

Econ 670: Financial Economics

Course Information and Syllabus

Spring 2022

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Office Hours: Mondays 5:30pm–6:30pm, and by appointment

Class: 6:45pm–7:30pm and 8:15pm–9:00pm on Wednesdays

Class Location: Online

Teaching Assistant: Eric Piato (Piato@umd.edu)

TA Office hours: Tuesdays 5:30pm-6:30pm

Midterm: 13-April-2022

Final: 18-May-2022

1 General Information

1.1 Online instruction

Everything in the course, **except midterm and final exams**, will be held online via Zoom. **The midterm and final exams will be administered in person with a proctor.** There will be no face-to-face meetings. I strongly encourage you to keep your video on and stay muted during the classes, unless asking a question. You are required to attend all of the

classes.

Note that because of the spring break, we will not meet on 23-March. Instead, we will meet on 12-March, Saturday, at the same time 6:45 pm. See Course Calendar below.

1.2 Course Objective

This course is designed to introduce students to key topics in financial economics: the fundamentals of modern financial analysis, instruments and institutions, corporate investment and financing decisions, the theory of portfolio choice, and theories of asset pricing. Topics include diversification, arbitrage, market efficiency, the valuation of bonds, stocks, and derivatives. We will examine how a set of underlying economic principles are applied to determine the value of basic financial instruments such as stocks and bonds, as well as to more complicated derivative securities such as futures and options.

Prerequisites: Econ 641 and Econ 644

1.3 Textbook

Our textbook will be: Corporate Finance, 5th Edition (*not* the core edition) by Jonathan Berk and Peter DeMarzo (You can use previous editions, but then you will be responsible for finding the right chapters to read).

We will also periodically read and discuss journal articles in the areas that we will be studying. These additional readings are listed below.

1.4 Course and Program Objectives

Our program has 7 general learning outcomes for students:

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.

1.5 Communication– Email

You are welcome to contact me via email, and I will try my best to respond within 36 hours (or as early as I am able). The course will be held online, but if you would like to speak with me “in person”, we can have an online chat (during my office hours or by appointment).

The University has adopted email as the primary means of communication outside the classroom, and I will use it to inform you of important announcements. The University creates an “@umd.edu” email address for every graduate student. All official UMD communications will be sent to students at their “@umd.edu” email address. You are responsible for reading your @umd.edu email address, including ELMS/Canvas Announcements I send to the class. You should make sure ELMS/Canvas Announcements and messages are forwarded to an email address that you check regularly. 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.

2 Grading and Related Issues

You are expected to read the assigned readings, and ideally lecture notes prior to class (listed below) and to participate actively in group assignments and discussions.

You will be assessed on the basis of: assignments (20%), data cases (15%), online discussions (15%), quizzes (5%), a midterm exam (20%), and a final exam (25%).

Note, online discussions include the “quality” of your presentation, your ability to lead the discussions, as well as your attendance on other students’ discussions.

Assignments: There will be two assignments (see class calendar below for due dates) with submission deadlines of 6:30pm (i.e. before class). The assignments must be submitted through ELMS. The assignments will be posted about two weeks prior to these due dates; you are encouraged to begin working on these assignments as we cover the material. You 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. 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. Marks will reflect assessments of both final answers and supporting work. If needed, you can use Stata or Excel for empirical work.

Data cases: There will be two data cases (see class calendar below for due dates) with submission deadlines of 6:30pm (i.e. before class). The solutions must be submitted through ELMS. The aim of data cases is to familiarize you with data and real-life applications of the concepts we are learning through the classes. You can work in groups (highly encouraged) but please submit

your answers separately. We will have applications using STATA or Excel. Your TA will provide the data or we will guide you on how to access and download the necessary data.

Quizzes: There will be several quizzes, which will allow me to assess the progress of the class and class participation. You can prepare for the quizzes by reviewing material covered in the previous class and reading the assigned materials. No makeup quizzes will be given under any circumstances. You will receive a credit if you participate in a quiz, even if your answers are wrong.

Presentations and online discussion: *I will be the presenter and the discussion leader for the first article to provide an example and set expectations for the presentation.* An important part of the class will be weekly presentations and online discussions. These discussions will cover the reading assignments for the upcoming class, listed below. We will use an asynchronous online discussion board in ELMS.

Presentation: You will team up with another student (so 2 students) to understand and read the paper. **Each one of you** will prepare and give one 10-12 minute presentation in total (starting in week 3) summarizing an article that is listed on the reading list. The summary includes (i) what the article is about, (ii) what the main findings/messages are, (iii) your critical thinking (what is your take from the article? What did you like the most?), and (iv) Your suggested two or three discussion questions related to the article.

The presenting team is expected to:

- Send me their first drafts of the slides a few days prior to the presentations so that I can provide feedback.
- Record their presentation and submit it through ELMS so that we will have an online discussion of the presentation.

- Answer possible questions coming from the audience (the rest of the students and myself).

Presenters will be evaluated on the quality of the presentation and their ability to lead the discussion.

Discussions: You will both post your previously recorded presentations on the same discussion and add three discussion questions. During the online discussions, we will discuss those journal articles. **All** students are expected to participate in **all** discussions by asking constructive questions or answering the posted discussion question. Both the quality and the number of entries per student will determine the final online participation grade. The discussions will be open from Friday Midnight to Tuesday midnight. The team will manage and lead the discussions.

Exams: Your exams will be in-person and proctored. No collaboration is permitted in midterm and final exams. It is a closed book exam. You can (and possibly should) use calculators or excel. See “Excused Absences” under “Other Policies” for permissible exceptions. The exams will take place in UMD DC suite: 1400 16th Street, NW, suite 140.

TA office hours: Each week, I will post practice questions through ELMS. Your TA will solve these questions during his office hours. I strongly advise you to try to solve the questions by yourselves before office hours and attend office hours to ask questions/go over the solutions.

3 Journal articles:

1. Monetary Policy Report, Part 1 –Recent Economic and Financial Developments, Board of Governors of the Federal Reserve System, July 2021. [Ilknur](#)
2. Monetary Policy Report, Part 2 –Monetary Policy, Board of Governors

- of the Federal Reserve System, July 2021. [Faisa and Shriya](#)
3. 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.
 4. 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. [Atklit and Clory](#)
 5. Fama, Eugene, and Kenneth French, 2005, “Financing decisions: Who issues stock?” *Journal of Financial Economics*, p. 549-582. [Michael and Rodney](#)
 6. Cochrane, John, 2011, “Presidential Address: Discount Rates”, *Journal of Finance*, 1047-1108 – Part I, II, and III [Azanaw and Brandon](#)
 7. Baker, Scott, Bloom B, Davis, S., Kost, K., Sammon, M. and Viratyosin, T., 2020, “The Unprecedented Stock Market Impact of COVID-19”, NBER Working Paper No. 26945 [Laura and Osamu](#)
 8. Correia, Sergio, Stephan Luck, and Emil Verner., 2020, “Pandemics depress the economy, public health interventions do not: Evidence from the 1918 flu.”, working paper. [Pierre and ?](#)
 9. Fama, Eugene, Kenneth French, 2004, “The Capital Asset Pricing Model: Theory and Evidence”, *Journal of Economic Perspectives*, 18(3): 25-46. [Carlos and Ryan](#)
 10. Fama, E.F. and French, K.R., 1993. Common risk factors in the returns on stocks and bonds. *Journal of financial economics*, 33(1), pp.3-56. [Ian and James](#)
 11. Baker, Malcom, Jeffrey Wurgler, 2007, “Investor Sentiment in the Stock Market”, *Journal of Economic Perspectives*, 21(2): 129-151. [Matthew and Sydney](#)

12. Barberis, N. and Thaler, R., 2002. “A survey of behavioral finance”, NBER Working paper. **Caleb and Connor**
13. Miller, Merton, 1988, “The Modigliani-Miller Propositions After Thirty Years”, Journal of Economic Perspectives 2, 99-120. **Jerome and Scarp**
14. Jorion, Philippe. 2000, “Risk Management Lessons from Long-Term Capital Management”, European Financial Management 6, 277-300. **Max and ?**

4 Course Calendar

| Week | Date | Topic | Chapter | Article |
|------|----------|---|---------|---------|
| 1 | 2-March | Time Value of Money | 4 | |
| 2 | 9-March | Interest Rates and the Federal Reserve | 5 | 1 |
| 3 | 12-March | Valuing Bonds | 6 | 2, 3 |
| 4 | 16-March | Investment decision rule | 7 | 4, 5 |
| 4 | 23-March | no class | | |
| 5 | 30-March | Valuing Stocks/ Assignment 1 | 9 | 6, 7, 8 |
| 6 | 6-April | Risk and Return/ Data case 1 | 10, 11 | |
| 7 | 13-April | Midterm Exam | | |
| 8 | 20-April | Asset pricing 1 | 11, 12 | 9, 10 |
| 9 | 27-April | Asset pricing 2 | 12, 13 | 11, 12 |
| 10 | 4-May | Capital Structure / Assignment 2 | 14, 15 | 13, 14 |
| 11 | 11-May | Options / Data case 2 | 20, 21 | |
| 12 | 18-May | Final Exam | | |

5 Other Policies

Other Standard Policies for the Program and the University of Maryland: Policies related to all graduate courses at the University of

Maryland are posted on this page of the Graduate School's website:

<https://gradschool.umd.edu/faculty-and-staff/course-related-policies>

Please familiarize yourself with these policies related to academic integrity, non-discrimination policy, accessibility, absences and accommodations, grading, academic standing, grievance procedures, and other important policies.

Course Website: Copies of the course syllabus, student's grades, and other relevant links and documents will be posted on the course's ELMS/Canvas website. Students can access the site via www.elms.umd.edu. They will need to use their University of Maryland "directory ID" and password.

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. The weekly workload when taking 2 of our DC courses per term is equivalent to the load from 2.5 "normal" 15-week courses - so $2.5/3.0=83\%$ of a full-time load. However, the DC program takes just 1 week off between terms. Students who take 2 courses per quarter in our program complete 8 courses per year. So over the course of a year, taking 2 courses per quarter in our DC program is equivalent to 133% of a "normal" full-time load in the traditional semester-based program ($8/6 = 1.33$).

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 be forced to leave the program 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.

Excused Absences: If you miss any class meetings for any reason, it is your responsibility to work with the instructor to make sure you catch up on the missed material. 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) The program director will also 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. When classes need to be canceled during the semester, we make every effort to schedule makeup classes.

UMD Counseling Center: Sometimes students experience academic, personal and/or emotional distress. The UMD Counseling Center in Shoemaker Hall provides free, comprehensive, and confidential counseling / mental health services that promote personal, social, and academic success. All Counseling Center services are completely free for enrolled students. Proactively explore the range of services available at the Counseling Center, including the Counseling Service and Accessibility and Disability Service described at <http://www.counseling.umd.edu/>

Graduate Academic Counselor: The UMD Graduate School also has an academic counselor available to support students who are having difficulty navigating mental health resources on campus, are considering a leave of absence and/or need assistance finding mental health care off-campus. The Graduate Academic Counselor also facilitates bi-weekly Graduate Student Circle Sessions which provide an opportunity to learn about resources and connect with other graduate students. Students can learn more about the Graduate Academic Counselor by going to: <https://gradschool.umd.edu/gradcounselor>

Course Evaluations: Near the end of the term, you will receive an email inviting you to submit a voluntary and anonymous course evaluation. Your feedback on courses will be very helpful in improving the quality of instruction in our program.

Building Access: There is a smartphone app that can be used to enter our building after normal business hours. The program coordinator will provide information about this. We will also provide information about the code for entering the front door of our suite. Please make sure you are receiving the ELMS-Announcements that we send out to the program about these and other important matters.

COVID Policies: Up-to date information about UMD COVID-19 policies and guidance are posted at

<https://umd.edu/4Maryland>

Given the evolving nature of the pandemic, the guidance and policies are subject to change. The plans are always coordinated with state and county health officials, with additional guidance provided by the University System of Maryland. The focus will always be on the health and well-being of our entire campus community.

We strongly urge all students, staff, and faculty to read announcements they receive about COVID-related guidance and policy, and to stay familiar with the information. We thank you all for your individual efforts to help protect the collective health of our entire community.