

Syllabus
INTERNATIONAL FINANCIAL MARKETS
BEM 112
Winter Quarter, 2018
Tuesday & Thursday, 1:00-2:20 p.m.

Text

Global Investments, 6th Edition
by Bruno Solnik and Dennis McLeavey

Cases

From the Bookstore

Instructor

Richard Roll, Baxter 235
rroll@caltech.edu

Office
p.m.

hours:

Thursday

3:00-5:00

Mon-Tues, 3-4 p.m.

Course Content

The course offers an introduction to international financial markets, their comparative behavior, and their inter-relations. The principal focus will be on assets traded in liquid markets: currencies, equities, bonds, swaps, and other derivatives. Attention will be devoted to (1) institutional arrangements, taxation, and regulation, (2) international arbitrage and parity conditions, (3) valuation, (4) international diversification and portfolio management, (5) derivative instruments, (6) hedging, (7) dynamic investment strategies, (8) topics of particular current relevance and importance.

Prerequisites

Prerequisites are BEM 103 and demonstrable knowledge of basic statistics.

Grading

The course grade will be based 20% on classroom participation, 20% on two written cases, 25% on a mid-term examination, and 35% on a final examination. Several other cases will be discussed in class during the quarter and presence is mandatory on those dates; (these discussions will count toward classroom participation.)

Written Assignments

Written analyses of cases must be handed in at the beginning of class on two occasions only: the “Bank for International Development” case on January 23 and the “DATA ANALYSIS: International Equity Return” on March 6. These written analyses can be completed as group projects; Maximum group size: four persons. Other cases and Problem Sets will be discussed in class and responses will

determine the class participation grade. No written submission is required for these cases, nor for the Problem Sets.

Examinations

The mid-term examination will be on February 8 during the regularly scheduled class period. The final examination is scheduled for one of the days from March 14 to 16 inclusive but it can be moved provided that everyone in the class agrees on the time and date. Anyone who cannot take the exams at the scheduled or agreed-upon times should not register for the course. Everyone must take the exams at the same time. Exams will be open book, open notes.

Bonus Points

In addition to the grades based on the assignments just mentioned, it is possible to earn **Bonus Points** (each point adds one percent to the final cumulative grade.) One **Bonus Point** will be awarded for each of the following:

- Correcting the instructor in class on three separate occasions
- On three occasions being the first to answer correctly a question during class
- Providing new information on software usage
- Pointing out a serious error in an analytical method or a reading assignment
- Helping a group of other students learn software or concepts¹
- Getting another student to improve 10 percentage points from midterm to final²

¹ The group of other students must inform the instructor of the helpful colleague.

² For instance, if the improving student scores 50 out of 100 points on the midterm, the final exam score would have to be 60 out of 100 and the improving student would have to convince the instructor that the helpful student was instrumental in the gain.

Schedule of Classes and Assignments³

Date	Topic	Assignment ⁴
January 4	Introduction to the International Monetary System and Financial Markets	ch. 1.
January 9	International Parity Relations: <i>Notes on Intl Parity Conditions</i> Problem Set #1	ch. 2.
January 11	<i>Balance of Payments</i> Problem Set #2	ch. 2.
January 16	Exchange Rate Determinants and Forecasting Central Bank Intervention <i>PPP and EMH</i> Problem Set #3	ch. 3.
January 18	The “Carry Trade” (or the Forward Premium “Puzzle”)	Handout.
January 23	CASE: Bank for International Development⁵	
January 25	International Fixed-Income Markets <i>Term Structure Arithmetic</i> Problem Set #4	ch. 7.
January 30	Costs of Financing CASE: J.C. Penney (B)	9-286-118.
February 1	Restructuring Sovereign Debt CASE: J.P. Morgan's Mexican Bank Debt	9-289-013.

³ Italicized items are readings from the course packet.

⁴All reading assignments are required. Supplementary non-required reading will be distributed at various class sessions. A number such as “9-186-079” refers to a Harvard Case. Cases and Homework are in the course packet. Homework will be discussed in class on the date indicated; (no written solutions are required.) Items in italics are special readings available on the course web page.

⁵This case requires an empirical analysis of exchange rates, inflation, and interest rates for the U.S. and Japan. Real data will be provided on the computer in spreadsheet form. A written analysis must be turned in at the beginning of the class period. You will have to be familiar with spreadsheets and statistical computations to successfully complete this assignment.

February 6	International Bond Portfolio Strategy	
February 8	Mid-Term Examination	
February 13	Currency Futures and Hedging <i>Continuous Hedging and Valuation</i>	ch. 10, pp. 433-452. ch. 11, pp. 485-496
February 15	Swaps <i>Valuing and Unwinding a Swap</i> CASE: Gaz de France	ch. 10, pp. 453-464. 9-288-030.
February 20	Currency Options	ch. 10, p. 464-476.
February 22	Equity Markets International Portfolio Management,	chs. 5-6. chs. 13 & 9, pp. 385-420.
February 27	Risk Control, and Performance Measurement <i>Mean Variance Optimization</i> Alternative Assets Emerging Markets I	ch. 12. ch. 8. ch. 9, pp. 421-425.
March 1	International Portfolio Selection <i>EV with FX hedging</i>	
March 6	Case: International Equity Returns⁶	
March 8	Emerging Markets II	
March 14-16	FINAL EXAMINATION	

⁶An extensive data sample of international equity returns (country indices) and exchange rates will be provided. You will be expected to analyze the scope of international diversification and suggest a strategy for diversifying across countries; i.e., what would be a sensible international asset allocation for a U.S. investor, a Japanese investor? A written analysis is due at the beginning of class. You will have to know some statistics to complete this assignment successfully.