

# EC421: International Economics

## International Macroeconomics

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London School of Economics

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### 1 Timings

- Lectures: **Mondays, 14.00-16.00** (N.A.B. 2.08, weeks 1-10 MT).
- Classes: **Mondays, 16.00-17.00** (N.A.B. 1.17, weeks 2-11 MT).
- Problem sets: Each week we will distribute a problem set, which will be reviewed in class the following week. Two problem sets will be marked for the formative coursework.
- Office hours: **Mondays, 13.00-14.00** (32LIF 4.15, weeks 1-11 MT).
- The first half of the course will be taught by Daniel Wales (Lectures 1-5, Classes 1-5), material in the second half will be taught by Emile Marin (Lectures 6-10, Classes 6-10).

### 2 Outline

The primary aim of this course is to give an overview of the recent literature in international macroeconomics and finance as well as to develop tools and ideas for writing research papers.

The first part of the course will focus on the real economy, with a particular focus on the international real business cycle and determinants of the current account (lectures 1-4). This part of the course will use established theory to answer a number of timeless questions in international macroeconomics.

The middle part of the course (lectures 5-8) will focus on extending these basic models into a nominal environment, to answer questions of monetary policy, and consider the implications of various international asset and pricing structures.

The final part of the course (lectures 9-10) will draw together material on financial crises and the nominal exchange rate.

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### 3 Books

There are two primary course texts. [Obstfeld and Rogoff \(1996\)](#) (hereafter [OR](#)) and [Schmitt-Grohé and Uribe \(2017\)](#) (hereafter [SGU](#)). Though written some time ago, the first is the classical reference textbook in modern international economics. The second supplements this, updates analysis and presents a useful alternative source for key explanations. In addition, substantial parts of the course will also be drawn from more recent literature, with key readings given for each topic. Please let us know if you have any trouble finding referenced articles.

### 4 Lecture Plan

#### Lecture 1: Intertemporal Trade and the Current Account

- Introduction to the current account.
- The 2 period small open economy model.
- The 2 period, 2 country model.
- The infinite horizon model.
- Dynamics of small open economies.

References: [OR](#) (Ch 1, 2.1-2.3), [SGU](#) (Ch 2-3) and [Engel and Rogers \(2006\)](#).

#### Lecture 2: Life-Cycle Models

- Ricardian equivalence.
- Overlapping generations model.
- Breaking Ricardian equivalence.
- Twin deficit hypothesis.
- Factor decomposition.

References: [OR](#) (Ch 3), [SGU](#) (Ch 4.11) and [Ferrero \(2010\)](#).

#### Lecture 3: Terms of Trade and the Real Exchange Rate

- Relationship between the terms of trade and real exchange rate.
- Breakdown of PPP.
- Home bias.
- Non-traded goods.
- Balassa-Samuelson effect.

References: [OR](#) (Ch 4) and [SGU](#) (Ch 7-8).

#### **Lecture 4: International Business Cycles**

- International business cycles - stylised facts.
- Insights from a simple model.
- Possible ways to reconcile.

**References:** [SGU](#) (Ch 1, 4), [Aguiar and Gopinath \(2007\)](#), [Backus et al. \(1992\)](#), [Backus et al. \(1994\)](#), [Corsetti et al. \(2008\)](#) and [Mendoza \(1991\)](#).

#### **Lecture 5: Monetary Policy**

- Basic nominal model.
- Flexible price.
- Fixed prices.
- Welfare considerations.
- Cashless limit.

**References:** [Benigno \(2004\)](#), [Corsetti and Pesenti \(2007\)](#), [Ferrero et al. \(2008\)](#) and [Galí and Monacelli \(2005\)](#).

#### **Lecture 6: Portfolio Diversification**

- Risk sharing.
- Uncertainty.
- Bacus-Smith puzzle.
- International Portfolio diversification.

**References:** [OR](#) (Ch 5), [Backus and Smith \(1993\)](#), [Corsetti et al. \(2008\)](#), [Heathcote and Perri \(2013\)](#) and [Stockman and Tesar \(1995\)](#).

#### **Lecture 7: International Monetary Transmission (1)**

- The structure of international financial markets.
- Incomplete Markets.
- Complete Markets.
- Financial Autarky.

**References:** [OR](#) (Ch 5), [Cole and Obstfeld \(1991\)](#), [Corsetti and Pesenti \(2001\)](#), [Corsetti et al. \(2008\)](#), [Feldstein and Horioka \(1980\)](#) and [Heathcote and Perri \(2002\)](#).

#### **Lecture 8: International Monetary Transmission (2)**

- The international pricing structure.
- Producer Currency Pricing.
- Local Currency Pricing.
- Dollar Currency Pricing.

**References:** [Gopinath and Rigobon \(2008\)](#), [Gopinath et al. \(2010\)](#) and as Lecture 7.

## Lecture 9: International Financial Frictions

- Financial crises.
- Sovereign default.
- Global imbalances.

**References:** [OR](#) (Ch 6), [Mendoza et al. \(2009\)](#) and [Mendoza \(2010\)](#).

## Lecture 10: Nominal Exchange Rate Determination

- Trade in multiple goods.
- Uncovered interest parity.
- Monetary policy.

**References:** [OR](#) (Ch 8), [SGU](#) (Ch 9), [Benigno and Benigno \(2008\)](#), [Engel and Matsumoto \(2009\)](#) and [Engel \(2016\)](#).

## References

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