ASIAN FINANCIAL MARKETS

Fall/Winter 2017
Graduate School of Public Policy
University of Tokyo
Offered by Masahiro Kawai

Course Description:

This course will provide an overview of the structure, development and challenges of financial markets in Asia, including ASEAN member countries, China, Japan, Korea, India and other emerging and developing economies in the region. Its primary focus is how policymakers can achieve the right balance between financial development (through liberalization, innovation and inclusion) and financial stability (through macroeconomic management, financial regulation and supervision, and international financial safety nets).

Japanese and emerging Asian financial markets went through fundamental changes in the 1990s. The Japanese banking crisis and the Asian financial crisis of 1997-98 were instrumental in inducing such changes. The global financial crisis of 2007-09 again affected Asian financial markets and has offered several lessons to be learned. The course emphasizes that open-economy financial policy would require significant attention to be paid to the trilemma hypothesis in international finance.

At the end of the course, students are expected to understand the key drivers of Asian financial market development and deepening in the past 30 years and be familiar with a range of ongoing policy debates to influence financial development and stability in the region.

Students are expected to attend all lectures, participate actively in class discussions, produce a lecture note for the session of the student's choice, write a term paper on any of the lecture topics or related issues, and present the term paper.

Each student taking the course for credit will be assessed as follows:

- 20% - class attendance and contribution to class discussion
- 20% - production of a lecture note (individual)
- 40% - production of a term paper (individual)
- 20% - term paper presentation with powerpoint (individual)

Lecture Note:

- Maximum length of 20 pages (Arial font, 1.5 space, 11pt), including tables and figures
- The lecture note is due 8 January 2018 (Monday)

Term Paper: Maximum length of 20 pages (Arial font, 1.5 space, 11 pt), excluding tables and figures.

- A term paper proposal is due on 6 November 2017 (Monday)
- An agreed term paper proposal is due on 20 November 2017 (Monday)
- A draft term paper is due on 4 December 2017 (Monday)
- PPT for term paper presentation is due on 18 December 2017 (Monday)
- The final term paper is due on 1 January 2018 (Monday)

(For more details on the term paper see the “Term Paper Process and Guidelines” note at the end of this document.)

### Lecture Topics and Readings

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<th>Lecture Topics and Readings</th>
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The lecture will begin with discussions on the interactions *between* economic growth and development *and* finance. It emphasizes that the interactions are two-ways, namely economic growth and development promotes financial market development and vice versa. The lecture then will review characteristics of financial systems of different Asian economies; some are highly developed and others are less developed; and some are financially open and others are financially closed. The lecture will examine the evolving role of bank loans, bond and equity markets over time and issues related to the timing of deregulation and opening of financial markets to external investors.

**Readings (main readings in gothic):**


### [2] Japan’s Banking Crisis and "Japanization"

The lecture will discuss the causes and impacts of Japan’s banking sector crisis in 1997-98, including the postcrisis reforms of the banking system and the long-term impact of the crisis on the Japanese economy. It explains how the postcrisis regulatory and supervisory structure has evolved in Japan and explores the limit and potential of Tokyo as an international financial center.

**Readings (main readings in gothic):**


### [3] Asian Financial Crisis

This lecture will discuss the causes and impacts of the Asian financial crisis of 1997-98 that severely affected Thailand, Malaysia, Indonesia and Korea. It discusses the role of the IMF in crisis management and how financial and corporate restructuring was undertaken in affected economies.

**Readings (main readings in gothic):**


One of the lessons of the Asian financial crisis was the need to develop local-currency bond markets in emerging Asia as the second wheel of financial intermediation. The first wheel was the banking sector which was devastated by the crisis and could not function well as an effective financial intermediary during and after the financial crisis. This lecture reviews the development of capital markets, including stock markets and local-currency bond markets, and their further challenges.

**Review (main readings in gothic):**


13 Oct.
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<th>20 Oct.</th>
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<td><strong>[5] Global Financial Crisis, the G20 and Asian Finance</strong></td>
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This lecture will review the causes and impacts of the global financial crisis of 2007-09 on Asia and macroeconomic and financial policy management. It discusses the evolution of markets and institutions leading to the financial crisis, with considerations given to different types of market participants and their roles in the financial crises. A tighter regulatory framework has been put in place in the US, the UK and Europe which were the origins of the global financial crisis. This lecture examines the role of G20 and lessons to be learned for financial market stability and long-term growth in Asia.

**Readings (main readings in gothic):**


### Central Banking: Price Stability and Financial Stability

This lecture discusses the traditional role of monetary policy in achieving price stability and the more recent focus of financial stability. First, it explains how the concept of price stability and inflation targeting has evolved. Various monetary policy instruments have been developed in conducting monetary policy. It discusses the role of inflation targeting, the Taylor rule, and unconventional monetary policy (such as quantitative easing and negative interest rate policy) in the context of Asia and Japan. Then, the lecture explains the role of a country’s central bank in maintaining financial stability.

**Readings (main readings in gothic):**


### Capital Account Liberalization and Managing Capital Flows

This lecture will examine recent developments and trends in Asia’s financial sector. A substitute date for 3 Nov.
integration through capital account liberalization. In particular, it will discuss the theoretical basis of financial integration and its benefits as well costs. Among the issues to be discussed are financial services liberalization and capital market opening. The lecture focuses on how international capital flows could be managed through capital flow management policies.

Readings (main readings in gothic):


www.bis.org/speeches/sp120625.pdf


6 November 2017 (Monday): Deadline for submission of term paper proposal

[8] Currency Internationalization: Yen and RMB

This lecture will study the concept of currency internationalization, how currencies are internationalized, and benefits and costs of currency internationalization. The lecture focuses on lessons from Japan and the policy efforts pursued in China to accelerate RMB internationalization. As currency internationalization by a large country, such as China, has the potential to develop the currency into an international reserve currency, the lecture explores the possibility of the RMB becoming an international reserve currency.
Readings (main readings in gothic):


### [9] Choice of Exchange Rate Arrangement

This lecture will discuss the role of exchange rate arrangements for economic development and macroeconomic and financial stability in Asia. The lecture attempts to explain how country authorities might choose exchange rate regimes in their country-specific contexts. The lecture finally presents the lecture’s own study that examines whether a RMB bloc is emerging in East Asia.

Readings (main readings in gothic):


17 Nov.


20 November 2017 (Monday): Deadline for submission of agreed term paper proposal

[10] Impossible Trinity or Trilemma

This lecture examines one of the most widely discussed concepts of “impossible trinity” or “trilemma” in international finance and open-economy macroeconomics. The idea is that authorities in a country attempt to achieve the best mix of exchange rate stability, financial market openness, and monetary policy independence under the constraint that they cannot achieve all of them at the same time. The lecture introduces the lecture’s most recent study that attempts to show how authorities might choose the best mix from theoretical as well as empirical perspectives.

Readings (main readings in gothic):


Ito, Hiro and Masahiro Kawai. 2014. “Determinants of the Trilemma Policy


This lecture will examine how financial resources could be mobilized for long-term investment for economic development, particularly infrastructure investment and small and medium-sized enterprise (SME) financing in Asia. The lecture discusses the investment needs for infrastructure in Asia and financial inclusion, and provides various options for financing such investment. Some discussions will be devoted to how public-private partnerships (PPPs) can be successful.

Readings (main readings in gothic):


The Economist Intelligence Unit. 2014. Evaluating the Environment for Public-Private Partnerships in Asia-Pacific.


[12] International Monetary System and Asia

This lecture will discuss the problems with the existing international monetary system and directions for its future reform. The lecture points out the issue of the US dollar as the most dominant global reserve currency and the problems of the Eurozone system. It provides an Asian perspective to improve the functioning of the international monetary system.

Readings (main readings in gothic):


This lecture will review the role of the central bank and financial supervisory authorities in promoting macroeconomic and financial stability, particularly in the context of Asia. One of the most significant developments following the global financial crisis is the revamping of financial regulation and supervision in the US, UK and the EU as well as at the global level (the Financial Stability Board, the Basel Committee on Banking Supervision, BIS, and IMF). Financial authorities have put greater focus on macroprudential supervision, introduction of Basel III, and crossborder coordination. The lecture emphasizes the need for a country’s central bank and financial supervisory agency (or agencies) to work together, while the central bank retaining its independence. The lecture examines implications of the global agreements on international financial regulation and supervision for Asian financial markets. The discussion will include the issue of “shadow banking” particularly in China.
**Readings (main readings in gothic):**


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<th>18 December 2017 (Monday): Deadline for submission of powerpoint presentation material</th>
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<td><strong>[14][15] Student Term Paper Presentations</strong></td>
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<td>Students will make presentations based on their Term Papers. Presentation schedules will be finalized with the students.</td>
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<th>1 January 2018 (Monday): Deadline for submission of Final Term Paper</th>
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<td>8 January 2018 (Monday): Deadline for submission of Lecture Note</td>
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**Process and Guidelines for Lecture Note and Term Paper**

Students are required to write a lecture note and a term paper and make a presentation on the term paper. Production of a lecture note accounts for 20% of student grades. Submitting the term paper accounts for 40% of student grades and presenting it accounts for 20% of student grades. The term paper should examine a topic covered by, or closely related to, course materials. The paper should be a maximum of 20 pages (Arial font, 1.5 space, 11 pt).

**Process:**
1. Each student selects a topic on one lecture and produces a lecture note, having attended the lecture. A good lecture note should be logically consistent and supported by evidence (data) and past literature.  
DEADLINE: 8 January 2018 (Monday) by 12pm (Noon)

2. Each student selects a topic and submits a “term paper proposal”.  
DEADLINE: 6 November 2017 (Monday) by 12pm (Noon)

(a) The term paper proposal should be no more than two pages. It should include: paper title, short abstract highlighting the key research question(s) to be addressed in the paper, tentative answers to the questions posed (called hypotheses), approach or methodology used to examine the validity of the tentative answers (or to test hypotheses), and initial literature review.

(b) Students need to consult Professor Kawai, agree with him on a final proposal, and submit the final term paper proposal.  
DEADLINE: 20 November 2016 (Monday) by 12pm (Noon)

(c) Students should consult Prof. Kawai as needed during preparation of their term paper. They should submit a draft term paper.  
DEADLINE: 4 December 2017 (Monday) by 12 pm (Noon)

(d) Each student will make a presentation based on his/her draft term paper during the week of 18 December. Each presentation will be a maximum of 15-20 minutes (depending on the number of students) and should be supported by relevant materials, i.e. powerpoint slides etc. Comments and questions from other students and Prof. Kawai will follow. Presentation materials should be submitted prior to the presentation.  
DEADLINE for submission of presentation materials: 18 December 2017 (Monday) 12 pm (Noon)

(e) Students should revise the draft term paper by incorporating comments and suggestions received during powerpoint presentation and also by consult Prof. Kawai as needed. They should submit the final term paper.  
DEADLINE: 1 January 2018 (Monday) by 12 pm (Noon)

Guidelines on the term paper:

In preparing their term paper students should consider the following guidelines.

- The paper should pose research questions that are highly relevant to Asian financial markets, and provide tentative answers (called hypotheses) to the questions. Then the paper should examine the validity of the tentative answers (i.e., test the hypotheses) using convincing evidence. Hypothesis testing can be conducted in a quantitative or qualitative manner, i.e., by using statistical methods or non-statistical, narrative logics.

- Basic econometrics is sometimes useful to do this but is not always necessary. Simple analysis of trends, or a good analysis of what others have done before, can sometimes be appropriate. The student must show that he/she has an ability to define and think about an issue, examine it in some depth, and draw important conclusions and implications for policy.
The paper should include a review of literature that places the research in the context of what other researchers have done and makes clear why the paper is a contribution (no matter how small) to the body of knowledge. Through the review, the student should explain why the proposed research is worth pursuing. The review is not a simple listing of other people’s work. It should examine how this work relates to the questions the student is investigating.

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TERM PAPER PROPOSAL

Asian Financial Markets

Graduate School of Public Policy
University of Tokyo
September 2017 – January 2018

This proposal should be a maximum of two pages. It should be submitted to mkawai.tokyo@gmail.com by 6 November 2017. Please put “[Your name] GraSPP, University of Tokyo Term Paper Proposal” in the subject line of your email.

Student name:

Term Paper Title:

Abstract:

[The abstract should briefly outline the key research question(s) to be addressed in the paper, the tentative answer(s) to the question(s), the approach or methodology to examine if the hypotheses can or cannot be rejected, and how the paper will contribute to knowledge in the selected topic area.]

Initial Literature Review:

[The literature review should indicate main papers, books, texts you plan to use in developing your term paper. Please list a maximum of ten.]