

Module 1
International Finance

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Lectures: Mon 11 am – 1 pm & Tue 2 – 4 pm

Office: Room # 328

Office Hours: Tue 11 am – 1 pm or by appointment

This module deals with a selection of topics from international finance and open economy macroeconomics. On completing this section, the students are expected to be familiar with standard contemporary models of small open economy, international asset pricing and exchange rate determination. They will also be acquainted with some of the recent developments in international financial system and financial instruments.

References and Textbooks: Selected chapters from following textbooks will be used for various sections, in addition to journal articles listed below. Each topic will have a set of required and optional readings, marked separately.

Martín Uribe and Stephanie Schmitt-Grohé (2017), *Open Economy Macroeconomics*, Princeton University Press (**USG**)

Nelson C. Mark (2001), *International Macroeconomics and Finance: Theory and Econometric Methods*, Wiley Blackwell (**NM**)

Geert Bekaert and Robert Hodrick (2012), *International Financial Management*, Prentice Hall (**BH**)

List of topics:

1. **A Few Recent Developments in International Asset Markets**

Microstructure of international asset markets, segmentation in international equity markets, carry trade, derivatives: futures, options (including American and European options) and swaps, credit default swaps, momentum and algorithmic trading.

Required Reference:

- Lecture slides / notes
- BH Chapt. 20 & 21 (selected sections)

Optional Reference:

- Sager and Taylor (2006), "Under the microscope: The structure of the foreign exchange market", *International Journal of Finance and Economics* 11: 81-95.
- Bekaert, Harvey, Lundblad and Siegel (2011), "What segments equity markets?", *The Review of Financial Studies* 24(12): 3841-3890.
- Akram, Rime and Sarno (2008), "Arbitrage in foreign exchange market: Turning on the microscope", *Journal of International Economics* 76: 237-253.
- Baba and Packer (2009), "From turmoil to crisis: Dislocations in the FX swap market before and after the failure of Lehman Brothers", *Journal of International Money and Finance* 28, 1350-1374.
- Chaboud, Chiquoine, Hjalmarsson and Vega (2014), "Rise of Machines: Algorithmic Trading in the Foreign Exchange Market", *The Journal of Finance* LXIX (5): 2045-2084.

2. Small Open Economy Models & International Asset Pricing

[Overview of small open economy models in presence of stochastic shocks: in Arrow-Debreu economy and with incomplete markets, six major puzzles in international macroeconomics]

Required Reference:

- USG Chapt. 3 & 4 (selected sections)
- Lecture slides / notes.

Optional Reference:

- Solnik (1974), "An equilibrium model of the international capital market", *Journal of Economic Theory* 8: 500-524.
- Stulz (1981), "A model of international asset pricing", *Journal of Financial Economics* 9: 383-406.
- Schmitt-Grohé and Uribe (2003), "Closing small open economy models", *Journal of International Economics* 61(1): 163-185.
- Obstfeld and Rogoff (2001), "Six major puzzles in international macroeconomics: is there a common cause?", in *NBER Macroeconomics Annual 2000*, (ed.) Bernanke and Rogoff, MIT Press.

3. Exchange Rates & Currency Markets: Theory & Policy

Theories of exchange rate determination and Meese-Rogoff puzzle, spot and forward currency markets, efficiency of foreign exchange markets: forward premium anomaly and peso problem, optimal exchange rate policy before and after Global Financial Crisis, optimal capital controls.

Required Reference:

- NM Chapt. 3, 4 & 6 (selected sections)
- USG Chapt. 9 (section 3 only) & 10 (selected sections)
- Lecture slides / notes

Optional Reference:

- Schmitt-Grohé and Uribe (2012), "Managing currency pegs", *American Economic Review: Papers & Proceedings* 102(3): 192-197.
- Fama (1984), "Forward and spot exchange rates", *Journal of Monetary Economics* 14: 319-338.
- Krasker (1980), "The peso problem in testing the efficiency of forward exchange markets", *Journal of Monetary Economics* 6(2): 269-276.