

# International Finance

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# Introduction

- World economy has been heavily influenced by globalisation
- Increase in the degree of connectivity and integration of countries, corporations, firms, and the people within them
- Over time this has affected both developed and developing economies
  - Countries continue to expand their trade in goods and services
  - Countries continue to reduce their barriers to capital flows
- These two aspects are largely interrelated
- While globalisation presents many opportunities it also poses many challenges, as became clear during the GFC of 2008
- Continued development and growth in the use of cryptocurrencies present a number of unique opportunities and challenges for those involved in the foreign exchange market
- During this semester we will discuss the fundamental concepts, principles, and analytical theories that define international finance

# Globalisation

- According to Wikipedia:

“Globalisation refers to the free movement of goods, capital, services, people, technology and information. It is the action or procedure of international integration of countries arising from the convergence of world views, products, ideas, and other aspects of culture.”

- Increase in the share of international and transnational transactions
- Integration of world markets and convergence of prices
- Cultural convergence and increased awareness of common global problems

# Economic globalisation

- From an economic perspective the primarily focus is on:
  - Actual degree of integration of markets and development of indexes to measure the degree of globalisation
  - Reducing the autonomy in policy making
  - Effects of globalisation on world income distribution
  - Potential benefits of a further increase or decrease in integration
  - Future role of international institutions that seek to promote stability
- These are both interesting and complex research topics

# Theory of international economic transactions

- Theory relating to international economic transactions is well established
  - Factors of production are generally less mobile between countries than within a single country
  - Perfect mobility (both within and between countries) of commodities
- Modern models account for barriers to trade and the role of non-tradable goods
- Allows us to investigate the effects of barriers and the behaviour of exchange rates
- These topics are important given the rise in the degree of openness and interdependence of economic systems
- We will consider various theoretical, descriptive, positive and normative aspects of this area of study

# International macroeconomics and finance

- Associated with aspects relating to international monetary economics, open-economy macroeconomics, or international macroeconomics
  - Focuses on balance-of-payments disequilibria and the automatic adjustment mechanisms
  - Interaction between the balance of payments and other macroeconomic variables
  - Role of various exchange-rate regimes, exchange-rate determination and forecasting
- Also incorporates a number of aspects that are prominent features of the finance literature
  - Role of international financial markets, international monetary systems, international policy coordination and international monetary integration (or currency unions)
  - Includes studies relating to international liquidity, currency crises, debt problems, etc.
  - Efficiency of international financial markets, development of trading strategies and management of foreign exchange risk

# Static and dynamic models

- Much of the traditional international finance literature considers the balance of payments as a relatively static phenomenon
  - Primary concerns relate to the specific determinants of trade and financial flows in the absence of dynamic interactions
- Modern view considers trade and financial flows as the outcome of intertemporal optimal saving and investment decisions that are made by forward-looking agents
  - Models are based on policy-invariant microfoundations and rational expectations, where stochastic components describe the effects of economic shocks

# Conclusion

- Future leaders will need to understand the issues relating to the effects of globalisation if they are to make sound international financial decisions
- Also need to manage the myriad of risks that their institution will face in a competitive global environment
- Objective of this course is to prepare students to deal with these and other real-world issues