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**ECO 554: International Monetary Theory II**  
**ECO 575: Topics in Financial Economics**  
**- Part I -**

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**Time and Location:**

Monday/Wednesday 10:40 am – 12:10 pm, Fisher Hall B04  
(alternative time: Friday 1:30 p.m.)

**Course Description:**

This course is essentially a “Macro, Money and Finance” course. It focuses on the interaction between price and financial stability. It covers important theoretical concepts and recent developments in modeling techniques in modeling the macroeconomy in which financial frictions and the financial sector plays a crucial role. The course will also study open economies. Special emphasis is place on carry trades and its connection to currency crashes as well as international capital flows and valuation effects.

The second part of the course will be taught by Oleg Itskhoki if you take Eco 554 or by Wei Xiong if you take Eco 575.

**Key reference:**

“Macroeconomics with Financial Frictions: A Survey”, Brunnermeier, Eisenbach and Sannikov and references therein.

**Requirements/grading:**

There will be a midterm exam. The general exams will be in International Monetary Theory and in Financial Economics.

Although the exams are closed book, you may bring into the exam one 8 ½ x 11 sheet of paper. You can write on both sides and as small as you wish, but I recommend using this only as a psychological support to have a formula available “just in case.” The exams won’t be “fill in the blanks” exercises, nor will they rely on intensive formula-based computations. Preparing lots of pre-fabricated solutions from previous exams or assignments will only be distracting during the exam.

You will be allowed to use a silent battery operated calculator during the exams. Laptops, while useful for assignments, are not needed (nor allowed) in my exams.

## **Structure of the Course:**

### **1) A Brief History of Macroeconomics**

- “The State of Macro”, Olivier Blanchard, 2009, *Annual Review of Economics*, Vol. 1, pp. 209-228.
- Money and Credit in Monetary Economics, Markus Brunnermeier and Yuliy Sannikov, 2011.
- “The Empirical Foundations of Calibration”, Lars Hansen and Jim Heckman, *Journal of Economic Perspectives*, Vol. 10(1), pp. 87-104.
- “A Dictionary Article on Axel Leijonhufvud’s On Keynesian Economics and the Economics of Keynes: A Study in Monetary Theory”, Peter Howitt, 2007, in *Dictionnaire des grandes oeuvres économiques*.
- “The Macroeconomists as Scientists and Engineer”, Greg Mankiw, 2006, *The Journal of Economic Perspectives*, Vol. 20(4), pp. 29-46.
- “Calibration”, Ed Prescott and Graham Candler, 2008. *The New Palgrave Dictionary of Economics*, 2<sup>nd</sup> edition.
- *Economics Evolving: A History of Economic Thought*, Agnar Sandmo, 2011, Princeton University Press.
- “Statistical Modeling of Monetary Policy and its Effects”, Chris Sims, 2011, Nobel Prize Lecture.
- “Working in the Dark”, Bob Solow, 2011, *The New Republic*, Oct. 20.
- *Interest and Prices*, Mike Woodford, 2003, Princeton University Press

### **2) Liquidity Concepts, Amplification and Persistence**

- “Macroeconomics with Financial Frictions: A Survey”, Brunnermeier, Eisenbach and Sannikov and references therein, Section 1-3.

### **3) Linking Macro and Finance: Liquidity Demand**

- “Macroeconomics with Financial Frictions: A Survey”, Brunnermeier, Eisenbach and Sannikov and references therein, Section 4.

### **4) Macro, Systemic Risk and Financial Data**

- “Risk Topography”, Brunnermeier, Gorton and Krishnamurthy
- “Liquidity Mismatch”, Brunnermeier, Gorton and Krishnamurthy
- “Systemic Risk Exposure: A 10-by-10-by-10 Approach”, Darrell Duffie
- “CoVaR”, Adrian and Brunnermeier

### **5) Endogenous Risk, Volatility Paradox**

- “A Macroeconomic Model with a Financial Sector”, Brunnermeier and Sannikov
- Sannikov handout

### **6) Money and Financial Institutions**

- “The I Theory of Money”, Brunnermeier and Sannikov
- “Money and Credit in Monetary Economics”, Brunnermeier and Sannikov

### **7) Bubbles, Crashes in FX Market**

- “Carry Trades and Currency Crashes”, Brunnermeier, Nagel and Pedersen
- “Bubbles and Crashes”, Abreu and Brunnermeier

### **8) Capital Controls: Breaking with the Washington Consensus**

- “Adjusting to Capital Account Liberalization”, Aoki, Benigno and Kiyotaki

### **9) Flow view vs. “Balance Sheet View” and the Current Account**

- [“Does the Current Account Still Matter?”](#), Maury Obstfeld, Ely Lecture 2012,
- [“International Financial Adjustment”](#), Gourinchas, Pierre-Olivier and Helene Rey, Journal of Political Economy

**10) New Keynesian Open Macroeconomics** (optional)

- [“Contrasting Different Forms of Price Stickiness: An Analysis of Exchange Rate Overshooting and the Beggar Thy Neighbour Policy”](#), Brunnermeier and Gafé, 1999

**11) European Currency Union** (optional)

- Brunnermeier, Gourinchas and Itkhoki, “Optimal Currency Area with Banking” (in progress)
- TRADE-OFF: INFLATE OR DEFAULT (*students project*)
- Macro-prudential tools

**12) New Financial Architecture** (optional)

- [“The fundamental principles of financial regulation”](#), 11<sup>th</sup> Geneva Report, Brunnermeier et al.
- Regulatory Reform (ex-ante vs. ex-post/ lean vs. clean)

Note: Titles that are underlined are hyperlinked.