

Econ 3633.001 International Finance, Theory and Problems

Instructor: Firat Demir

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Class time: MW 3:00-4:15 Physical Sciences Center Rm. 0363

1. Course Objective

This course is an introduction to international finance and is designed to introduce students to both theoretical and empirical analysis of global financial markets. In this era of globalization no student of economics, finance or any other field can fully understand current economic and political developments without a strong background in international finance.

Traditionally, international economics can be divided into two broad subfields: the study of international trade and the study of international finance. International trade analysis focuses primarily on the *real* transactional economy, that is, on those transactions that involve a physical movement of goods or a tangible commitment of economic resources. International finance focuses on the monetary side of international economy, that is, on financial transactions such as foreign purchases of U.S. dollars. It should also be pointed out that while international trade analysis primarily uses microeconomic theory, international finance uses macroeconomic theory.

We will first study the macroeconomic accounting system in an open economy framework using the balance-of-payments accounts. Next we will cover the foreign exchange market and apply no arbitrage ideas to derive parity conditions for exchange rates. Once these corner stones are in place we will study the past and present international monetary arrangements, issues and problems. We will also explore the determinants of international capital flows, foreign exchange risk and financial derivatives as well as different theories of exchange rate determination. We will conclude by visiting the current challenges and dilemmas faced by the existing international financial order. Overall, the subjects can be broken down into two sections: open economy macroeconomics (Chapters 12 through 17) and the applications of the theory to international monetary policy (Chapters 18 through 22).

Briefly, the main objectives of the course are:

- To provide students with theoretical knowledge regarding the functioning of international finance including a variety of methods and models used for this purpose.
- To locate, organize, and analyze international finance data to get insightful conclusions.
- To enable students to develop necessary skills to apply the methods and models to policy making as well as to current economic debates.

2. Course Structure

The course is designed around lectures, assigned readings, and class discussions. The students are expected to come to each class after having read the assigned readings, and to participate in classroom discussions. The topics covered in the lectures will overlap the materials found in the textbook. However, the lectures and discussions will, on occasion, cover some materials that are not found in the textbook or in the assigned readings. Students will be responsible on examinations for ALL ASSIGNED MATERIALS. Note, since each examination will include some material that is not in your textbook, it is strongly recommended that you attend the formal lectures.

3. Course Requirements

The final grade will be based on your performance from: a) three midterms (20%, 15% and 20%, respectively) and a final exam (30%); b) homework assignments and quizzes (10%); c) attendance and class participation (5%).

4. Exam Structure

The midterm exams are non-comprehensive. However, all three parts of the course are closely related and therefore you need to have a good understanding of the previous material in order to understand the later parts. The purpose of exams is twofold: to enhance your understanding of fundamental theories and concepts, and to encourage you to apply the theories to the real world. Therefore you may expect applied as well as theoretical questions.

5. Policy on Make-up Exam

There are no make-up midterms. If you miss an exam because of *a valid reason* the weight of all other exams will be increased accordingly. Otherwise you will obtain a score equal to zero.

6. Homework Assignments, Quizzes and Attendance Policy

For the homework assignments, you *can* work with a partner and form a group of maximum 2 people. In that case submit only ONE assignment under both names. There will a total of 6 - 9 homework assignments and quizzes and late submissions will *not* be accepted. Although attendance is voluntary, it is strongly recommended. I will take attendance every class and your overall attendance and class participation will count towards 5% of your final grade (I will waive 3 days of missing attendance).

Also, keep in mind that “the economics department reserves the right to drop students from economics courses for non-attendance during the first week of classes or failure to meet course prerequisites. Students who wish to drop economics courses after enrolment still have the responsibility for the drop.”

7. Textbook and Additional Readings

Required: - Krugman, P. and Obstfeld, M. (2008) International Economics: Theory and Policy, 8th edition, Addison-Wesley.

- Eatwell, J. and Taylor, L. (2000 or 2001), Global Finance at Risk: the Case for International Regulation, The New Press: New York.

Additional readings are available from the course website at learn.ou.edu.

Major References:

Yarbrough, B. V. and Yarbrough, R. M. (2006), The World Economy, Open-Economy Macroeconomics and Finance, 7th edition, Thomson South-Western.

Melvin, M. (2004) International Money and Finance, 7th edition, Pearson Addison-Wesley.

8. Academic Ethics

Cheating on assignments and exams, or plagiarizing (misrepresenting as one's own anything done by another) is penalized by the University of Oklahoma. A student found in such a situation will be given an F and will be brought to University of Oklahoma Honor Council for further penalties as defined under Academic Misconduct. For further information, refer to <http://www.ou.edu/honorcouncil/index.html>

9. Students with Disabilities

Any student who feels he or she may need an accommodation based on the impact of a disability should contact me privately as soon as possible to discuss his or her specific needs. For details refer to <http://drc.ou.edu/>

10. Grading Scale

97.5-100:	A+	77.5-79.9:	C+
95-97.49:	A	72.5-77.49:	C
90-94.49:	A-	70-72.49:	C-
87.5-89.9:	B+	67.5-69.9:	D+
82.5-87.49:	B	62.5-67.49:	D
80-82.49:	B-	60-62.49:	D-
		<60	F

Your final grade will follow the University of Oklahoma's grading scale, that is A, B, C, D, and F without the intermediate grades on the left.

I reserve the right to adjust this schedule of grade equivalents in the student's favor.

11. Course Outline and Reading Assignments

The following is a tentative list of topics and required readings. All readings should be completed (except those marked *, which are optional). Additional readings may be assigned from time to time. Chapter numbers refer to the Krugman and Obstfeld textbook.

Course Outline

I. Exchange Rates and Open-Economy Macroeconomics

1. National Income Accounting and the Balance of Payments, Ch. 12
2. Exchange Rates and the Foreign Exchange Market, Ch. 13
3. Money, Interest Rates, and Exchange Rates, Ch. 14

Exam 1: February 18

4. Price Levels and the Exchange Rate in the Long Run, Ch. 15
 - [*Rogoff, K. \(1996\), The Purchasing Power Parity Puzzle, *Journal of Economic Literature* 34 \(2\): 647-668.](#)
5. Output and the Exchange Rate in the Short Run, Ch. 16
 - [*Goldberg, P. and Knetter, M. \(1997\), Goods Prices and Exchange Rates: What Have We Learned? *Journal of Economic Literature* 35\(3\): 1243-72.](#)

Exam 2: March 11

II. International Macroeconomic Policy

6. Fixed Exchange Rates and Foreign Exchange Intervention, Ch. 17
7. The International Monetary System, 1870-1973, Ch. 18
 - Eatwell and Taylor, Ch.1 (pp.1-28); Ch.2 (pp.30-36)
 - [McKinnon, R. \(1993\), The Rules of the Game: International Money in Historical Perspective, *Journal of Economic Literature* 31\(1\): 1-44.](#)
 - Eichengreen, B. (2004) Global Imbalances and the Lessons of Bretton Woods, NBER Working Paper 10497.
8. Macroeconomic Policy and Coordination Under Floating Exchange Rates, Ch. 19
 - [*Obstfeld, M. and Rogoff, K. \(1995\), The Mirage of Fixed Exchange Rates, *Journal of Economic Perspectives* 9\(4\): 73-96.](#)

Exam 3: April 15

III. The Global Capital Market: Performance and Policy Problems

9. Costs and Benefits of Liberalization of Financial Markets, Ch. 21
 - Eatwell and Taylor, Ch. 2 (pp.36-53)
10. Developed Countries and the New Financial Order
 - Eatwell and Taylor, Ch. 4 (pp.96-139)
 - Setser, B. and Roubini, N. (2005), How Scary is the Deficit, *Foreign Affairs*, July/August.
 - Obstfeld, M. (2005), America's Deficit, World's Problem, *Monetary and Economic Studies*, October: 25-35.
 - Weisbrot, M. , Rosnick, D. and Baker, D. Going Down With the Dollar: The Cost to Developing Countries of a Declining Dollar, CEPR Issue Brief.
11. Developing Countries and the New Financial Order, Ch.22
 - Eatwell and Taylor, Ch. 5 (pp.140-179)
 1. Contagion
 2. Capital Market Integration and Financial Crisis:
 - a. Theory
 - Stiglitz, J. E. (2000), Capital Market Liberalization, Economic Growth, and Instability, *World Development* 28(6): 1075-1086.
 - b. Empirical Evidence
 - Taylor, L. (2001), Argentina: A poster Child for the Failure of Liberalized Policies? *Challenge* (November-December).
 - [*Krugman, P. "Currency Crises." available on Krugman's website.](#)
 3. Determinants of International Capital Flows: Pull vs. Push
12. International Regulation and Financial Infrastructure
 - Ch.21 (pp.603-610), Ch. 22 (pp.649-659).
 - Eatwell and Taylor, Ch. 3 (pp. 54-95); 6,7 (pp.180-239)
 - Tobin, J. (2000), Financial Globalization, *World Development*, 28(6): 1101-1104.
 - Davidson, P. (2000), Is a Plumber or a New Financial Architect Needed to End Global International Liquidity Problems? *World Development* 28(6): 1117-1131.

Final Exam: Monday, May 11, 04:30 PM - 06:30 PM

12. Tentative Schedule

Week	Date	Chapter/Section
1	21-Jan	12
	26-Jan	12
2	28-Jan	12
	2-Feb	13
3	4-Feb	13
	9-Feb	14
4	11-Feb	14
	16-Feb	14
5	18-Feb	Exam 1
	23-Feb	15
6	25-Feb	15
	2-Mar	16
7	4-Mar	16
	9-Mar	16
8	11-Mar	Exam 2
	16-Mar	Spring Break
9	18-Mar	Spring Break
	23-Mar	17
10	25-Mar	17
	30-Mar	17
11	1-Apr	18
	6-Apr	18
12	8-Apr	18
	13-Apr	19
13	15-Apr	Exam 3
	20-Apr	Section III. The Global Capital Market 9. Costs and Benefits of Liberalization of Financial Markets
14	22-Apr	9. Costs and Benefits of Liberalization of Financial Markets
	27-Apr	10. Developed Countries and the New Financial Order
15	29-Apr	11. Developing Countries and the New Financial Order
	4-May	12. International Regulation and Financial Infrastructure
16	6-May	12. International Regulation and Financial Infrastructure
	11-May	Final Exam 04:30 - 06:30 PM