

International Financial Markets, FNCE 219/719
University of Pennsylvania
The Wharton School

Fall Term 2010
Professor Urban J. Jermann

Office hours: Wednesday 1:10 to 3:00 pm, SH/DH 2327

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Webpage: <http://finance.wharton.upenn.edu/~jermann/teaching.html> (Webcafe has a link to the class webpage)

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Prerequisites For 219: FNCE 100, FNCE 101 or ECON 4, STAT 101
For 719: FNCE 601 + 602 (FNCE 602 can be taken concurrently)

Materials

(1) A customized book with readings has been prepared for this class by McGraw-Hill Create, ISBN # 978-0390-65964-4, it is available at the bookstore.

(2) 2 chapters from the book *International Finance Theory into Practice* by Piet Sercu are available on www.study.net

(3) Lecture notes, additional readings, assignments, homework questions and answers, and other material will be made available on the class webpage. There is no bulkpack for this class. You may want to print lecture notes beforehand and bring them to class.

(4) A small number of handouts will be distributed in class. There will a bursar-billed fee for these that is estimated to be less than \$10.

Course Requirements

- **Two Examinations** are scheduled for
Tuesday, **October 19**, in class
Thursday, **December 2**, in class

Each exam will count for 35% of the final grade. Unexcused absences from exams will result in a zero score in the calculation of the final grade. Excused absences from exams require approval prior to the exam. Exams are closed book, but you may prepare a letter sized sheet (8.5 by 11-inch) with your notes.

- **Five Written Assignments** will count together for 25% of the final grade; the lowest assignment score will be dropped. Each student is expected to join a project group consisting of 3-5 members. The project groups will jointly prepare and submit written assignments. The individuals constituting a group must remain the same over the semester, so please choose your groups carefully. To help reduce problems due to free-riding etc., group members will be asked near the end of the term to evaluate the participation of the other group members. This confidential evaluation may affect the individual grade obtained for the assignments.

Assignments will be available on the class webpage at least one week before they are due. LATE ASSIGNMENTS WILL NOT BE ACCEPTED. The written assignments will be discussed in class and answers will not be distributed.

• **One Short Quiz** of about 15 minutes will take place during the last class, on Thursday December 9. This quiz will count for 5% of your final grade and will cover material from the preceding lecture

Regrading exams and graded assignments

Any request for regrading must be submitted in writing within two weeks from the date the exams or assignments have been returned. The exam or assignment should be placed in my mailbox in the Finance Department.

The request for regrading must be very specific. When you request a regrade, the entire exam or assignment may be regraded. Unambiguous errors in grading will be promptly corrected. In order to avoid possible attempts to alter exams before a regrade is requested, a substantial fraction of the exams will be photocopied.

Homework

Several problem sets will be assigned during the semester and you will be given the answers to these. The purpose of these exercises is to give you the opportunity to make sure you fully understand topics covered in class. By regularly doing these exercises you get excellent training for exams and assignments and you will maximize your return from this class. These problem sets will not be graded, and you should feel free to work in groups.

Course Outline

This class is about the international financial markets and their financial instruments. The central themes are currency exchange rates, related derivative securities, and international asset allocation. The class will adopt the perspective of international investors as well as the perspective of internationally active firms.

Each of the following numbered topics covers approximately one week of classes.

FX basics

1. Introduction: Derivative usage, exchange rates since 1971
2. Spot Foreign Exchange Markets
Manipulating exchange rates, FX market structure, arbitrage
3. Eurocurrency Markets, Forward Contracts and Interest Rate Parity
4. Forwards: Valuation, Hedging and Markets

FX derivatives

5. Currency Futures: Futures markets, hedging and speculating with futures
6. Currency Options
Put-call parity, hedging with options, option pricing issues, Black-Scholes model
7. Currency and Interest Rate Swaps
Examples and motivations for swaps, swap valuation
8. Specialized FX derivatives: US Dollar Index contract, quantos

International asset allocation / Exchange rate theories

9. Exchange Rate Theories and Evidence: Purchasing Power Parity, Balance of Payments
10. International Equity Portfolios: International diversification, hedging fx risk
11. Expectations, Forward Rates and Interest Rates
Uncovered interest parity, carry trades, risk reversal
12. Quantifying Exchange Rate Risk

Several current event topics are treated at various points in the semester.

Classes, Assignments and Exams

Thu, Sept 9

Tue, Sept 14

Thu, Sept 16

Tue, Sept 21

Thu, Sept 23

Tue, Sept 28

Thu, Sept 30 Assignment #1 discussed, project groups are fixed

Tue, Oct 5

Thu, Oct 7

Tue, Oct 12 No Class: Fall Break

Thu, Oct 14 Assignment #2 discussed

Thu, Oct 19 Exam 1— in class

Thu, Oct 21

Tue, Oct 26

Thu, Oct 28

Tue, Nov 2

Thu, Nov 4 Assignment #3 discussed

Tue, Nov 9

Thu, Nov 11

Tue, Nov 16

Thu, Nov 18 Assignment #4 discussed

Tue, Nov 23

Thu, Nov 25 No Class: Thanksgiving

Tue, Nov 30

Thu, Dec 2 Exam 2 — in class

Tue, Dec 7

Thu, Dec 9 Short Quiz — in class // Assignment #5 discussed