

# Economics 112, Financial Markets and Institutions

Fall 2017

Professor Martin Schneider

## Course Syllabus

### Objectives

This class is about recent developments in the U.S. financial system as well as proposals for how to change it. The course material is relevant for (i) personal financial decisions, such as saving for retirement, (ii) financial decisions by businesses and government, (iii) a host of current public policy issues, in particular preventing and dealing with financial crises.

Most of the course will consist of discussion of recent research papers and policy proposals. A secondary goal of the course is therefore to learn how to read empirical research.

### Class meetings

We meet MW 1.30-3.20pm in Landau 139

### Contact Information

My office hours are Tuesdays from 1.30pm-2.30pm in my office (Landau 340). Outside of these hours, the best way to contact me is via email ([schneidr@stanford.edu](mailto:schneidr@stanford.edu)).

### TA

The TA for the class is Pavel Krivenko ([pavel.krivenko@gmail.com](mailto:pavel.krivenko@gmail.com)) Section times and office hours are TBA. The purpose of section is to review material from class and help you with questions about the readings.

## Organization of the class

Lectures provide facts about financial markets and institutions and introduce economic models used to think about those facts. Those models are the background for the empirical analysis in the research papers.

For most classes, there is assigned reading; often this is a research paper and sometimes it is a shorter policy paper or a blog post. One week in advance there will be a set of questions about the paper to guide your reading; we will then go over the questions in class. You should be prepared to answer any of the questions.

## Grades

Class participation counts for 50% of the grade. To make sure everyone gets a chance to participate, I may cold call as we go over the questions. If you cannot attend class or do not want to be called on in a given class, please send me an email beforehand. This option is supposed to be insurance for exceptional circumstances – using it too often will negatively affect your grade.

There will be a take home final exam that counts for the other 50% of the grade. The final will consist of essay questions – you may be asked to assess policy proposals or discuss the relevance of some economic mechanism. The final will be handed out December 6 and is due December 15.

## Class schedule with links to readings

1. Introduction, [Mon Sep 25](#)
2. Risk and asset valuation (with emphasis on defaultable debt)
  - a. Asset pricing theory & facts, [Wed Sep 27](#)
  - b. [Risk premia on defaultable bonds](#), part 1, [Mon Oct 2](#)
  - c. More theory: valuing the option to default, [Wed Oct 4](#)
  - d. Distinguishing cash flow risk & risk compensation, [Mon Oct 9](#)
  - e. [Risk premia on defaultable bonds](#), part 2, [Wed Oct 11](#)

- f. [Investor experience & portfolio choice](#), Mon Oct 16
- 3. Contract design, borrowing & investment (with emphasis on housing finance)
  - a. Theory on financial innovation & risk sharing [Wed Oct 18](#)
  - b. [Who chooses complex mortgages?](#), Mon 23
  - c. The next innovation? [Shared equity mortgages?](#), [Wed Oct 25](#)
- 4. Securitization & credit ratings
  - a. [Basic tradeoffs \(banks vs market\) & history](#) [Mon Oct 30](#) & [Wed Nov 1](#)
  - b. [What do credit ratings measure?](#), [Mon Nov 7](#)
  - c. [Ratings bias & its price effect](#), [Mon Nov 9](#)
- 5. Credit default swaps
  - a. Theory & [use of CDS by nonfinancial corporations](#), [Mon Nov 13](#)
  - b. [Counterparty risk](#) & policy issues, [Mon Nov 27](#)
- 6. Wholesale funding, payments & monetary policy
  - a. [Repo market mechanics](#) & [repo runs](#), [Wed Nov 29](#)
  - b. Financial markets & monetary policy, [Mon Dec 4](#)
- 7. Recap, [Wed Dec 6](#)