

Econ 3633.001 International Finance, Theory and Problems

Instructor: Firat Demir

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Class time: TR 09:00-10:15 am Cate Center One 0174

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 (and financial crisis!) 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. Furthermore, 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. 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. Once these corner stones are in place we will study the past and present international monetary arrangements, issues and problems. We will conclude by visiting the current challenges and dilemmas faced by the existing international financial order, including the US current account problems and the 2008- global financial crisis. Overall, the subjects can be broken down into two sections: open economy macroeconomics (Chapters 2 through 7) and the applications of the theory to international monetary policy (Chapters 8 through 11).

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) two midterms (25% and 30%, 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 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 (for *non-essay* questions). In that case submit only ONE assignment under both names. There will be a total of 6 - 10 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).

7. Textbook and Additional Readings

Required:

- Krugman, P., Obstfeld, M., and Melitz, M. J. 2015. *International Finance: Theory and Policy*. 10th edition, Addison-Wesley.

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

Major References:

- Montiel, P. 2009. *International Macroeconomics*. Wiley-Blackwell.
- Yarbrough, B. V. and Yarbrough, R. M. 2006. *The World Economy, Open-Economy Macroeconomics and Finance*. 7th edition, Thomson South-Western.
- Melvin, M. and Norrbin, S. 2012. *International Money and Finance*. 8th edition (or any other earlier edition), Academic press.
- Eatwell, J. and Taylor, L. 2000/2001 *Global Finance at Risk: the Case for International Regulation*. The New Press: New York.

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://integrity.ou.edu/>

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. Laptop and Phone Policy

The use of laptop computers and tablets is subject to permission from the instructor and their use should be limited to access the lecture notes and/or PowerPoint slides. Mobile phones must either be switched off or set to the silent mode during lectures. This rule will be strictly enforced.

11. Religious Holidays

“It is the policy of the University to excuse the absences of students that result from religious observances.”

12. 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.

13. 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, Obstfeld and Melitz textbook.

Course Outline

I. Exchange Rates and Open-Economy Macroeconomics

1. National Income Accounting and the Balance of Payments, Ch. 2
2. Exchange Rates and the Foreign Exchange Market, Ch. 3
3. Money, Interest Rates, and Exchange Rates, Ch. 4
4. Price Levels and the Exchange Rate in the Long Run, Ch. 5
 - [*Rogoff, K. 1996. The Purchasing Power Parity Puzzle, *Journal of Economic Literature* 34 \(2\): 647-668.](#)

Exam 1: September 27

II. International Macroeconomic Policy

5. Output and the Exchange Rate in the Short Run, Ch. 6
 - [*Goldberg, P. and Knetter, M. 1997. Goods Prices and Exchange Rates: What Have We Learned? *Journal of Economic Literature* 35\(3\): 1243-72.](#)
6. Fixed Exchange Rates and Foreign Exchange Intervention, Ch. 7
7. The International Monetary System, 1870-1973, Ch. 8 (pp. 236-270)
 - [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.](#)
 - [*Obstfeld, M. and Rogoff, K. 1995. The Mirage of Fixed Exchange Rates, *Journal of Economic Perspectives* 9\(4\): 73-96.](#)

Exam 2: November 3

III. The Global Capital Market: Performance and Policy Problems

8. Costs and Benefits of Liberalization of Financial Markets, Ch. 8 (pp. 270-274; 281-285) Ch. 9 (pp.295-313; 320-327); *Handout*.
9. Developing Countries and the New Financial Order, Ch.11
 - [Stiglitz, J. E. 2000. Capital Market Liberalization, Economic Growth, and Instability, *World Development* 28\(6\): 1075-1086.](#)
 - [Krogstad, E. 2007. The Post-Washington Consensus, *Challenge* \(March-April\).](#)

- Rodrik, D. and Subramanian, A. (2009) Why Did Financial Globalization Disappoint? *IMF Staff Papers* (2009) 56, 112–138.
 - *[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.](#)
10. U.S. Current Account Deficit, Ch.8 (pp. 275-281)
- 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.](#)
11. a. The Great Recession: Global Financial Crisis of 2008, Ch.9 (pp.303-320)
- Montiel (2009) (*handout*); [Krugman \(2009\)](#); [Blanchard \(2009\)](#); [Stiglitz, J. \(2008\)](#); [Roubini \(2009\)](#); [Stiglitz \(2011\)](#).
- b. The Birth of Euro and the European Financial Crisis of 2009, Ch. 10
- [Krugman \(2011\) *NYT Magazine*.](#)

13. Tentative Schedule

Week	Date	Chapter (from the textbook) / Section (from the syllabus)
1	8/23	Introduction/Ch. 1
	8/25	Ch. 2 / Section 1
2	8/30	Ch. 2 / Section 1
	9/1	Ch. 2 / Section 1
3	9/6	Ch. 3 / Section 2
	9/8	Ch. 3 / Section 2
4	9/13	Ch. 4 / Section 3
	9/15	Ch. 4 / Section 3
5	9/20	Ch. 5 / Section 4
	9/22	Ch. 5 / Section 4
6	9/27	Exam 1
	9/29	Ch. 6 / Section 5
7	10/4	Ch. 6 / Section 5
	10/6	Ch. 6 / Section 5
8	10/11	Part II: International Macroeconomic Policy Ch. 7 / Section 6
	10/13	Ch. 7 / Section 6
9	10/18	Ch. 7 / Section 6
	10/20	Ch. 8 / Section 7
10	10/25	Ch. 8 / Section 7
	10/27	Ch. 8 / Section 7
11	11/1	*
	11/3	Exam 2
12	11/8	Part III: The Global Capital Market Section 8. Costs and Benefits of Liberalization of Financial Markets
	11/10	Section 8. Costs and Benefits of Liberalization of Financial Markets
13	11/15	Section 8. Costs and Benefits of Liberalization of Financial Markets
	11/17	Section 9: Developing Countries and the New Financial Order
14	11/22	Section 9: Developing Countries and the New Financial Order
	11/24	Section 10: U.S. Current Account Deficit
15	11/29	Section 11a: Global Financial Crisis of 2007- 2011
	12/1	Section 11a: Global Financial Crisis of 2007- 2011
16	12/6	Section 11b: European Financial Crisis of 2009 - 2011
	12/8	Section 11b: European Financial Crisis of 2009 - 2011
	Dec 14	Final Exam: 8:00 am – 10:00 am