

Topics in Macroeconomics I: International Finance

2021-22 Academic Year
Master of Research in Economics, Finance and Management

1. Description of the subject

- Topics in Macroeconomics I
 - Total credits: 3 ECTS
 - Type of subject: Optative
 - Department of Economics and Business
 - Teaching team: Luca Fornaro / Room 23.306, lfornaro@crei.cat, twitter: [@lucafornaro3](https://twitter.com/lucafornaro3)
Office hours by appointment
- Code: 32080
Workload: 75 hours
Term: 1st

- **2. Teaching guide**

- **Introduction**

In this topic course we will study recent advances in the literature on international macroeconomics. We will consider monetary and fiscal policy in open economies, capital flows and international financial crises, macroprudential policies and capital controls, exchange rate policy, financial globalization and international macroeconomic dependence. Substantial attention will be devoted to current policy debates, such as global imbalances and the 2008 global financial crisis, the past and future of the euro area, secular stagnation, the emergence of China as a global player and the global productivity slowdown

- **Assessment**

The evaluation is based on a term paper (80%) and class participation (20%). The term paper consists in extending in some interesting direction the model of one of the papers listed at the end of the syllabus. For example, you could modify some assumption to think about different scenarios, consider alternative policy interventions, provide a quantitative analysis or reinterpret some historical event. You can work on the term paper in pairs, unless you plan to use the material of the term paper as basis for your master thesis.

- **Contents**

Background reading

Foundations of International Macroeconomics, 1996, M. Obstfeld and K. Rogoff.
Open Economy Macroeconomics, 2017, M. Uribe and S. Schmitt-Grohe.

Course Outline (this is only indicative, some topics may be added or removed)

1. **Capital flows over the business cycle**. We will review some basic facts about the behavior of capital flows over the business cycle, and introduce the intertemporal approach to the current account.

Required readings

Lecture slides

Additional readings

Obstfeld and Rogoff, Chapter 2

Uribe and Schmitt-Grohe, Chapters 1-4

2. **International financial crises and regulation of capital flows.** Since the early 1980s, several countries have gone through boom-bust cycles in capital flows. During the typical episode, a protracted period of capital inflows was followed by a sudden stop and a deep recession. To rationalize these episodes, we will study the interactions between capital flows, asset prices and the real exchange rate. We will also derive some lessons about capital controls and macroprudential policies in open economies.

Required readings

Bianchi, J. (2011). Overborrowing and systemic externalities in the business cycle. *American Economic Review*, 101(7):3400–3426

Additional readings

Korinek, A. (2017). Regulating capital flows to emerging markets: An externality view. *Journal of International Economics*

Mendoza, E. G. (2010). Sudden stops, financial crises, and leverage. *The American Economic Review*, 100(5):1941–1966

Schmitt-Grohé, S. and Uribe, M. (2018). Underborrowing. Columbia University Working Paper

3. **Exchange rates and monetary policy.** We will introduce a simple model to think about exchange rate and monetary policy in open economies. We will also consider the role of macroprudential policies as an aggregate demand management tool.

Required readings

Schmitt-Grohé, S. and Uribe, M. (2016). Downward nominal wage rigidity, currency pegs, and involuntary unemployment. *Journal of Political Economy*, 124(5):1466–1514

Additional readings

Farhi, E. and Werning, I. (2016). A theory of macroprudential policies in the presence of nominal rigidities. *Econometrica*, 84(5):1645–1704

4. **The economics of monetary unions.** Since the introduction of the euro, capital flows among member countries have been large and volatile. To understand these facts, we will study the interactions between the exchange rate regime and international financial integration. We will then consider policy reforms to ensure that financial integration is managed appropriately in the euro area.

Required readings

Farhi, E. and Werning, I. (2017). Fiscal unions. *American Economic Review*, 107(12):3788–3834

Fornaro, L. (2021). A theory of monetary union and financial integration. *The Review of Economic Studies*, forthcoming

Additional readings

Benigno, P. (2004). Optimal monetary policy in a currency area. *Journal of International Economics*, 63(2):293–320

Benigno, P. and Romei, F. (2014). Debt deleveraging and the exchange rate. *Journal of International Economics*, 93(1):1–16

Fornaro, L. (2018). International debt deleveraging. *Journal of European Economic Association*

5. **The world in secular stagnation.** The current state of the global economy is characterized by very low interest rates. This poses a challenge to the conduct of monetary policy, given by the effective lower bound on the policy rate. We will study how, in this scenario, monetary policy should be complemented with fiscal policy. We will also see, however, that international cooperation in the design of fiscal policy is needed, or the world can fall prey of a paradox of global thrift.

Required readings

Fornaro, L. and Romei, F. (2019). The paradox of global thrift. *American Economic Review*, 109(11):3745–79

Additional readings

Caballero, R. J., Farhi, E., and Gourinchas, P.-O. (2008). An equilibrium model of global imbalances and low interest rates. *American Economic Review*, 98(1):358–393

Caballero, R. J., Farhi, E., and Gourinchas, P.-O. (2021). Global imbalances and currency wars at the zlb. *The Review of Economic Studies*, forthcoming

Eggertsson, G. B., Mehrotra, N., Singh, S., and Summers, L. H. (2016). A contagious malady? open economy dimensions of secular stagnation. *IMF Economic Review*

6. **The role of the dollar in the international monetary system.** We will study the role of the dollar in the international monetary system. In particular, we will focus on its use as international currency in trade invoicing, unit of account in international financial transactions and reserves holdings by central banks in developing countries.

Required readings:

Gopinath, G. and Stein, J. C. (2021). Banking, trade, and the making of a dominant currency. *Quarterly Journal of Economics*

Additional readings

Farhi, E. and Maggiori, M. (2018). A model of the international monetary system. *The Quarterly Journal of Economics*, 133(1):295–355

7. **Global imbalances and the productivity growth slowdown.** Since the late 1990s, the global economy has experienced two spectacular trends. First, there has been a surge of capital flows from developing countries - mainly China and other Asian countries - toward the United States. Second, global productivity growth has declined dramatically. To understand these trends we will use a simple model connecting financial globalization and productivity growth. We will use the model to revisit the export-led growth strategy followed by some developing countries, as well as the impact of policies aiming at reducing the U.S. trade deficit.

Required readings

Benigno, G., Fornaro, L., and Wolf, M. (2020). The global financial resource curse. CREIworking paper

Additional readings

Benigno, G. and Fornaro, L. (2014). The financial resource curse. *The Scandinavian Journal of Economics*, 116(1):58–86

Material for term paper

1. Amador, M., Bianchi, J., Bocola, L., and Perri, F. Exchange rate policies at the zero lowerbound. *The Review of Economic Studies*
2. Benigno, G. and Fornaro, L. (2018). Stagnation traps. *The Review of Economic Studies*, 85(3):1425–1470
3. Benigno, G., Fornaro, L., and Wolf, M. (2020). The global financial resource curse. CREIworking paper
4. Bocola, L. and Lorenzoni, G. (2019). Financial crises, dollarization, and lending of last resort in open economies
5. Eggertsson, G. B., Mehrotra, N., Singh, S., and Summers, L. H. (2016). A contagious malady? open economy dimensions of secular stagnation. *IMF Economic Review*
6. Farhi, E. and Maggiori, M. (2018). A model of the international monetary system. *The Quarterly Journal of Economics*, 133(1):295–355
7. Fornaro, L. and Romei, F. (2019). The paradox of global thrift. *American Economic Review*, 109(11):3745–79
8. Fornaro, L. (2021). A theory of monetary union and financial integration. *The Review of Economic Studies*, forthcoming
9. Gabaix, X. and Maggiori, M. (2015). International liquidity and exchange rate dynamics. *The Quarterly Journal of Economics*, 130(3):1369–1420
10. Gopinath, G. and Stein, J. C. (2021). Banking, trade, and the making of a dominant currency. *Quarterly Journal of Economics*
11. Schmitt-Grohé, S. and Uribe, M. (2016). Downward nominal wage rigidity, currency pegs, and involuntary unemployment. *Journal of Political Economy*, 124(5):1466–1514.