

## **JUNIO 1 – JUNIO 12**

**Fechas:** Junio 1 a Junio 12 (incluye sábado 12 de junio)

**Horario:** Del 1 al 4 de junio de 2:00pm – 5:00pm

Del 8 al 11 de junio de 2:00pm – 6:00pm

El sábado 12 de junio de 8:00am - 11:30am

**Prerrequisitos:** Macroeconomía III, Microeconomía III, Sexto semestre

This course covers from the basic tools of open macro economic models to some of the most exciting questions we are facing today in this area. The course covers the material at a relatively high pace, and hence students are encouraged to reproduce some of the results by themselves.

The course is supposed to be self-explanatory and we only expect students to have some basic knowledge on international economics and calculus. We will first devote some time to study the basic models on financial crises and determination of the real exchange rate. Second, we will discuss the concept of purchasing power parity (PPP) and the recent discussion present in the literature. We will then proceed to study Brownian processes and Ito's Lemma so that we can understand an interesting and relevant topic in international economics which is contagion and global imbalances.

### ***Texts***

Maurice Obstfeld and Kenneth Rogoff, Foundations of International Macroeconomics, MIT Press, 1996 is an excellent background for many of the topics in this reading list.

### ***Course Requirements***

All students who take the course for credit must submit a short research proposal. The student has to pick one of the topics of the course and write a short research proposal that consists of two pages of literature review, a maximum of three pages describing the research question and finally a maximum of three pages describing the research strategy that would be adopted in order to be able to answer the proposed question. Class attendance and participation are essential.

### ***Outline of the course***

The following outline gives a guide to the material that will be covered in the course. Updates to this outline may be given during class. Lectures are indicative: we may well find that some topics require more (or less) time to cover. The emphasis of the course is on financial markets and their imperfections. We will start with the foundations and gradually build in context.

## Outline

### ***Basic tools of open macro economics: Intertemporal approach to the current account (2 lectures)***

- \* Obstfeld, Maurice, and Kenneth Rogoff. 1995. "The Intertemporal Approach to the Current Account." In Handbook of International Economics, vol. 3, Gene M. Grossman and Kenneth Rogoff, eds. (Amsterdam: Elsevier). Chapter 34, pp. 1731-1799. Earlier version published as NBER working paper no. 4893.
- \* Engel, Charles, and John H. Rogers. 2006. "The U.S. Current Account Deficit and the Expected Share of World Output." Journal of Monetary Economics, vol. 53, no. 5, July 2006, pp. 1053-1093.
- \* Perri Fabrizio and Vincenzo Quadrini "International recessions" WP.

### ***Real Exchange Rate Puzzle (1 Lecture)***

- \* Engel, Charles. 1993. "Real Exchange Rates and Relative Prices: An Empirical Investigation." Journal of Monetary Economics, vol. 32, no. 1, August 1993, pp. 35-50.
- Engel, Charles, and John H. Rogers. 1996. "How Wide is the Border?" American Economic Review, vol. 86, no. 5, December 1996, pp. 1112-1125.
- Canzoneri, Matthew B.; Robert E. Cumby; Behzad Diba. 1999. "Relative Labor Productivity and the Real Exchange Rate in the Long Run: Evidence from a Panel of OECD Countries." Journal of International Economics, vol. 47, no. 2, April 1999, pp. 245-266.
- Engel, Charles. 1999. "Accounting for U.S. Real Exchange Rate Changes." Journal of Political Economy, vol. 107, no. 3, June 1999, pp. 507-538.
- Burstein, Ariel; Martin Eichenbaum; Sergio Rebelo. 2005. "Large Devaluations and the Real Exchange Rate." Journal of Political Economy, vol. 113, no. 4, August 2005, pp. 742-784.
- Corsetti, Giancarlo, and Luca Dedola. 2005. "A Macroeconomic Model of International Price Discrimination." Journal of International Economics, vol. 67, no. 1, pp. 129-155.
- Atkeson, Andrew, and Ariel Burstein. 2008. "Trade Costs, Pricing to Market, and International Relative Prices." American Economic Review vol. 98, no. 5, December 2008, pp. 1998-2031.

### ***Monetary Exchange Rate Models (1 Lecture)***

- \* Dornbusch, Rudiger. 1976. "Expectations and Exchange Rate Dynamics." Journal of Political Economy, vol. 84, no. 6, December 1976, pp. 1161-1176.
- \* Meese, Richard, and Kenneth Rogoff. 1983. "Empirical Exchange Rate Models of the Seventies: Do They Fit Out of Sample?" Journal of International Economics, vol. 14, no. 1-2, February 1983, pp. 3-24.
- Engel, Charles, and Jeffrey Frankel, 1984. "Why Interest Rates React to Money Announcements: An Explanation from the Foreign Exchange Market." Journal of Monetary Economics, vol. 13, no. 1, pp. 31-39.
- Mark, Nelson C. 1995. "Exchange Rates and Fundamentals: Evidence on Long-Horizon Predictability." American Economic Review, vol. 85, no. 1, March 1985, pp. 201-218.
- Mark, Nelson C., and Donggyu Sul. 2001. "Nominal Exchange Rates and Monetary Fundamentals: Evidence from a Small Post-Bretton Woods Sample." Journal of International Economics, vol. 53, no. 1, February 2001, pp. 29-52.

- Engel, Charles, and Kenneth D. West. 2005. "Exchange Rates and Fundamentals." *Journal of Political Economy*, vol. 113, no. 3, June 2005, pp. 485-517.
- Bacchetta, Philippe, and Eric van Wincoop. 2006. "Can Information Heterogeneity Explain the Exchange Rate Determination Puzzle?" *American Economic Review*, vol. 96, no. 3, June 2006, pp. 552-576.
- Engel, Charles, and Kenneth D. West, 2006. "Taylor Rules and the Deutschmark-Dollar Real Exchange Rate." *Journal of Money, Credit and Banking*, vol. 38, no. 5, August 2006, pp. 1175-1194.
- Clarida, Richard, and Daniel Waldman, 2008. "Is Bad News about Inflation Good News for the Exchange Rate?" In John Y. Campbell, ed., *Asset Prices and Monetary Policy* (University of Chicago Press), pp. 371-396.

### ***Purchasing Power Parity Puzzle (2 Lectures)***

- \* Lecture Notes
- \* Rogoff, Kenneth. 1996. "The Purchasing Power Parity Puzzle." *Journal of Economic Literature*, vol. 34, no. 2, pp. 647-668.
- \* Imbs, Jean; Haroon Mumtaz; Morten O. Ravn; and, Helene Rey. 2005. "PPP Strikes Back. Aggregation and the Real Exchange Rate." *Quarterly Journal of Economics*, vol. 120, no. 1, February 2005, pp. 1-43.
- \* Rogoff, K. (1996): "The Purchasing Power Parity Puzzle," *Journal of Economic Literature*, 34, 647-668.
- Chen, S. and C. Engel, 2004. "Does Aggregation Bias Explain the PPP Puzzle", NBER WP No.10304.
- Engel, Charles, 2000, "Long Run PPP May Not Hold After All." *Journal of International Economics*, vol. 51, no. 2, August 2000, pp. 243-273.
- Taylor, Mark P.; David A. Peel; and, Lucio Sarno. 2001. "Nonlinear Mean Reversion in Real Exchange Rates: Towards a Solution to the Purchasing Power Parity Puzzles," *International Economic Review*, vol. 42, no. 4, November 2001, pp. 1015-1042.

### ***International Asset Pricing (2 lectures)***

#### **Traditional International Asset Prices**

- \* Lecture notes
- \* Obstfeld and Rogoff, Chapter 5.
- Cole, H. and M. Obstfeld, 1991. "Commodity Trade and International Risk Sharing: How much do Financial Markets Matter?" *Journal of Monetary Economics* 28, pp. 3-24, August.
- Lucas, R (1982) "Interest Rates and Currency Prices in a Two-Country World," *Journal of Monetary Economics*, 10, 335-359.
- Helpman, E., and A. Razin (1978): *A Theory of International Trade under Uncertainty*. Academic Press, San Diego. Chapter 13.
- Zapatero, F. (1995): "Equilibrium Asset Prices and Exchange Rates" *Journal of Economic Dynamics and Control*, 19, 787-811.

#### **Stochastic Open Economy Models**

- \* Pavlova Anna and Roberto Rigobon 2007 "Asset Prices and Exchange Rates," *Review of Financial Studies*, forthcoming.

- Obstfeld, M., and K. Rogoff (2000): “New Directions for Stochastic Open Economy Models,” *Journal of International Economics*, 50, 117-153.

### **Home Bias**

- \* Baxter, M. and U. Jermann, 1997. “The International Diversification Puzzle Is Worse Than You Think”, *American Economic Review* 87 (1), pp. 170-180.
- Coeurdacier, N., 2005. “Do trade costs in goods markets lead to home bias in equities?” Paris-Jourdan Sciences Economiques mimeo.
- Heathcote, J. and F. Perri, 2004. “The International Diversification Puzzle is not as bad as you think”, mimeo, University of Minnesota.
- Arellano, C., 2007 "Default Risk and Income Fluctuations in Emerging Economies," forthcoming, *American Economic Review*.
- Bottazzi, L., P. Pesenti, and E. van Wincoop, 1996. “Wages, Profits and the International Portfolio Puzzle,” *European Economic Review* 40 (2), pp. 219-254.
- Corsetti, G., L. Dedola, and S. Leduc, 2004. “International Risk-Sharing and The Transmission of Productivity Shocks”, *European Central Bank WP No. 308*, also *International Finance Discussion Papers 826*, Board of Governors of the Federal Reserve System, 2005.
- Kehoe, P. and F. Perri, 2002. “International Business Cycles with Endogenous Incomplete Markets”, *Econometrica* 70, pp. 907-928, May.
- Pesenti, P. and E. van Wincoop, 2002. “Can Nontradables Generate Substantial Home Bias?” *Journal of Money, Credit and Banking* 34 (1), pp. 25-50.
- Veldkamp, L. and S. Van Nieuwerberg, 2007. “Information Immobility and the Home Bias Puzzle”, NYU Stern mimeo.
- Martin, P. and H. Rey, 2000. “Financial Integration and Asset Returns”, *European Economic Review* 44, pp. 1327-1350.
- Martin, P. and H. Rey, 2001. “Financial Supermarkets: Size Matters for Asset Trade”, *Journal of International Economics* 64(2), pp. 335-361.
- De Marzo, P., Ron Kaniel, and Ilan Kremer, 2004. “Diversification as a Public Good: Community Effects in Portfolio Choice”, *Journal of Finance* 59, pp. 1677-1715.

## ***Contagion and Portfolio Constraints (1 Lecture)***

### **Basic explanations of contagion**

- \* Gerlach, S. and Smets, F. (1995). Contagious speculative attacks. *European Journal of Political Economy*, 11:45—63.
- Drazen, A. (1998). Political contagion in currency crisis. University of Maryland Mimeo.
- Masson, P. (1997). Monsoonal effects, spillovers, and contagion. IMF Mimeo

### **Empirical**

- \* Dungey, M. and Martin, V. L. (2001). Contagion across financial markets: An empirical assessment. Australian National University Mimeo.
- Eichengreen, B., Rose, A., and Wyplosz, C. (1996). Contagious currency crises. NBER Working Paper 5681.
- Forbes, K. and R. Rigobon “No Contagion, Only Interdependence: Measuring Stock Market Co-movements”, *Journal of Finance*, Volume 57, Number 5, October, PP 2223-2261, 2002.

### **New theories and structural estimation**

- \* Pavlova, Anna and Roberto Rigobon 2007. “The Role of Portfolio Constraints in the International Propagation of Shocks” Review of Economics Studies

### ***Price Stickiness (1 Lecture)***

- \* Alvarez Fernando, Francesco, and Luigi Paciello “Optimal price setting with observation and menu costs” WP
- Woodford, Michael ““Information-Constrained State-Dependent Pricing,” April 2008, revised June 2009
- Atkeson, A. and A. Burstein, 2007. “Trade Costs, Pricing to Market, and International Relative Prices”, UCLA mimeo. (paper)
- Dornbusch, R., 1987. “Exchange Rates and Prices”, American Economic Review 77 (1), pp. 93 – 106, March. (paper)
- \* Gopinath, G. and R. Rigobon “Sticky Borders” Quarterly Journal of Economics, forthcoming. (paper)
- \* Gopinath, G. O. Itskhoki, and R. Rigobon “Pass-Through at the Dock” MIT mimeo. (paper)
- Krugman, P., 1986. “Pricing to Market When the Exchange Rate Changes”, NBER WP No. 1926. Also in S. Arndt and J.D. Richardson (eds.) Real-Financial Linkages among Open Economies. Cambridge, Mass. MIT Press (1993). (paper)
- \* Cavallo, Alberto "Scraped Data and Sticky Prices: Frequency, Hazards, and Synchronization", November 2009

### **NOTA:**

La nota definitiva se aproximará al múltiplo de 0.5 más cercano de acuerdo a la siguiente regla: 2.75 a 3.24 = 3.0; 3.25 a 3.74 = 3.5, etc.

**Fecha de retiro:** El estudiante podrá retirar el curso, sin devolución, hasta un día hábil antes de la fecha de entrega del documento final.