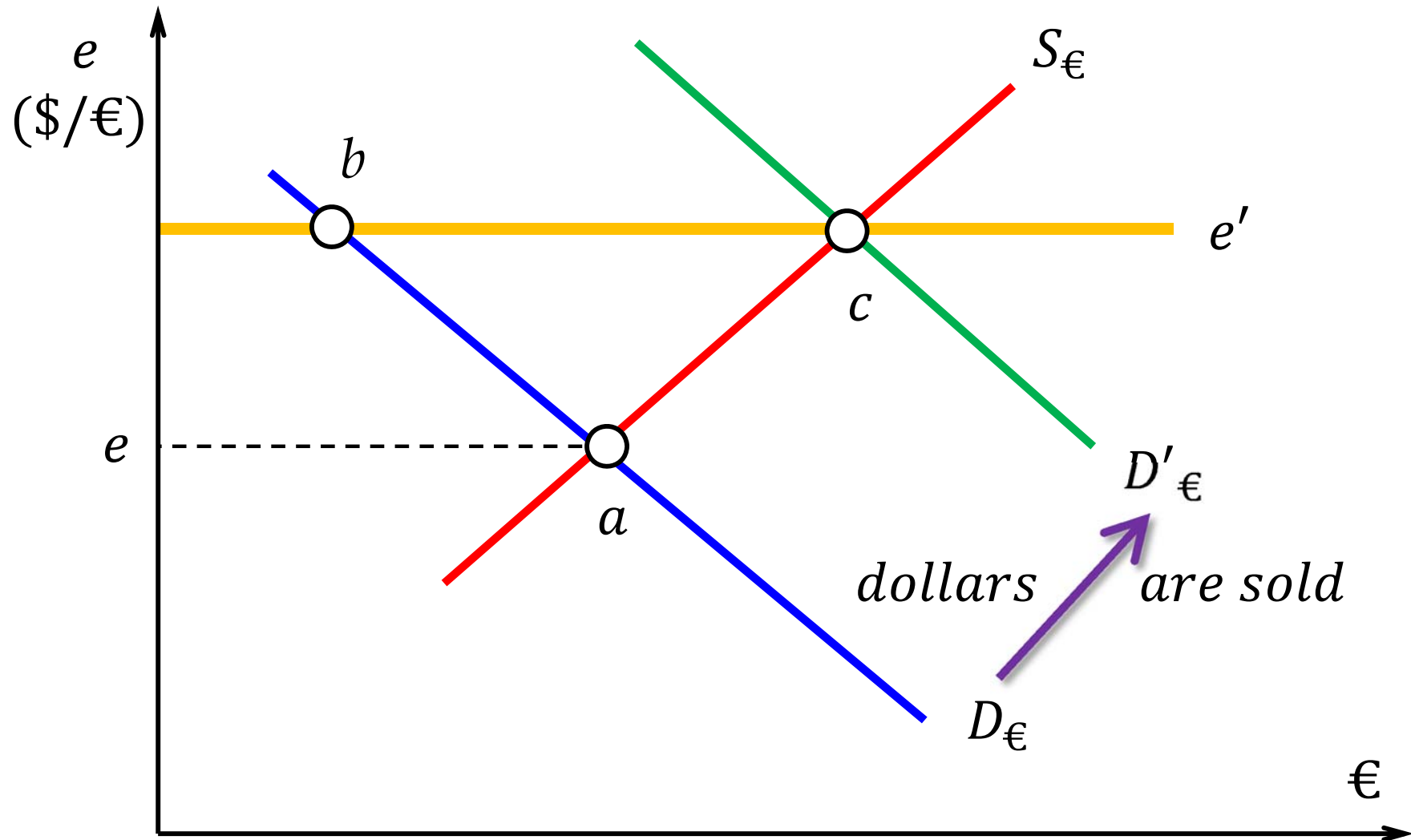


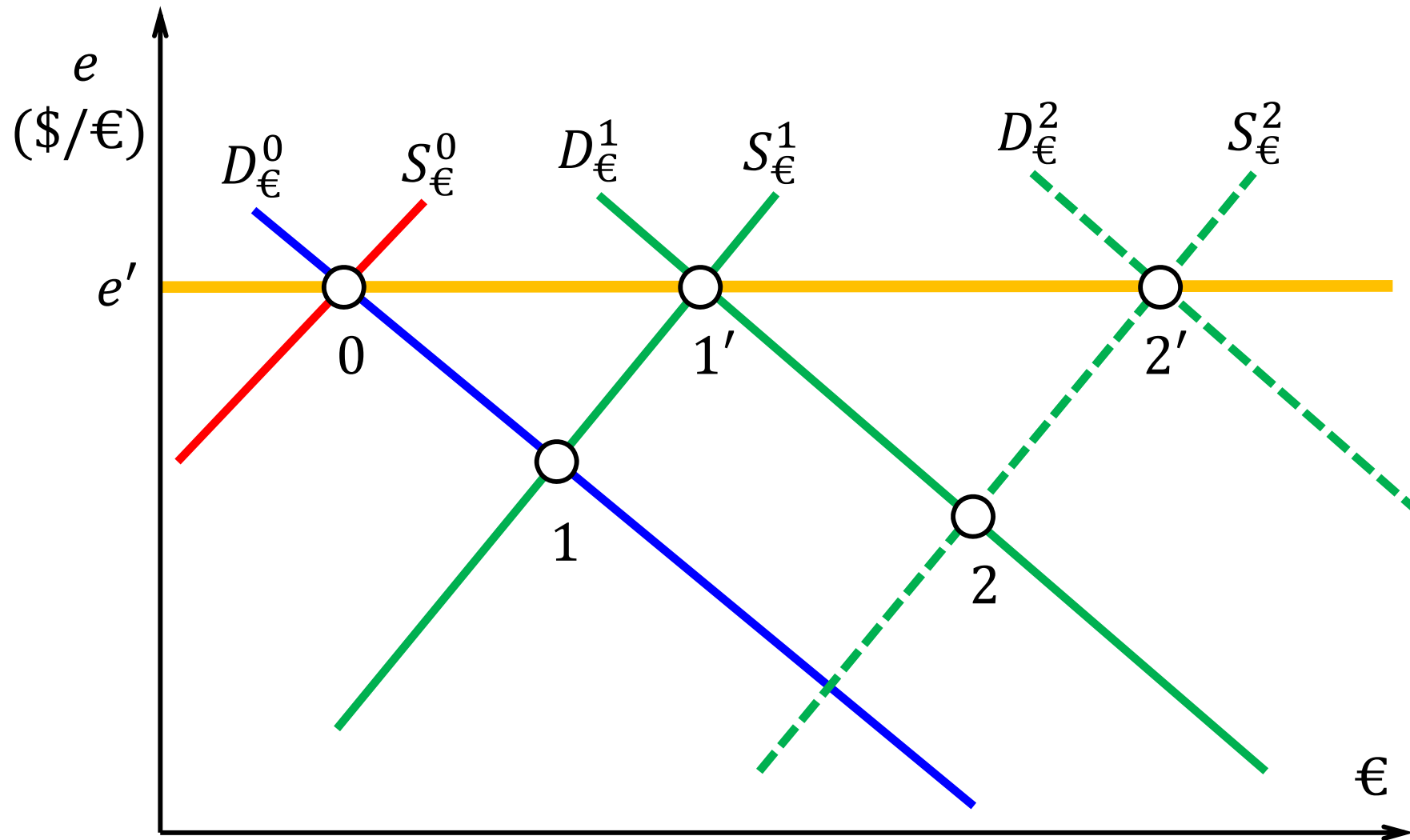
Exchange rate regimes

- Flexible or floating exchange rate
- Fixed exchange rate: revaluation / devaluation
- Managed float
- CB intervention in the currency market
- Anatomy of a typical currency crisis and speculative attacks

Intervention in the currency market



Currency crisis

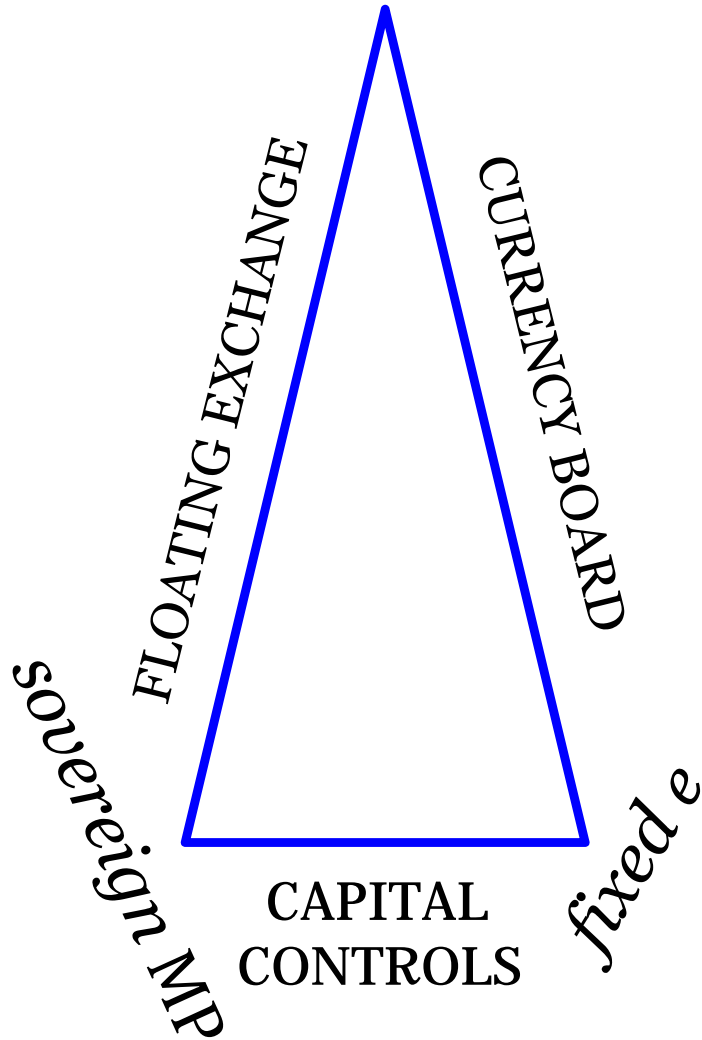


Trilemmas

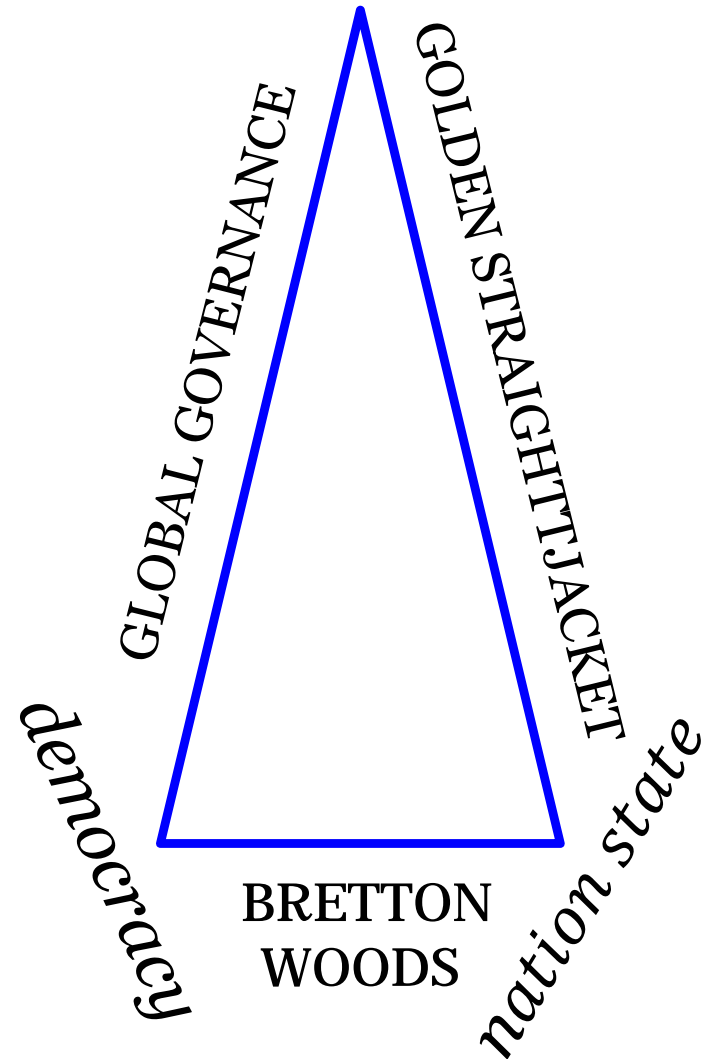
- Impossible trinity: you can only have two of
 - fixed exchange rate
 - independent monetary policy
 - unrestricted international mobility of capital
- Rodrik's trilemma: you can only have two of
 - domestic democracy
 - independent domestic policy (sovereign state)
 - hyperglobalization

Trilemmas

free capital flows



hyperglobalization



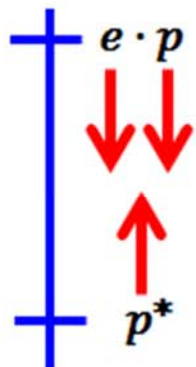
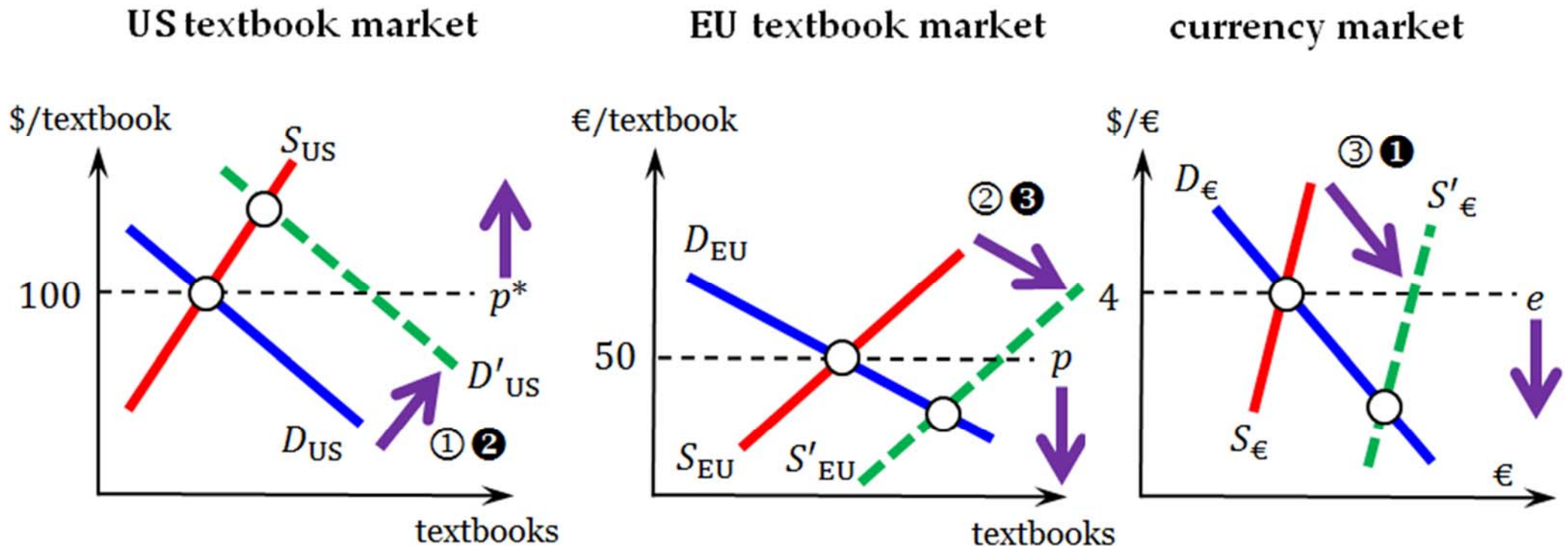
Real exchange rate

- Defined as
$$e_r = e \cdot \frac{P}{P^*}$$
- Competitiveness / real appreciation & depreciation
- Purchasing power parity exchange rate

$$e_{PPP} = \frac{P^*}{P}$$

- Commercial arbitrage and PPP
- The Big Mac index

Commercial arbitrage



- ① = Americans buy textbooks in US ② = sell them in EU ③ = and convert € in to \$
 ① = Europeans convert € into \$ ② = buy textbooks in US ③ = and sell them in EU

US = home economy	P^* = BM home price	BM price in \$ = P^*/e	PPP of \$ = P^*/P	market e on 11 Jan 2017	Over (+) under (-) valuation against the \$
US	$P = 5.06$	—	—	—	—
Brazil	16.5 R\$	5.11	3.26	3.22	1.14
UK	3.09 £	3.72	0.61	0.82	-26.31
China	19.6 ¥	2.83 \$	3.87 ¥/\$	6.92 ¥/\$	-44.07
Spain	3.95 €	4.13	0.78	0.95	-18.27
India	170 ₹	2.48	33.59	68.32	-50.83
Russia	130 руб	2.15	25.69	60.43	-57.49
Sweden	48 kr	5.26	9.48	9.12	3.96
Switzerland	6.5 CHF	6.35	1.28	1.02	25.49
Venezuela	3550 Bs.F	5.24	701.58	676.6	3.6

US = home economy	P^* = BM home price	BM price in \$ = P^*/e	PPP of \$ = P^*/P	market e on 22 Jan 2015	Over (+) under (-) valuation against the \$
US	$P = 4.79$	—	—	—	—
Brazil	13.5 R\$	5.21	2.82	2.59	8.70
UK	2.79 £	4.63	1.66 \$/£	1.66 \$/£	0.06
China	17.2 ¥	2.77 \$	3.59 ¥/\$	6.21 ¥/\$	-42.19
Eurozone	3.68 €	4.26	0.77 \$/€	0.86 \$/€	-10.98
India	116.25 ₹	1.89	24.27	61.62	-60.61
Russia	89 руб	1.36	18.58	65.23	-71.51
Sweden	40.7 kr	4.97	8.50	8.19	3.73
Switzerland	6.5 CHF	7.54	1.36	0.86	57.49
Venezuela	132 Bs.F.	2.53	27.56	52.10	-47.119

US = home economy	P^* = BM home price	BM price in \$ = P^*/e	PPP of \$ = P^*/P	market e on 22 Jan 2014	Over (+) under (-) valuation against the \$
US	$P = 4.62$	—	—	—	—
Brazil	12.4 R\$	5.25	2.68	2.36	13.48
UK	2.79 £	4.63	1.66 \$/£	1.66 \$/£	0.06
China	16.6 ¥	2.74 \$	3.59 ¥/\$	6.05 ¥/\$	-40.68
Eurozone	3.65 €	4.96	1.26 \$/€	1.35 \$/€	7.3
India	95 ₹	1.54	20.54	61.85	-66.78
Russia	89 руб	2.62	19.25	33.94	-43.29
Sweden	40.7 kr	6.29	8.8	6.47	35.97
Venezuela	45 Bs.F.	7.15	9.73	6.29	54.66

More parities

- Relative purchasing power parity (PPP \Rightarrow relative PPP)

$$\hat{e} \approx \pi^* - \pi$$

- Uncovered interest rate parity

$$\hat{e}^e \approx i^* - i$$

