

**Econ 871: Advanced International Economics**  
**Fall 2008**

**Date:** 3 September, 2008

**Instructor:** Lukasz Drozd

**Office hours:** Thursday, 5pm-6pm in SOC SCI 7426

**Time and location:** Mon/Wed 9:30am - 10:45am, 52 Bascom

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**Prerequisite**

First year PhD macro sequence.

**Course Description**

The course covers international trade and selected topics in open economy macro at the PhD level. The objective of the class is to prepare you to start your own independent research in this area.

It is recommended that you take both Econ 871 and Econ 872 (taught later by Charles Engel). The first 4-5 weeks of Econ 871 will be devoted to cover some introductory material on international trade. Rest of the class will focus on open economy macro.

**Revisions**

There will be revisions to the syllabus during the course. I may add topics, drop topics and modify the reading list. Make sure that you have the most recent version.

**Webpage**

Course materials, including the most recent version of the syllabus will be available at: <http://www.econ.wisc.edu/~ldrozd/871.htm>

**Requirements**

There will be 2-3 homework assignments. At the end of the introductory part of the course, there will be an exam (approx. after about 8-9 weeks of classes). In addition, each of you will give a 1.15 min. presentation of a recent job market paper from the list that I will post online later online. You will be asked to present the paper, defend it, and address the questions. It will require from you to read some of the related literature.

**Grading Policy**

Homework 30%, Exam 30%, Presentation: 30%, Class participation and attendance: 10%.

**Textbooks**

I will not follow any textbook, and there is no textbook for this course. However, you may find the following books helpful for some topics:

Obstfeld and Rogoff, *Foundations of International Macroeconomics*, MIT Press

Ljungqvist and Sargent, *Recursive Macroeconomic Theory*, MIT Press

## Reading List and Tentative List of Topics

\*To be partially discussed in class

\*\*Likely to be mentioned or partially discussed in class

### *International Trade*

- \*Anderson, J. E. and E. van Wincoop (2003) “Gravity with Gravitas: A Solution to the Border Puzzle,” *American Economic Review*, 93: pp. 170-192.
- \*McCallum, J. “National Borders Matter: Canada-US Regional Trade Patterns,” *AER* 1995.
- \*Dornbusch R., S. Fischer and P. A. Samuelson: “Comparative Advantage, Trade, and Payments in a Ricardian Model with a Continuum of Goods”, *The American Economic Review*, Vol. 67, No. 5 (Dec., 1977), pp. 823-839
- \*Eaton, J. and S. Kortum, “Technology, Geography, and Trade,” *Econometrica*, 70 (5), 2002, 1741-1779.
- \*Krugman Paul R. and Elhanan Helpman, *Market Structure and Foreign Trade* (MIT, 1986), Chapters 6-11
- \*Melitz, M. J., “The Impact of Trade on Intra-Industry Reallocations and Aggregate Industry Productivity,” *Econometrica*, 71 (2003), pp. 1695-1725.
- \*Chaney, T., “Distorted Gravity: Heterogeneous Firms, Market Structure, and the Geography of International Trade,” University of Chicago, 2005.
- \*\*Bernard, A., J.Eaton, B. Jensen, and S. Kortum, “Plants and Productivity in International Trade,” *American Economic Review*, Vol. 93(4), pp. 1268-1290, September 2003.
- \*\*Alvarez, F. and R. Lucas, “General Equilibrium Analysis of the Eaton-Kortum Model of International Trade”, Working Paper, 2004
- \*\*Broda, Christian and David E. Weinstein, “Globalization and the Gains from Variety,” *Quarterly Journal of Economics*, May 2006, CXXXI (2), pp. 541-585.
- \*\*Helpman, E., M.J. Melitz and Y. Rubinstein, “Trading Partners and Trading Volumes,” Harvard University manuscript, 2004.
- \*\*Obstfeld M., and K. Rogoff, 2000, “The Six Major Puzzles in International Macroeconomics: Is There a Common Cause?”, NBER working paper.
- Eaton J., S. Kortum, and F. Kramarz, “An Anatomy of International Trade: Evidence from French Firms,” University of Minnesota, manuscript, 2005.

*International Business Cycle and International Risk Sharing*

- \*Harold L. Cole and Maurice Obstfeld, “Commodity Trade and International Risk Sharing: How Much Do Financial Markets Matter?,” NBER Working Papers 3027, 1991
- \*David, Patrick Kehoe, and Finn Kydland, 1995 “International Business Cycles: Theory vs. Evidence,” in Thomas F. Cooley, ed., *Frontiers of Business Cycle Research*, Princeton University Press
- \*Heathcote and Perri, “Financial autarky and international business cycles” *Journal of Monetary Economics*, 2002
- \*Mendoza, E. “Real Business Cycles in a Small Open Economy,” *American Economic Review*, 81(4), September 1991.
- \*Schmitt-Grohe and Uribe, 2003, “Closing Small Open Economy Models” *Journal of International Economics*
- \*Drozd L., and J. Nosal, 2008, “Understanding International Prices: Customers as Capital”, manuscript, UW-Madison.
- \*\*Drozd L., and J. Nosal, 2008, “Long-Run Price Elasticity of Trade and the Trade-Comovement Puzzle”, manuscript, UW-Madison.
- \*\*Kehoe P. and F. Perri, 2002, “International Business Cycles with Endogenous Incomplete Markets” *Econometrica* 2002. (+Chapter 20, Lundquist and Sargent)
- \*\*Chari V.V., P.J. Kehoe, and E. McGrattan, 2002, “Can Sticky Price Models Generate Volatile and Persistent Real Exchange Rates?” *Review of Economic Studies*, July.
- \*\*Kehoe P.J. and V. Midrigan, 2007, “Sticky prices and sectoral real exchange rates,” Working Papers 656, Federal Reserve Bank of Minneapolis.
- \*Schmitt-Grohe S. and M. Uribe, 2004, “Solving Dynamic General Equilibrium Models Using a Second-Order Approximation to the Policy Function,” *Journal of Economic Dynamics and Control*, vol. 28, January, pp. 755-775.
- \*\*Heathcote J., Perri F, 2008, “The International Diversification Puzzle is Not as Bad as You Think”
- Lucas, Robert Jr., 1982. “Interest rates and currency prices in a two-country world,” *Journal of Monetary Economics*, Elsevier, vol. 10(3), pages 335-359.
- Stockman, A. C. and L. Tesar. 1995. “Tastes and Technology in a Two-Country Model of the Business Cycle: Explaining International Comovements,” *American Economic Review*, 85, 168-185.

### *Business Cycle in Emerging Markets*

- \*Aguiar, M. and G. Gopinath. 2004. Emerging Market Business Cycles: The Cycle is the Trend. *Journal of Political Economy*, Vol 115(1), pp. 69-102, February 2007
- \*Neumeyer, Pablo A. and Perri, Fabrizio. “Business Cycles in Emerging Economies: The Role of Interest Rates.” National Bureau of Economic Research (Cambridge, MA), Working Paper 10387, 2004.
- \*\*Uribe, M. and Z. V. Yue. “Country Spreads and Emerging Countries: Who Drives Whom?”, *JIE* 2004

### *Sudden Stops*

- \*Kehoe, P.J., V. V. Chari and E. McGrattan. “Sudden Stops and Output Drops,” Federal Reserve Bank of Minneapolis Staff Report 353, January 2005.
- \*Mendoza, Enrique G. “ ‘Sudden Stops’ in an Equilibrium Business Cycle Model with Credit Constraints: A Fisherian Deflation of Tobin’s  $q$ ,” manuscript, University of Maryland, 2004.
- \*Kaminsky, G. and C. Reinhart. 1999. “The Twin Crises: The Causes of Banking and Balance of Payments Problems,” *American Economic Review* 89, 473-500.
- \*\*Milesi-Ferretti, G. and A. Razin, “Current Account Sustainability: Selected East Asian and Latin American Experiences,” NBER Working Paper Series, No. 5791, October 1996.

### *Sovereign Debt and Default Risk*

- \*Eaton, J. and R. Fernandez: “Sovereign Debt”, *Handbook of International Economics III*, North-Holland, 1995.
- \*Bulow J. and K. Rogoff. “Sovereign Debt: Is to Forgive to Forget?,” *The American Economic Review*, Vol. 79, No. 1 (Mar., 1989), pp. 43-50
- \*Bulow, J. and K. Rogoff. “A Constant Recontracting Model of Sovereign Debt,” *Journal of Political Economy*, 97, 155-78, February 1989.
- \*Zame, W. (1993). “Efficiency and the Role of Default When Security Markets are Incomplete,” *American Economic Review*, 83(5): 1142—1164.
- \*Eaton, J., and M. Gersovitz (1981). “Debt with Potential Repudiation: Theoretical and Empirical Analysis,” *Review of Economic Studies*, vol XLVII, 289-309.

- \*Arellano, C. 2004. “Default Risk and Income Fluctuations in Emerging Economies,” mimeo, University of Minnesota (forthcoming American Economic Review).
- \*\*Cole, Harold L. and Patrick J. Kehoe. “Reputation Spillover Across Relationships: Reviving Reputation Models of Debt,” Federal Reserve Bank of Minneapolis Staff Report 209, March 1996
- \*\*Kletzer, K. and B. D. Wright. “Sovereign Debt as Intertemporal Barter,” American Economic Review, (90): 621-39, June 2000

### *Capital Flows and Global Imbalances*

- \*Quadrini, V., E. Mendoza and V. Rios-Rull, “Financial Integration, Financial Deepness and Global Imbalances,” mimeo, 2007
- \*Fogli A. and F. Perri. “The ”Great Moderation” and the US External Imbalance,” NBER Working Papers 12708, 2006
- \*\*Andres Arias, Gary D. Hansen, Lee E. Ohanian: “Why Have Business Cycle Fluctuations Become Less Volatile?”, NBER Working Paper No. 12079
- Caballero, F., Fahri, E., and J. P. Gourinchas. “An Equilibrium Model of “Global Imbalances” and Low Interest Rates”, American Economic Review, 98(1), 2007
- \*Pierre-Olivier Gourinchas, H. Ray, 2007,: “International Financial Adjustment,” Journal of Political Economy, vol 115, no. 4.
- \*Pierre-Olivier Gourinchas, Olivier Jeanne: “Capital Flows to Developing Countries: The Allocation Puzzle,” NBER Working Paper No. 13602