

UNIVERSITY OF COLORADO

Department of Economics

**ECON4423: International Finance**

Outline Spring 2007

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**Course Description**

This course reviews selected topics from both international finance and open-economy macroeconomics. From international finance, we will discuss international financial markets and their operations. From open-economy macroeconomics, we will discuss macroeconomic policies and their implications. Obviously, most of our time will be devoted to further our understanding of “exchange rates.”

Here are some stylized facts:

1. Real and nominal exchange rates are highly correlated.
2. Changes in both real and nominal exchange rates are persistent.
3. Forward exchange rates are poor and biased predictors of future spot exchange rates.
4. International differences in interest rates are large and persistent.
5. Portfolios are not internationally diversified.
6. The extent of international consumption risk-sharing is less than expected.
7. Savings and investment are highly correlated.
8. The trade balance and the current account are countercyclical.
9. Business cycles are correlated across countries.

**Web Page**

The course has a web page. The URL is

<http://www.colorado.edu/Economics/courses/boileau/4423/econ4423.html>

The page will be the main vehicle for disseminating information about the course.

## Evaluation

The assessment for this class consists of three assignments, two tests, and one final examination. The tests and final are closed notes and closed books. No make-up tests will be given. The schedule and grade distribution is

	Week	Date	Time	Location	%
Assignment 1	5	12 February	10:00	Gugg 205	5
Term Test 1	6	23 February	10:00	Gugg 205	25
Assignment 2	10	21 March	10:00	Gugg 205	5
Term Test 2	13	9 April	10:00	Gugg 205	25
Assignment 3	16	4 May	10:00	Gugg 205	5
Final Exam	Finals	7 May	10:30–13:00	Gugg 205	35

**Note:** Students who may need academic accommodations should discuss options with the professor no later than 26 January.

## Required Text

Krugman, P. and M. Obstfeld, *International Economics: Theory and Policy*. New York: Addison Wesley.

## Advanced Texts

Frankel, J. and A. Razin (1996) *Fiscal Policies and the World Economy*, Cambridge: The MIT Press.

Grossman, G. and E. Helpman (1991) *Innovation and Growth in the Global Economy*, Cambridge: The MIT Press.

Grossman, G. and K. Rogoff (1995) *Handbook of International Economics*, vol. 3, Amsterdam: North-Holland.

Jones R. and P. Kennen (1985) *Handbook of International Economics*, vol. 1 and 2, Amsterdam: North-Holland.

Obstfeld, M. and K. Rogoff (1996) *Foundations of International Macroeconomics*, Cambridge: The MIT Press.

van der Ploeg, F. (1994) *The Handbook of International Macroeconomics*, Oxford: Basil Blackwell Ltd.

# Course Outline

## 1. Introduction

- 1.1 International Finance
- 1.2 Exchange rates

## 2. The Balance of Payments

- 2.1 National Income Accounting
- 2.2 The Balance of Payments

Krugman and Obstfeld: Chapter 12.

## 3. The Foreign Exchange Market

- 3.1 The Foreign Exchange Market
- 3.2 Interest Rate Parity

Krugman and Obstfeld: Chapter 13.

Devries, C. (1994) Stylized Facts of Nominal Exchange Rate Returns, in F. van der Ploeg (ed.) *The Handbook of International Macroeconomics*, Oxford: Basil Blackwell Ltd, 506–534.

Mussa, M. (1979) Empirical Regularities in the Behavior of Exchange Rates and Theories of the Foreign Exchange Market, *Carnegie-Rochester Conference Series on Public Policy* **11**, 9–57.

Stockman, A. (1988) On the Role of International Financial Markets and their Relevance for Economic Policy, *Journal of Money, Credit, and Banking* **20**, 205–226.

## 4. The Money Market

- 4.1 The Demand for Money
- 4.2 The Money Market

Krugman and Obstfeld: Chapter 14.

Dornbusch, R. (1976) Expectations and Exchange Rate Dynamics, *Journal of Political Economy* **84**, 1161–1176.

Obstfeld and Rogoff (1995) Exchange Rate Dynamics Redux, *Journal of Political Economy* **103**, 624–660.

## **5. The Exchange Rate in the Long Run**

5.1 Purchasing Power Parity

5.2 The Real Exchange Rate

Krugman and Obstfeld: Chapter 15.

Devereux, M. (1997) Real Exchange Rates and Macroeconomics: Evidence and Theory, *Canadian Journal of Economics* **30**, 773–808.

Froot, K. and K. Rogoff (1995) Perspectives on PPP and Long Run Exchange Rates, in G. Grossman and K. Rogoff, eds., *Handbook of International Economics* **3**, Amsterdam: North-Holland.

Rogoff, K. (1996) The Purchasing Power Parity Puzzle, *Journal of Economic Literature* **34**, 647–688.

## **6. The Exchange Rate in the Short Run**

6.1 The Aggregate Output Market

6.2 Macroeconomic Policy

Krugman and Obstfeld: Chapter 16.

Backus, D. and P. Kehoe (1992) International Evidence on the Historical Properties of Business Cycles, *American Economic Review* **82**, 864–888.

Dornbusch, R. and P. Krugman (1976) Flexible Exchange Rates in the Short Run, *Brookings Papers on Economic Activity* **3**, 537–575.

Obstfeld and Rogoff (1995) Exchange Rate Dynamics Redux, *Journal of Political Economy* **103**, 624–660.

## **7. Exchange Rate Regimes**

7.1 Fixed Exchange Rates

7.2 Balance of Payments Crisis

Krugman and Obstfeld: Chapter 17.

Baxter, M. and A. Stockman (1989) Business Cycles and the Exchange Rate Regime: Some International Evidence, *Journal of Monetary Economics* **23**, 377–400.

Kaminsky, G. and C. Reinhart (1999) The Twin Crises: The Causes of Banking and Balance-of-Payments Problems, *American Economic Review* **89**, 473–500.

Obstfeld, M. and K. Rogoff (1995) The Mirage of Fixed Exchange Rates, *Journal of Economic Perspectives* **9**, 73–96.

## **8. The International Monetary System**

8.1 The Gold Standard

8.2 The Bretton Woods System

Krugman and Obstfeld: Chapter 18.

## **9. Macroeconomic Policy and Coordination**

9.1 The Case for and Against Floating Exchange Rates

9.2 Macroeconomic Policy Coordination

Krugman and Obstfeld: Chapter 19.

Feldstein, M. (1988) Distinguished Lecture on Economics in Government: Thinking about International Economic Coordination, *Journal of Economic Perspectives* **2**, 3–13.

Rogoff, K. (1985) Can International Monetary Policy Coordination Be Counterproductive? *Journal of International Economics* **18**, 199–217.

## **10. Optimum Currency Areas**

10.1 The Theory of Optimum Currency Areas

10.2 The European Monetary Union

Krugman and Obstfeld: Chapter 20.

Bean, C. (1992) Economic and Monetary Union in Europe, *Journal of Economic Perspectives* **6**, 31–52.

Levin, J.H. (2000), *A Guide to the Euro*, Boston: Houghton Mifflin.

## **11. The International Capital Market**

11.1 Risk Sharing and Diversification

11.2 International Banking

Krugman and Obstfeld: Chapter 21.

Devries, C. (1994) Stylized Facts of Nominal Exchange Rate Returns, in F. van der Ploeg (ed.) *The Handbook of International Macroeconomics*, Oxford: Basil Blackwell Ltd, 506–534.

Feldstein, M. and C. Horioka (1980) Domestic Saving and International Capital Flows, *Economic Journal* **90**, 314–329.

Froot, K. and R. Thaler (1990) Anomalies: Foreign Exchange, *The Journal of Economic Perspectives* **4**, 179–192.

Lewis, K. (1995) Puzzles in International Financial Markets, in G. Grossman and K. Rogoff (eds.) *Handbook of International Economics*, vol. 3, Amsterdam: North-Holland.

## 12. Developing Countries

12.1 Wealth and Growth

12.2 Income Distribution

Krugman and Obstfeld: Chapter 22.

Barro, R. (1991) Economic Growth in a Cross-Section of Countries, *Quarterly Journal of Economics* **106**, 101-121.

Kaminsky, G. and C. Reinhart (1999) The Twin Crises: The Causes of Banking and Balance-of-Payments Problems, *American Economic Review* **89**, 473–500.

Lucas, R. (1990) Why Doesn't Capital Flow from Rich Countries to Poor Countries, *American Economic Review* **80**, 92–96.

Sachs, J. (1989) *Developing Country Debt and the World Economy*, Chicago: University of Chicago Press.