

# Syllabus: Financial Economics I – International Financial Markets

Spring term 2021 – subject to slight changes

Lecture: Prof. Dr. Philip Sauré  
Time: Monday, 10:15 – 11:45 am  
Location: online class until further notice

Tutorial: Leandro Navarro  
Time: Wednesday, 8:30 – 10:00 pm  
Location: online class until further notice

The first part of this course reviews the principles of international risk sharing through asset trade. We initially develop and study the core theories topics under complete markets and subsequently discuss the predictions in view of empirical regularities. Students deepen their knowledge of standard tools of economic modelling and analysis. The second part then turns to a specific form of asset market imperfection: limited enforcement of debt contracts, especially contracts of sovereign debt. The costs of sovereign default is shown to play a central role, and their determinants, channels and magnitude are analyzed. Time permitting, this analysis includes the role of financial institutions, transmission and contagion of sovereign risk and the self-fulfilling nature of debt crises.

## Textbooks

Obstfeld, Maurice and Kenneth S. Rogoff. Foundations of international macroeconomics. Cambridge, MA: MIT press, 1996.

Harms, Philipp (2016): International Macroeconomics, 2nd edition, Tübingen (Mohr Siebeck).

### I. International borrowing and lending under complete markets

#### *Required readings*

OR: Chapter 5 (pp. 269 – 291)

#### *Optional readings*

French, Kenneth R., and James Michael Poterba 1991. "Investor Diversification and International Equity Markets." American Economic Review 81.2 222-226.

Brennan, Michael J., and H. Henry Cao 1997: "International portfolio investment flows." Journal of Finance 52.5, 1851-1880.

Van Nieuwerburgh, Stijn, and Laura Veldkamp 2009: "Information immobility and the home bias puzzle." Journal of Finance 64.3, 1187-1215.

Obstfeld, Maurice, and Kenneth Rogoff 2000: "The six major puzzles in international macroeconomics: is there a common cause?" NBER macroeconomics annual 15, 339-390.

Coeurdacier, Nicolas, and Helene Rey 2012. "Home bias in open economy financial macroeconomics." Journal of Economic Literature 51.1 63-115.

## **II. Sovereign solvency**

### *Required readings*

Harms, p 231 - 238

### *Optional readings*

Reinhart, Carmen M., Kenneth S. Rogoff, and Miguel A. Savastano 2003: Addicted to dollars. NBER WP 10015.

Blanchard, Olivier Paolo Mauro, Julien Acalin 2016: "The case for growth-indexed bonds in advanced economies today" Voxeu Column

IMF Country Report 2016: Greece. Preliminary Debt Sustainability Analysis – Updated Estimations and Further Considerations

## **III. Sovereign borrowing, enforcement and the willingness to pay**

### *Required readings*

OR, pp. 349 - 362

### *Optional readings*

Aguiar, Mark, and Manuel Amador. "Sovereign debt." Handbook of International Economics. Vol. 4. Elsevier, 2014. 647-687.

Tomz, Michael, and Mark LJ Wright. 2013. "Empirical research on sovereign debt and default." Annual Review of Economics pp. 5:247–72.

Eaton, Jonathan, and Mark Gersovitz 1981. "Debt with potential repudiation: Theoretical and empirical analysis." Review of Economic Studies 48.2 289-309.

Bulow, Jeremy, and Kenneth Rogoff 1989 "A constant recontracting model of sovereign debt." Journal of political Economy 97.1 155-178.

Cole, Harold L., and Patrick J. Kehoe 1998. "Models of sovereign debt: Partial versus general reputations." *International Economic Review* 55-70.

Amador, Manuel 2003. "A political economy model of sovereign debt repayment." Manuscript, Stanford University

Cole, Harold L., and Timothy J. Kehoe 1996. "A self-fulfilling model of Mexico's 1994–1995 debt crisis." Journal of international Economics 41.3-4 309-330.

Morris, Stephen, and Hyun Song Shin 1998. "Unique equilibrium in a model of self-fulfilling currency attacks." American Economic Review 587-597.

European Commission 2018: Debt Sustainability Monitor 2017, Institutional Paper 071

#### **IV. Costs of sovereign default**

##### *Required readings*

Harms, pp. 238 - 249

Borensztein, Eduardo, and Ugo Panizza 2009. "The costs of sovereign default." IMF Staff Papers 56.4 683-741.

##### *Optional readings*

Trebesch, Christoph, and Michael Zabel 2017. "The output costs of hard and soft sovereign default." European Economic Review 92 416-432.

Broner, Fernando, Alberto Martin, and Jaume Ventura 2010. "Sovereign risk and secondary markets." American Economic Review 100.4 1523-55.

Brutti, Filippo, and Philip Sauré 2016 "Repatriation of debt in the euro crisis." Journal of the European Economic Association 14.1 145-174.

#### **V. Contagion and Transmission of Sovereign Default Risk**

##### *Required readings*

Harms, p 249 - 253

Kaminsky, Graciela L., and Carmen M. Reinhart 2000. "On crises, contagion, and confusion." Journal of international Economics 51.1 145-168.

##### *Optional readings*

Forbes, Kristin J., and Roberto Rigobon 2002. "No contagion, only interdependence: measuring stock market comovements." The journal of Finance 57.5 2223-2261.

Corsetti, Giancarlo, Marcello Pericoli, and Massimo Sbracia 2005. "'Some contagion, some interdependence': More pitfalls in tests of financial contagion." Journal of International Money and Finance 24.8 1177-1199.

Forbes, Kristin J., and Menzie D. Chinn 2004. "A decomposition of global linkages in financial markets over time." Review of economics and statistics 86.3 705-722.

Brutti, Filippo, and Philip Sauré 2015. "Transmission of sovereign risk in the euro crisis." Journal of International Economics 97.2 231-248.