

AEA Continuing Education
International Trade and Finance
January 8-10, 2012
Gita Gopinath and Gene Grossman

Gita Gopinath
Harvard University
Email: gopinath@harvard.edu
<http://www.economics.harvard.edu/faculty/gopinath>

Gene Grossman
Princeton University
Email: grossman@princeton.edu
<http://www.princeton.edu/~grossman/>

Introduction

This mini-course will review some of the more important research and teaching developments in International Economics in the last fifteen or so years. It will be divided evenly between topics in *International Trade* (Grossman) and topics in *International Macroeconomics and Finance* (Gopinath). Each lecturer will present three sub-topics under the broader headings.

Grossman will begin with a review of recent research that incorporates firms into the theory and empirics of international trade. In the last decade, numerous data sets have become available that reveal the trading behavior of individual firms. Sparked by the observation that firm participation in international trade is very heterogeneous but also systematic, researchers have sought to document the patterns in the data, to model firm heterogeneity (beginning with the now-famous "Melitz Model") and to test the main predictions of the models.

Another well-known trend in world trade has been the increasing fragmentation and globalization of the production process. Whereas historically most trade involved the exchange of finished goods or of intermediate goods that comprise a substantial portion of the value of a completed good, increasingly trade involves an ever finer international division of the production process. Grossman will review empirical and theoretical research on "vertical specialization" and "task trade," as well as research that investigates firms' decisions whether to engage in direct foreign investment or outsourcing as a means to offshore production tasks.

Grossman will also review a slightly older literature on the political economy of trade policy. Recognizing that politics play an important role in trade policy formation along with economics, researchers have sought to include political actors--politicians, voters and lobbyists--in their models and empirical studies of trade policy. If time permits, attention will be turned to more recent research that seeks to understand the motivations for the various institutions of international trade as, for example, embodied in the General Agreement on Tariffs and Trade (GATT) and the World Trade Organization (WTO).

Gopinath will first review recent empirical and theoretical developments in understanding international capital flows. Capital flows will be related to the traditional movements in trade balances and to the more recent emphasis on movements in international asset values referred to as "valuation effects". In addition the direction and composition (equities versus bonds) of capital flows will be discussed in environments with heterogeneity across countries in levels of growth and financial development. This

will speak to the important recent topic of “global imbalances” and the phenomenon of south (China) to North (US) capital flows.

In the second international finance topic Gopinath will cover recent developments in the area of sovereign and private sector debt. The recent worldwide debt crisis has refocused attention on the special features of debt (as compared to equity) that is associated with the possibility of “default” and “debt deflation”. We will discuss recent empirical evidence on sovereign debt and financial crisis, quantitatively evaluate sovereign default models, review a modern treatment of the Fisherian debt-deflation mechanism, and relate these to the current debt and financial crisis episode.

Lastly, Gopinath will revisit the classic question of real exchange rate behavior and international monetary policy. On the topic of real exchange rates the new developments relate to empirical studies that use extensive micro data on detailed products and new theoretical applications of industrial organization based price-setting models. The specific nature of price setting impacts the international dimension of monetary policy and recent theoretical advances in this area will be discussed. If time permits we will evaluate policy options for countries in a currency union, such as the Euro, that lack an exchange rate tool to stabilize their economies.

Topics in International Trade

Topic 1: Firms in International Trade

Readings Prior to Program:

*Andrew Bernard, Brad Jenson, Stephen Redding and Peter Schott. “Firms in International Trade,” Journal of Economic Perspectives 21, no. 3 (Summer 2007): 105–130.

*Stephen Redding. “Theories of Heterogeneous Firms and Trade,” Annual Review of Economics 3 (September 2011): 77-105.

Other Useful Readings:

Marc Melitz. “The Impact of Trade on Intra-Industry Reallocations and Aggregate Industry Productivity,” Econometrica 71, no. 6 (Nov., 2003): 1695-1725.

Marc Melitz and Gianmarco Ottaviano. “Market Size, Trade and Productivity,” Review of Economic Studies 75 (2008): 295-316.

Thomas Chaney. “Distorted Gravity: The Intensive and Extensive Margins of International Trade,” American Economic Review 98 (2008): 1707-1721.

Andrew Bernard, J. Bradford Jenson, Jonathan Eaton, and Samuel Kortum. "Plants and Productivity in International Trade," American Economic Review 93 (2003): 1268-1290.

Jonathan Eaton, Samuel Kortum and Francis Kramarz. "[An Anatomy of International Trade: Evidence from French Firms](#)," Econometrica (*forthcoming*).

Elhanan Helpman, Marc Melitz and Yona Rubinstein. "Estimating Trade Flows: Trading Partners and Trade Volumes," The Quarterly Journal of Economics 123, no. 2 (2008): 441-487.

Costas Arkolakis, Arnaud Costinot, and Andres Rodriguez-Clare. "New Trade Models, Same Old Gains," American Economic Review (*forthcoming*). [NBER Working Paper No. 15628](#).

Andrew Bernard, J. Bradford Jenson, Stephen Redding and Peter Schott. "[The Empirics of Firm Heterogeneity and International Trade](#)," Annual Review of Economics (*forthcoming*).

Topic 2: Offshoring, Outsourcing, and the Fragmentation of Production

Readings Prior to Program:

*Pol Antràs and Esteban Rossi-Hansberg. "Organization and Trade," Annual Review of Economics 1 (2009): 43-64.

*Gene Grossman and Esteban Rossi-Hansberg. "Trading Tasks: A Simple Theory of Offshoring," American Economic Review 98, no. 5 (2008): 1978-1997.

Other Useful Readings:

David Hummels, Jun Ishii and Kei-Mu Yi. "The Nature and Growth of Vertical Specialization in World Trade," Journal of International Economics 54, no. 1 (June 2001): 75-96.

Elhanan Helpman. "Trade, FDI and the Organization of Firms," Journal of Economic Literature 44, no. 3 (2006): 589-630.

Pol Antràs. "Firms, Contracts, and Trade Structure," Quarterly Journal of Economics 118, no. 4 (2003): 1375-1418.

Pol Antràs and Elhanan Helpman. "Global Sourcing," Journal of Political Economy 112, no. 3 (2004): 552-580.

Nathan Nunn. "Relationship-Specificity, Incomplete Contracts and the Pattern of Trade," Quarterly Journal of Economics 122, no. 2 (2007): 569-600.

Pol Antràs, Luis Garicano, and Esteban Rossi-Hansberg. "Offshoring in a Knowledge Economy," The Quarterly Journal of Economics 121, no. 1 (2006): 31-77.

Lorenzo Calliando and Esteban Rossi-Hansberg. "The Impact of Trade on Organization and Productivity," [NBER Working Paper No. 17308](#).

Topic 3: The Political Economy of Trade Policy

Readings Prior to Program:

*Gene Grossman and Elhanan Helpman. "Protection for Sale," American Economic Review 84, no. 4 (Sept. 1994): 833-850.

Other Useful Readings:

Dani Rodrik. Chapter 28 The Political Economy of Trade Policy, In: Gene M. Grossman and Kenneth Rogoff, Editor(s), Handbook of International Economics, Elsevier, 1995, Volume 3, Pages 1457-1494.

Pinelopi Goldberg and Giovanni Maggi. "Protection for Sale: An Empirical Investigation," American Economic Review 89 (1999): 1135-1155.

Robert E. Baldwin and Christopher S. Magee. "Is Trade Policy for Sale? Congressional Voting on Recent Trade Bills," Public Choice Vol. 105, No. 1/2 (2000): 79-101.

Robert Staiger and Kyle Bagwell. "An Economic Theory of the GATT," American Economic Review 89, no. 1 (March 1999): 215-248.

Robert Staiger and Kyle Bagwell, "The World Trade Organization: Theory and Practice," Annual Review of Economics Vol. 2 (September 2010): 223-256.

Giovanni Maggi and Andrés Rodríguez-Clare. "The Value of Trade Agreements in the Presence of Political Pressures," Journal of Political Economy Vol. 106, No. 3 (June 1998): 574-601.

Topics in International Finance

Topic 1: Capital Flows, Global Imbalances, Financial Crisis

Readings Prior to Program:

*Enrique G. Mendoza, Vincenzo Quadrini and José-Víctor Ríos-Rull. "Financial Integration, Financial Development, and Global Imbalances," Journal of Political Economy Vol. 117, No. 3 (June 2009): 371-416.

Other Useful Readings:

Mark Aguiar and Gita Gopinath. "Emerging Market Business Cycles: The Cycle is the Trend," Journal of Political Economy Vol. 115, No. 1 (February 2007): 69-102.

Caballero, R., E. Farhi and P.-O. Gourinchas. "An Equilibrium Model of Global Imbalances and Low Interest Rates," American Economic Review 98(1) (2008): 358-393.

Gourinchas, Pierre-Olivier, and H el ene Rey. "International Financial Adjustment." Journal of Political Economy 115, no. 4 (August 2007): 665-703.

Obstfeld, Maurice. "External Adjustment." Review of World Economics 140, no. 4 (December 2004): 541-568. From *Obstfeld's website*: <http://elsa.berkeley.edu/~obstfeld/Lecture.pdf>

Schneider, Martin and Tornell, Aaron. "Balance Sheet Effects, Bailout Guarantees, and Financial Crisis", Review of Economic Studies 71(3) (2004): 883-913.

Topic 2: Debt, Sovereign Debt, Debt Overhang

Readings Prior to Program:

*Aguiar, M. and G. Gopinath. "Defaultable Debt, Interest Rates and the Current Account." Journal of International Economics 69 (1) (2006): 64-83.

Other Useful Readings:

Bulow, J. and K. Rogoff . "Sovereign Debt: Is to Forgive to Forget?" American Economic Review 79(1) (1989): 43-50.

Arellano, C. "Default Risk and Income Fluctuations in Emerging Economies," American Economic Review 98(3) (2008): 690-712.

Aguiar, M., M. Amador and G. Gopinath. "Investment Cycles and Sovereign Debt Overhang" Review of Economic Studies 76(1) (2009) : 1-31.

Broner, Fernando, Alberto Martin, and Jaume Ventura. "Sovereign Risk and Secondary Markets." American Economic Review 100(4) (2010): 1523–55.

Mendoza, Enrique G.. 2010. "Sudden Stops, Financial Crises, and Leverage." American Economic Review, 100(5): 1941–66.

Reinhart, Carmen M., and Kenneth S. Rogoff. "From Financial Crash to Debt Crisis." American Economic Review, 101(5) (August 2011): 1676–1706.

Topic 3: Real Exchange rates, Exchange Rate Pass-through, Monetary Policy

Readings Prior to Program:

*Gopinath, G., O. Itskhoki and R. Rigobon. "Currency Choice and Exchange Rate Pass through" American Economic Review (*forthcoming*).

<http://www.economics.harvard.edu/faculty/gopinath/files/cp15f.pdf>

*Atkeson, Andrew, and Ariel Burstein. "Pricing-to-Market, Trade Costs, and International Relative Prices." American Economic Review, 98(5) (2008):1998–2031.

*Engel, Charles. "Currency Misalignments and Optimal Monetary Policy: A Reexamination," American Economic Review (*forthcoming 2011*). [NBER Working Paper No. 14829](#).

Other Useful Readings:

Engel, Charles. "Accounting for U.S. Real Exchange Rate Changes." Journal of Political Economy 107(3) (June 1999): 507-538.

Burstein, Ariel, Martin Eichenbaum, and Sergio Rebelo. "Large Devaluations and the Real Exchange Rate." Journal of Political Economy 113(4) (August 2005): 742-784.

Gopinath, G., P.-O. Gourinchas, C.-T. Hsieh and N. Li. "Estimating the Border Effect: Some New Evidence." Harvard University Working Paper (2009).

Carlos Carvalho and Fernanda Nechio. "Aggregation and the PPP Puzzle in a Sticky-Price Model." Federal Reserve Bank of New York Staff Reports, no. 351, (October 2008; revised November 2008) http://www.newyorkfed.org/research/staff_reports/sr351.html

Jordi Galí and Tommaso Monacelli. "Monetary Policy and Exchange Rate Volatility in a Small Open Economy," Review of Economic Studies 72(3) (2005): 707-734.

E. Farhi, G. Gopinath and O. Itskhoki. "Fiscal Devaluations," (*working paper*). http://www.economics.harvard.edu/faculty/gopinath/files/fiscal_devaluations_071911.pdf

Lorenzoni, Guido and Ricardo Caballero, 2009, "Persistent Appreciations and Overshooting: A Normative Analysis." <http://econ-www.mit.edu/files/4454>