

**DEPARTMENT OF ECONOMICS
INTERNATIONAL MONETARY THEORY**

Spring 2023

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Office hours: T, Th., 8.50am-9.50a.m. and by appointment

GOALS AND OVERVIEW

The goal of this course is to motivate and initiate innovative graduate student research in international macroeconomics. The course complements lectures with in-class student presentations of significant research papers in the literature, and by asking students to complete an original research project in the form of a substantial research proposal. However, recognizing that many students have limited backgrounds in international macroeconomics, the lectures provide a foundation of knowledge of core models and key papers.

The course readings and presentations are not intended to provide an exhaustive review of all international macroeconomic topics. We focus on a few core areas in which some of the most exciting directions of the field originate. Within these core areas, both empirical and theoretical developments are studied. Some readings represent seminal contributions, some frontier research. Similarly, the reading lists for topics are not exhaustive; in developing their research projects, students should use citations and bibliographies of papers on the list to deepen their knowledge of the literature.

STRUCTURE

There is one, three hour and twenty-minute class per week. In general, the first half of each class is lecture material that develops the core models and concepts of international macroeconomics, based largely on the instructor's own notes. Students are expected to complete any companion textbook and paper readings independently.

The second half of each class we allocate to two student presentations of existing research papers, except in the final two weeks of the semester when students present a summary of their own research project. The goal of the presentations is to improve reading, comprehension, and communication skills and familiarize students with the methods, models, and results in the established core and at the brink of this research field. Students

submit their presentation materials to the instructor via email ahead of the in-class presentation. The presentations constitute graded written assignments for the course.

Finally, students develop an original research project during the semester, along similar lines as a doctoral dissertation proposal; it should contain the motivation, goals, and marginal contribution of a planned research project, a proposed structure of the project, and any preliminary or incomplete results. The papers are due by the final examination date and students present them in class during weeks 14 and 15 of the course. The research paper cannot be the same as that submitted to another class, in this or any other semester.

PRE-REQUISITES

The pre-requisites for this class are ECONOMICS 602 and ECONOMICS 605.

TEXTBOOKS

The course does not follow any textbook. However, students may draw on and are expected to read specific chapters on the reading list from the following books:

Open Economic Macroeconomics (2017) by Martin Uribe and Stephanie Schmitt-Grohe, Princeton University Press

Foundations of International Macroeconomics (1996) by Maurice Obstfeld and Kenneth Rogoff, MIT Press: Cambridge

EVALUATION

Your final grade in the class will be determined as the following weighted average of your work throughout the semester:

1. In-class presentations of papers in the literature (50%)
2. Written research proposal and its presentation (50%)

ACADEMIC CONDUCT

Plagiarism – presenting someone else’s ideas as your own, either verbatim or recast in your own words – is a serious academic offense with serious consequences. Please familiarize yourself with the discussion of plagiarism in SCampus in Part B, Section 11, “Behavior Violating University Standards” policy.usc.edu/scampus-part-b. Other forms of academic dishonesty are equally unacceptable. See additional information in SCampus and university policies on scientific misconduct, policy.usc.edu/scientific-misconduct.

SUPPORT SYSTEMS

Counseling and Mental Health - (213) 740-9355 – 24/7 on call

studenthealth.usc.edu/counseling Free and confidential mental health treatment for students, including short-term psychotherapy, group counseling, stress fitness workshops, and crisis intervention.

National Suicide Prevention Lifeline - 1 (800) 273-8255 – 24/7 on call

suicidepreventionlifeline.org Free and confidential emotional support to people in suicidal crisis or emotional distress 24 hours a day, 7 days a week.

Relationship and Sexual Violence Prevention Services (RSVP) - (213) 740-9355(WELL), press “0” after hours – 24/7 on call

studenthealth.usc.edu/sexual-assault Free and confidential therapy services, workshops, and training for situations related to gender-based harm.

Office of Equity and Diversity (OED) - (213) 740-5086 | Title IX – (213) 821-8298

equity.usc.edu, titleix.usc.edu Information about how to get help or help someone affected by harassment or discrimination, rights of protected classes, reporting options, and additional resources for students, faculty, staff, visitors, and applicants.

Reporting Incidents of Bias or Harassment - (213) 740-5086 or (213) 821-8298

usc-advocate.symplicity.com/care_report Avenue to report incidents of bias, hate crimes, and microaggressions to the Office of Equity and Diversity |Title IX for appropriate investigation, supportive measures, and response.

The Office of Disability Services and Programs - (213) 740-0776

dsp.usc.edu Support and accommodations for students with disabilities. Services include assistance in providing readers/notetakers/interpreters, special accommodations for test taking needs, assistance with architectural barriers, assistive technology, and support for individual needs.

USC Campus Support and Intervention - (213) 821-4710

campussupport.usc.edu Assists students and families in resolving complex personal, financial, and academic issues adversely affecting their success as a student.

Diversity at USC - (213) 740-2101

diversity.usc.edu Information on events, programs and training, the Provost's Diversity and Inclusion Council, Diversity Liaisons for each academic school, chronology, participation, and various resources for students.

USC Emergency - UPC: (213) 740-4321, HSC: (323) 442-1000 – 24/7 on call
dps.usc.edu, emergency.usc.edu Emergency assistance and avenue to report a crime.
Latest updates regarding safety, including ways in which instruction will be continued if an officially declared emergency makes travel to campus infeasible.

USC Department of Public Safety UPC: (213) 740-6000, HSC: (323) 442-120 24/7
dps.usc.edu Non-emergency assistance or information.

Office of the Ombuds - (213) 821-9556 (UPC) / (323-442-0382 (HSC)
ombuds.usc.edu A safe and confidential place to share your USC-related issues with a University Ombuds who will work with you to explore options or paths to manage your concern.

OUTLINE AND READINGS

1. INTRODUCTION TO PUZZLES

Data, models, and puzzles in international macroeconomics

Readings: Uribe and Schmitt-Grohe, chapter 1

Obstfeld, M. and K. Rogoff (2000) "The Six Major Puzzles in International Macroeconomics: Is There a Common Cause?" NBER Macroeconomics Annual, **15**, 339-412.

Eaton, J., S. Kortum, and B. Neiman (2016) "Obstfeld and Rogoff's International Macro Puzzles: A Quantitative Assessment," *mimeo*.

Engel, C. (2000) "Comments on Obstfeld and Rogoff's "The Six Major Puzzles in International Macroeconomics: Is There a Common Cause?"" NBER WP#7818.

Itskhoki, O. (2022) "Research Agenda: Exchange Rate Puzzles and Policies," prepared for the Society for Economic Dynamics newsletter.

Mussa, M. (1986) "Nominal Exchange Rate Regimes and the Behavior of Real Exchange Rates," *Carnegie-Rochester Series on Public Policy* **25** 117-214.

2. INTERTEMPORAL CURRENT ACCOUNT DETERMINATION

Small open economy and multi-country endowment and production models, with and without uncertainty

Readings: Obstfeld and Rogoff, chapters 1, 2, and 3
Uribe and Schmitt-Grohe, chapters 2 and 3

3. INTERNATIONAL CAPITAL FLOWS AND GROWTH

The Lucas paradox: Reconciling capital flows with relative income, capital account liberalization and economic development

Readings: Aizenmann, J., Y. Jinjark, and D. Park (2013) "Capital Flows and Economic Growth in the Era of Financial Integration and Crisis, 1990-2010," *Open Economies Review* **24** 371-396.

Henry, P.B. (2003) "Capital Account Liberalization, the Cost of Capital, and Economic Growth," *American Economic Review* **93(2)** 91-96.

Kehoe, T.J. (1995) "What Happened in Mexico in 1994-1995?" in P.J. Kehoe and T.J. Kehoe, eds., *Modeling North American Integration* (1995) Kluwer Academic Publishers, 131-147.

Lucas, R.E. Jr. (1990) "Why Doesn't Capital Flow from Rich to Poor Countries?" *American Economic Review* **80(2)** 92-96.

Levine, R. (2002) "International Financial Liberalization and Economic Growth," *Review of International Economics* **9(4)** 688-702.

4. MULTI-SECTOR MODELS AND RELATIVE PRICES

Multi-sector models of terms of trade, real exchange rate, sectoral reallocation, and capital flows.

Readings: Obstfeld and Rogoff, chapter 4
Uribe and Schmitt-Grohe, chapters 7 and 8

Fernandez de Cordoba, G. and T. J. Kehoe, "Capital Flows and Real Exchange Rate Fluctuations Following Spain's Entry into the European Community," *Journal of International Economics*, 51 (2000), 49-78.

Kehoe, T.J. and K. J. Ruhl (2008) "Are Shocks to the Terms of Trade Shocks to Productivity?" *Review of Economic Dynamics* **11** 804–819.

Kehoe, T.J. and K. J. Ruhl (2009) "Sudden Stops, Sectoral Reallocations, and the Real Exchange Rate," *Journal of Development Economics* **89** 235–249.

5. STRUCTURAL CHANGE IN THE OPEN ECONOMY

Structural change and growth, facts, models, and the role of trade.

Readings: Herrendorf, B., R. Rogerson, and A. Valentinyi (2014) "Growth and Structural Transformation," in *Handbook of Economic Growth*, v.2, eds. P. Aghion and S. Durlauf, 855-941

Betts, C., R. Giri, and R. Verma (2017) "Trade, Reform, and Structural Transformation in South Korea", *IMF Economic Review* **65(4)** 745-791

Echevarria, C. (2008) "International Trade and the Sectoral Composition of Production." *Review of Economic Dynamics* **11** 192-206

Kehoe, T.J., K. Ruhl, and J.B. Steinberg (2018) "Global Imbalances and Structural Change in the United States," *Journal of Political Economy* **126(2)** 761-796

Mastuyama, K. (2009) "Structural Change in an Interdependent World: A Global View of Manufacturing Decline," *Journal of the European Economic Association* **7** 478-486.

Stokey, N. (2001) "A Quantitative Model of the Industrial Revolution." *Carnegie-Rochester Conference Series on Public Policy* **55** 55-109

Uy, T., K-M. Yi, and J. Zhang (2013) "Structural Transformation in an Open Economy," *Journal of Monetary Economics* **60(6)** 667-682.

6. INTERNATIONAL REAL BUSINESS CYCLES

International business cycle data, real business cycles in small and large open economies, and international transmission.

Readings: Uribe and Schmitt-Grohe, chapters 1 and 4

Aguiar, M. and G. Gopinath (2007), “Emerging Market Business Cycles: The Cycle is the Trend,” *Journal of Political Economy* **115** 69-102.

Backus, D. K. and P.J. Kehoe (1992) “International evidence on the historical properties of business cycles,” *American Economic Review* **82** 864-888.

Backus, D., P.J. Kehoe, and F. Kydland (1992) “International Real Business Cycles,” *Journal of Political Economy* **100** 745-775.

Baxter, M. and A.C. Stockman (1989) “Business cycles and the exchange-rate regime: some international evidence,” *Journal of monetary Economics* **23(3)** 377-400.

Chang, R. and A. Fernández (2013) “On the sources of aggregate fluctuations in emerging economies”, *International Economic Review* **54(4)** 1265-1293.

Cooley, T. and E.C. Prescott (1995) “Economic growth and business cycles,” in T. Cooley, ed., *Frontiers of Business Cycle Research* Princeton University Press.

Garcia-Cicco, J., R. Pancazi, and M. Uribe (2010) “Real Business Cycles in Emerging Countries?” *American Economic Review* **100** 2510-2531.

Heathcote, J. and F. Perri (2013) “Assessing international efficiency,” NBER Technical Report 18956.

Imbs, J. (2010) “The first global recession in decades”, *IMF Economic Review* **58(2)** 327-354.

Justiniano, A. and B. Preston (2010) “Can structural small open-economy models account for the influence of foreign disturbances?” *Journal of International Economics* **81(1)** 61-74.

Mendoza, E.G. (1991) “Real Business Cycles in a Small Open Economy,” *American Economic Review* **81** 797-818.

Mendoza, E. G. (1995) “The terms of trade, the real exchange rate, and economic fluctuations”, *International Economic Review* **36(1)** 101-137.

7. REAL AND NOMINAL EXCHANGE RATES

Exchange rate data and puzzles, and monetary models of real and nominal exchange rate determination, currency of invoicing issues.

Readings: Obstfeld and Rogoff, chapters 4, 5, 8, and 9
Uribe and Schmitt-Grohe, chapters 8 and 9

Betts, C. and M. Devereux (2000) "Exchange Rate Dynamics in a Model of Pricing-to-Market," *Journal of International Economics* **50** 215-244.

Betts, C. and T. Kehoe (2008) "Real Exchange Rate Movements and the Relative Price of Non-Traded Goods", NBER WP# 14437

Betts, C. and T. Kehoe (2006) "US Real Exchange Rate Fluctuations and Relative Price Fluctuations," *Journal of Monetary Economics* **53** 1297-1326.

Chari, V. V., P.J. Kehoe, and E.R. McGrattan, (2002) "Can Sticky Price Models Generate Volatile and Persistent Real Exchange Rates?" *Review of Economic Studies* **69** 533-63.

Crucini, M., C. Telmer, and M. Zachariadis (2005) "Understanding European Real Exchange Rates," *American Economic Review* **95** 724-738.

Engel, C. (1999) "Accounting for US Real Exchange Rate Changes", *Journal of Political Economy*, **107**, 507-538.

Engel, C., N.C. Mark, and K.D. West (2007), "Exchange Rate Models Are Not as Bad as You Think," *NBER Macroeconomics Annual* 381-441.

Engel, C. and J. Rogers (1996) "How Wide is the Border?" *American Economic Review* **86** 1112-1125.

Engel, C. and K. West (2005), "Exchange Rates and Fundamentals." *Journal of Political Economy* **113(3)** 485-517.

Itskhoy, O. and D. Mukhin (2021) "Exchange Rate Disconnect in General Equilibrium," *Journal of Political Economy* **129(8)** 2183-2232.

Hellerstein, R. (2008) "Who Bears the Cost of a Change in the Exchange Rate? Pass-through Accounting for the Case of Beer," *Journal of International Economics* **76(1)** 14-32

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

8. MONETARY MODELS AND INVOICING ISSUES

Readings: Amiti, M, O. Itskhoki, and J. Konings (2022) "Dominant Currencies: How Firms Choose Currency Invoicing and why it matters," *Quarterly Journal of Economics* **137(3)** 1435-1493.

Amiti, M, O. Itskhoki, and J. Konings (2019) "International Shocks, Variable Markups and Domestic Prices," *Review of Economic Studies* **86(6)** 2356-2402.

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

Benigno, G., and P. Benigno (2009) "Exchange Rate Determination under Interest Rate Rules," *Journal of International Money and Finance* **27(6)** 971-993.

Corsetti, G., L. Dedola, and S. Leduc (2010) "Optimal Monetary Policy in Open Economies," in *Handbook of Monetary Economics* v.3 eds. B. Friedman and M. Woodford.

Devereux, M.B., and C. Engel (2003) "Monetary Policy in the Open Economy Revisited: Price Setting and Exchange-Rate Flexibility," *Review of Economic Studies* **70** 765-83.

Goldberg, G. and R. Hellerstein (2013) "A Structural Approach to Identifying the Sources of Local Currency Price Stability", *Review of Economic Studies* **80(1)** 175-210

Gopinath, G., and O. Itskhoki (2022) "Dominant Currency Paradigm: A Review," *Handbook of International Economics* **6** 45-90.

Gopinath, G., O. Itskhoki, and R. Rigobon (2010) "Currency Choice and Exchange-rate Pass-through," *American Economic Review* **100(1)** 304-336.