

**University of Maryland**  
**Master of Professional Studies in Applied Economics**  
**ECON 670: Financial Economics (Fall 2017)**  
 Lubomir Petrasek  
 Petrasek@umd.edu

Class	Wednesdays 6:45 to 9:30pm, 1400 16 <sup>th</sup> St N.W., suite 140. There will be a 15-minute break around 8pm.
Office Hours	By appointment before class
Midterm	<b>October 11, 2017</b>
Final	<b>November 15, 2017</b>
TA Name	Hidehiko Matsumoto
TA Email	DCmastersTA@econ.umd.edu
TA Office Hours	One day per week from 3:00-7:00, and by appointment. Not the same day each week. See program's ELMS/Canvas page for the schedule. Hide also sends weekly reminders via ELMS/Canvas Announcement.

### Overview

This course applies microeconomic theory and applied econometric techniques to the study of financial institutions and markets for financial assets. Students will learn how economists model and estimate the value of financial assets. The economic and empirical models are of interest to public policy makers and private wealth managers. Specific topics can include financial intermediation, the regulation of financial institutions, risk management, portfolio theory, the capital asset pricing model and the efficient markets hypothesis.

Prerequisites: ECON 641 and ECON 644 (can be taken concurrently with ECON 644)

### Course Objectives

1. Ability to understand, evaluate and analyze economic data
2. Ability to understand and interpret statistical evidence from economic data
3. Ability to apply empirical evidence to assessing economic arguments
4. Ability to apply macroeconomic theories to policy discussions
5. Ability to apply microeconomic theories to policy discussions
6. Ability to communicate economic ideas to a broader audience
7. Ability to evaluate the effectiveness of policy programs using sound economic techniques

The learning outcomes that pertain to this course are: 1, 2, 3, 5, and 6

**Required Readings:**

*Textbook:* Corporate Finance by Jonathan Berk and Peter DeMarzo, 4th edition<sup>1</sup>

*Journal Articles and Other Materials:*

1. Monetary Policy Report, Board of Governors of the Federal Reserve System, July 7, 2017 – Part 1 (Financial and Economic Developments)
2. Monetary Policy Report, Board of Governors of the Federal Reserve System, July 7, 2017 – Part 2 (Monetary Policy Developments) & July 2017 FOMC minutes.
3. Monetary Policy Report, Board of Governors of the Federal Reserve System, July 7, 2017 – Box on Monetary Policy Rules and Their Role in the Federal Reserve’s Policy Process.
4. Merton, Robert C., 1974, On the Pricing of Corporate Debt: The Risk Structure of Interest Rates, *Journal of Finance* 29, 449-470.
5. Jefferson, Duarte, Francis A. Longstaff, and Fan Yu, 2007, Risk and Return in Fixed-Income Arbitrage: Nickels in Front of a Steamroller? *Review of Financial Studies* 20, 769-811.
6. Graham, John R., and Campbell R. Harvey, 2001, The Theory and Practice of Corporate Finance: Evidence from the Field, *Journal of Financial Economics*, 187-243.
7. Jegadeesh, Narasimhan, and Sheridan Titman, 1993, Returns to Buying Winners and Selling Losers, *Journal of Finance* 48, 65-91
8. Asness, Clifford, 2003, Fight the Fed Model, *Journal of Portfolio Management*, 11-24.
9. Frazzini, Andrea, David Kabiller, and Lasse H. Pedersen, 2013, Buffet’s Alpha, *NBER Working Paper* 19681, November 2013.
10. Fama, Eugene F., and Kenneth R. French, 1996, Multifactor Explanations of Asset Pricing Anomalies, *Journal of Finance* 51, 55-84
11. Miller, Merton, 1988, The Modigliani-Miller Propositions after Thirty Years, *Journal of Economic Perspectives* 2, 99-120.
12. Jensen, Michael, and William Meckling, 1976, Theory of the Firm: Managerial Behavior, Agency Costs and Capital Structure, *Journal of Financial Economics* 3, 305-360 – Part 1, 2, and 3 (Agency costs of equity).
13. Jensen, Michael, and William Meckling, 1976, Theory of the Firm: Managerial Behavior, Agency Costs and Capital Structure, *Journal of Financial Economics* 3, 305-360 – Part 5, and 6 (Agency costs of debt).
14. Brau, James C. and Stanley. E. Fawcett, 2006, Initial Public Offerings: An Analysis of Theory and Practice, *Journal of Finance* 61, 399-436.
15. Jorion, Philippe. 2000, Risk Management Lessons from Long-Term Capital Management, *European Financial Management* 6, 277-300.
16. Pedersen, Lasse H., 2009, When Everyone Runs for the Exit, *NBER Working Paper* 15297.
17. Dechow, Patricia M., Richard G. Sloan, and Amy P. Sweeney, 1996, Causes and Consequences of Earnings Manipulation: An Analysis of Firms Subject to Enforcement Actions by the SEC, *Contemporary Accounting Research* 13, 1-36.

---

<sup>1</sup> The reading list is based on the numbering of chapters in the 4<sup>th</sup> edition. Students who decide to buy an earlier edition are responsible for comparing and finding the chapters to read.

Week	Date	Topic	Textbook Chapters	Article Numbers
1	30-Aug	Financial Markets, Time Value of Money	1, 4	1
2	6-Sep	Interest Rates and the Federal Reserve	5	2, 3
3	13-Sep	Valuing Bonds	6	4, 5
4	20-Sep	Valuing Projects and Firms	7, 8	6
5	27-Sep	Valuing Stocks	9	7, 8, 9
6	6-Oct* (Friday)	Risk and Return, midterm review	10, 11, Assignment 1	10
7	11-Oct	Midterm Exam, Cost of Capital	12, 13	
8	18-Oct	Capital Structure	14, 15, 16	11, 12, 13
9	25-Oct	Raising Equity and Debt	23, 24	14
10	1-Nov	Derivatives and Risk Management	20, 21, 30	15, 16
11	8-Nov	Financial Reporting, Regulation, final review	2, 29, Assignment 2	17
12	15-Nov	Final Exam		

\* Note that the course of week 6 has been rescheduled to Friday, October 6<sup>th</sup> to allow students to attend a placement/recruiting event on Wednesday, October 4<sup>th</sup> from 6:00 to 8:00pm in College Park. The time and place for the rescheduled course remain unchanged.

### Course Website

ELMS/Canvas will be used to post lecture materials and assignments. Students are responsible for everything covered in lectures, even material which may not be posted on ELMS/Canvas. You can access the site via [www.elms.umd.edu](http://www.elms.umd.edu). You will need to use your University of Maryland “directory ID” and password.

### Grading Policy

Midterm	30%
Final - Cumulative	40%
Assignments	10%
Presentation	10%
Online Discussion	5%
Class Discussion	5%
<b>Total</b>	<b>100%</b>

### ***Exam Policy***

There will be two exams: a mid-term and a cumulative final. Calculators allowed, except no cellphone calculators and no computers. Exams are closed book, closed notes. The midterm and final must be taken on the scheduled dates. See “Excused Absences” under “Other Policies” for permissible exceptions.

### ***Assignments***

There will be two assignments with due dates **October 6, 2016** and **November 8, 2016**, including problems and business cases. The assignments will be posted at least two weeks prior to these due dates; students are encouraged to begin working on these assignments as we cover the material. Students are also encouraged to meet with the TA to discuss any questions regarding assignments. Being able to understand and solve the assignment problems is the best way to succeed on the exams, together with reading the assigned materials and actively participating in the class. Some problems will require the use of STATA or other econometric software or your choice. You may work together on the assignments, but please write and submit your answers separately. Solutions will be posted before the midterm and final exam, respectively. All graded assignments will be returned to students within 7 days after submitting the assignments. As graded assignments may not be returned in time before the midterm and final exam, students are encouraged to make a copy of their submitted assignments.

### ***Presentations and Discussion Leaders***

Each student will be a *discussion leader* for one paper on the reading list (assigned during the 1<sup>st</sup> class) and prepare a *brief presentation* (7 minutes) to summarize the discussion of the article (see “Online Discussion” below) in front of the class. The summary should not be limited to discussing the article itself; it should also include the discussion leader’s critical analysis of the article, practical examples, important questions raised during the online discussion, and additional insights to connect the article to current developments. The presentation will be followed by a 15-minute discussion moderated by the discussion leader. Presenters will be evaluated on the quality of the presentation and their ability to lead the discussion online and in the class room. The instructor will be the discussion leader for Article #1 to provide an example and set expectations for the presentation.

### ***Online Discussion***

An important part of the class will be weekly only discussions. These discussions will cover the reading assignments for the *upcoming* class, including both the book chapters and journal articles. Each journal article will have its discussion leader (see “Presentations and Discussion Leaders” above) who will be primarily responsible for asking questions/posting comments on the article. However, all students are expected to participate in the discussion *each week*, either by asking questions/comments or by providing informed answers/responses to questions/comments asked by the discussion leader, other students or the instructor. Both the quality and the quantity of entries per student will determine the final online participation grade. Discussions will generally occur on Monday and Tuesday before the upcoming class, and stay open for 48 hours.

### ***Participation***

Students are expected to actively participate in the class, in particular during discussions and problem solving. Credit will be given for active participation, especially volunteering to solve a problem or answer difficult questions in front of the class.

**Late Penalty**

All assignments and discussions are subject to late penalties. The penalties are as follows: 20% for late work submitted after the specified time on the due date, 50% for second day. Assignments are not accepted after the second day. Late penalties apply except when prior approval is obtained.

**Final Course Grades**

Final letter grades are based on the weighted score. Numerical course grades will be translated into letter grades as follows:

93-100	A
90-92	A-
80-89	B+
70-79	B
60-69	B-
50-59	C+
40-49	C
30-39	C-
20-29	D+
10-19	D
0-9	F

A+ may be given for exceptional achievement to a student or two at the very top of the class' grade distribution.

## Other Policies

**Email:** Email is the primary means of communication outside the classroom, and I will use it to inform you of important announcements. Students are responsible for updating their current email address via <http://www.testudo.umd.edu/apps/saddr/> AND for paying attention to messages I send to the class via ELMS. Failure to check email, errors in forwarding email, and returned email due to “mailbox full” or “user unknown” will not excuse a student from missing announcements or deadlines. I will do my best to respond to email within 36 hours.

**Contact Hours:** Three credit courses at the University of Maryland require a minimum amount of contact between instructors and students. Our courses’ 12 weekly 3-hour meetings only satisfy 80% of the university’s contact requirement. The other 20% is satisfied by weekly mandatory and graded online contact. In principle, the contact hours requirement could be satisfied by scheduling 3 additional 150-minute meetings per term, or 6 additional 75-minute meetings, or 10 additional 45-minute meetings. But in practice the contact hours requirement is satisfied by the weekly online discussions. The weekly online discussions are a more flexible way to ensure that our program’s courses in DC provide the same level of student-instructor contact as the traditional 15-week, face-to-face, version of the same course when it is taught on campus in College Park.

**Work Load:** Mastering the material covered in this course requires a significant amount of work outside of class. Students should expect to spend more time outside of class than in class – typically at least twice as much time. The courses in our DC program are 12-week courses that cover all the same material as a traditional semester-long 3-credit course (15 weeks). The compressed schedule makes it possible to complete our degree in just 15 months if you take 2 courses each term. But the compressed schedule also implies an accelerated pace with an average of 25% more work per week in a given course ( $15/12 = 1.25$ ). The normal full-time load in a master’s program is 3 courses per semester, or 6 courses per year. Students who take 2 courses per quarter in our program complete 8 courses per year. So taking 2 courses per quarter in our program is equivalent to 133% of a full-time load per year ( $8/6 = 1.33$ ).

**Academic Integrity:** The University of Maryland has a nationally recognized Code of Academic Integrity, administered by the Student Honor Council. This Code sets standards applicable to all undergraduate and graduate students, and you are responsible for upholding these standards as you complete assignments and take exams in this course. Please make yourself aware of the consequences of cheating, fabrication, facilitation, and plagiarism. For more information see [www.studenthonorcouncil.umd.edu](http://www.studenthonorcouncil.umd.edu).

**Student Conduct:** Students are expected to treat each other with respect. Disruptive behavior of any kind will not be tolerated. Students who are unable to show civility to one another or myself will be referred to the Office of Student Conduct. You are expected to adhere to the Code of Student Conduct.

**Excused Absences:** The University of Maryland’s policy on excused absences is posted here: <http://www.president.umd.edu/administration/policies/section-v-student-affairs/v-100g>

Please note:

If you miss any class meetings for any reason, you are still responsible for all material covered during the meeting you missed. It is your responsibility – not the instructor’s – to get yourself caught up in the course. Instructors routinely facilitate things by posting lecture notes, etc.

If you need to miss an exam or other graded course requirement because of illness, injury, or some other emergency: Follow doctor's orders and get documentation. Get in touch with the instructor as soon as you’re able – preferably prior to missing the exam or deadline. Communicate with the instructor to make up the course requirement as soon as possible. You are entitled to recover before you make up the course requirement, but you are not entitled to extra days to study beyond the time the doctor's note says you’re incapacitated. If you are incapacitated for more than a week or so beyond the end of the term, your grade in the course will be an

“Incomplete”. In such cases you must negotiate a plan with your instructor for completing the course requirements. Once you make up the course requirement the instructor will change your "I" to the appropriate letter grade.

**School Closings and Delays:** Information regarding official University closing and delays can be found on the campus website and the snow phone line: (301) 405-SNOW (405-7669). Since our program is an evening program in downtown Washington, DC, rather than a day program in College Park, we do not always cancel classes on the same days as the College Park campus. The program director will always announce cancellation information to the program as an announcement on the program’s ELMS/Canvas site. This will generally be done by 1:00 p.m. on days when weather or other factors are an issue.

**Students with Disabilities:** The University of Maryland does not discriminate based on differences in age, race, ethnicity, sex, religion, disability, sexual orientation, class, political affiliation, and national origin. Reasonable accommodations will be made to students with documented disabilities. I will make every effort to accommodate students who are registered with the Disability Support Services (DSS) Office and who provide me with a University of Maryland DSS Accommodation form.

**Academic Progress:** The graduate school requires that students maintain a GPA of at least 3.0. Students whose cumulative GPA falls below 3.0 will be placed on academic probation by the graduate school. Students on academic probation must ask the program’s director to petition the graduate school if they want to remain in the program. The petition must include a plan for getting the student’s GPA up to at least 3.0. Students who do not live up to their plan can have their enrollment in the program terminated without having earned the degree. Note: a grade of "B" corresponds to a GPA of 3.0. A grade of "B-" corresponds to a GPA of 2.7.

**Building Access:** The door to the building at 1400 16th Street is unlocked on weekdays until 7:00 p.m. Students who arrive after 7:00 p.m. or on weekends will find the door locked. The building’s security guard is stationed at a desk just inside the door until 11:00 p.m. and will let you in. You can also call the phone on the security guard’s desk by dialing (202) 328-5158. If the security guard is off duty or happens to be away from his or her desk when you arrive, you can go around to the other door at 1616 P Street and pick up the black phone to the right of that door. You will be connected to the company that handles security for our building. If you tell them you are with the University of Maryland, they should ask you for a password. When you tell them the password, they will be able to unlock the door for you. You can get the password from the program coordinator, the TA, or the program director. Please note: the building security staff are not able to buzz you in at the 1400 16th Street door. You have to go around to the 1616 P Street door to be buzzed in.