

**McMaster University**  
**Department of Economics**

**ECON 752**

**International Finance**

**Winter 2016**

**Instructor:** César Sosa-Padilla  
+1 905-525 9140 X23816  
cesarspa@gmail.com  
<https://sites.google.com/site/cesarsosapadilla/>  
Office hours: after class or by appointment

**Class times:** Th, 4:00 - 6:50  
**Room:** KTH 334

**Background and Course Description**

The course is organized in two parts. Part I covers terms of trade determination, exchange rate determination, current account dynamics, and international business cycles. Part II is devoted to the study of financial frictions and international financial crises, with special emphasis on sovereign debt and default. Note that the course uses the optimization methods and builds on the asset pricing and business cycle models covered in ECON 723.

**Textbooks and other reading materials**

The course does not follow a specific textbook, hence there is no book to purchase. The required readings will be a mix of lecture notes prepared by the instructors, journal articles, research papers and chapters from books. You will find links to some of these items on Avenue to Learn. Book chapters will come from:

Martin Uribe. Open Economy Macroeconomics, Manuscript, November 2013. The PDF file for this entire set of notes is at <http://www.columbia.edu/~mu2166>.

Foundations of International Macroeconomics. Obstfeld and Rogoff. MIT Press, 1996.

Open Economy Macroeconomics in Developing Countries. Carlos Vegh. MIT Press, 2013.

Other (more specific) books that you may find useful are:

Dynamic Economics: Quantitative Methods and Applications. Adda and Cooper. MIT Press, 2003.

Debt Defaults and Lessons from a Decade of Crises. Sturzenegger and Zettelmeyer. MIT Press, 2006.

This Time is Different: Eight Centuries of Financial Folly. Reinhart and Rogoff. Princeton University Press, 2009.

**Course web site and communication**

In this course we will be using Avenue to Learn. Students should be aware that, when they access the electronic components of this course, private information such as first and last names, user names for the McMaster e-mail accounts, and program affiliation may become apparent to all other students in the same course. The available information is dependent on the technology used. Continuation in this course will be deemed consent to this disclosure. If you have any questions or concerns about such disclosure please discuss this with the course instructor.

## Tentative schedule and (some) readings

**1/21:** Introduction and review of main stylized facts.

Readings: Uribe's notes chapter 1.

**1/28:** Small Open Economy (SOE) - Endowment model

Readings: Uribe's notes chapter 2.

**2/1:** (Make-up class) Small Open Economy (SOE) - Adding Capital to the model

Readings: Uribe's notes chapter 3.

**2/4:** SOE-RBC: workhorse model.

Readings: Uribe's notes chapters 4 and 5, Mendoza (1991), Schmitt-Grohé and Uribe (2003), Aguiar and Gopinath (2007), García-Cicco et al. (2010).

**2/11:** Midterm Exam 1

**2/18:** Winter Break – No Classes.

**2/25:** Financial Crises: Main stylized facts.

Readings: Reinhart and Rogoff (2009) chapters 2, 5, and 6, Sturzenegger and Zettelmeyer (2005) chapter 1, Uribe's notes chapter 13 (first part).

**3/3 - 3/10:** Sovereign Defaults: Main Theories.

Readings: Uribe's notes chapter 13, Obstfeld and Rogoff (1996) chapter 6, Eaton and Gersovitz (1981), Arellano (2008), Aguiar and Gopinath (2006), Mendoza and Yue (2012).

**3/17 - 3/24:** New Issues and Developments in the Sovereign Debt literature.

Readings: Hatchondo et al. (2011), Benjamin and Wright (2008), D'Erasmus (2011), Yue (2010), Sosa-Padilla (2012), Chatterjee and Eyigungor (2011), Arellano and Ramanarayanan (2008), Cuadra et al. (forthcoming), Gennaioli et al. (2010).

**3/31:** Midterm Exam 2

**4/7:** Student Presentations.

## Paper presentations

Each student will present a paper from the list below. Presentations should be done professionally, as if you were presenting your own research in a conference/seminar. Slides are expected to be well organized and to be legible. Tedious mathematical derivations should be left to a written summary/handout. The use of Latex/Beamer is highly encouraged.

For each presentation day, the total class time (80 minutes) will be allocated as follows: the presenter will have 40 minutes to motivate the paper (putting it in context), present the research question(s) and explain the main results. Then a discussant will have 15 minutes to briefly summarize the paper and criticize it. The remaining time will be left for general Q&A. Each non-presenting student is expected to read the paper and provide at least 3 questions/suggestions related to the paper and the overall literature. Questions and comments during wither the presentation or the discussion of the papers are encouraged. The papers to be presented are (**tentatively**) the following and they will be assigned to students on a first-come first-served basis:

- Neumeyer, Pablo A., and Fabrizio Perri. “Business cycles in emerging economies: the role of interest rates.” *Journal of monetary Economics* 52.2 (2005): 345-380.
- Mendoza, Enrique G., “Sudden Stops, Financial Crises and Leverage.” *American Economic Review*, Dec. 2010.
- Ernesto Talvi, Carlos A. Végh, Tax base variability and procyclical fiscal policy in developing countries, *Journal of Development Economics*, Volume 78, Issue 1, (2005): 156-190.
- Mendoza, Enrique G., and Vivian Z. Yue. ”A general equilibrium model of sovereign default and business cycles.” *The Quarterly Journal of Economics* 127.2 (2012): 889-946.
- D’Erasmus, Pablo. “Government reputation and debt repayment in emerging economies.” Manuscript, University of Maryland, 2011.
- Bocola, Luigi. “The Pass-Through of Sovereign Risk.” Manuscript, University of Pennsylvania, 2014.

### Assessment and Grading Scheme

1. The assessment will be based on two midterm exams, a class presentation, and class participation. There will be no cumulative final exam.
2. Midterm Exam 1 is scheduled for February 12th and Midterm Exam 2 for March 24th.
3. Your grade for the course will be calculated as follows:

Item	Weight
Participation to class discussion	10%
Class presentation	20%
Better test	40%
Other test	30%

4. If a student fails to provide a satisfactory reason for missing a test or exam, he/she will get the mark zero for that test.

### Academic Dishonesty

You are expected to exhibit honesty and use ethical behavior in all aspects of the learning process. Academic credentials you earn are rooted in principles of honesty and academic integrity.

Academic dishonesty is to knowingly act or fail to act in a way that results or could result in unearned academic credit or advantage. This behavior can result in serious consequences, e.g. the grade of zero on an assignment, loss of credit with a notation on the transcript (notation reads: “Grade of F assigned for academic dishonesty”), and/or suspension or expulsion from the university.

It is your responsibility to understand what constitutes academic dishonesty. For information on the various types of academic dishonesty please refer to the Academic Integrity Policy, located at <http://www.mcmaster.ca/academicintegrity>. The following illustrates only three forms of academic dishonesty:

1. Plagiarism, e.g. the submission of work that is not one’s own or for which other credit has been obtained.
2. Improper collaboration in group work.

3. Copying or using unauthorized aids in tests and examinations.

**At certain points in the course it may make good sense to modify the course content described on page 1. The instructor reserves the right to modify elements of the course and will notify students accordingly (in class and post any changes to Avenue to Learn).**

## References

- Aguiar, M. and Gopinath, G. (2006). 'Defaultable debt, interest rates and the current account'. *Journal of International Economics*, volume 69, 64–83.
- Aguiar, M. and Gopinath, G. (2007). 'Emerging markets business cycles: the cycle is the trend'. *Journal of Political Economy*, volume 115, no. 1, 69–102.
- Arellano, C. (2008). 'Default Risk and Income Fluctuations in Emerging Economies'. *American Economic Review*, volume 98(3), 690–712.
- Arellano, C. and Ramanarayanan, A. (2008). 'Default and the Maturity Structure in Sovereign Bonds'. Mimeo, University of Minnesota.
- Benjamin, D. and Wright, M. L. J. (2008). 'Recovery Before Redemption? A Theory of Delays in Sovereign Debt Renegotiations'. Manuscript.
- Chatterjee, S. and Eyigungor, B. (2011). 'Maturity, Indebtedness and Default Risk'. Federal Reserve Bank of Philadelphia Working Paper 11-33.
- Cuadra, G., Sanchez, J. M., and Sapriza, H. (forthcoming). 'Fiscal policy and default risk in emerging markets'. *Review of Economic Dynamics*.
- D'Erasmus, P. (2011). 'Government Reputation and Debt Repayment'. Manuscript, University of Maryland.
- Eaton, J. and Gersovitz, M. (1981). 'Debt with potential repudiation: theoretical and empirical analysis'. *Review of Economic Studies*, volume 48, 289–309.
- García-Cicco, J., Pancrazi, R., and Uribe, M. (2010). 'Real Business Cycles in Emerging Countries?' *The American Economic Review*, volume 100, no. 5, 2510–2531.
- Gennaioli, N., Martin, A., and Rossi, S. (2010). 'Sovereign Default, Domestic Banks and Financial Institutions'. Working Paper, CREi.
- Hatchondo, J. C., Martinez, L., and Sosa-Padilla, C. (2011). 'Debt dilution and sovereign default risk'. Manuscript, University of Maryland.
- Mendoza, E. (1991). 'Real business cycles in a small open economy'. *The American Economic Review*, pages 797–818.
- Mendoza, E. and Yue, V. (2012). 'A General Equilibrium Model of Sovereign Default and Business Cycles'. *Quarterly Journal of Economics*.
- Obstfeld, M. and Rogoff, K. (1996). *Foundations of international macroeconomics*. The MIT Press.
- Reinhart, C. M. and Rogoff, K. S. (2009). *This Time is Different*. Princeton Press.

- Schmitt-Grohé, S. and Uribe, M. (2003). ‘Closing small open economy models’. *Journal of International Economics*, volume 61, 163–185.
- Sosa-Padilla, C. (2012). ‘Sovereign Defaults and Banking Crises’. Working Paper. McMaster University.
- Sturzenegger, F. and Zettelmeyer, J. (2005). *Debt Defaults and Lessons from a Decade of Crises*. MIT Press.
- Yue, V. (2010). ‘Sovereign default and debt renegotiation’. *Journal of International Economics*, volume 80, 176–187.