

INTERNATIONAL FINANCE

Business Economics 527
Winter 2016
PACCAR 393
Mon-Wed: 3:30-5:20

Professor Kathy Dewenter
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Office Hrs: Mon. 12:30-1:30 or by appt.

Course Objective:

This course is designed to give you an understanding of the international environment in which firms and individuals operate and an introduction to international financial management.

Upon completion of this course, you should be able to:

1. Understand the link between individual or firm trade and investment flows and a country's debt level, as well as the causes and implications of Europe's sovereign debt crisis.
2. Understand the relationship between a country's choice of exchange rate system and the value of its currency and how these directly and indirectly affect business decisions.
3. Understand the organization of international financial markets, including spot and derivative markets for foreign exchange.
4. Identify the currency-related risks a company faces when engaging in cross-border activities.
5. Be familiar with the range of financial and operational techniques available to a company for managing these cross-border risks, and the advantages and disadvantages of each.

Course Materials:

Eun & Resnick, International Financial Management, Irwin McGraw-Hill, Inc. 7th edition.

- The bookstore will have two versions of this text, you need only select one. It will have a hard copy of the full textbook, and also a hard copy version of my custom edition that only includes the chapters we cover during the quarter (8 out of 21). The custom version should be about 1/5th the cost of the full text.
- You could also order an on-line version of the custom book (which, surprisingly, will be about \$15 more expensive than the hard copy). You can purchase it here: <https://create.mheducation.com/shop/> using the isbn 9781308696126.
- You could also buy an older 6th edition of the book. I note in the assignments where the page numbers differ for the 6th edition.

Overhead slides, on Canvas (required)

Miscellaneous readings on reserve, on Canvas, or handed out in class (required)

Course Grading:

The course grade will be based on homeworks and two group projects (no final exam).

During the quarter, we will cover 5 sections of material. Following each section, you will have a homework assignment. You can discuss these assignments with your peers, but you must complete them on your own (i.e., no cutting and pasting of answers). The assignments are due at the beginning of the next class session. Each assignment is worth a total of 15 points. I will count the 4 highest grades from these assignments towards your final grade. (In other words, you can choose not to turn in one assignment.)

During the quarter, groups of 2 or 3 students will give 5-minute PowerPoint presentations on a topic selected from the list at the end of the syllabus. This presentation is worth 15 points.

A 3-4 person group project, with presentation, is due during the final exam period of class. This project is worth 25 points. A detailed description of the project is at the end of the syllabus.

I will also consider class participation when determining final grades.

Course Outline and Reading List

(Each section will take approximately four class sessions to complete)

1. Balance of Payments

(or, the supply and demand of foreign currencies)

Topics:

BOP accounting

Analyzing the BOP

Is the US current account deficit (or its net debtor position) a bad thing?

Reading:

E&R, Chapter 3 Balance of Payments

(6th edition: Chapter 3)

2. Exchange Rate Regimes

(or, macro rules and institutions to manage foreign currency supply and demand)

Topics:

Evolution of the international financial system

The fixed vs. flexible exchange rate debate

Can Central Banks control (or influence) currency values?

Why has the IMF changed its view on capital controls?

European Monetary Union: Status report

Currency crises: Causes and consequences

Reading:

E&R: Chapter 2 International Monetary System, Chapter 11 International Banking and Money Market pp 281-294

(6th edition: Chapter 2 and pp 283-294)

Dewenter, "Answers to Basic Questions About the Current Crisis in Mexico," on Canvas.

3. Exchange Rate Markets

(or, micro market structure: who, where, when and how foreign currencies are traded)

Topics:

Spot market and Bid-Ask spreads

Forward markets

Currency futures and options

3. Exchange Rate Markets Cont.

Readings:

E&R: Chapter 5 The Market for Foreign Exchange, Chapter 7 Futures and Options on Foreign Exchange pp 173-176, 181-182 up to Currency Futures and Options (6th edition: Chapter 5 and pp 172-175 and 180-181)

4. Exchange Rate Determination

(or, frameworks for thinking about changes in currency values)

Topics:

Empirical regularities

Purchasing power parity

Interest rate parity

Other models of exchange rates

Track record and best uses for the models

Is the FX market efficient? (Or, is currency speculation profitable?)

Reading:

Chapter 6 International Parity Relationships and Forecasting Foreign Exchange Rates (skip subsection on Fisher effects)

(6th edition: Chapter 6, skip subsection on Fisher effects)

Speaker: Ben Graves, Gates Foundation

5. Exchange Rate Exposure and Hedging

(or, frameworks and tools for managers in a global economy)

Topics:

Transaction, translation and economic and exposure

Hedging

Case studies in hedging exchange rate exposure: Merck and Western Mining

Readings:

E&R: Chapter 8 Management of Transaction Exposure, Chapter 9 Management of Economic Exposure pp 225-237

(6th edition: Chapter 8 and pp 227-241).

Lewent and Kearney, "Identifying, Measuring and Hedging Currency Risk in Merck," on Canvas

Maloney, "Managing Currency Exposure: The Case of Western Mining," on Canvas

Speaker: JoAnn Tillerman, private consultant to firms on managing currency exposure.

1. Small group presentations during the quarter:

Possible topics for the 2- or 3-person group projects are listed below. You can also propose a topic to Kathy. At the end of the second session, Kathy will ask people for their topics – she will get back to them during the next week to confirm presentation dates.

You should present your topic after the section that provides background information. The presentation should include PowerPoint slides and last about 5 minutes, providing background and links to issues discussed in the prior lectures.

Grading: 5 points for background (adequate, relevant); 5 points for linkages to concepts covered in class (appropriate, illuminating); 5 points for presentation (clear, engaging)

After Section 1: Balance of payments

- Japan's high level of debt/GDP
- Recent movements in the US, Japan, and China trade balance, with explanations

After Section 2: Exchange rate regimes

- China's moves to loosen controls on the Yuan
- Recent attempts to create an alternative to the US dollar as the world's reserve currency
- Discuss Bitcoin's prospects as a global currency

After Section 3: Exchange rate markets

- Tobin tax on currency trading
- Status report for publicly traded firms that trade currencies
- Status and repercussions from recent law suites against major banks that trade currencies for fixing rates and also misleadingly billing customers for trades.

After Section 4: Exchange rate determination

- Link between the US Federal Reserve and the falling value of India's Rupee
- Update on two currencies with big recent movements – how move and why

After Section 5: Exchange rate exposure and hedging

- Profile a firm that was accused of speculating with its foreign currency hedging program. Do you agree that they were speculating?
- Profile two firms that implemented operational hedges
- Profile two firms whose hedging strategies backfired

Final Large Group Assignment* “BECON527 in the movies”

The summer movie season is approaching and, once again, there are no movies about international finance. The Foster Movie Company (FMC) wants to fill that gap in the market. FMC has asked your team to pitch a movie idea based on take-aways from BECON527.

Presentation

You will make your pitch to FMC producers during the final exam session. You will have 5-8 minutes to present. Your pitch should include:

- Movie title
- Plot outline/synopsis
- Casting ideas

Think big! Think exciting! Think blockbuster hit!

But, also think about international finance. The movie critics at the *Wall Street Journal* and the *Financial Times* will write brutally negative reviews if your movie’s plot is not consistent with economic principles and market realities.

Similarly, the critics grading your presentation will be looking for correct application of BECON527 course concepts in your plot outline. This project is worth 25 points. Kathy will hand out a grading rubric later in the quarter to provide more detail on the grading.

Your pitch may have any format. Bonus points will be awarded for creativity.

Hard copy deliverable

Turn in one copy (per team) of a half page summary of your pitch (movie title, plot outline) when you do your presentation, plus copies of your slides.

List all the team members’ names at the top.

* Project idea “lifted” (with permission) from Debra Glassman, but originally based on a series of discussions that she and I had with someone pitching a book/movie deal to Hollywood about a global financial meltdown.