

ECON 551

International Finance

Module 3, 2020-2021

Course Information

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Classes:

Lectures: 3:30PM – 5:20PM, Monday & Thursday

Venue: 313 PHBS

1. Course Description

1.1 Context

Course overview:

This is an elective class open to graduate students in Master Programs in Economics, Finance, and Management. The purpose of the class is twofold. On the one hand, we broadly survey academic literature on various issues in international finance, and learn how theoretical models are used to explain (or more interestingly at times, weren't able to explain) stylized empirical facts. On the other hand, each student will explore one specific topic of interest, learn broadly about relevant background facts, and identify possible future research by delving deeply into existing literature.

Prerequisites:

Knowledge of intermediate level Macroeconomics & Econometrics (For example, textbooks such as “Intermediate Macroeconomics” by Mankiw and “Introductory Econometrics” by Wooldridge)

1.2 Textbooks and Reading Materials

Main reference:

- Krugman, Obstfeld, and Melitz, “International Economics – Theory & Policy” (Volume II: International Finance), 9th edition, Pearson and Tsinghua University Press

Lecture notes and supplemental materials will be provided to students, by in-class handouts and by documents archives in the Course Management System. Check also the reading lists of papers.

Recommended References:

- Obstfeld & Rogoff, "Foundations of International Economics." (Advanced theoretical reference)

2. Learning Outcomes

2.1 Intended Learning Outcomes

Learning Goals	Objectives	Assessment
1. Our graduates will be effective communicators.	1.1. Our students will produce quality business and research-oriented documents.	Group project Research proposal
	1.2. Students are able to professionally present their ideas and also logically explain and defend their argument.	In-class presentation
2. Our graduates will be skilled in team work and leadership.	2.1. Students will be able to lead and participate in group for projects, discussion, and presentation.	Group project
4. Our graduates will have a global perspective.	4.1. Students will have an international exposure.	Class material and homework
5. Our graduates will be skilled in problem-solving and critical thinking.	5.1. Our students will have a good understanding of fundamental theories in their fields.	Group project Homework
	5.2. Our students will be prepared to face problems in various business settings and find solutions.	Group project Research proposal
	5.3. Our students will demonstrate competency in critical thinking.	Research proposal

2.2 Course specific objectives

2.3 Assessment/Grading Details

Component	Weight
Homework assignments	15%
Quizzes	15%
Project:	60%
Background Facts	20%
Literature Review	25%
Presentation (or Referee report)	15%
Class Participation	10%

Homework: There will be several homework assignments. Homework covers the more technical part of the class (i.e. models and data). Students are expected to complete these homework assignments independently, unless otherwise specified.

Quizzes: There will be 3-4 in-class quizzes. Quizzes cover the non-technical part of the class (i.e. concepts and intuition). Material we covered in class, as well as in required readings, may appear in the quizzes.

Project: The project has two main parts: a background facts section and a literature review. Each group selects one specific topic, and completes a report that consists of a survey of relevant facts and a review of previous academic literature. Students are expected to present the knowledge acquired in a coherent and organized manner. All members of a group receive the same grade on the group report. The grade is then adjusted using outcome of an intragroup peer evaluation.

Participation: Class attendance is expected. Please notify me before the class for any *foreseeable* absence.

Students who miss class beyond reasonable frequency will automatically lose the class participation grade. In-class discussion and participation are strongly encouraged, and I reserve the right to make small upward adjustments to your final grade using participation performance.

2.4 Academic Honesty and Plagiarism

It is important for a student's effort and credit to be recognized through class assessment. Credits earned for a student work due to efforts done by others are clearly unfair. Deliberate dishonesty is considered academic misconducts, which include plagiarism; cheating on assignments or examinations; engaging in unauthorized collaboration on academic work; taking, acquiring, or using test materials without faculty permission; submitting false or incomplete records of academic achievement; acting alone or in cooperation with another to falsify records or to obtain dishonestly grades, honors, awards, or professional endorsement; or altering, forging, or misusing a University academic record; or fabricating or falsifying of data, research procedures, or data analysis.

All assessments are subject to academic misconduct check. Misconduct check may include reproducing the assessment, providing a copy to another member of faculty, and/or communicate a copy of this assignment to the PHBS Discipline Committee. A suspected plagiarized document/assignment submitted to a plagiarism checking service may be kept in its database for future reference purpose.

Where violation is suspected, penalties will be implemented. The penalties for academic misconduct may include: deduction of honour points, a mark of zero on the assessment, a fail grade for the whole course, and reference of the matter to the Peking University Registrar.

For more information of plagiarism, please refer to *PHBS Student Handbook*.

3. Topics, Teaching and Assessment Schedule

Time	Class Coverage
Week 1	<p>Course introduction: Globalization and China</p> <ul style="list-style-type: none"> - China as an open economy - Renminbi exchange rate regime through the years <p>Exchange rates</p> <ul style="list-style-type: none"> - Nominal exchange rate: introductions <p>Focal point: Bilateral and effective exchange rate in China mainland and Hong Kong</p>
Weeks 2 - 3	<p>Nominal exchange rate determination</p> <ul style="list-style-type: none"> - The foreign exchange markets <p><u>Reading</u>: Chapter 14</p> <p>Focal point: the offshore Renminbi exchange rate</p> <p>Focal point: Renminbi forward rate and expectation</p> <ul style="list-style-type: none"> - Models of exchange rate determination <p><u>Reading</u>: Chapter 15</p> <p>Focal point: Exchange rate, monetary policy, and market expectation</p> <ul style="list-style-type: none"> - Empirical evaluation of nominal exchange rate models <p><u>Reading</u>: Rossi (2013), Engel and West (2005)</p> <p>Focal point: Renminbi/US Dollar exchange rate forecast</p> <ul style="list-style-type: none"> - Optimal exchange rate regime

Weeks 4 - 5	<p>The real exchange rate and price levels in the long run</p> <ul style="list-style-type: none"> - The fair value of exchange rate Focal point: The Big Mac Index and law of one price - International price dispersion and the Purchasing Power Parity - Real exchange rate determination in the long run <u>Reading:</u> Chapter 16, Cheung, Chinn, and Fujii (2010) Focal point: The fair value of Renminbi exchange rate Focal point: Does PPP hold in the long run? Focal point: Comparing China and Japan
Week 6 - 7	<p>Balance of payment account</p> <ul style="list-style-type: none"> - Balance of payment account: an introduction <u>Reading:</u> Chapter 13 Focal point: A look at the Chinese Balance of Payment - Models of current account <u>Reading:</u> Chapter 17, Bernanke (2005), Chinn and Ito (2008) Focal point: Exchange rate and external imbalances Focal point: Global saving glut and double deficits - The external wealth and valuation effect Focal point: The external wealth of China Focal point: The Belt and Road initiative and China's external investment - Global imbalances before and after the 2008 financial crisis <p>Macroeconomic model of international transmission in the short run</p> <ul style="list-style-type: none"> - Economic spillover in an interconnected world - Monetary policy in the international context <u>Reading:</u> Supplementary notes on short run general equilibrium model
Week 8	<p>Additional topics*:</p> <ul style="list-style-type: none"> - A brief history of the international monetary system <u>Reading:</u> Chapter 19 Focal point: The Silver Act and the Chinese hyperinflation in the 1930s - Exchange rate regimes and capital control <u>Reading:</u> Chapter 18 Focal point: China at the crossroad - Optimal currency area and the Euro <u>Reading:</u> Chapter 20
Week 9	Students' presentations

* Tentative and subject to adjustment

Important Project Deadlines:

February 27th by the end of lecture: Group timeline due

March 16th by the end of day: Early report due

April 16th by the end of day: Group report due

4. Miscellaneous: Project Guidelines

The project will test students' ability to select a topic of interest, learn widely of related facts and previous researches, and think deeply and critically about existing literature. This is a class offered to graduate students. Students are expected to demonstrate these qualities by identifying possible ways to extend or mend the existing literature. The final report should resemble a serious proposal of master thesis.

The project contains two parts: background facts and literature review, and will be communicated in two ways: presentation and writing.

Choose a topic: you can select any topic in international finance according to your interest. In principle you can also select a topic in international trade, if that is what your hearts really desire, but you must consult me first in that case. The topic should not be too broad. For example, "the behavior of exchange rate" would be too large and vague. Topics such as "the long-run effectiveness of nominal exchange rate control" or "the role of capital control in avoiding financial crisis for developing countries" are likely to give better guidance regarding where to look. It is a good idea to start with a specific question. Do not worry if you think the initial topic is too small. It helps to focus your attention and effort, and once you have a deep understanding of the issue, it is always easy, and natural, to extend to related questions.

Background facts: These are the facts that are relevant for your topic. For example, if you intend to examine the effectiveness of exchange rate control, this section can examine past experiences of several representative countries. You can plot time series of some key variables. Institutional background, policies, and regulations also belong to this section.

It is critical that you obtain *first-hand information* for the background facts section. Please do not simply restate another researcher's observation, or copy a graph or a table from an earlier paper. Instead I expect you to obtain, play with, and present the data, even if in some case this is an exact replication of an earlier work. This is important because in existing papers, an author presents facts in a way that is most supportive of his or her own points. You will likely import another person's opinion if you take his graph as the "fact". Having the data at hand also makes it easy for you to explore patterns or check a simple idea, although it is not necessary to perform regression analysis with data.

When submitting your report, I expect you to *submit data together with the essay*. The background facts section will be judged based on relevance, accuracy, coherence, and organization.

Literature review: Each student should read at least three papers very carefully. Group members should communicate with each other and supplement each other's knowledge on the topic, and eventually come up with a coherent map of the *current* state of knowledge on the topic. While literatures on some issues have a long history, your literature review should weigh toward the newer papers.

It is essential that the final literature review is well *synthesized*, instead of being a list of summaries. The set of papers you select should be published or publishable in a good peer-reviewed academic journal. Guidance on how to write a literature review will be provided in separate files.

You should conclude the literature review section with a **proposal of future research**. The proposal should demonstrate your ability to think critically about the previous literature surveyed. When reading the papers, think about whether the paper takes into account all important facts, and whether overlooking a fact could lead to biased conclusion. Think about the limitation of the current research and how additional steps can be taken to improve it. Extending a paper is a possible way to go. Reconciling two papers that differ in opinions or findings could also yield fruitful new idea.

Your proposed study should be well motivated. If everything you propose to do work out optimistically, the research should make a *significant contribution to the literature*.

Avoid focusing on technical details, or simply replicating the work using Chinese data. Only propose to make an econometrics check if you think it will likely change the main result of the paper. Replicating a previous work using Chinese data is okay only if you clearly identify the aspects in which you expect China

to differ from other countries in the previous study. In that case, you should also analyze the consequences of those expected differences.

In every case, it is important that you precisely identify the *expected contribution* of your research to the literature. To do this, you need to first pinpoint the weakness of the previous paper(s), and then talk about how you plan to fix or improve it.

This simple proposal is intended to serve as a first step towards a full-scale thesis. It should be detailed and specific. The steps been proposed must be executable. That is to say, another person with necessary knowledge should be able to carry out the analysis proposed. Data availability check is not required for this class project, but it must be reasonable that the data you propose to use exists.

Presentation: Each group is going to give a mini-lecture to the class. The presentation should convey what you have learned by doing the project.

A large part of the presentation grade depends on your communication skills. The central idea should be effectively communicated. Slides should be well-organized to facilitate the flow of speech. We look for good verbal and non-verbal delivery. You should be responsible to control the pace of the presentation and finish within the designated time. The audience is invited to ask questions at any point of the presentation, and you should be well-prepared to answer them.

The presentation is graded by a group of classmate referees. To facilitate absorption of information, you should prepare a one-page, single-sided handout for classmates. The material on the handout can be tested in the in-class quiz.

Group work: Each member should make a substantive contribution to the project. Expect frictions as you have a diversified group. Respect each other's time constraint and schedule. Try your best to construct a positive and active team climate.

Group timeline and early report: These are mechanisms to ensure continuous effort and timely progress. Groups should meet before the end of the second week and come up with a mutually agreed *timeline* for the project. The timeline should reflect your commitments to work solidly and orderly toward an excellent project. The timeline should include, but not limited to, these elements: date of finalizing a topic, data collection, research question specification, finalizing set of papers to read, etc.

An *early report* is due at approximately the mid-module. Ten percent of final grade depends on the early report. (5% from the background facts & 5% from the literature review) The report should contain three components. First, you should pin down your research question. Second, complete citation of the set of papers you plan to read for the literature review should be submitted. Third, preliminary data examination should be presented. The papers and data analysis do not need to be complete *compared with your final report*, as you likely will add more paper or data when the needs arise. But it should be consistent with your final report on one hand, and be self-contained at the time of submission on the other.

A word on future research: By the end of the semester you will have a research proposal at hand. This is your initial plan on the project. I hope you do go ahead and extend it into a full paper. When doing so, keep in mind that your goal is to fix/improve previous literature, and your plan is only one possible way to do so. The nature of doing research is to embrace uncertainty, as you are solving a problem that has never been solved before. Unless you are doing something uninterestingly routine, there is only a slight chance that your initial plan can be carried out smoothly. Stick to your goal, but be flexible with the path. Re-optimize your plan periodically, as you will likely find better ways to achieve your goal.

Appendix: Examples of project topics

- RMB exchange rate misalignment estimation
- The financial crisis and global imbalances
- The development of currency union
- Relationship between exchange rate regime and current account
- Recent advances in currency crises literature
- RMB internationalization: what are the benefits and costs?