

GEORGE WASHINGTON UNIVERSITY
Department of Economics

International Finance: Economics 295, Fall 2005

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Syllabus

I. Course Description

This course focuses on macroeconomic issues and policies in open economies. It begins with a review of a traditional model of an open economy under different exchange rate regimes. It continues with the study of some of the most relevant topics in international finance, such as, determinants of international capital flows, currency crises, financial contagion, current account sustainability and the real exchange rate, and macropolicies in emerging markets and mature economies. Based on this discussion, the course ends by revisiting the debate of fixed versus flexible exchange rate regimes. At this time, special attention is dedicated to the debate about dollarization and currency unions.

II. Examinations

Midterm: October 24, 2005

Final: December 19, 2005

III. Problem Sets

There will be 4 problem sets, two before the midterm and the rest before the final. While problem sets are not required, it is advisable for students to do the problem sets so as to be prepared for the exams.

IV. Basis of Grades

The course grade will be based on: the midterm (35%), the final exam (45%), and class participation (20%).

Reading List

I. Fixed and Floating Exchange Rate Regimes: A Review

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapters 13, 14, 16 (pages 407-434), and 17 (pages 447-463).

II. International Capital Flows

Calvo, Guillermo, Leonardo Leiderman, and Carmen Reinhart, "Inflows of Capital to Developing Countries in the 1990s," *Journal of Economic Perspectives*, vol. 10, (2), Spring 1996, pages 123-139.

Claessens, S., M. Dooley, and A. Warner, 1995, "Portfolio Capital Flows: Hot or Cold?" *World Bank Economic Review*, 9, pages 153-174.

Eichengreen, Barry, "Trends and Cycles in Foreign Lending," in Siebert, Horst, ed., *Capital Flows in the World Economy*, Tubingen: Mohr, 1991, pages 3-28.

Fernandez-Arias, Eduardo, "The New Wave of Private Capital Flows: Push or Pull?" *Journal of Development Economics*, vol. 48, (2), 1996, pages 389-418.

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapter 21.

III. Currency Crises

Goldstein, Morris, Graciela Kaminsky, and Carmen Reinhart, *Assessing Financial Vulnerability: An Early Warning System for Emerging Markets*, Institute for International Economics, 2000. chapters 2, 3, and 5

Kaminsky, G. and C. Reinhart, "The Twin Crises: The Causes of Banking and Balance-of-Payments Problems," *American Economic Review*, June 1999. Also in <http://home.gwu.edu/~graciela>

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapter 17 (pages 460-463 and 482-484).

IV. Contagion

Kaminsky, G. and C. Reinhart, "On Crises, Contagion, and Confusion," *Journal of International Economics*, June 2000. Also in <http://home.gwu.edu/~graciela>

Kaminsky, G., C. Reinhart and C. Végh, “The Unholy Trinity of Financial Contagion,” *Journal of Economic Perspectives*, Vol. 17, Issue 4, Fall 2003, 51-74. Also in <http://home.gwu.edu/~graciela>

Goldstein, Morris, Graciela Kaminsky, and Carmen Reinhart, *Assessing Financial Vulnerability: An Early Warning System for Emerging Markets*, Institute for International Economics, 2000, chapter 6.

Kaminsky, Graciela, Richard Lyons, and Sergio Schmukler, “Economic Fragility, Liquidity, and Risk: The Behavior of Mutual Funds during Crises,” January 2000, in <http://gwu.edu/~graciela>.

Kaminsky, Graciela and Carmen Reinhart, “Bank Lending and Contagion: Evidence from the Asian Crisis,” in Takatoshi Ito and Anne Krueger (eds), *Regional and Global Capital Flows: Macroeconomic Causes and Consequences*, (Chicago: University of Chicago Press for the NBER, 2001), 73-99. Also in <http://home.gwu.edu/~graciela>.

V. Capital Controls

Eichengreen, B. and M. Mussa, (with G. Dell'Araccia, E. Detragiache, G. M. Milesi-Ferretti, and A. Tweedie), “Capital Account Liberalization: Theoretical and Practical Aspects,” International Monetary Fund Occasional Paper No. 172, 1998.

Fischer, Stanley, Richard Cooper, Rudi Dornbusch, Peter Garber, and Dani Rodrick, *Should the IMF Pursue Capital Account Convertibility*, Essays in International Finance, No. 207, May 1998.

Kaminsky, G. and S. Schmukler, “Short-Run Pain, Long-Run Gain: The Effects of Financial Liberalization,” National Bureau of Economic Research Working Paper No. 9787, June 2003. Also in <http://home.gwu.edu/~graciela>.

Prasad, E., K. Rogoff, S. Wei, A. Kose, 2003, Effects of Financial Globalization on Developing Countries: Some Empirical Evidence,” IMF Working Papers.

VI. Fiscal and Monetary Policies

Kaminsky, Graciela, Carmen Reinhart, and Carlos Végh, “When It Rains, It Pours: Procyclical Macropolicies and Capital Flows,” in Mark Gertler and Kenneth S. Rogoff (eds.), *NBER Macroeconomics Annual 2004*, 11-53. NBER Working Paper 10780, September 2004. Also in <http://home/gwu.edu/~graciela>.

VII. Purchasing Power Parity and Real Exchange Rate Fluctuations

Bergin, Paul, Reuven Glick and Alan Taylor, “Productivity, Tradability, and the Long –Run Price Puzzle,” National Bureau of Economic Research Working Paper No. 9739. 2003.

Chinn, Menzie, A Primer on Real Effective Exchange Rates: Determinants, Overvaluation, Trade Flows, and Competitive Devaluations,” National Bureau of Economic Research No. 11521, July 2005.

Froot, Kenneth and Kenneth Rogoff, 1995, “Perspective on PPP and Long-Run Real Exchange Rates,” in Handbook of International Economics, G Grossman and K. Rogoff, eds, Amsterdam, North Holland, pages 1647-88, also in NBER Working Paper No. 4952, April 1996

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapters 15.

Lothian, James, 1990, “A Century Plus of Japanese Exchange Rate Behavior, Japan and the World Economy, 2, pages 47-50.

Taylor, Alan, A Century of Purchasing Power Parity, Review of Economics and Statistics, 84:1, pages 139-150, 2002.

VIII. Current Account Sustainability

Dooley, Michael, David Folkerts-Landau, and Peter Garber, “Savings Gluts and Interest Rates: The Missing Link to Europe,” National Bureau of Economic Research Working Paper No 11520, July 2005.

Edwards, Sebastian, “Is the U.S. Current Account Deficit Sustainable? And if not, How Costly is Adjustment Likely to Be?” National Bureau of Economic Research Working Paper No. 11541, August 2005.

Krugman, P. 2000, “Crises: The Price of Globalization?” paper presented at the Federal Reserve Bank of Kansas City Symposium on *Global Opportunities and Challenges*, August 24-26, 2000, in <http://www.kc.frb.org/publicat/sympos/2000draft.htm>.

Milesi-Ferretti, Gian Maria and Assaf Razin, “Current Account Reversals and Currency Crises: Empirical Regularities,” in *Currency Crises* edited by Paul Krugman, Chicago: University of Chicago Press for NBER (also IMF Working Paper 98/89 in <http://www.imf.org>).

Milesi-Ferretti, Gian Maria and Assaf Razin, “Current Account Sustainability,” Princeton Studies in International Finance, 81, October 1996.

Obstfeld, M. and K. Rogoff, 2000, “Perspectives on OECD Economic Integration: Implications for US Current Account Adjustment,” paper presented at the Federal Reserve Bank of Kansas City Symposium on *Global Opportunities and Challenges*, August 24-26, 2000, in <http://www.kc.frb.org/publicat/sympos/2000draft.htm>.

Obstfeld, Maurice and Kenneth Rogoff, 2005, "The Unsustainable US Current Account Position Revisited," National Bureau of Economic Research Working Paper No. 10869, October 2004.

Reinhart, Carmen, Kenneth Rogoff, and Miguel Savastano, "Debt Intolerance," National Bureau of Economic Research Working Paper No. 9908, August 2003

Taylor, A. M. "A Century of Current Account Dynamics." *Journal of International Money and Finance* 21 (November 2002): 725–48.

IX. Fixed Versus Floating Once More

Calvo, Guillermo and Carmen Reinhart, "Fear of Floating," University of Maryland, Working Paper, 2000, in <http://www.bsos.umd.edu/econ/ciecalvo.htm>

Calvo, Guillermo and Carmen Reinhart, "When Capital Inflows Come to a Sudden Stop: Consequences and Policy Options," June 1999 University of Maryland, in <http://www.bsos.umd.edu/econ/ciecalvo.htm>.

Calvo, Guillermo, "Capital Flows and Capital-Market Crises: The Simple Economics of Sudden Stops," July 1998, University of Maryland, Working Paper, 2000. in <http://www.bsos.umd.edu/econ/ciecalvo.htm>.

Calvo, Guillermo and Carmen Reinhart, "Fixing for Your Life," August 2000, University of Maryland, in <http://www.bsos.umd.edu/econ/ciecalvo.htm>.

Krugman, Paul and Maurice Obstfeld, *International Economics: Theory and Policy*, Addison-Wesley, Seventh Edition, 2005, Chapter 20.

Obstfeld, M., J. C. Shambaugh, and A. M. Taylor. "The Trilemma in History: Tradeoffs among Exchange Rates, Monetary Policies, and Capital Mobility." *Review of Economics and Statistics* (2005).