BGP-620: International Macroeconomics  
Syllabus, Spring 2018  
Harvard Kennedy School, Harvard University  

Staff:  Professor: Jeffrey Frankel  Littauer 217, HKS  
Faculty Assistant: Minoo Ghoreishi  Belfer 505  (617) 384-7329  
Teaching Fellow: Haiyang Zhang  Course Assistant: Abhisek Ghosh  

Times:  Lectures: Tuesdays-Thursdays 2:45-4:00, Littauer 280.  
Prof. office hours: Tuesday 4:15-5:15 and Wednesday 1:15-2:30 p.m., Littauer 217.  
Final exam: Wednesday, May 2, 2-5:00, Littauer 382.  

Prospectus  

Topics covered: What is the role of monetary and fiscal policy in an open economy? What determines the balance of payments, the level of economic activity, and inflation? Should countries fix their exchange rates, or let them float? How does the globalization of financial markets affect these and other policy questions?  

This course deals with the macroeconomics of open economies. The emphasis will be on models appropriate to major countries. Topics include the foreign exchange market, devaluation, and import and export elasticities; the simultaneous determination of the trade balance, national income, the balance of payments, money flows and price levels; capital flows and our increasingly-integrated financial markets; monetary and fiscal policy in open economies; international macroeconomic interdependence and policy coordination; supply relationships and nominal anchors for monetary policy; currency unions, the determination of exchange rates in international money markets; and international portfolio diversification.  

Nature of the approach: The course is a relatively comprehensive treatment of standard textbook models in the area of open-economy macroeconomics. Although real-world examples are sprinkled throughout, the course relies very heavily on algebraic and graphical analysis, as is customary in economics classes.  

Who should take the course: Only those who are quite comfortable with algebraic and graphical analysis should enroll. This is not an appropriate course for students who want some basic general exposure to international economics.  

Prerequisites: Familiarity with the principles of economics and with intermediate-level macroeconomics is necessary, particularly standard models of monetary and fiscal policy and their effects on interest rates and income. API-101 and API-121, respectively, satisfy the prerequisites for micro and macroeconomics, as do Econ 1010a (or 1011a) and 1010b (or 1011b) in FAS. Some knowledge of international trade theory and econometric techniques is also desirable, but definitely not essential. Students must be comfortable with algebra.  

Problem Sets: Seven quantitative problem sets are planned. For each problem set, students can choose whether to work alone or in groups, but must indicate which option they have chosen when handing in the problem set. Those who work alone will receive a small point boost on that problem set.  

Grading: Problem sets -- 25%; mid-term exam -- 25%; final exam -- 50%.  

Please check the dates for the exams, especially the final exam. If you cannot take the exams, you should not enroll in the course.
## BGP 620 – International Macroeconomics

### Course Outline

**Prof. Jeffrey Frankel, Harvard Kennedy School**

Friday sessions will consist of review, extensions, applications, and questions and answers regarding the week’s topic.


<table>
<thead>
<tr>
<th>Topic</th>
<th>Chapter in WT &amp; P</th>
<th>Lecture number and date</th>
<th>PS due dates (approx.)</th>
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</thead>
<tbody>
<tr>
<td><strong>ELASTICITIES &amp; THE TRADE BALANCE</strong></td>
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<tr>
<td>Balance of payments accounting</td>
<td>15</td>
<td>1</td>
<td>Jan. 23</td>
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<tr>
<td>Supply and demand for foreign exchange</td>
<td>16.1</td>
<td>2</td>
<td>Jan. 25</td>
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<tr>
<td>Export and import elasticities</td>
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<tr>
<td>Empirical effects of devaluation on the trade balance</td>
<td>16.2</td>
<td>3</td>
<td>Jan. 30</td>
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<tr>
<td><strong>THE KEYNESIAN MODEL</strong></td>
<td></td>
<td></td>
<td>Problem set 1 due</td>
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<tr>
<td>National saving identity; fiscal multiplier in an open economy</td>
<td>17.1-17.2</td>
<td>4</td>
<td>Feb. 1</td>
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<tr>
<td>Export multiplier; &amp; the transfer problem.</td>
<td>17.3 }</td>
<td>5</td>
<td>Feb. 6</td>
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<tr>
<td>Large-country repercussions &amp; Transmission of disturbances.</td>
<td>17.5-17.6</td>
<td>6</td>
<td>Feb. 8</td>
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<tr>
<td>Expenditure-reducing policies vs. -switching policies</td>
<td>18.2</td>
<td>7</td>
<td>Feb. 13</td>
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<tr>
<td><strong>MONEY &amp; THE BALANCE OF PAYMENTS</strong></td>
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<td>Problem set 3 due</td>
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<tr>
<td>Monetary factors</td>
<td>18.3</td>
<td>8</td>
<td>Feb. 15</td>
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<tr>
<td>Reserve flows &amp; the gold standard</td>
<td>19.1 }</td>
<td>9</td>
<td>Feb. 20</td>
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<tr>
<td>Purchasing Power Parity</td>
<td>19.2-19.4</td>
<td>10</td>
<td>Feb. 22</td>
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<tr>
<td>Topic</td>
<td>Chapter in WT &amp; P</td>
<td>Approx. lecture number and date</td>
<td>Problem</td>
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<tr>
<td>GLOBALIZATION OF FINANCIAL MARKETS</td>
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<tr>
<td>Financial integration; spot &amp; forward exchange market</td>
<td>21.1-21.3</td>
<td>11 Feb.27 set 4 due</td>
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<tr>
<td>Emerging markets; Pros &amp; cons of financial opening</td>
<td></td>
<td>12 Mar. 1</td>
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<tr>
<td>FISCAL &amp; MONETARY POLICY UNDER INTERNATIONAL CAPITAL MOBILITY</td>
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<tr>
<td>Mundell-Fleming - with exchange rate fixed</td>
<td>22.1-22.3</td>
<td>13 Mar. 6</td>
<td>Midterm exam 14 Mar. 8</td>
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<tr>
<td>Applications/problems of policymaking Mundell-Fleming model</td>
<td>22.4-22.7; 24.1</td>
<td>15 Mar. 20</td>
<td>Spring break March 10 - 18</td>
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<td>-- with the exchange rate floating.</td>
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<td>16 Mar. 22</td>
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<td>Perfect capital mobility &amp; Impossible Trinity</td>
<td>23.3-23.4</td>
<td>17 Mar. 27</td>
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<td>EM countries and crises</td>
<td>24.2-24.5, 24.7-24.9</td>
<td>18 Mar. 29</td>
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<tr>
<td>INTERDEPENDENCE AND COORDINATION</td>
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<td>Problem</td>
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<tr>
<td>Effects of fiscal expansion in a large country</td>
<td>25.1</td>
<td>19 Apr. 3 set 5</td>
<td>due</td>
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<td>Estimates of transmission</td>
<td>25.2</td>
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<tr>
<td>International policy coordination</td>
<td>25.3</td>
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<td>SUPPLY AND INFLATION</td>
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<td>Problem</td>
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<tr>
<td>Aggregate Supply and wages</td>
<td>26.1</td>
<td>20 Apr. 5 set 6</td>
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<tr>
<td>Inflation and anchors for money</td>
<td>26.3-26.4</td>
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<tr>
<td>Exchange rate regimes and monetary unions</td>
<td>26.5-26.6</td>
<td>21 Apr. 10 due</td>
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<tr>
<td>Case study: recent macroeconomics in China</td>
<td>26.6</td>
<td>22 Apr.12</td>
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<tr>
<td>EXPECTATIONS AND EXCHANGE RATE MODELS</td>
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<td>Problem</td>
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<tr>
<td>Interest parity conditions</td>
<td>27.1</td>
<td>23 Apr.17 set 7</td>
<td></td>
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<tr>
<td>The monetarist/Lucas model</td>
<td>27.2-27.3</td>
<td>24 Apr.19 due</td>
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<tr>
<td>The overshooting model &amp; forecasting</td>
<td>27.4-27.6, 28.1</td>
<td>25 Apr.24</td>
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<tr>
<td>Currency risk &amp; portfolio diversification</td>
<td>28.1-28.4</td>
<td>26 Apr.26</td>
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**Final exam:** Wednesday, May 2, 2:00-5:00 p.m., Littauer 382.
Readings

The required textbook reading is the second half of *World Trade and Payments*, R.Caves, J.Frankel, and R.Jones, 10th ed. (Addison-Wesley), 2007.

Unless otherwise indicated, links to readings listed below are posted on the course webpage.

* asterisk denotes recommended readings
** double asterisk denotes most highly required
(L numbers correspond to scheduled lectures.)

**Balance of Payments Accounting** (Lecture 1)

“The Other Deficit,” *The Economist*, October 17, 2015. **

**The Trade Balance**

The effect of currency depreciation on the trade balance (L2-L3)

“Swiss cheesemakers long for a stronger euro,” *Financial Times*, August 1, 2017. *

Application of the marginal propensity to import to the Great Recession of 2008-09 (L4)


**Fiscal Policy and Keynesian Multipliers** (L5-7, L13-16)


“Swiss central bank blames strong franc as eurozone pulls away,” *Financial Times*, June 16, 2017. *
Money and the Balance of Payments (L8-L9)
The gold standard and Bretton Woods (L9)

Purchasing power parity (L10)
*The Big Mac index: Interactive Currency Comparison Tool* [E.g., January  2018.] **

The Globalization of Financial Markets
The growth of forex trading and other financial markets (L11)
“Future Perfect,” *The Economist*, Nov. 27, 1999, pp. 81-82. *

Pros and cons of open financial markets (L12)

The Impossible Trinity (L17)

Emerging markets: inflows and crises (L18)
The Global Macroeconomic System

International macroeconomic policy coordination (L19)

“What a carry-on” Buttonwood, Economist Nov.21, 2015. *

Monetary expansion, supply and inflation (L20)
“Some like it hot: Which emerging economies are at greatest risk of overheating?” Economist, July 2, 2011, p. 65.  **
“The desperation of independents: Stubbornly low interest rates may mean the end of central-bank autonomy,” The Economist, August 6, 2016

Case Study: Recent macroeconomic policy in China (L22)

Exchange Rates

Monetary union (L21)
Jürgen Stark, “German prudence is not to blame for the eurozone's ills,” Financial Times, Feb.11, 2015. *

Monetary determination of exchange rates (L23-L25)

The carry trade and bias in the forward exchange market (L26)