

AEB 7240 Macroeconomic Theory in Open Economies II
Spring 2017

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Office hours – By appointment

Course Description: Essential elements of macroeconomic theory and policy in world of interdependent nations. Lectures, student discussions, and problem sets are designed to give students an advanced background in the essential elements of macroeconomic theory and policy in a world of interdependent nations.

Prerequisites: Permission of the instructor. Calculus and intermediate macroeconomics are helpful.

Course Objective: To enable students to read and comprehend current economic literature in the area of open macroeconomics and to give students the necessary foundation to continue self-study and to begin research in this area.

Methods by which students will be evaluated and grading system

Two mid-term exams	45%
Final exam	45%
Class participation/problem sets	<u>10%</u>
	100%

Grade Scale

A	94-100%
A-	93-90%
B+	87-89%
B	84-86%
B-	80-83%
C+	77-79%
C	74-76%
C-	70-73%
D+	67-69%
D	64-66%
D-	60-63%
E	Below 60%

Attendance Policy

Students are expected to prepare for class meetings by completing assigned readings and problem sets. Students are encouraged to attend all classes. Frequent absences will reflect negatively on class participation evaluation.

Make-up policy

No make-up mid-term exams will be administered. If a student misses a mid-term exam, the lower grade of the other mid-term exam and of the final exam will be awarded for the grade of the missed examination. A final exam must be taken in order to receive the final grade.

Textbooks

Required

- Friedman, M. and A. J. Schwartz. *The Great Contraction, 1929-1933*, new edition. Trenton, NJ: Princeton University Press, 2008, Paper.

Recommended

Main text providing the framework for the course:

- Stevenson, A., V. Muscatelli and M. Gregory. *Macroeconomic Theory and Stabilisation Policy*. London: Philip Allen, 1988.

Core texts for open macroeconomics:

- Argy, V. *International Macroeconomics: Theory and Policy*. London: Routledge, 1994:
- Dornbusch, R. *Open Economy Macroeconomics*. New York: Basic Books, Inc., 1980.

Course Outline and Reading Guide

I have provided chapter references for the basic course textbooks as well as several others in the following outline. You should be able to use these chapter references to select alternative chapters from any other texts you may choose to pursue. If in doubt, see me.

1. Aggregate Demand and IS: LM
 - A. *Stevenson et al., Chapter 1.
 - B. Crystal and Price, Chapter 1, pp. 1-14.
 - C. Romer, Chapter 5.1, 5.2, 5.4.
2. Aggregate Supply and the Neoclassical synthesis
 - A. Romer, Chapter 5.4.
 - B. *Stevenson et al., chapter 2, pp. 26-44.
 - C. Chrystal and Price, chapter 1, pp. 15-21, and chapter 2.
3. Aggregate supply and new classical macroeconomics
 - A. Romer, Chapter 5.5, 5.6, and chapter 6, Parts A & B.
 - B. *Stevenson et al., Chapter 3.
 - C. Crystal and Price, Chapter 3, 4, and 7.
 - D. Peel, D. "New Classical Macroeconomics, " Chapter 3 in Greenaway.
 - E. Fischer, S. "Recent Developments in Macroeconomics," *The Economic Journal*, June 1988, Sections H and HI, P. 301-315.
 - F. Blanchard and Fisher, Chapter 7 (relevant sections).
 - G. Lucas, R. E., Jr., and L. A. Rapping. "Real Wages, Employment, and Inflation." *Journal of Political Economy* 77 (1969):721-754.
 - H. Lucas, R. E., Jr. "Some International Evidence on Output-Inflation Tradeoffs." *American Economic Review* 63 (1973): 326-334.
 - I. Lucas, R. E., Jr. "An Equilibrium Model of the Business Cycle." *Journal of Political Economy* 83 (1975):1113-1144.
 - J. Lucas, R. E., Jr. "Methods and Problems in Business Cycle Theory." *Journal of Money, Credit and Banking* 12 (1980): 696-715.
 - K. Sargent, T. J. and N. Wallace. "Rational Expectations, the Optimal Monetary Instrument, and the Optimal Money Supply Rule." *Journal of Political Economy* 83 (1975): 241-254.

- L. Sargent, T. J. "The Observational Equivalence of Natural and Unnatural rate Theories of Macroeconomics." *Journal of Political Economy* 84 (1976): 631-640.
- M. Barro, R. J. "Unanticipated Money, Output, and the Price Level in the United States." *Journal of Political Economy* 86 (1978): 549-580.
4. New Keynesian model of aggregate supply
- A. Romer, Chapter 6, Part C, Chapter 10.
 - B. *Stevenson et al., Chapter 4.
 - C. *Fischer, Stanley. "Long-Term Contracts, Rational Expectations, and the Optimal Money Supply Rule." [The Journal of Political Economy](#), Vol. 85, No. 1 (Feb., 1977), pp. 191-205.
 - D. Crystal and Price, Chapter 5.
 - E. Blanchard and Fisher, Chapter 8.
 - F. Fischer, S. "Recent Developments in Macroeconomics," *The Economic Journal*, June 1988, Section IV, pp. 315-325.
 - G. *Blanchard, O. and L. F. Katz. "What We Know and Do Not Know about the Natural rate of Unemployment." *Journal of Economic Perspectives* 11, 1 (1997): 51-72.
 - H. *Clarida, R., J. Gali, and M. Gertler. "The Science of Monetary Policy: A New Keynesian Perspective." *Journal of Economic Literature* 37 (1999), pages 161-1707.
 - I. *Greenwald, B. and J. Stiglitz. "New and Old Keynesians," *Journal of Economic Perspectives* 7 (1993): 23-44.
 - J. *Galbraith, J. K. "Time to Ditch the NAIRU." *Journal of Economic Perspectives* 11,1 (1997): 98-103.
 - K. *Gordon, R. "The Time-Varying NAIRU and Its Implications for Economic Policy." *Journal of Economic Perspectives* 11 (1997): 11-32.
 - L. *Gordon, R. "What is New Keynesian Economics?" *Journal of Economic Literature* 28 (1990), pages 1135-1163.
 - M. King, R. G. "Will the New Keynesian Macroeconomics Resurrect the IS: LM Model?" *Journal of Economic Perspectives* 3 (1993): 67-82.
 - N. Rogerson, R. "Theory Ahead of Language in the Economics of Unemployment." *Journal of Economic Perspectives* 11,1 (1997): 73-92.
 - O. Stiglitz, J. "Reflections on the Natural Rate Hypothesis." *Journal of Economic Perspectives* 11,1 (1997): 3-10.
 - P. Tobin, J. "Price Flexibility and Output Stability: An Old Keynesian View." *Journal of Economic Perspectives* 7 (1993): 45-66.
5. Real Business Cycles
- A. *Mankiw, N. G. "Real Business Cycles: A New Keynesian Perspective," *Journal of Economic Perspectives* 3 (1989): 79-90.
 - B. *Plosser, Charles I. "Understanding Real Business Cycles." *Journal of Economic Perspectives* 3 (1989): 51-77.
6. Balance of payments concepts, income determination, and the trade balance
- A. *Dornbusch, *Open Macroeconomics*, Chapters 1-3.
 - B. Gandolfo, Chapters 13, 14.
 - C. Husted and Melvin, Chapter 12.
7. Exchange Rates and the Balance of Payments: The Elasticity Approach
- A. *Dornbusch, *Open Macroeconomics*, Chapter 4.
 - B. *Argy, Chapter 12.
 - C. Pilbeam, Chapter 2 and 3.
 - D. Harberger, Arnold C. "Currency Depreciation, Income, and the Balance of Trade." *Journal of Political Economy* 58, No. I (Feb. 1950): 47-60. Reprinted in Caves and Johnson (1968): 341-58.

- E. Husted and Melvin, Chapter 13-17.
8. Open macroeconomics, Mundell-Fleming
- A. Romer, Chapter 5.3.
 - B. *Dornbusch, *Open Macroeconomics*, Chapter 10.
 - C. *Argy, Chapter 6-8.
 - D. *Stevenson et al., Chapter 7, pp. 211-233, and chapter 8, pp. 265-28 1.
 - E. Pilbeam, chapter 2 and 4.
 - F. Chrystal and Price, Chapter 6, pp. 93-98.
9. Open macroeconomics, Mundell-Fleming, cont.
- A. Romer, Chapter 5.3.
 - B. *Dornbusch, *Open Macroeconomics*, Chapter I 1, Section 1.
 - C. *Argy, Chapter 13-15.
 - D. *Stevenson et al., chapter 8, pp. 257-265.
 - E. Pilbeam, chapter 5, 7, pp. 165-186, and chapter 8.
10. The Monetary Approach to the Balance of Payments
- A. *Dornbusch, *Open Macroeconomics*, Chapter 7.
 - B. *Argy, Chapter 17.
 - C. *Stevenson et al., Chapter 7, pp. 234-245.
 - D. Pilbeam, chapter 5, 7, pp. 165-186, and chapter 8.
 - E. Chrystal and Price, Chapter 6, pp. 98-101.
 - F. *Dornbusch, Rudiger. "Devaluation, Money, and Nontraded Goods." *American Economic Review* 63, No. 5 (Dec. 1973): 871-83. Also in Frenkel and Johnson (eds.), *The Monetary Approach: 168-86*, and in ERI.
 - G. Frenkel, Jacob A. and Harry G. Johnson. "The Monetary Approach to the Balance of Payments: Essential Concepts and Historical Origins." In Frenkel, J.A. and H.G. Johnson (eds.) *The Monetary Approach to the Balance of Payments*.
 - H. Johnson, Harry G. "Towards a General Theory of the Balance of Payments." In his *International Trade and Economic Growth*. Cambridge: Harvard University Press, 1961: 153-68. Reprinted in Caves and Johnson (1968): 374-88 and in Frenkel and Johnson (1976): 46-63.
 - I. Johnson, Harry G. "The Monetary Approach to Balance of Payments Theory." In Frenkel, J.A. and Johnson, H.G. (eds.) *The Monetary Approach to the Balance of Payments*. London: Allen & Unwin, and Toronto: University of Toronto Press, 1976.
 - J. Connolly, Michael and Taylor, Dean. "Testing the Monetary Approach to Devaluation in Developing Countries." *Journal of Political Economy* 84, No. 4 (Aug. 1976): 849-60.
 - K. Magee, Stephen P. "The Empirical Evidence on the Monetary Approach to the Balance of Payments and Exchange Rates." *American Economic Review* 66 (May 1976): 163-70.
 - L. Husted and Melvin, Chapter 18.
11. The Determination of Exchange Rates: The Monetary Approach
- A. *Argy, Chapter 17.
 - B. *Stevenson et al., Chapter 8, pp. 265-274.
 - C. Pilbeam, chapter 5, 7, pp. 165-186, and chapter 8.
 - D. Chrystal and Price, Chapter 6, pp. 10 I - 104.
 - E. Bailey & McMahon, Chapter 3, sec. 3.1, 3.2, 3.3; 8.2, 8.3.
 - F. Dornbusch, R. "Purchasing Power Parity." In ERI, pp. 265-79.
 - G. Dornbusch, Rudiger, *Dollars, Debts, and Deficits*, chapter 2.

- H. Frenkel, J.A., "A Monetary Approach to the Exchange Rate: Doctrinal Aspects and Empirical Evidence," in Frenkel and Johnson (eds.), *The Economics of Exchange Rates*: 1-25.
- I. Dornbusch, Rudiger. "The Theory of Flexible Exchange Rate Regimes and Macroeconomic Policy." *Scandinavian Journal of Economics* 78, No. 2 (May 1976): 255-75. Reprinted in Frenkel, J. A., and H. G. Johnson (eds.) *The Economics of Exchange Rates: Selected Studies*. Also in ERI.
- J. Dornbusch, Rudiger. "Capital Mobility, Flexible Exchange Rates and Macroeconomic Equilibrium." In Claassen, E. and Salin, P (eds.) *Recent Issues in International Monetary Economics*. Amsterdam: North-Holland, 1976. Pp. 29-48. Also in ERI.
- K. Hodrick, R.J., "An Empirical Analysis of the Monetary Approach to the Determination of the Exchange Rate," in Frenkel and Johnson (eds.), *The Economics of Exchange Rates*: 97-116.
- L. Husted and Melvin, Chapter 18.

12. Sticky Prices and Exchange Rate Dynamics

- A. Romer, Chapter 5.3.
- B. *Dornbusch, *Open Macroeconomics*, Chapter I 1, Section 11.
- C. *Argy, Chapter 18.
- D. *Stevenson et al., Chapter 8, pp. 274-28 1.
- E. Pilbeam, chapter 5, 7, pp. 165-186, and chapter 8.
- F. Chrystal and Price, Chapter 6, pp. 104-1 10.
- G. Bailey & McMahon, Chapter 3.4.
- H. Husted and Melvin, Chapter 18.
- I. *Dornbusch, R., "Expectations and Exchange Rate Dynamics," *Journal of Political Economy* 84 (1976):1161-76. Also in ERI.
- J. Dornbusch, R. "Exchange Rates and Prices." *American Economic Review* 77 (March 1987)-93-106. Also in ERI,
- K. Frankel, Jacob and C.A. Rodriguez, "Exchange Rate Dynamics and the Overshooting Hypothesis", RAF Staff Papers (March 1982): 1-30.
- L. Obstfeld, M. and A. C. Stockman, "Exchange Rate Dynamics", in Jones and Kenen (eds.), *Handbook of International Economics* vol. II, (1985).
- M. Obstfeld, M. and K. Rogoff, "Exchange Rate Dynamics with Sluggish Prices Under Alternative Price Adjustment Rates", *International Economic Review* (February 1984): 159-74.

13. Portfolio Theory of exchange rates

- A. Dornbusch, *Open Macroeconomics*, Chapter 13.
- B. *Argy, Chapter 10 and 19.
- C. *Stevenson et al., Chapter 7, pp. 245-256, and chapter 8, 281-296.
- D. Pilbeam, chapter 5, 7, pp. 165-186, and chapter 8.
- E. Chrystal and Price, Chapter 6, pp. I 10- 1 13.
- F. Husted and Melvin, Chapter 18.

14. Design of macroeconomic policies

- A. Romer, Chapter 9.
- B. *Stevenson et al., Chapter 9.
- C. *Argy, Chapter 34 and 35.
- D. Husted and Melvin, Chapter 20.

15. International interdependence and policy coordination

- A. Romer, Chapter 4.
- B. *Stevenson et al., Chapter 10.
- C. *Argy, Chapter 45.
- D. Chrystal and Price, Chapter 9.

16. Economic Growth

- A. Romer, Chapter 1-3.
- B. Dornbusch, *Open Macroeconomics*, Chapter 14.
- C. Barro, R. J. and X. Sala-I-Martin. *Economic Growth*. New York: McGraw-Mil, Inc., 1995.

17. External debt

- A. Cohen, D. "Growth and External Debt." In Van der Ploeg, Frederick, ed. *The Handbook of International Macroeconomics*. Oxford: Basil Blackwell Ltd., 1994.

Supplemental reading texts for theory:

- Chrystal, K. A. and S. Price. *Controversies in Macroeconomics*, 3rd ed. London: Harvester Wheatsheaf, 1994.
- Dornbusch, Rudiger. *Exchange Rates and Inflation*. Cambridge, MA: MIT Press, 1988. (Referred to as ERI).
- Frankel, Jeffrey A. *On Exchange Rates*. Cambridge, MA: MIT Press, 1993.
- Greenaway, D. (ed.). *Current Issues in Macroeconomics*. New York: Macmillan, 1989.
- Husted, Steven and Michael Melvin. *International Economics*, 6th ed. Boston: Pearson Addison-Wesley, 2002.
- Romer, David. *Advanced Macroeconomics*. McGraw-Hill Higher Education, 2000.

Supplemental texts for Policy

- Dominiquiz, K. and J. Frankel. *Does Exchange Rate Intervention Work?* Washington, D.C.: Institute for International Economics, 1993.
- Dornbusch, Rudiger. *Dollars, Debts, and Deficits*. MIT Press, 1986. (Cited as DDD).
- Dornbusch, R. and Steve Marcus, ed. *International Money and Debt. Challenges for the World Economy*. San Francisco: ICS Press, 1991. (Cited as D&M)
- Dornbusch, R. and E.C.C.H. Holmes, ed. *The Open Economy: Tools for Policy Makers in Developing Countries*. Oxford University Press, 1988. (Referred to as D&H)
- Frenkel, Jacob A. and Assaf Razin. *Fiscal Policies and the World Economy*, 2nd ed. Cambridge, MA: IT Press, 1992.

Other Useful Texts

There are many other intermediate and advanced texts in macroeconomics and international finance that may be of use to you; a small selection follows. You will find that the texts generally have different emphases, so choose carefully.

General Macroeconomics

- Abel, A. B. and B. S. Bernanke. *Macroeconomics*, 3rd ed. Addison-Wesley Publishing Co., 1998.
- Barro, R. J. *Macroeconomics*. John Willey, 1993.
- Branson, W. H. *Macroeconomic Theory and Policy*, 3rd ed. Harper and Row, 1989.
- Burda, M. and C. Wyplosz. *Macroeconomics: A European Text*. Oxford: Oxford Press, 1993.
- Carlin, W. and D. Soskice. *Macroeconomics and the Wage Bargain*. Oxford: Oxford Press, 1990.
- Cuthbertson, K. and M. Taylor. *Macroeconomic Systems*. Basil Blackwell, 1987.
- Dornbusch, R. and S. Fischer. *Macroeconomics*, 6th ed. McGraw-Hill, 1994.
- Gordon, R. J. *Macroeconomics*, 6th, ed. Harper Collins, 1993.

- Hoover, K. D. *The New Classical Macroeconomics*, Blackwell, 1988.
- Leslie, D. *Advanced Macroeconomics*. McGraw Hill, 1993.
- Parkin, M. and R. Bade. *Modern Macroeconomics*. Philip Allan, 1988.

Open Macroeconomics or International Finance

- Baillie, Richard and Patrick McMahon. *The Foreign Exchange Market: Theory and Econometric Evidence*. Cambridge, England: Cambridge University Press, 1989. (Referred to as B & M).
- Caves, Richard E. and Johnson, Harry G. (eds.), *Readings in International Economics*. Homewood, IL: Irwin, 1968.
- Dornbusch, Rudiger and Frenkel, Jacob A. (eds.), *International Economic Policy: Theory and Evidence*. Baltimore: Johns Hopkins University Press, 1979.
- Frenkel, Jacob A. and Johnson, Harry G. (eds.) *The Monetary Approach to the Balance of Payments*. London: Allen and Urwin and Toronto: University of Toronto Press, 1976. Paperback edition, 1977.
- Frenkel, Jacob A. and Johnson, Harry G. (eds.) *The Economics of Exchange Rates. Selected Studies*. Reading, Mass.: Addison Wesley, 1978.
- Gandolfo, Giancarlo. *International Economics II*. New York-. Springer-Verlag, 1987.
- Isard, P. *Exchange Rate Economics*. Cambridge University Press, 1995.
- Jones, Ronald W. and Peter B. Kenen. *Handbook of International Economics, Volume 2*. Amsterdam: Elsevier Science Publishers B.V. (North-Holland), 1985.
- Krugman, Paul R. *Currencies and Crises*. Cambridge, MA: MIT Press, 1993.
- Mundell, Robert A. *International Economics*. New York: Macmillan, London: Collier-Macmillan, 1968.
- Mundell, Robert A. *Monetary Theory*. Pacific Palisades, CA: Goodyear Publishing Co., 1971.
- Van der Ploeg, Frederick, ed. *The Handbook of International Macroeconomics*. Oxford: Basil Blackwell Ltd., 1994.

Economic Growth

- Barro, R. J. and X. Sala-I-Martin. *Economic Growth*. New York: McGraw-Hill, Inc., 1995.

UF Policies & Resources

UF Grading Policy

Information on UF grading policies for assigning grade points may be found at:
<http://www.registrar.ufl.edu/catalog/policies/regulationgrades.html> .

Honor Code

In 1995 the UF student body enacted a new honor code and voluntarily committed itself to the highest standards of honesty and integrity. When students enroll at the university, they commit themselves to the standard drafted and enacted by students. In adopting this honor code, the students of the University of Florida recognize that academic honesty and integrity are fundamental values of the university community. Students who enroll at the university commit to holding themselves and their peers to the high standard of honor required by the honor code. Any individual who becomes aware of a violation of the honor code is bound by honor to take corrective action. The quality of a University of Florida education is dependent upon community acceptance and enforcement of the honor code. **The Honor Code: We, the members of the University of Florida community, pledge to hold ourselves and our peers to the highest standards of honesty and integrity.** On all work submitted for credit by students at the university, the following pledge is either required or implied: **—On my honor, I have neither given nor received unauthorized aid in doing this assignment.”**

The university requires all members of its community to be honest in all endeavors. A fundamental principle is that the whole process of learning and pursuit of knowledge is diminished by cheating, plagiarism and other acts of academic dishonesty. In addition, every dishonest act in the academic environment affects other students adversely, from the skewing of the grading curve to giving unfair advantage for honors or for professional or graduate school admission. Therefore, the university will take severe action against dishonest students. Similarly, measures will be taken against faculty, staff and administrators who practice dishonest or demeaning behavior. Students should report any condition that facilitates dishonesty to the instructor, department chair, college dean or Student Honor Court. (*Source: 2007-2008 Undergraduate Catalog*) It is assumed all work will be completed independently unless the assignment is defined as a group project, in writing by the instructor. This policy will be vigorously upheld at all times in this course.

Software Use

All faculty, staff and students of the university are required and expected to obey the laws and legal agreements governing software use. Failure to do so can lead to monetary damages and/or criminal penalties for the individual violator. Because such violations are also against university policies and rules, disciplinary action will be taken as appropriate.

Campus Helping Resources

Students experiencing crises or personal problems that interfere with their general well-being are encouraged to utilize the university's counseling resources. Both the Counseling Center and Student Mental Health Services provide confidential counseling services at no cost for currently enrolled students. Resources are available on campus for students having personal problems or lacking clear career or academic goals, which interfere with their academic performance. The Counseling Center is located at 301 Peabody Hall (next to Criser Hall). Student Mental Health Services is located on the second floor of the Student Health Care Center in the Infirmary.

University Counseling Center, 301 Peabody Hall, 392-1575, www.counsel.ufl.edu

Career Resource Center, CR-100 JWRU, 392-1602, www.crc.ufl.edu/

Student Mental Health Services, Rm. 245 Student Health Care Center, 392-1171, www.shcc.ufl.edu/smhs/

Alcohol and Substance Abuse Program (ASAP)

Center for Sexual Assault / Abuse Recovery & Education (CARE)

Eating Disorders Program

Employee Assistance Program

Suicide Prevention Program

Students with Disabilities

The Disability Resource Center coordinates the needed accommodations of students with disabilities. This includes registering disabilities, recommending academic accommodations within the classroom, accessing special adaptive computer equipment, providing interpretation services and mediating faculty-student disability related issues. Students requesting classroom accommodation must first register with the Dean of Students Office. The Dean of Students Office will provide documentation to the student who must then provide this documentation to the instructor when requesting accommodation.