs of capital account liberalization and why trade in capital is not the same as trade in goods? What are the factors determining the large US current account deficits and why is capital flowing into the US? Why is there relatively little international diversification of portfolios, even among advanced economies? Why do countries peg, float or manage their exchange rates and why pegged exchange rate arrangements are likely to be more susceptible to speculative attacks? Why do emerging market economies experience periodic financial crises, with sharp drops in output, a collapsing exchange rate, and sudden outflows of capital? What should be the role for monetary policy when there are speculative attacks on the currency?

**Prerequisites:** Students should be familiar with intermediate microeconomics. Intermediate macroeconomics is not required, but would be useful. I will cover the key macroeconomic concepts in class, but in a manner that brings us to international applications quickly. The main overlap with macroeconomics will concern national income accounting and short-run macroeconomic stabilization (using an open economy version of “IS-LM”).

**Assignments and Grading:** There will be in-class exams (October 24 and December 12) and a short writing assignment, which will be due during the exam period. There will be no final during exam period. All exams are closed book. Details on the writing assignment will be posted on Blackboard. Make-up exams will not be offered. Please notify me or the preceptors of any potential conflicts regarding the exam dates within the first two weeks of the semester for the October exam, and before the fall break for the December exam. Any unexcused absence from the exam will result in a failing grade. Requests for re-grades of exams must be made within one week of the day exams are returned. Please be aware that your points and grade could go down during the regrading process. In computing the final grade, the exams will be weighted 35% each, the writing assignment 16%, and the problem sets 14%.

There will be 9 problem sets but I will drop the lowest two marks on the problem sets in calculating the grade, which means 7 problem sets worth two points each. There will be

no make-up problem sets, because it would appear that all of the contingencies are covered by dropping not one but two of the problem sets with the lowest marks. Problem sets will be posted on the Blackboard almost every Monday and are due in class the following Monday. The problem sets will be posted on 9/17, 9/24, 10/1, 10/8, 10/15, 11/5, 11/12, 11/26, and 12/3.

### **Attendance:**

Attending classes will help you keep up with the materials covered in the lectures. The textbook is not a substitute for the instructor. Students are responsible for all material presented and/or assigned in the class as well as any announcements made in the class.

**Web Page:** I will post lecture and reading materials, announcements, etc., on the Blackboard website.

**Course Outline:** Readings are listed below and additional readings will be posted on the Blackboard website. I try to incorporate current events and will post related newspaper and magazine articles during the semester. The textbook for the course is Feenstra and Taylor's International Macroeconomics, 4th edition (FT below). This is the macroeconomics half of their international economics textbook (excluding the trade chapters), and so if you have the full version, add 11 to the chapter numbers below. Using the 3rd edition is also acceptable, but if you obtain an old edition, you are responsible for checking with the 4th edition (at the library or from a friend) to make sure you do the correct homework problems. The text is meant to complement the class notes. You will not be responsible for material in the text that we do not cover in the class, and, similarly, you will be responsible for material covered in the class lectures that is not in the textbook. The "Additional Readings" are optional, and are listed for the student who wants to learn more about a topic, perhaps relating to the research work for the junior paper or the senior thesis.

The topics that will be covered in the course with a (rough) outline of the time line are the following:

### **Week 1: Nominal Exchange Rates--Parity Conditions**

\* FT Chapter 2.

#### Additional Readings:

1. Burnside, Craig (2012): <http://www.nber.org/papers/w17278> "Carry Trades and Risk", in Jessica James, Ian W. Marsh and Lucio Sarno, eds., *Handbook of Exchange Rates*, Hoboken: John Wiley & Sons, 2012.

2. Brunnermeier, Markus, Nagel, Stefan, and Lasse Pedersen. 2008.  
[http://www.princeton.edu/~markus/research/papers/carry\\_trades\\_currency\\_crashes.pdf](http://www.princeton.edu/~markus/research/papers/carry_trades_currency_crashes.pdf)  
 “Carry Trades and Currency Crashes.” National Bureau of Economic Research.
3. Engel, Charles, Nelson C. Mark, and Kenneth D. West (2007) “Exchange Rate Models Are Not as Bad as You Think,” *NBER Macroeconomics Annual 2007*, pp. 381-441. Link: [http://www.ssc.wisc.edu/~cengel/published\\_papers.htm](http://www.ssc.wisc.edu/~cengel/published_papers.htm).
4. Burnside, Craig, Martin Eichenbaum, and Sergio Rebelo (2011), “Carry Trade and Momentum in Currency Markets,” *Annual Review of Financial Economics*, Link: <http://arjournals.annualreviews.org/eprint/CdDwFbwREd8HNpdXPhKb/full/10.1146/annurev-financial-102710-144913>

## **Week 2: Real Exchange Rates**

\* FT Chapter 3

### Additional Readings:

1. Rogoff, Kenneth (1996) “The Purchasing Power Parity Puzzle,” *Journal of Economic Literature*, 34, pp. 647 -668. Link: <http://www.jstor.org/stable/2729217>.
2. Burstein, Ariel, Gopinath, Gita, 2013.  
[http://www.economics.harvard.edu/faculty/gopinath/files/prices\\_oct20\\_2012.pdf](http://www.economics.harvard.edu/faculty/gopinath/files/prices_oct20_2012.pdf)  
 “International Prices and Exchange Rates," Prepared for the *Handbook of International Economics*, Vol IV, edited by Gopinath, Helpman and Rogoff.

## **Week 3: Nominal Exchange Rates–Money, Inflation, and Equilibrium**

\* FT Chapter 4

### Additional Readings:

Rogoff, Kenneth “Dornbusch’s Overshooting Model After Twenty-Five Years,” *IMF Staff Papers*, Vol. 49, Special Issue, 2002, pp.1-35.

## **Week 4: Current Account Deficits and Balance of Payments Adjustment Problems**

\* FT Chapter 5

\* Summers, Lawrence, “The US Current Account Deficit and the Global Economy,” *Per Jacobsson Lecture*, International Monetary Fund, October 2004.

\* Eichengreen, Barry, “Global Imbalances: The New Economy, the Dark Matter, the Savvy Investor and the Standard Analysis,” March 2006.

<http://www.econ.berkeley.edu/~eichengr/matter.pdf>

\* Feldstein, Martin, “Resolving the Global Imbalance: The Dollar and the U.S. Saving Rate”, *Journal of Economic Perspectives*, 2008, Vol. 22, Issue 3, pp. 113–25.

<http://pubs.aeaweb.org/doi/pdfplus/10.1257/jep.22.3.113>

#### Additional Readings:

1. Gourinchas, Pierre-Olivier. 2008. <http://www.bcentral.cl/eng/studies/central-banking/pdf/v12/195-236.pdf> “Valuation Effects and External Adjustment: A Review.”

2. Maurice Obstfeld 2012 <http://www.nber.org/papers/w17877> Does the Current Account Still Matter? NBER wp 17877.

3. Obstfeld, Maurice, and Kenneth Rogoff (2005) “Global Current Account Imbalances and Exchange Rate Adjustment,” *Brookings Papers on Economic Activity*, No. 1 (2005), pp. 67 -123. Link: <http://www.jstor.org/stable/3805083>.

### **Weeks 5 and 6: Financial Globalization, Growth and International Capital Markets**

#### FT Chapter 6

Obstfeld, Maurice, “The Global Capital Market: Benefactor or Menace,” *Journal of Economic Perspectives*, Fall 1998, Vol. 12 (4), pp. 9-30.

\* Independent Evaluation Office, *IMF’s Approach to Capital Account Liberalization*, International Monetary Fund, 2005, pp. 9-15.

<http://www.ieso-imf.org/eval/complete/pdf/04202005/report.pdf>

#### Additional Readings:

1. Obstfeld, Maurice and Kenneth Rogoff. 2004. [http://elsa.berkeley.edu/~obstfeld/NBER\\_final.pdf](http://elsa.berkeley.edu/~obstfeld/NBER_final.pdf) “The Unsustainable US Current Account Position Revisited.” Working Paper.

2. Bernanke, Ben. March 2005.

<http://www.federalreserve.gov/boarddocs/speeches/2005/200503102/> “The Global Saving Glut and the U.S. Current Account Deficit.” Sandridge Lecture, Virginia Association of Economics }.

3. Maurice Obstfeld. 2007.

[http://emlab.berkeley.edu/~obstfeld/280c\\_sp07/commission.pdf](http://emlab.berkeley.edu/~obstfeld/280c_sp07/commission.pdf) “International Finance and Growth in Developing Countries: What Have We Learned?” mimeo, UC Berkeley.

## **Weeks 7 and 8: Open Economy Macroeconomics**

\* FT Chapter 7

### Additional Readings:

Obstfeld, Maurice and Kenneth Rogoff, "The Six Major Puzzles in International Macroeconomics: Is There a Common Cause?" *NBER Macro Annual*, 2000.

Clarida, R., Gali, J. (1994), "Sources of Real Exchange Rate Fluctuations: How Important Are Nominal Shocks?" NBER Working Papers Number 4658.

## **Weeks 9 and 10: Exchange Rate Regimes and Currency Crises**

\* FT Chapters 8 and 9

\* Independent Evaluation Office, *IMF and Recent Capital Account Crises: Indonesia, Korea, Brazil*, International Monetary Fund, 2005, pp. 1-24.  
<http://www.ieo-imf.org/eval/complete/pdf/07282003/all.pdf>

\*Independent Evaluation Office, *Evaluation of the Role of the IMF in Argentina, 1991–2001*, International Monetary Fund, 2004, pp. 8-16.  
<http://www.ieo-imf.org/eval/complete/pdf/07292004/report.pdf>

### Additional Reading:

Fischer, Stanley, "Exchange Rate Regimes: Is the Bipolar View Correct?" *Journal of Economic Perspectives*, Spring 2001, Vol 15, No. 2, pp. 3-24.

Calvo, Guillermo A., and Frederic S. Mishkin, "The Mirage of Exchange Rate Regimes for Emerging Market Countries," *Journal of Economic Perspectives*, Vol. 17, No. 4, Fall 2003.

## **Weeks 11 and 12: The Euro and the Recent Crisis**

\*FT Chapter 10

### Additional Readings:

\* Eichengreen, Barry, "Stress Test for the Euro," *Finance & Development*, June 2009, Volume 46, Number 2, pp. 19-21.

<http://www.imf.org/external/pubs/ft/fandd/2009/06/eichengr.htm>

\* Boughton, James M., "A New Bretton Woods?" *Finance and Development*, March 2009, Volume 46, Number 1.

Additional Readings:

1. Jay Shambaugh, 2012 "The Euro's Three Crises,"  
[http://www.brookings.edu/~media/Files/Programs/ES/BPEA/2012\\_spring\\_bpea\\_papers/2012\\_spring\\_BPEA\\_shambaugh.pdf](http://www.brookings.edu/~media/Files/Programs/ES/BPEA/2012_spring_bpea_papers/2012_spring_BPEA_shambaugh.pdf)
2. Martin Feldstein, 2013, "Coordination in the European Union,"  
<http://www.nber.org/papers/w18672> *NBER wp 18672*
3. Blanchard, Olivier. 2006. <http://econ-www.mit.edu/files/740> "Adjustment with the Euro: The Difficult Case of Portugal," mimeo, MIT.
4. Lane, Philip. 2006. <http://www.jstor.org/stable/30033683> "The Real Effects of European Monetary Union," *Journal of Economic Perspectives*, 20, 47 -66.
5. Alan Taylor, 2012. <http://www.nber.org/papers/w18672> "External Imbalances and Financial Crises", *NBER wp 18606*.
6. Silvana Tenreyro, J.M.C Santos Silva "Currency Unions in Prospect and Retrospect," *Annual Review of Economics*, Volume 2, September 2010, Pages 51 -74.
7. Reinhart, Carmen and Kenneth Rogoff, 2009, *This Time is Different*, Princeton University Press, Chapters 4 and 6.
8. Eichengreen, Barry, 2003, "Restructuring Sovereign Debt," *Journal of Economic Perspectives*, Vol. 17, No. 4, pp. 75-98.