

Course Syllabus

International Macro

September 2014 - January 2015

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1. Course Objectives

This graduate level course familiarizes students with key concepts in international macroeconomics. The focus is on the new open macroeconomics, as well as on issues financial stability and development. Particular attention is given to the recent financial crisis.

The course draws on a wide range of scientific articles of varying difficulty. Students with no background in economics are strongly recommended to master an introductory textbook in macroeconomics. A basic knowledge of statistical and econometric inference is also essential.

2. Course Organization

The course is a blend of lectures and research paper discussions. The required reading assignment for each session consists of one (or at most two) journal article. Students are expected to have carefully read these articles (marked by RR) and be prepared to summarize and discuss their key insights. Other optional reading includes suggested reading (SR) and advanced reading (AR).

The grading will be based on class participation (30%), group assignments (40%), and the final exam (30%). For the group assignments, groups of (at most) 3 students are formed. A *single joint* solution to each group assignment needs to be sent to matthias.efing@gmail.com before the class (in which the solution is discussed). Please adhere to the following naming convention: The e-mail "subject" and word file "name" should correspond to the following form: Assignment_1_group_8 for group 8 handing in assignment #1.

Late submissions are not accepted. The word file has to name (on the top) all group participants who have worked on the solution. You also have to adhere to the page or word restriction on the length of the document. Additional documentation (programs, calculations, etc.) you can put into an appendix. You should be able to present and defend your solution in class.

3. Course Material

Principle course textbook:

- Obstfeld, Maurice, and Kenneth Rogoff, *Foundations of International Macroeconomics* (MIT Press, 1996)

Other recommended books:

- Gali, Jordi, *Monetary Policy, Inflation, and the Business Cycle* (Princeton University Press, 2008)
- Piketty, Thomas, *Capital in the Twenty-First Century* (Harvard University Press, 2014)

4. Course Administration

Class participants can contact me or the course assistant any time by e-mail and/or make direct appointments.

COURSE SCHEDULE

Student Presenters

Part I: Basic Building Blocks of International Macro

Sessions 1: The Intertemporal Approach to the Current Account (Sept 15)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Macroeconomics*, chapters 1

Sessions 2: Dynamics in Small Open Economies (Sept 16)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Macroeconomics*, chapters 2

SR: Syverson, C., 2011, "What determines productivity?" *Journal of Economic Literature*, Vol. 49(2), pp 326-65.

Session 3: External Adjustment in Europe and the Sovereign Debt Crisis (Sept 22)

AR: Gourinchas, Pierre-Olivier, and Helene Rey, 2007, "International Financial Adjustment," *Journal of Political Economy*, 115(4), also at:

http://socrates.berkeley.edu/~pog/academic/IFA_JPE07.pdf

Student Assignment #1 (for Session 3): External Adjustment

Watch the following video: <http://www.youtube.com/watch?v=4F4kVZr1LXs>

Answer the following questions:

- What is at the origin of Ireland's problem?
- What is particular about Ireland's external position? Compare Ireland to Greece.
- What does Euro membership mean for the Irish adjustment? Compare Ireland to Estonia.
- What can Ireland do to stabilize its situation?

Length restrictions: 2 pages (max 800 words).

Session 4: The Life Cycle, Tax Policy and the Current Account (Sept 23)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Macroeconomics*, chapter 3

Session 5: The Real Exchange Rate and the Terms of Trade (Sept 29)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Macroeconomics*, chapter 4

Session 6: Uncertainty and International Financial Markets (Sept 30)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Macroeconomics*, chapter 5, pages 269-280

SR: Feldstein, Martin, and Charles Horioka, 1980, "Domestic Saving and International Capital Flows", *Economic Journal*, vol. 90, no 358, 314-29.

Student Assignment #2 (for Session 6): Feldstein and Horioka Update

Read careful pages 161-4 of the textbook and answer the following questions:

- Use the saving, investment and GDP data on the 22 countries in the FH study and reproduce their findings for the 1982-1991 period? Do you get a scatter plot like in Figure 3.4?
- Use the set of EMU countries and repeat the FH regression for the 10 year pre-EMU period 1989-1998 and the post EMU period 1999-2008? Has the regression fit changed? What is the change in R-squared? Take all regression residual from each period and test if there is a change in variance.
- For OECD countries not part of the EMU, do we also find a looser relationship between I/Y and S/Y for 1999-2008 relative to 1989-1999? What is the change in R-squared?
- Bonus question: Use now yearly (panel) data on the current account surplus $CA=(S-I)/Y$ for all countries over the period 1989-2008. Can you propose a test to see if the absolute current account imbalance $|CA|$ increased for countries joining the EMU? You should control for a time trend in your analysis and serial correlation in the current account imbalances.

Length restrictions: 6 pages with graphs (max 1000 words).

Part II: The Role of the Financial Markets

Session 7: Functions of the Financial Markets (Oct 6)

RR: Hayek, Friedrich, "The use of knowledge in society", *American Economic Review*, XXV, no 4, September 1945, 519-530

RR: Friedman, Milton, "The Social Responsibility of Business is to Increase its Profits", *The New York Times Magazine*, September 13, 1970.

Student Assignment #3 (for Session 7): On the Role of the Financial Market

Read careful the required reading for session 7 and sum up each in no more than 100 words.

Length restrictions: 0.5 pages (max 200 words).

Session 8: Financial Markets and Corporate Investment I (Oct 7)

Lecture

Session 9: Risk Pricing in Financial Markets (Oct 13)

Lecture

Student Assignment #4 (for Session 9): Portfolio Theory

Assume you have two assets (stock A and B) with yearly expected returns of 12% and 4%, respectively and standard deviations (of the expected return) of 25% and 8% respectively. Their correlation is 30%.

- Plot a graph with the of feasible portfolios in terms of expected return and standard deviations if you vary the portfolio weights in stock A and B from 0 to 100%?
- What happens if the correlation of the two stocks drops to 20%?
- What portfolio do you obtain if you invest 200% in stock A and -100% in stock B (= you sell or go short in stock B)?

Length restrictions: 1 page, 1 graph (max 50 words).

Session 10: Risk Pricing in Practice (Oct 14)

Lecture

Session 11: Financial Market Efficiency (Oct 27)

Lecture

Session 12: Financial Markets and Wealth Distribution (Oct 28)

Student Presentation

RR: Piketty, Thomas, *Capital in the Twenty-First Century* (Harvard University Press, 2014), Part II and III
Bareerah Hoorani and Christian Doll

SR: Rodrik, Dani, How the Rich Rule (VoxEu.org, 2014), <http://www.project-syndicate.org/commentary/dani-rodrik-says-that-widening-inequality-drives-economic-elites-toward-sectarian-politics>

Part III: Money, Exchange Rates and Flexibel Prices

Session 13: The Money Supply Process (Nov 10)

SR: Abel and Bernanke, *Macroeconomics*, Chapter 15

SR: Bernanke, B., 1983, Nonmonetary Effects of the Financial Crisis in the Propagation of the Great Depression, *American Economic Review*, 73, 257-276.

SR: Temin, P., 1993, *Journal of Economic Perspective*, vol. 7(2), 87-102

SR: Schularick M., and A. Taylor, 2012, Credit Booms Gone Bust: Monetary Policy, Leverage Cycles, and Financial Crises, 1870-2008, *American Economic Review*, 102(2), 1029-61.

Session 14: Models of the Money Demand (Nov 11)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Economics*, chapters 8.1-8.3

Session 15: Models of Exchange Rate Crisis (Nov 17)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Economics*, chapters 8.4

SR: Krugman, Paul (1979). "A Model of Balance-of-Payments Crises", *Journal of Money, Credit, and Banking* 11(3), 311-25. http://www.tau.ac.il/~yashiv/krugman_1979.pdf

Session 16: Banking Instability and Asymmetric Information (Nov 18)

Student Presentations

RR: Diamond, Douglas, and Philip Dybvig (1983). "Bank runs, deposit insurance and liquidity", *Journal of Political Economy*, pp 401-19

Sabina Neacsu and Robert Toscan

SR: Stiglitz, J., Weiss, A., 1981, "Credit rationing in markets with imperfect information", *American Economic Review* 71, 393-410.

Part IV: Money, Exchange Rates and Sticky Prices

Session 17: An introduction to the New Keynesian Monetary Economics (Nov 24)

Student Presentation

RR: Clarida, Richard, Gali, Jordi and Gertler, Mark (1999), "The Science of Monetary Policy: A New Keynesian Perspective", *Journal of Economic Literature* 37(4), pp. 1661-1707.

Bruno Marechal

Student Assignment #5 (for Session 17): Optimal Monetary Policy

Carefully read the required reading for Session 17. The authors distinguish rule based policy with commitment and a discretionary regime without commitment.

Answer the following questions:

- Which regime generally can achieve better welfare results and why?
- What are the problems associated with the rule based regime?

Length restrictions: 1 pages (400 words).

Session 18: New Keynesian Open Macroeconomics and Exchange Rates (Nov 25)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Economics*, chapter 9.

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

SR: Rogoff, Kenneth, "Dornbusch's Overshooting Model after 25 Years," IMF Staff Papers 49 (Special Issue 2002): 1-34.

<http://www.imf.org/external/pubs/ft/wp/2002/wp0239.pdf>

SR: Dornbusch, Rudiger, (1976, "Expectations and Exchange Rate Dynamics," *Journal of Political Economy* 84(6), pp. 1161-1176.

<http://jpkc.sysu.edu.cn/guojijinrong/ckwx/5/Expectation%20and%20exchange%20rate%20dynamic.pdf>

Session 19: New Keynesian Open Macroeconomics in General Equilibrium (Dec 1)

RR: Obstfeld, Maurice, and Kenneth Rogoff (1996), *Foundations of International Economics*, chapter 10.

SR: Bernanke, Ben, and Kevin Carey, 1996, "Nominal Wage Stickiness and Aggregate Supply in the Great Depression," *Quarterly Journal of Economics* Vol. 111, No. 3 (Aug., 1996), pp. 853-883

SR: Rogoff, K. and C. Reinhart, 2008, "This Time Is Different: A Panoramic View of Eight Centuries of Financial Crises", NBER Working Paper 13881

Student Assignment #6 (for Session 19): Nominal Rigidities in the Eurocrisis

Carefully watch the second speaker, Prof. Dr. Hans-Werner Sinn, in the following webcast:

<http://www.aeaweb.org/webcasts/2014/Austerity/NewStandardPlayer.html?plugin=HTML5&mimetype=video%2Fmp4>

Answer the following questions:

- What different scenarios does he distinguish?
- What role do nominal rigidities play in his account?

Length restrictions: 1 pages (400 words).

Part V: Financial Development, Financial Stability and Governance

Session 20: Governance and Globalization (Dec 2)

Student Presentation

RR: Morck, R., D. Wolfenzon and B. Yueng, 2008, "Corporate Governance, Economic Entrenchment, and Growth", *Journal of Economic Literature* 43, 655-720.

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SR: Ferreira, M., and P. Matos, 2008, "The Color of Investors' Money: The Role of Institutional Investors Around the World?" *Journal of Financial Economics* 88 (3), 499-533.

SR: Hau, Harald, and Thum, Marcel P., "Subprime Crisis and Board (In-)Competence: Private vs. Public Banks in Germany," *Economic Policy*, Vol. 24(60), 701-751, October 2009. Available at SSRN:

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1360698

AR: Fernandes, N, 2008, "Sovereign Wealth Funds: Investment Choices and Implications around the World," IMD Working Paper. http://www.imd.org/research/publications/upload/wp_2009_01_fernandes_level_1.pdf

AR: Jiang, G., Ch. Lee, and H. Yue, 2009, Tunneling through Inter-corporate Loans: The China Experience, Working Paper. <http://ideas.repec.org/a/eee/jfinec/v98y2010i1p1-20.html>

Peijia Huang and Xueye Bao

Session 21: Governance in Emerging Countries: Example Russia (Dec 8)

Student Presentation

RR: Maxim Mironov, 2012, [Taxes, Theft, and Firm Performance](#), Forthcoming in the *Journal of Finance*, presented at the 2012 AFA Annual Meeting in Chicago

Maria Sarabia Vega and Monica Avila

SR: Maxim Mironov, 2012, [Should One Hire a Corrupt CEO in a Corrupt Country?](#), presented at the 2013 AFA Annual Meeting in San Diego

SR: Maxim Mironov, and Ekaterina Zhuravskaya, 2012, [Corruption in Procurement and Shadow Campaign Financing: Evidence from Russia](#)

Anastasia Tayganko, Nadia Goviadynska, Inesa Porta

SR: Maxim Mironov, 2006, [Economics of Spacemen. Estimation of Tax Evasion in Russia, June 2006](#)

Session 22A: Conflicts of Interest in Rating Agencies (Dec 9)

Student Presentation

RR: Matthias Efing, and Harald Hau, 2013, “Structured Debt Ratings: Evidence on Conflicts of Interest,” SFI Working Paper, http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2253970
Nathalie Meier and Lisa Messi and Giulia Bardoni

SR: Jess Cornaggia, Kimberly J. Cornaggia, and Han Xia. 2013, “Revolving Doors on Wall Street,” Working paper, http://www.cicfconference.org/schedule_files/12_5_3.pdf

Session 22B: Global Banking (Dec 9)

Student Presentation

RR: Admati, Anat R., DeMarzo, Peter M., Hellwig, Martin F. and Pfleiderer, Paul C., “Fallacies, Irrelevant Facts, and Myths in the Discussion of Capital Regulation: Why Bank Equity is not Expensive” (March 23, 2011). Rock Center for Corporate Governance at Stanford University Working Paper No. 86 ; MPI Collective Goods Preprint, No. 2010/42. Available at SSRN: <http://ssrn.com/abstract=1669704> or <http://dx.doi.org/10.2139/ssrn.1669704>
Antoine Didisheim

SR: Duffie, D., 2010, “The Failure Mechanics of Dealer Banks”, BIS working paper no 301
http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1599482

Also available as a book:

How Big Banks Fail and What to Do about It,

http://www.amazon.com/How-Banks-Fail-What-bout/dp/0691148856/ref=pd_bxgy_b_img_y

SR: Admati, A., and M. Hellwig, 2013, “The Bankers' New Clothes: What's Wrong with Banking and What to Do about It”,
http://www.amazon.com/Bankers-New-Clothes-Whats-Banking/dp/0691156840/ref=sr_1_1?s=books&ie=UTF8&qid=1361785431&sr=1-1&keywords=admati+hellwig

Session 23: Regulatory Arbitrage (Dec 15)

Presentation by Matthias Efing

SR: M. Efing, 2014, “Arbitraging the Basel Securitization Framework: Evidence from German Banks”

Session 24: Final Exam (December 16, 10-12am)