

Second semester 2007/08  
Physics Lecture Theatre  
Wednesday 9 - 11 a.m.

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## **ECN209 International Finance**

### **Course web page**

<http://webspaces.qmul.ac.uk/gfella/intfinance07.htm>

### **Office hours**

Room W302, Tuesdays 2 - 3 p.m., Wednesdays 11-12 a.m.

### **Course structure**

The course is articulated in eleven two-hour lectures and ten one-hour classes. The purpose of the classes is to discuss the solutions to the weekly problem sets.

### **Assessment**

The final mark for the course will be made up of two components. 20% of the overall mark will be determined by your average mark in two problem sets that you are supposed to hand in in weeks 5 and 9.

### **Content**

The balance of payments: definitions and measurement.  
The intertemporal approach to the current account.  
The real exchange rate and its determinant.  
Theories of the nominal exchange rate.  
Pros and cons of fixed versus floating exchange rates.  
Costs and benefits of monetary unions.

### **Aims**

The course introduces the analytical tools to think about macroeconomic issues in open economies. It aims at providing a critical understanding of the policy debate and a working knowledge of the tools of the trade.

### **Learning outcomes**

On successful completion of the course you should:

1. be familiar with the main open economy macroeconomic models;
2. understand why countries run current account imbalances;
3. understand how technological factors, fiscal and monetary policy, and other shocks affect the real and nominal exchange rate and the composition of demand;
4. be aware of the relative costs and benefits of alternative exchange rate regimes.

## Required readings

All the lecture notes constitute required reading. I will post them and the text of the weekly problem sets at <http://webspace.qmul.ac.uk/gfella/intfinance07.htm>. Check the same page for any last-minute information.

Also, starred items in the reading list below are required readings. The official textbooks for the course are Krugman Paul and Maurice Obstfeld (**KO** in what follows), *International Economics: Theory and Policy*, 7<sup>th</sup> edition (Addison Wesley) and Blanchard, Olivier *Macroeconomics*, 4<sup>th</sup> edition (Prentice Hall). For a few topics you may find useful Sachs, Jeffrey and Felipe Larrain (**SL** in what follows), *Macroeconomics in the Global Economy*, 1<sup>st</sup> edition (Harvester Wheatsheaf).

## Suggested readings

You are strongly advised to read the Finance and Economics section of *The Economist* from time to time. The keenest among you might also want to read the Comments & Analysis pages in the *Financial Times*. Trying to rephrase what you read in terms of the models you will learn is a great exercise and should make it much more fun. You may also find the RGE Monitor (TM) Global Macroeconomics page useful.

It is at [http://www.rgemonitor.com/10002/Global\\_Macroeconomics](http://www.rgemonitor.com/10002/Global_Macroeconomics)

## SYLLABUS

- 1. Balance of payments: definition and measurement. Gains from intertemporal trade: the intertemporal approach to the current account .**  
\*KO chapter 12, chapter 7 p. 155-1157 and appendix p. 170-173  
Chapter 1 p. 1-12 in Obstfeld and Rogoff, *Foundations of International Economics*, MIT Press 1995  
SL chapter 6
- 2. Tradeable and non-tradeable goods: the law of one price, the real exchange rate. Purchasing power parity. Determinants of the real exchange rate in the long run.**  
\*KO chapter 15 p. 369-373, p. 379-393  
SL chapter 21
- 3. The relationship between the real exchange rate and the current account.**  
\*KO chapter 16, p. 407-411, p. 434-438  
\*Blanchard chapter 19.4-19.5 and appendix to chapter 19.
- 4. The nominal exchange rate as an asset price. Uncovered and covered interest rate parity. The impact of macroeconomic shocks on the real exchange rate.**  
\*KO chapter 13 including the appendix, chapter 15 p. 397-399 and appendix

- 5. Nominal exchange rate determination with flexible prices. The monetary model of the exchange rate.**  
\*KO chapter 15, p. 373-379  
SL chapter 10 p. 303-306
- 6. Nominal exchange rate determination with fixed prices and exogenous expectations. The Mundell-Fleming model of the exchange rate.**  
\*Blanchard chapter 20
- 7. Overshooting of the nominal and real exchange rate with sticky prices and endogenous expectations. Dornbusch model.**  
\*KO chapter 14, p. 362-365  
\*“Why currencies overshoot,” *The Economist*, Dec.1, 1990
- 8. Speculative attacks on fixed exchange rate regime.**  
\*Blanchard chapter 21.2  
R. Flood and P. Garber (1984), “Collapsing Exchange-Rate Regimes,” *Journal of International Economics* 17, 1-13
- 9. The case for fixed and flexible exchange rates. Optimum currency areas. Is the European Monetary Union an optimum currency area?**  
\*KO chapter 20  
\*C. Bean (1992), “Economic and Monetary Union in Europe,” *Journal of Economic Perspectives* 6, 31-52