Course Overview

The area of international macroeconomics is one of the most active in macroeconomics. This course surveys some of the recent developments in the field. The course will focus both on “real” (i.e., non-monetary) and monetary open-economy macro models. There will be three main sources of required readings:


We will also refer to the following book for certain topics:


In addition, there will be a set of assigned readings for each topic we will discuss.

Course Requirements

Your final grade will be determined by three factors: (i) Presentation of an assigned article in class, (ii) your participation in class discussions, and (iii) a take-home final examination. The class paper-presentation will carry a weight of 40 percent, discussion and participation will fetch you up to 10 percent, and the take-home final examination will have a weight of 50 percent. The details and requirements for each of the above categories will be described in class.
Course Outline and Required Readings

Approximately, the first half of the course covers “real” (i.e., non-monetary) open-economy macro models. For that section of the course, Obstfeld and Rogoff (henceforth referred to as “OR”) is the primary text and Nelson Mark (henceforth referred to as “NM”) is supplementary. The second half of the course deals with monetary models. Nelson Mark is primary and Obstfeld-Rogoff supplementary for that section. The readings assigned from these two books (on this syllabus) are required. You are also encouraged to read as many of the “additional readings” listed below as you can.

1. Dynamics of Small Open Economies: OR 1.1-1.3, 2.1-2.3; NM 1.2

2. The Real Exchange Rate: OR 4.1-4.2; NM 7

3. Uncertainty and International financial markets: OR 5.1-5.5

4. MonetaryExchange Rate Models: M 1.1, 1.3, 3; OR 8.2-8.3

5. The Lucas Model: M 4; OR 8.7

6. Foreign Exchange Market Efficiency: M 6; OR 8.7

7. The Mundell-Fleming Model: M 8; OR 9.1-9.4

8. New Open-Economy Macroeconomics: M 9; OR 10.1

9. Balance-of-Payments Crises: M 11; OR 8.4

10. Sovereign Risk: OR 6.1

11. Growth in Open Economies: OR 7.1-7.3

12. International Real Business Cycle Models: OR 7.4; M 5
Additional Readings

Dynamics of Small Open Economies

This paper is discussed in Obstfeld and Rogoff in section 2.3.

This paper is much cited and discussed.

This is an excellent survey, with lots more citations.

Chapters 2 and 3 lay out the basic dynamics of small open economies.

The Real Exchange Rate


Several other interesting papers can be found in this October 1994 special issue on the Balassa-Samuelson model in the Review of International Economics.


This paper has a different view from the first two cited above.


Uncertainty and Financial Markets

Here are a few papers that construct international models with complete markets, and discuss the correlation of consumption and output.


Devereux, Michael B.; Allan Gregory; and Gregor W. Smith, 1992, Realistic cross-country consumption correlations in a two-country equilibrium business-cycle model, Journal of International Money and Finance 11, 3-16.


This paper shows how restricted asset markets can help explain consumption and output correlations.

Here are a couple of papers that try to explain the countercyclical movement of the trade balance:


*This is an empirical study of the consumption and income correlation puzzle.*

*A lot of the insights about international asset pricing stem from this seminal paper, which we will return to later in the semester.*

*Here are some empirical papers that document the home bias in asset holdings:*


*This is a good survey of the home-bias puzzle.*

Lewis, Karen K., 1999, Trying to explain home bias in equities and consumption, *Journal of Economic Literature* 37, 571-608. 
*This paper connects the home-bias puzzle and the consumption-correlation puzzle.*

*This paper offers a potential explanation for several of the above puzzles.*

**Monetary Exchange Rate Models**

*These two articles are two of the earliest that model the exchange rate in a monetary, rational expectations environment (assuming flexible goods prices):*


*This paper models money demand in a cash-in-advance framework. (We have already encountered this paper in our discussion of complete markets.)*

This paper investigates why we have exchange rates and multiple currencies:


These papers offer some empirical support for the monetary models in the long run:


This is a survey of empirical work on exchange rates:


This paper summarizes current exchange-rate arrangements and discusses the sense in which “fixed” exchange rates don’t really exist:


See also the papers from the recent exchange-rate conference in Madison, Wisconsin:

http://www.ssc.wisc.edu/~cengel/ExchangeRateConference/manuscripts.htm
International Finance and the Foreign-Exchange Risk Premium

The following are some of the papers that examine the bias in the forward exchange-rate forecast:


Two surveys of this area are:


Here are some papers that examine the foreign exchange risk premium in a general equilibrium setting:


The Mundell-Fleming Model

*These are the classic articles on the Mundell-Fleming-Dornbusch model:*


Dornbusch, R., 1976, Expectations and Exchange Rate Dynamics. *Journal of Political Economy* 84(6), 1161-76.


Some papers that extended the Dornbusch framework are:


Empirical examinations of the Dornbusch model:


*Empirical evidence on price stickiness:*


*Some other empirical papers:*


**New Open Economy Macroeconomics**


Betts, Caroline, and Michael B. Devereux, 2000, Exchange rate dynamics in a model of pricing to market, *Journal of International Economics* 50, 215-244.

Chari, V.V.; Patrick J. Kehoe; and, Ellen R. McGrattan, 2000, Can sticky price models generate volatile and persistent real exchange rates?, *NBER working paper* no. 7869.


Balance of Payments Crises (1st and 2nd generation):

These are the basic readings on balance-of-payments-crises:


Obstfeld, Maurice, 1984, Balance of payments crises and devaluation, *Journal of Money, Credit and Banking* 16, 208-217.


Some other papers:


Sovereign Risk

Here are four influential papers:


Two excellent surveys are:


Growth in a Small Open Economy


International Real Business Cycle Models
