

ECON 202: APPLIED INTERNATIONAL MACROECONOMICS

Brandeis International Business School, Spring 2009

Professor Osler

International Hall: Tuesdays and Fridays, 9:00-10:30 and 10:30-12:00

Professor Osler
cosler@brandeis.edu

Office Hours: Open door policy
Office: Sachar 107-14

OVERVIEW: This course focuses on the major macroeconomic challenges facing countries today: economic volatility, inflation, exchange-rate instability, international payments imbalances, and banking crises. You will learn to understand the forces driving these developments and the policy options available to countries trying to tame them. You will apply this understanding to explain recent developments in a country that interests you.

This course differs from standard macro courses, whether international or domestic in three ways. First, the course teaches you how to interpret and manipulate macro data. You will learn how to interpret logarithmic charts and why economists typically prefer “seasonally adjusted” data. These skills will help those who move into careers in either policy or finance.

Second, the course covers subjects that are central to understanding today’s macro issues but that are not typically covered elsewhere. One such subject is banking crises, which have triggered, or at least intensified, many of the major macro crises in recent decades. This course teaches you the origins of banking crises, strategies to resolve them efficiently, and regulatory best practice for reducing the likelihood of future banking crises.

Third, the course is structured to help you apply the material to the real world. You will see it applied repeatedly in class, you will practice applying it in problem sets and exams, and you will apply it to analyzing the recent macroeconomic history of a particular country.

By the end of the semester you will feel competent to discuss issues like these: The U.S. is running a record-breaking current account deficit vis-à-vis the rest of the world: should we worry? Most European countries have decided to share a currency, and now there may be reasons for regret: Was it a mistake? Zimbabwe is just getting over a painful hyperinflation: Why would a government do this to people, and how can they stop it?

EVALUATION: Five dimensions of performance will be considered:

1. Project: You will join three other students in applying the class material to evaluating the current exchange-rate regime of the country of your choice. A description of how your country ended up with this regime is due mid-semester (absolute maximum 8 pages double-spaced). These will be edited and returned, and a suitably revised version will serve as part of your final paper. At the end of the semester you will present your evaluation in a short **presentation** to the class (max 10 minutes) and in a *written paper* (max 15 pages for text, tables, and charts). The final paper is due at the beginning of the last class. (Greater detail about the paper is provided at the end of this syllabus.)

2. Practice Problems: Often the material that seems clear during a lecture turns out to be hard to apply later on. To help you bridge the gap between listening to the material and applying

it, you will be assigned practice problems, about one every two weeks. Your answers will be graded.

You will work on these problems with the others in your country focus/project group. This should help you learn from each other. However, you must write up your own answers. This should ensure you understand your answers.

Part of your homework will be to evaluate how closely your economy illustrates the principles presented in class. You should always be ready to share these evaluations with the class.

Problem sets will be due at the “Brandeis” beginning of class (10 minutes after the officially stated time) one week from the day they are distributed. Because answers are often handed out at the time assignments are turned in, late assignments will be given no credit. Late arrival to class is not an acceptable excuse. All problem sets will count towards your grade.

There will be regular sessions with the T.A.s to review old problem sets, go over technical aspects of the course, and get help with current problem sets. Students with no background in macroeconomics are especially encouraged to attend.

3. Midterm exams: There will be two. The first will be Friday February 15 in class. The second will be Thursday March 27 in the afternoon **YOU MUST BE THERE. NO EXCEPTIONS except for dire medical emergencies (or class conflicts in March).**

4. Final exam: This will cover material from the entire semester. It will be closed book. The time of the final is being negotiated with the registrar. There will be no alternative except for documented exam conflicts. **DO NOT MAKE TRAVEL ARRANGEMENTS UNTIL THE TIME IS FINALIZED.**

5. Class participation: Participation in class discussion is critical. This does not require that you stun your classmates with insight. Sharing relevant experiences is very valuable. Clarification questions are also highly valued (if it’s not clear to you, chances are it’s not clear to others). In your homework assignments, you will always be asked to note some recent news item of relevance to current class discussion, and you will sometimes evaluate whether your country fits the principles presented in class. You should always be ready to share these with the class.

Good class participation also involves (i) arriving on time, (ii) remaining seated until class is over, and (iii) remaining quiet and attentive unless contributing to class discussion. To get credit for participation, be sure to use your name card ALL SEMESTER. Attendance will be taken and will count towards your class participation grade.

Grading: In calculating the final grade, the five performance dimensions will be weighed as follows:

Project:	15%
Practice Problems:	15%
Midterm exams:	30%
Final exam:	30%
Class participation:	10%

Note: IBS requires all master’s students to get a B- or better by undergraduate standards to get course credit (in some cases C+ or better). This will require that you fully understand all the important concepts covered in class. Top grades will be assigned to those who not only understand the material but can readily apply it to real-world situations.

DISABILITIES: If you are a student with a documented disability on record at Brandeis and wish to have a reasonable accommodation made for you in this class, please see me immediately.

ACADEMIC INTEGRITY: You are expected to be honest in all of your academic work. You should be familiar with and follow the University's policies on academic integrity (see <http://www.brandeis.edu/studentlife/sdje/ai/>). Instances of alleged dishonesty will be forwarded to the Office of Campus Life for possible referral to the Student Judicial System. Potential sanctions include failure in the course and suspension from the University.

It is academically dishonest to:

- **Copy anyone else's work on practice problems and exams**
- **Let someone copy your work on practice problems and exams**
- **Use anyone else's words without giving credit on the project**

Academic integrity is a very serious matter at IBS. Any potential issue in 202a WILL be referred to the Student Judiciary Committee.

READINGS: The course notes are your primary readings for the course

These are available on Latte. Last year's notes are available from the beginning of the semester. However, I always revise them both before and after class. This year's final version will be posted after the relevant class.

Additional required and optional readings are listed below. Most of them are short since they come from magazines, the web, or newspapers. One magazine frequently used is:

"FD" = *Finance and Development*, The World Bank's magazine for economics practitioners.

Additional readings come from two books:

Krugman/Obstfeld = *International Economics: Theory and Policy*, by Paul Krugman and Maurice Obstfeld (HarperCollins Publishers, NY). Any edition of it is fine. This is the required text for "International Trade" so it shouldn't involve any additional expense.

"Manias" = *Manias, Panics, and Crashes; A History of Financial Crises* (Fifth Edition) by Kindleberger and Aliber (Wiley). I recommend you buy this one—it's cheap, and you have to read a lot of it.

Everything is required if it is not listed as "optional." Big-picture content of articles may be tested on midterms and the final, whether or not the article is discussed in class.

If the article is listed as "handout" then it is not available on the web. Otherwise it will be on Latte or the URL will be provided or both.

Read strategically! Before looking at a chapter or an article ask yourself this: What am I supposed to learn? How is this article related to what was covered in class? Most key lessons can be summarized in a few sentences.

Part of your education here concerns time management. How to prioritize?

- To repeat: **The course notes are your primary readings**
- Chapters from *Manias* and other books. are intended to give you greater in-depth knowledge of critical issues and greater familiarity with macro history.
- “Reference” material from the web is intended to provide another explanation for topics discussed in class. If my presentation doesn’t clarify an issue, perhaps someone else’s will.
- The articles have two purposes: (1) to show you how the concepts covered in class come up in practical situations, and (2) to bring you up-to-date on policy debates.

COURSE OUTLINE AND READING LIST

OVERVIEW: WHY MACROECONOMICS MATTERS

Asset Management, Sales and Trading

“*It is the big picture that makes the big difference*”: Top Down Investing Strategies

http://www.investors-routemap.co.uk/Guidebook_investing_strategies.htm

Money Manager Interview: William Wells, Pope Asset Management , Latte

Interest Rate Overview May 2006 Latte

People’s Lives at Stake

“Zimbabwe_07_07”

“Zimbabwe Beatings” NYTimes March 2007

Central Bank of the Republic of Turkey, “Disinflation Program 2000 short” Latte

Diary of Central Bank Governor Syahril Sabirin Latte

Indonesia - Sabirin supported by Indonesia Central Bank 02 Latte

Bank Indonesia’s Independence in Political Turbulence: Book Review Latte

Venezuela: Central Bank Independence Threatened Latte

MACROECONOMIES IN THE LONG RUN

Prices and Money in the Long Run

Reference: Cecchetti, Money, Banking, and Financial Markets, Chapter 20:

Money Growth, Money Demand, and Modern Monetary Policy (Handout)

Manias, Chapter 1: Financial Crises, A Hardy Perennial

Hyperinflation Episodes in History (Latte)

Reinhart and Savastano, “Realities of Modern Hyperinflation: Despite falling inflation rates worldwide, hyperinflation could happen again,” *Finance and Development* (FD) June2003:

<http://www.imf.org/external/pubs/ft/fandd/2003/06/pdf/kumar.pdf>

Prices and Exchange Rates in the Long run

Reference: *Krugman/Obstfeld*, Chapter 15: Up to (not including) "Beyond PPP: A General Model ..."

Do people really respond to changes in international relative prices? See "Weak Dollar Boosts Growth Without Fueling Inflation": Bloomberg 10/8/07

The Money Supply Process

"In on the ground floor: Jacqueline Irving interviews Linah Mohohlo, Botswana's award-winning central banker," *FD*, December 2004:
<http://www.imf.org/external/pubs/ft/fandd/2004/12/pdf/people.pdf>

Reference: http://en.wikipedia.org/wiki/Money_multiplier

Reference: The Fed's interpretation: "Fedpoints: Reserve Requirements" (Latta)

Optional: What ARE current reserve requirements? If you're curious, here are those for the US: http://en.wikipedia.org/wiki/Reserve_requirements

High Inflation: Deficits, deficits, deficits

Czech National Bank: "Objective of Monetary Policy":

http://www.cnb.cz/en/monetary_policy/objective.html

Reread: Central Bank of Turkey, "Disinflation Program 2000 short" Latta

Rockoff: "Price Controls"

Haman and Prati, "Beating Inflation: The Importance of Luck, Timing, and Political Institutions," *FD* June 2003:

<http://www.imf.org/external/pubs/ft/fandd/2003/06/pdf/hamann.pdf>

Carstens and Jacome, "Taming the monster: How Latin America's central banks survived hyperinflation to become guardians of price stability," *FD*, December 2005:

<http://www.imf.org/external/pubs/ft/fandd/2005/12/carstens.htm>

For curiosity: Hyperinflation Banknotes, <http://tomchao.com/hb1.html>

THE SHORT RUN

Business Cycles, Monetary and Fiscal Policies

"Supply Side Economics to Go," Bruce Bartlett, *NYT* 4/6/07

"India Inflation_02-07," Keith Bradsher, *NYT*

"ECB demotes money supply," Ralph Atkins, July 13, 2007

"Housing Equity and Consumption" *NYT* 11-07

Poole, William, "How predictable is Fed Policy?" *Federal Reserve Bank of St. Louis*

Review Nov/Dec 2005: http://www.stlouisfed.org/news/speeches/2005/10_04_05.htm

Deflation (falling prices)

Kumar: "Deflation: A New Threat?" *Finance and Development*, June 2003:

<http://www.imf.org/external/pubs/ft/fandd/2003/06/pdf/kumar.pdf>

Taka Ito on Japan's Mess: "Monetary Policy Beyond the Zero Bound Interest Rate Policy Under Deflation"

Day-to-day Exchange-Rate Dynamics

Reference: Krugman/Obstfeld Chapter 13, 14

EXCHANGE-RATE REGIMES

Fixed Exchange Rates: Intervention

Ito, "Intervention: Myths and Realities," on web.

"Chinese Reserve Ratio at 14.5" on web

Feldstein, Martin, "Avoiding Currency Crises"

<http://www.nber.org/feldstein/kcfed99.2.pdf>

Reference: Krugman/Obstfeld Chapter 17

Fixed vs. Floating Exchange Rates

Reference: Krugman/Obstfeld Chapter 19, 20

Taylor, Alan, "Global finance: Past and Present. Policymakers in two eras ...
faced the same trilemma of difficult policy trade-offs," FD, March 2004:

<http://www.imf.org/external/pubs/ft/fandd/2004/03/pdf/taylor.pdf>

Schadler, Susan, "Charting a Course Toward Successful Euro Adoption: Newest
EU entrants should reap net gains from joining the euro area," FD, June 2004:

<http://www.imf.org/external/pubs/ft/fandd/2004/06/pdf/schadler.pdf>

Masson and Pattillo, "A Single Currency for Africa?," FD, December 2004:

<http://www.imf.org/external/pubs/ft/fandd/2004/12/pdf/masson.pdf>

Specific Fixed Exchange-Rate Regimes

Reference: Krugman/Obstfeld Chapter 18, Chapter 22

Fischer, Stanley, "Exchange rate regimes: Is the bipolar view correct?" Mimeo
January 2001.

Faruqee, "The Euro turns five: Europe's grand experiment," FD, June 2004:

<http://www.imf.org/external/pubs/ft/fandd/2004/06/pdf/basics.pdf>

Speigel, Mark, "A Currency Board for Indonesia?" *Federal Reserve of San Francisco
Economic Letter* March 1998:

<http://www.sf.frb.org/econsrch/wklyltr/wklyltr98/el98-09.html>

Optional References: Currency Boards: "Introduction to Currency Boards"

<http://users.erols.com/kurrency/intro.htm>

Reem Heakal: "What is a currency board?"

<http://www.investopedia.com/articles/03/051503.asp>

FINANCIAL MARKETS AND ECONOMIC PERFORMANCE

Manias, Chapters 1, 2, Chapter 3 pages 38 (beginning "Speculation often develops in two
stages"). Chapters 5, 6, 8, 9, and 10 are recommended but not required.

"The Norwegian Banking Crisis," Chapter 1, Bent Vale, **pages 1 – 21 only!**

"Greenspan, Bush errors finally home to roost." Stiglitz-on-Greenspan-Bush 08-07

"Basel II Implementation in the U.S.," Randall Krozner speech, July 12, 2007.

Prasad, Eswar S., "Next Steps for China: Why financial sector reform is a crucial
element of a long-term growth strategy," FD, Sept. 2005:

<http://www.imf.org/external/pubs/ft/fandd/2005/09/prasad.htm>

Nicolo et al., "Bridging the 'Great Divide': Poorly developed financial systems in the CIS-7 countries may jeopardize their sustained growth," FD, December 2003:
<http://www.imf.org/external/pubs/ft/fandd/2003/12/pdf/nicolo.pdf>
Felstein versus Meltzer versus Samuelson (office)
Fraud seen as Driver_12-07
Krugman, "Blindly into the Bubble," 12-07
Roubini, Nouriel, "Why monetary policy should respond to asset prices and asset bubbles," Mimeo, September 2005. (Handout)

GLOBAL IMBALANCES

Reference: Krugman/Obstfeld Chapter 12

Dim Sums: Economist on China's investment

"Remittances Down" Samantha Henry, Herald News, 9/4/07

"New Paradigm: Global Imbalances No Big Worry," Alan Wood, The Australian Business <http://www.theaustralian.news.com.au/story/0,25197,22538386-31478,00.html>

McKinsey Global Institute, "The U.S. Imbalancing Act: Can the U.S. Current Account Deficit Continue?" June 2007. Executive summary, pages 9-17 only.

Doi, Ihori, Mitsui: "Sustainability, Debt Management, and Public Policy in Japan," NBER WP 12,357, July 2006. First 4 ½ pages ONLY.

http://www.cfr.org/content/publications/attachments/Twin_DeficitsTF.pdf

Optional Reference: For more on the balance of payments, see: Reem Heikal, "What is the balance of payments?" <http://www.investopedia.com/articles/03/060403.asp>

Today's Understanding of Monetary Policy Best Practice

The old view: Quirk, "Exchange rates as inflation anchors," FD, March 1996:

<http://www.imf.org/external/pubs/ft/fandd/1996/03/pdf/quirk.pdf>

The new view: Croce and Kahn: Monetary regimes and inflation targeting,"

FD, September 2000: <http://www.imf.org/external/pubs/ft/fandd/2000/09/croce.htm>

"The move to inflation targeting," Finance and Development, June 2003:

<http://www.imf.org/external/pubs/ft/fandd/2003/06/pdf/basics.pdf>

Reserve Bank of Australia, "Future Directions for Monetary Policies in East Asia,"

Bulletin October, 2001:

http://www.rba.gov.au/PublicationsAndResearch/Bulletin/bu_oct01/bu_1001_1.pdf

COUNTRY PROJECT

With three other students you will ask, with regard to a country of your choice: What kind of exchange-rate regime do they have now and why? Is it the right regime for that country?

The groups will be assigned very early in the semester. Within one week of that assignment you should have chosen your group and your country. Within a week you should get a spreadsheet with some basic data. Thereafter, you are on your own for data.

Throughout the semester, as part of your homework, you will evaluate how the principles discussed in class are (or are not) reflected in your country. This will require you to become familiar with the variety of basic macro series available and with manipulating them. Guidance will be provided. You should be prepared to discuss your analysis in class.

In the middle of the semester you will submit a history of your country's exchange-rate regimes. This is not a survey of the overall macroeconomy ("GDP went up, then GDP went down"). Instead it should focus on exchange rate regimes, with macro content included to support your interpretation of why the country changed from one regime to the next. You will receive copious comments on this draft. A revised version will be part of your project.

Your grade depends on (1) your understanding of the issues and (2) the quality of your exposition (organization, sentence construction, clarity). Your analysis should be illustrated with charts or tables. The written document should be roughly 20 pages, double-spaced, including all charts and tables. **You will have to edit your text multiple times.**

Citing sources: **You must cite every source and you may not quote other writers without attribution! Direct quotes are appropriate when a particular author had a unique insight you want to share. They are not appropriate for basic macroeconomic information.**

More information on this project is available on Latte.

THE FOLLOWING COUNTRIES WILL NOT BE AVAILABLE THIS YEAR ('09):

Bolivia	Brazil	El Salvador
Hong Kong	Iran	Japan
Malaysia	Morocco	Norway
Peru	Romania	Singapore
South Africa	Sweden	Switzerland
Thailand	Tunisia	Turkey
United Arab Emirates	United Kingdom	U.S.A.
Uruguay	Venezuela	Vietnam

In choosing your country, consider data availability. Small countries and transition countries usually have limited data. Note also: Countries that have experienced hyperinflation provide dramatic stories, but their data can be difficult to deal with. Exchange rates and prices will be either infinitesimally small (early on) or astronomically big (more recently).

Your main source of data is Datastream. Other potentially good sources of data include your country's central bank, the World Bank, and the Economist Intelligence Unit (to which we have limited access through the Library). Jason Bernard, a reference librarian, is extremely helpful: x6-4740.