

16I035

Sovereign Debt and International Financial Markets

Spring Term - 3 ECTS

Elective Course

Prof. Fernando Broner

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Prerequisites to Enroll

None

Overview and Objectives

This course provides the analytical and empirical tools necessary to address these questions: Why do countries borrow? Why do they repay their debts in the absence of international courts? What is the effect of international borrowing on domestic financial markets and macroeconomic stability? Why do countries often borrow too much? Is there a role for capital controls? Under what conditions is debt forgiveness optimal? What is the optimal way of restructuring defaulted debts? What happened during the European sovereign debt crisis?

Course Outline and Materials

I. Background Reading

Obstfeld, M., and A. Taylor, Global Capital Markets: Integration, Crisis, and Growth, Cambridge University Press, 2004

* Reinhart, C., and K. Rogoff, This time is different: Eight centuries of financial folly, Princeton University Press, 2009

II. Why countries repay their debts? Sanctions and reputation

* Obstfeld, M., and K. Rogoff, Foundations of International Macroeconomics, Ch. 6.1

Eaton, J., and R. Fernández, "Sovereign debt," in G. Grossman and K. Rogoff (eds.), Handbook of International Economics III, 1995, sections 1 and 2

Bulow, J., and K. Rogoff, "Sovereign debt: Is to forgive to forget?" *American Economic Review* 79, 1989

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Aguiar, M., and G. Gopinath, "Defaultable Debt, Interest Rates and the Current Account," *Journal of International Economics* 69, 2006.

Arellano, C., "Default Risk and Income Fluctuations in Emerging Economies," *American Economic Review* 98, 2008.

* Cruces, J., and C. Trebesch, "Sovereign defaults: The price of haircuts," *American Economic Journal: Macroeconomics* 5, 2013

* Gelos, G., R. Sahay, and G. Sandleris, "Sovereign borrowing by developing countries: What determines market access?" *Journal of International Economics* 83, 2011

* Rose, A., "One reason countries pay their debts: Renegotiation and international trade," *Journal of Development Economics* 77, 2005

Tomz, M., Reputation and international cooperation: Sovereign debt across three centuries, Princeton University Press, 2007

III. International and domestic financial markets

* Obstfeld, M., and K. Rogoff, Foundations of International Macroeconomics, Ch. 6.4

* Broner, F., A. Martin, and J. Ventura, "Sovereign risk and secondary markets," *American Economic Review* 100, 2010

Broner, F., and J. Ventura, "Rethinking the effects of financial globalization," *Quarterly Journal of Economics* 131, 2016.

* Martin, A., and F. Taddei, "International capital flows and credit market imperfections: A tale of two frictions," *Journal of International Economics* 89, 2013

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* Gennaioli, N., A. Martin, and S. Rossi, "Sovereign default, domestic banks, and financial institutions," *Journal of Finance* 69, 2014

Caballero, R., and A. Krishnamurthy, "International and domestic collateral constraints in a model of emerging market crises," *Journal of Monetary Economics* 48, 2001

* Kose, M., E. Prasad, and M. Terrones, "Financial integration and macroeconomic volatility," *IMF Staff Papers* 50, 2003

* Kose, M., E. Prasad, K. Rogoff, and S. Wei, "Financial globalization: A reappraisal," *IMF Staff Papers* 56, 2009

Reinhart, C., and K. Rogoff, "From financial crash to debt crisis," *American Economic Review* 101, 2011.

Kaminsky, G., and C. Reinhart, "The twin crises: The causes of banking and balance-of-payments problems," *American Economic Review* 89, 1999

Arteta, C., and G. Hale, "Sovereign debt crises and credit to the private sector," *Journal of International Economics* 74, 2008

IV. International financial architecture

* Cole, H., and T. Kehoe, "Self-fulfilling debt crises," *Review of Economic Studies* 67, 2000.

Jeanne, O., "Debt maturity and the international financial architecture," *American Economic Review* 99, 2009

* Broner, F., G. Lorenzoni, and S. Schmukler, "Why do emerging economies borrow short term?" *Journal of the European Economic Association* 11, 2013.

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* Broner, F., A. Erce, A. Martin, and J. Ventura, "Sovereign debt markets in turbulent times: Creditor discrimination and crowding-out effects," *Journal of Monetary Economics* 61, 2014

* Acharya, V., I. Drechsler, and P. Schnabl, "A pyrrhic victory? Bank bailouts and sovereign credit risk," *Journal of Finance* 69, 2014

* Reinhart, C., V. Reinhart, and K. Rogoff, "Public debt overhangs: Advanced-economy episodes since 1800," *Journal of Economic Perspectives* 26, 2012

* Obstfeld, M., and K. Rogoff, Foundations of International Macroeconomics, Ch. 6.2.

Eaton, J., and R. Fernández, "Sovereign debt," in G. Grossman and K. Rogoff (eds.), Handbook of International Economics III, 1995, sections 3 and 4.

* Fischer, S., and W. Easterly, "The economics of the government budget constraint," *World Bank Research Observer* 5, 1990.

Krugman, P., "Financing versus forgiving a debt overhang," *Journal of Development Economics* 29, 1988.

* Krugman, P., "Reducing developing country debt," in Currencies and Crises, MIT Press, 1992.

Bolton, P., and O. Jeanne, "Structuring and restructuring sovereign debt: The role of a bankruptcy regime," *Journal of Political Economy* 115, 2007.

Rogoff, K., and J. Zettelmeyer, "Bankruptcy procedures for sovereigns: A history of ideas, 1976–2001," *IMF Staff Papers* 49, 2002.

Evaluation

Final exam (80%), problem sets (20%)

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Competences

- To (be able to) communicate with determination and in the English Language, the results and implications of the required analytical study using a language that the receiver can relate to.
- To work within a heterogeneous team of researchers as economic analyst using specific group techniques.
- To fit in diverse professional environments and varied types of collaborations in different professional projects
- To possess and understand the knowledge that provides a basis or opportunity to be original in the development and / or application of ideas, often in a research context.
- That students know how to apply the acquired knowledge and their ability to solve problems in new or unfamiliar environments within broader (or multidisciplinary) contexts related to their field of study.
- That the students be able to integrate knowledge and face the complexity of making judgments based on information that, being incomplete or limited, include reflections on the social and ethical responsibilities linked to the application of their knowledge and judgments.
- That the students be able to communicate their conclusions and the knowledge and the ultimate reasons that sustain them to both, specialized and non-specialized publics in a clear and unambiguous way.
- That students possess the learning skills that allow them to continue studying in a way that will be largely self-directed or autonomous.
- To identify and apply the insights of the theory, the models, and the analytical tools of modern economy to its global dimension.
- Understand and apply economic theory related to the regulation of markets and competition policy.
- Understand and apply the economics of international trade and finance and economic development
- To understand and apply the quantitative methods used to solve complex problems of the economy.
- To evaluate, with theoretical and quantitative instruments, the complex realities of the

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economy to understand the way it works.

Learning Outcomes

- Deep knowledge of the economics of international trade, finance and development.
- Applies economic concepts to economic pressure policy problems related to growth, economic stability and poverty.
- Analyze economic data rigorously.

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