Financial Economics

The objective of this course is to give the student an understanding of the operation of financial markets and pricing of financial assets. In the first part of the course basic principles of decision making under uncertainty will be developed. These principles will then be applied to portfolio selection problem in financial asset markets. Models of financial asset markets and their implications for valuation of stocks, bonds and derivative assets will be discussed.

Recent events in financial markets, such as the Financial Crisis of 2007-2009, will be discussed.

Course Textbook:


Course Outline:

1. Financial Markets: Basic Concepts and Ideas
   Bailey, Chapters 1 and 2; Hall, Chapters 1, 2

2. Information in Financial Markets
   Bailey, Chapter 3.

3. Uncertainty and Portfolio Choice
   Bailey, Chapters 4, 5

4. Capital Asset Pricing Model
   Bailey, Chapter 6

5. Arbitrage and Valuation
   Bailey, Chapter 7

6. Factor Models of Asset Pricing
   Bailey, Chapter 8

7. Empirical Tests of the CAPM and APT
   Bailey, Chapter 9

8. Discounted Present Value Rule
   Bailey, Chapter 10

9. Equity Premium Puzzle
   Bailey, Chapter 11
10. Bond Markets and Term Structure of Interest Rates  
   Bailey, Chapters 12 and 13, Hull, Chapter 4

11. Futures and Options  
   Bailey, Chapters 14-20; Hull, Chapters 3, 6-7

12. Topics in Market Microstructure  
   (time permitting)

**Supplementary Course Material:**


- Nobel Prize Committee 2013, “Understanding Asset Prices”.

- Articles: Each chapter in Bailey’s textbook has a list of references. Other references will be announced in class.


**Exams and Homework:**

There will be a midterm, a final exam, and two 30-minute long quizzes. The final exam is scheduled for Thursday, May 12, 8–10 am. The midterm will be on Thursday, March 10, in class. Homework assignments will be regularly given.

**In-class Presentation:**

Each student is required to present a journal article in class. Presentations will be 30-45 minute long.

**Grade Determination:** REVISED!

- Problem Sets: 15%
- In-class Presentation: 10%
- Midterm Exam: 25%
- Final Exam: 35%
- Quizzes: 15%

**Office Hours, Course Website, etc**

- Professor’s office hours: Mondays, 1:00-2:30 p.m.  
  4-139 Hanson Hall, 625-0708,  
  Email: jwerner@umn.edu

- Course Website: www.econ.umn.edu/~jwerner

**Incomplete Grades, Make-up Exams, and Scholastic Dishonesty:**