Macroeconomics In Open Economies:
Course Readings and Outline

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The readings below are intended to give a representative flavor of the field, and hence have a certain bias towards integrative survey pieces rather than the original articles. The references in the surveys are excellent starting points for a more in-depth perusal of some issues. Required readings are marked with an *. Note: it may be possible to print out NBER working papers from the NBER website (www.nber.org) . In addition, lecture notes will summarize some of the debates.

Textbooks

Graduate:
Obstfeld and Rogoff, Foundations of International Macroeconomics, MIT Press, 1996
Intermediate:
Larrain and Sachs, Macroeconomics in the Global Economy, Prentice Hall.
Policy Focused:
Dornbusch, Policymaking in the Open Economy, World Bank/EDI
Financial Markets Focused:
Levich, International Financial Markets, Irwin-McGraw Hill

Up to Date Backgrounds
Latest issue of the **World Economic Outlook** (WEO) published by the IMF
Latest issue of **Global Development Finance** (GDF) published by the World Bank

Part I: Preliminaries: Concepts and History

We will begin by reviewing some of the key concepts. Much of the progress of international economics reflects concerns with particular (recurring) historical puzzles - from the resumption of the gold standard after the first world war to the debt crisis to attacks on fixed exchange rate regimes. A familiarity with the broad strokes of monetary history often comes in rather useful in understanding where the field has come from and where it is heading.

(*) Eichengreen, Barry (1994); "History Of The International Monetary System"; Chapter 6 in Rick van der Ploeg (ed.) The Handbook of International Macroeconomics

Dornbusch, Rudiger (1980); Open Economy Macroeconomics; Chapter 2. [Or another capsule summaries of definitions and concepts in an advanced textbooks]

IMF, World Economic Outlook.

Part II: Core Topics

II.A. The Current Account

The time path of external balances has long been one of the key concerns of international macroeconomics. We will look at the current account from a number of angles. We begin with a simple one good representative agent infinite horizon model, then allow for capital accumulation, and for terms of trade movements, next turn to some recent work abandoning the assumption of the representative agent and conclude with a look at the evidence. The readings are arranged in this order. The readings exhibit substantial overlap.

1. Theory

(*) Obstfeld, Maurice and Andrew Rose (1996); "The Intertemporal Approach To The Current Account"; in Gene Grossman and Kenneth Rogoff (eds) Handbook of International Economics; Vol. 3.

Obstfeld, Maurice and Kenneth Rogoff (1996); Foundations of International Macroeconomics; MIT Press, Chapters 1-2.

Frenkel, J. And A. Razin (1996); Fiscal Policies In The World Economy; 3rd edition, MIT Press, Chapter 4.

Sen, Partha (1994); "Savings, Investment, and the Current Account"; Chapter 15 in Rick van der Ploeg (ed.) The Handbook of International Macroeconomics

2. Evidence

(*) James Nason and John Rogers, 2003, “The Present-Value Model of the Current Account Has Been Rejected: Round Up The Usual Suspects”; Federal Reserve Board International finance Discussion Paper No. 760, February 2003.

Glick Reuven and Kenneth Rogoff (1995); "Global Versus Country Specific Productivity Shocks and the Current Account”; Journal of Monetary Economics.

Lewis, Karen (1996); "Puzzles in International Financial Markets”; in Gene Grossman and Kenneth Rogoff (eds) Handbook of International Economics; Vol. 3.

Backus, David and Patrick Kehoe (1992); "International Evidence On The Historical Properties of Business Cycles”; American Economic Review; September.

Freund, Caroline (2000); “Current Account Adjustment in Industrialized Countries” International Finance Discussion paper No. 692, Federal Reserve Board.

Baxter, Marianne and Mario Crucini (1991); "Explaining Savings-Investment Correlations"; American Economic Review; September.

Lane, Philip (1998); "Do International Investment Income Flows Smooth Income?"; Mimeo (on his website http://www.economics.tcd.ie/plane/

3. External Debt and Long Run Issues

(*) Eaton, Jonathan and Raquel Fernandez (1996); "Sovereign Debt"; in Gene Grossman and Kenneth Rogoff (eds) Handbook of International Economics; Vol. 3.

Phillip Lane and Gian Maria Milesi-Ferretti, 2002, "External Wealth, the Trade Balance and the Real Exchange Rate", European Economic Review, Vol. 46: 6: June: 1049-1072.

Obstfeld, Maurice and Kenneth Rogoff (1996); Foundations of International Macroeconomics; MIT Press, Chapter 7.

II.B. Exchange Rates

The determination of nominal and real exchange rates, and their linkages with economic activity, provides the second mainstay of international macroeconomics. Thinking about exchange rates has evolved considerably over the last two decades, and we will briefly touch on all the major schools of thought. The readings are again in rough chronological order.

1. Theory

(*) Obstfeld, Maurice and Kenneth Rogoff (1996); Foundations of International Macroeconomics; MIT Press, Chapter 8 and 9.

Dornbusch, Rudiger (1976); "Expectations and Exchange Rate Dynamics"; Journal of Political Economy; 84:6: 1161-76.

Stockman, Alan (1980); "A Theory of Exchange Rate Determination"; Journal of Political Economy; 88:41.

Grilli, Vittorio and Nouriel Roubini (1995); "Liquidity and Exchange Rates"; NBER Working Paper No. 5313.

Gourinchas, P. and Aaron Tornell (1996); "Exchange Rate Dynamics and Learning"; NBER Working Paper No. 5530.

2. Empirical Evidence

(*) Frankel, Jeffrey and Andrew Rose (1996); "Empirical Research on Nominal Exchange Rates"; in Gene Grossman and Kenneth Rogoff (eds) Handbook of International Economics; Vol. 3.

De Vries, Casper (1994); "Stylized Facts of Nominal Exchange Rate Returns"; Chapter 11 in Rick van der Ploeg (ed.) The Handbook of International Macroeconomics

Levich, Richard (1998), International Financial Markets, Chapters 3-8.

2.A Expectations

Chinn, Menzie and Jeffrey Frankel (1994); "Patterns of Exchange Rate Forecasts For 25 Currencies"; Journal of Money, Credit and Banking; 26.

2.B Specific Models

(*) Froot, Kenneth and Kenneth Rogoff (1995); "Perspectives on PPP and Long Run Real Exchange Rates"; in Gene Grossman and Kenneth Rogoff (eds.) Handbook of International Economics; Vol. 3.

(*) Taylor, Mark (1995); "The Economics of Exchange Rates"; Journal of Economic Literature; March, pp. 13-47.

Froot, Kenneth and Richard Thaler (1990); "Anomalies: Foreign Exchange"; Journal of Economic Perspectives; Summer.

Clarida, Richard and Jordi Gali (1994); "Sources of Real Exchange Rate Fluctuations"; NBER Working Paper No. 4658.

John Rogers (2001); "Price Level Convergence, Relative Prices and Inflation in Europe"; International Finance Discussion Papers No. 699, Fed Board.

Lyons, Richard (1993); "Tests of Microstructural Hypothesis In The Foreign Exchange Market"; NBER Working Paper No. 4471.

2.C. State of Affairs

(*) Cheung, Yin-Wong, Menzie Chinn and Antonio Garcia Pascual, 2002, "Empirical Exchange Rate Models of the Nineties: Are Any Fit to Survive?"; NBER Working Paper No. 9393, December 2003.

Jerome L. Stein, 2001, "The Equilibrium Value of the Euro/$ Exchange Rate: An Evaluation of Research", CESifo Working Paper No. 525.

II.C. Pricing In Open Economies

Closely linked to the behavior of nominal exchange rates is the behavior of prices of traded goods. The apparently lackluster response of such prices to exchange rate movements (or "imperfect passthrough") has attracted particular attention, partly because of the implied consequences for current account adjustments.

1. Theory

Delgado, Francisco (1991); "Hysteresis, menu costs, and pricing with random exchange rates"; Journal of Monetary Economics; 28, 461-84.

Dornbusch, Rudiger (1987); "Exchange Rates and Prices"; American Economic Review; March, 93-106.

Philippe Bacchetta and Eric van Wincoop, 2002, "Why Do Consumer Prices React Less Than Import Prices To Exchange Rates?", NBER Working Paper No. 9352, November 2002.

Dixit, Avinash (1989); "Hysteresis, Import Penetration and Exchange Rate Passthrough"; Quarterly Journal of Economics; May, 205-28.

Froot, Kenneth and Paul Klemperer (1989); "Exchange Rate Pass-Through When Market Share Matters"; American Economic Review, September, 79:637-654.

Kasa, Kenneth (1992); "Adjustment Costs and Pricing-to-Market: Theory and Evidence"; Journal of International Economics; February, 1-27.

2. Evidence

(*) Goldberg, Pinelopi and Michael Knetter (1997); "Goods Prices And Exchange Rates"; Journal of Economic Literature; 35:1243-72, September.

Jose Campa and Linda Goldberg, 2002, “Exchange Rate Passthrough Into Import Prices: A Macro or Micro Phenomenon?”, NBER Working Paper No. 8934, May 2002.

Knetter, Michael (1993); “International Comparisons of Pricing-to-Market Behavior”; American Economic Review, 83: 473-486.

Jonathan Haskel and Holger Wolf “(Why) Does the Law of One Price Fail?”, Scandinavian Journal of Economivds.

Feenstra, Robert, Joseph Gagnon and Michael Knetter (1996); “Market Share and Exchange Rate Pass-Through in World-Automobile Trade”; Journal of International Economics; 40:187-207, February.

3. Consequences

Obstfeld, Maurice, 2002, “ Exchange Rates and Adjustment: Perspectives from the New Open Economy Macroeconomics”, NBER Working Paper No. 9118.

II.D. Exchange Rate Regimes

The role of the nominal exchange rate regime is the third of the perennial topics in international macroeconomics, going back a few centuries. Two key questions are examined in this literature. First, does the choice of the nominal regime make a difference in terms of real variables, and hence welfare? Second, why are pegged regimes so hard to sustain? We will look at both issues.

Properties and Tradeoffs

(*) Svensson, Lars (1993); "Fixed Exchange Rates As A Means Of Price Stability: What Have We Learned?”; NBER Working Paper No. 4504.

(*) Fischer, Stanley (2001); "Exchange Rate Regimes"; Is the Bipolar View Correct?"; IMF.

Felipe Larrain and Andres Velasco, 2000, Exchange Rate Arrangements for Emerging Market Economies, Group of Thirty Occasional Paper No. 60.

Ghosh, Atish, Anne-Marie Gulde and Holger Wolf, Exchange Rate Regimes, MIT Press, 2003.

Obstfeld, Maurice and Kenneth Rogoff (1996); Foundations of International Macroeconomics; MIT Press, Chapter 8.4, 9.4, 10.1.

Identification

(*) Calvo, Guillermo and Carmen Reinhart, “Fear of Floating”, Quarterly Journal of Economics, 117: 2: May: 2002: pp 379-408.

Frankel, J., E. Fajnzylber, S. Schmukler and L. Servén, „Veryfying Exchange Rate Regimes“, Journal of Development Economics, 66: 2: 2001: December: 351-386.

Evidence

(*) Sebastian Edwards and Miguel Savastano, 1999, “Exchange Rates in Emerging Economies: What Do We Know? What Do We Need To Know?”, NBER Working Paper No. 7228, July 1999.

Frankel, Jeffrey, Sergio Schmukler and Luis Servén, „Global Transmission of Interest Rates“; NBER Working Paper No. 8828, March 2002.

Flood, Robert and Andrew Rose (1993); "Fixing Exchange Rates”; NBER Working Paper No. 4503.

Glick, Reuven and Andrew Glick, 2002, “Does a Currency Union Affect Trade?”; European Economic Review, 46:6: June: 1125-1151. Also read the preceeding article by Thom and Walsh.

Ghosh, Atish, Anne-Marie Gulde and Holger Wolf, Exchange Rate Regimes, MIT Press, 2003.

Mussa, Michael (1987); "Nominal Exchange Rate Regimes and the Behavior Of Real Exchange Rates”; Carnegie-Rochester Conference Series on Public Policy; No. 25.

Obstfeld, Maurice and Kenneth Rogoff (1995); "The Mirage Of Fixed Exchange Rates”; NBER Working Paper No. 5191.

Special Cases

Anne-Marie Gulde, Atish Ghosh and Holger Wolf (2000); “Currency Boards: More Than a Quick Fix”; *Economic Policy*, October 2000, 271-335.

Alberto Alesina, Robert Barro and Silvana Tenreyro, 2002, “Optimal Currency Areas”, NBER Working Paper No. 9072, July 2002.

The EURO Homepage: http://www.econ.yale.edu/~corsetti/euro/Euroit.html
(Peruse, content is changing)

Eduardo Levy-Yeyati and Federico Sturzenegger (eds.) , 2002, Dollarization, MIT Press.

II.E. Asset Markets

The frequency and rapid spread of financial crisis has placed the international linkage of asset markets into the forefront of research over the last decade. Among the questions examined in this literature are the source of capital flow reversals, and the presence of financial transmission channels.

Asset Markets I: Speculative Attacks

(*) Garber, Peter and Lars Svensson (1996); "The Operation and Collapse Of Fixed Exchange Rate Regimes”; in Gene Grossman and Kenneth Rogoff (eds) Handbook of International Economics; Vol. 3.

Agenor, Pierre-Richard and Richard Flood (1994); "Macroeconomic Policy, Speculative Attacks and Balance Of Payments Crisis”; Chapter 8 in Rick van der Ploeg (ed.) The Handbook of International Macroeconomics

Eichengreen, Barry, Andrew Rose and Charles Wyplosz (1994); "Speculative Attacks On Pegged Exchange Rates: An Empirical Exploration with Special Reference to the EMS”; NBER Working Paper No. 4898.

Obstfeld, Maurice (1994); "The Logic Of Currency Crisis”; NBER Working Paper No. 4640.

Svensson, Lars (1992); "An Interpretation of Recent Research on Exchange Rate Target Zones”; Journal of Economic Perspectives; Fall.

Asset Markets II: Contagion

(*) Dornbusch, Rudiger, Yung Chul Park and Stijn Claessens (2000); “Contagion: Understanding How It Spreads”; The World Bank Research Observer; Vol. 15, 2: 177-97.

Calvo, Guillermo and Carmen Reinhart (1999); “When Capital Inflows Come To A Sudden Stop”; http://www.bsos.umd.edu/econ/ciecpp.htm

Calvo, Guillermo (1998); Understanding the Russian Virus; http://www.bsos.umd.edu/econ/ciecpn3.pdf

Capital markets Homepage: http://www.stern.nyu.edu/globalmacro/

Kamin, Steven (1999); "The Current International Financial Crisis"; Board of Governors of the Federal Reserve System Working Paper No. 636

Chapters 1-2 in Morris Goldstein, Graciela Kaminsky and Carmen Reinhart (2000); Assessing Financial Vulnerability, Institute for International Economics.

Asset Markets III: Government Policy

(*) Dooley, Michael (1995); "A Survey of Academic Literature On Controls Over International Capital Transactions"; NBER WP No. 5352.

Hali Edison, Michael Klein, Luca Ricci and Torsten Sloek, 2002, "Capital Account Liberalization and Economic Performance: Survey and Synthesis", NBER Working Paper No. 9100, August 2002.

Michael Klein, 2003, "Capital Account Openness and The Varieties of Growth Experiences", NBER Working Paper No. 9500, February.

IMF Occasional Paper No. 190 (2000); Capital Controls.

Anna Schwartz (2000); "The Rise and Fall of Foreign Exchange Market Intervention"; NBER Working Paper No. 7751.

Bartolini, Leonardo and Alan Drazen (1996); "Capital Account Liberalization As A Signal"; NBER Working Paper No. 5725.

Dominguez, Karen and Jeffrey Frankel (1992); "Does Foreign Exchange Intervention Matter?"; NBER Working Paper No. 3299.

Asset Markets IV: International Financial Architecture

(*) Dornbusch, Rudiger, The New International Architecture, CESifo Working Paper No. 769, September 2002 (www.CESifo.de)

(*) Fischer, Stanley, "Financial Crises and Reform of the International Financial System", Weltwirtschaftliches Archiv (Harms Lecture 2002), Vol. 139, 2003:1, pp. 1-37.

Fischer, Stanley (2000); On the Need for an International Lender of Last Resort; Essays in International Economics; No. 220.

II.F. Stabilization: The External Component

While fundamentally a problem of domestic fiscal policy, inflation-stabilization programs typically comprise an important international aspect through both signal and output effects.

(*) Rebelo, Sergio and Carlos Vegh (1995); "Real Effects Of Exchange-Rate Based Stabilization"; NBER Working Paper No. 5197.

Dornbusch, Rudiger, Federico Sturzenegger and Holger Wolf, "Extreme Inflation: Dynamics and Stabilization"; *Brookings Paper on Economic Activity,* 1990:2; p.1-84