

Economics 1544: Foundations of International Macroeconomic Policy

Department of Economics, Harvard University

Spring 2023

Class Meetings: Tuesday and Thursday, 10:30 to 11:45 a.m.

Location: Sever 202

Instructor: Professor Anusha Chari

Email: anushachari@fas.harvard.edu

(When sending an email, please put EC 1544 in the subject header)

Office Hours: Thursdays 2:00-3:30 p.m. or by appointment. Please send me an email if you plan to stop by my office hours.

Office Location: M13 Littauer Center

Teaching Assistants:

Eni Dervishi (edervishi@mba2023.hbs.edu)

Sections:

Thursdays 4-5 pm, Science Center 110

Office hours:

Tuesdays 6-7 pm, Science Center 113.

Download Syllabus: [Economics 1544 Syllabus Spr2023.pdf](https://canvas.harvard.edu/courses/116869) from <https://canvas.harvard.edu/courses/116869>

Course Overview

This is an intermediate level international finance and macroeconomics course that uses simple models and empirical methods to analyze key macroeconomic policy challenges confronting the world economy. The core objective of the course is to develop simple macroeconomic models of open economies that can be usefully applied to international economic phenomena. We will examine the balance of payments, the determinants of exchange rates, fiscal policy, monetary policy, exchange rate policy, the effect of fiscal and monetary policies under fixed and floating exchange rate regimes, balance of payment crisis, international macroeconomic dependence, financial globalization, and the challenges facing developing economies. Recent issues that

highlight the interconnected world in which we live such as the Covid-19 pandemic, the war in Ukraine and the implications for the Euro area, China's exchange rate policy, the global transmission of the financial crisis, sovereign debt crises, global imbalances, macroprudential policies, among others, will receive attention. While sophisticated economic reasoning will be involved, purely mathematical technicalities will be kept to a minimum.

Course prerequisites: Students taking this course should have taken an intermediate macroeconomics class (1010b or 1011b). Knowledge of univariate calculus and basic statistics will be assumed.

Course Materials

The required text for the course is International Economics by Paul Krugman, Maurice Obstfeld, and Marc Melitz (KOM), twelfth edition (Pearson 2022). Additional material will be available through the course web site.

Readings can be accessed online on the course website through the links below. Required readings are provided. Additional readings and materials allow you to explore the topics in further depth. This material is optional.

Journal articles can be accessed online through the Harvard Library's e-Journals and e-Resources web site. You should check the web site fairly often for updates and additional material.

Students are expected to take note of economic events of relevance in the world. Empirical knowledge of key relationships, data, and current policy issues will be necessary for passing the course. You are also strongly encouraged to read The Economist magazine and the Financial Times.

Lectures

Lecture slides and notes will be posted on the class web page. You should check the web site fairly often for updates, announcements, and additional material. I will not bring copies to class.

<https://canvas.harvard.edu/courses/116869>

Course Requirements and Grades

In Class Quizzes: Learning Catalytics

Problem Sets: 4 problem sets will be assigned.

Midterm: There will be a 90 minute in-class midterm examination on Thursday, March 9th. If you miss the midterm for any reason, I scale up the remaining work. No makeups under any circumstance.

Final: There will be a 90 minute in-class examination on Tuesday, April 25th. This will test material covered in the second half of the course (post-midterm).

Final Grade Calculations

In Class Quizzes: 10%

Problem sets: 20%

Midterm: 30%

Final: 40%

Accommodations for students with disabilities

Students needing academic adjustments or accommodations because of a documented disability must present their Faculty Letter from the Accessible Education Office (AEO) and speak with the professor by the end of the second week of the term. Failure to do so may result in the Course Head's inability to respond in a timely manner. All discussions will remain confidential, although faculty are invited to contact AEO to discuss appropriate implementation.

Outline of Lectures

1. Exchange Rates and The Foreign Exchange Market

Required Reading: KOM: Chapter 14 (pages 355-364) and Chapter 20 (633-634)

Watch 2-minute video: [A Century of Decline for the British Pound](#) from the Bank of England

Watch 2-minute video: [BIS 2022 Triennial Central Bank Survey](#) by Patrick McGuire

Project Syndicate Commentary: [In the Dollar we Trust](#) by Jeff Frankel. September 2022

Additional materials:

BIS Commentary on [OTC foreign exchange turnover in April 2022](#).

Podcasts | Money Talks: [What's behind the dollar's strength?](#) The Economist

BIS Quarterly Review: [Revisiting the International Role of the US dollar](#). December 2022.

2. Forex Markets, Arbitrage and Parity Conditions

Required Readings:

KOM: Chapter 14 (pages 364-386)

John Cochrane, "[Covered interest parity](#)" and "[More covered interest parity](#)"

Additional Readings:

[Carry Trades and Currency Crashes](#) by Brunnermeier, Nagel and Pedersen. NBER Macroannual 2008. Slides [here](#).

3. **Money, Interest Rates and Exchange Rates**

Required Readings:

KOM Chapter 15

Boesler Matthews, [A breakdown in old rules leads to a rethink on how global markets work](#), Bloomberg news, June 2016.

Additional readings:

Rogoff, Ken, [Dornbusch's Overshooting Model After Twenty-Five Years](#), IMF working paper, February 2002.

Rogoff, Ken, [Perspectives on Exchange Rate Volatility](#), in M. Feldstein ed, International Capital Flows, University of Chicago Press and the NBER, 1999.

Clarida, R. and D. Waldman, [Is Bad News about Inflation Good News for the Exchange Rate?](#) NBER Working paper 13010, April 2007.

Rey, Helene. [Dilemma not Trilemma: The Global Financial Cycle and Monetary Policy Independence](#). Jackson Hole Symposium Paper. August 2013.

4. **Exchange Rates and Prices in the Long Run**

Required Readings:

KOM Chapter 16

World Bank: [New results from the International Comparison Program shed light on the size of the global economy](#)

The Big Mac Index, The Economist, [July 21, 2022](#) and Interactive Tool: [July 21, 2023](#).

Additional readings:

ICP 2017 Report: [Purchasing Power Parities and the Size of World Economies: Results from the 2017 International Comparison Program](#)

[Measuring the Real Size of the Global Economy](#) (Executive Summary (pages xv-xxii) and Conceptual Framework and Overview of Methodology (pages 13-43).

Rogoff, Kenneth. 1996. "[The Purchasing Power Parity Puzzle](#)." Journal of Economic Literature 34: 647-68.

[A less fiery dragon](#). Economics Focus, The Economist, Nov. 29, 2007.

Baker, Dean. [China is the World's Largest Economy: Get Over It](#). CEPR. September 15, 2022.

5. **Current Accounts and Balance of Payments**

Required Readings:

KOM Chapter 13

The Economist, [Schools Brief on Current Account Deficits](#). December 16, 1995

The Economist, [Has Covid-19 killed globalization?](#) May 14, 2020.

Additional readings:

Obstfeld, M. and K. Rogoff, Foundations of International Macroeconomics Chapter 1, "[Intertemporal Trade](#)." (pp. 1-27).

Bernanke, Ben. [The Global Saving Glut and the U.S. Current Account Deficit](#). Sandridge Lecture, Virginia Association of Economics (March 2005).

6. **Fixed Exchange Rates and Foreign Exchange Interventions**

Required Readings:

KOM Chapter 18 (pp. 517-526, 534-537)

Federal Reserve History, "[East Asian Financial Crisis](#)."

[Ilzetki, Ethan, Reinhart, Carmen, and Rogoff, Kenneth, "Exchange Arrangements Entering the Twenty-First Century: Which Anchor will Hold?", Quarterly Journal of Economics, January 2019 - Focus on Section III.](#)

Additional readings:

IMF's Classification of Exchange Rate Arrangements, 2021.

Calvo, Guillermo and Carmen Reinhart, "Fear of Floating", Quarterly Journal of Economics May 2002, available as [NBER Working Paper 7993](#).

7. **Balance of Payments Crises and External Sustainability**

Required Readings:

KOM Chapter 18 (pp. 531-533)

Additional readings:

Bernanke, Ben, ["The dollar's international role: An exorbitant privilege?"](#), Brookings, January 7, 2016.

8. **The Global Capital Market and the Gains from Financial Globalization**

Required Readings:

KOM Chapter 20

Chari, Anusha, Peter Blair Henry, and Hector Reyes (2021). ["The Baker Hypothesis: Stabilization, Structural Reforms, and Economic Growth,"](#) *Journal of Economic Perspectives*, 35 (3), 83–108.

Gourinchas, Pierre-Olivier and Olivier Jeanne (2006). ["The Elusive Gains from International Financial Integration."](#) *Review of Economic Studies*, 07, 73 (3), 715–741.

Chari, Anusha, Peter Blair Henry, and Racha Moussa (2022). ["Do Finite Horizons Matter? The Welfare Consequences of Capital Account Liberalization."](#) *Economic Modelling*, 114, 105903.

Additional readings:

Fischer, Stanley (2003). ["Globalization and Its Challenges."](#) *American Economic Review*, 93 (2), 1–30.

Obstfeld, Maurice (1998) [“The Global Capital Market: Benefactor or Menace?”](#) Journal of Economic Perspectives, Fall 1998, 12 (4), 9–30.

9. Optimum Currency Areas and the European Monetary Union

Required Readings:

KOM Chapter 21

Maya Jolles Matteo Salto Marco Buti, [“The euro – a tale of 20 years: The priorities going forward.”](#) VoxEu, February 2019.

Agnès Bénassy-Quéré et. al. [How to reconcile risk sharing and market discipline in the euro area.](#) VoxEu, January 2018.

10. The International Monetary System & Macro-Financial Linkages

Required Readings:

KOM Chapter 19

Rogoff, Kenneth (1999). [“International Institutions for Reducing Global Financial Instability,”](#) Journal of Economic Perspectives, Fall 1999, 13 (4), 21–42.

Additional readings:

Rey, Helene (2013). [Dilemma not trilemma: The global financial cycle and monetary policy independence.](#) VoxEu.

Chari, Anusha, Karlye Dilts-Stedman, and Christian Lundblad (2021). “Taper Tantrums: QE, its Aftermath and Emerging Market Capital Flows.” *Review of Financial Studies*. <https://doi.org/10.1093/rfs/hhaa044>, March 2021.