Financial Economics

Spring 2025
Master in Economics
Washington University in St. Louis

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Time	Mondays 4:00-6:50 pm
Venue	Siegle 204
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Course description: This course provides an introduction to financial economics. We start with the basic macro-finance frameworks and follow up with special topics such as bank runs, financial crisis, and liquidity.

Materials: A textbook reference is Recursive Macroeconomic Theory by Ljungqvist and Sargent (chapter numbers refer to the 4th edition). We will also use additional papers or lecture notes for the second part of the course. Course announcements will be posted on Canvas. All course materials will be posted on Canvas. Additional reading materials (aside from the textbook) are listed below and are accessible at the library.

Grading: The course evaluation has four components:

1. 10% of the grade consist on class participation. Hence, attendance and participation is encouraged. Attending a class without participating won't give full credit.
2. 30% of the grade consist on the problem sets.
3. 60% of the grade consist of the first and second mid-term exams (30% each one).

If you miss a mid-term exam you cannot retake it, and you do need to provide an approved excuse. In this case your mid-term exam grades will be based on your other mid-term grade. If you miss both mid-terms you get 0 points for the midterms portion.

Problem sets: The problem sets are designed to help you prepare for the mid-term exams. You will complete these assignments in groups. During the first week of class, we will form the groups that you will work with throughout the course. Each group can have up to three students.

Schedule:

- **January 13.** Introduction to Macro-Finance. Macro-Finance trends, the global financial crisis, and the COVID crisis.
  - References: Farhi and Gourio (2018); Ebsim, Faria-e Castro, and Kozlowski (2022).
  - Problem set #1 (Macro-Finance data).
- **January 27.** Competitive equilibrium.
  - References: LS Ch. 7.
  - Problem set #2 (competitive equilibrium).
- **February 3.** Complete Markets.
  - References: LS Ch. 8.
  - Problem set #3 (complete markets).
- **February 10.** Incomplete Markets.
  - References: LS Ch. 18.
  - Problem set #4 (incomplete markets).
- **February 17.** Asset pricing.
  - References: LS Ch 13, 14.
- **February 24.** Asset pricing and mid-term review.
  - References: LS Ch 13, 14.
  - Problem set #5 (asset pricing).
- **March 3.** First mid-term exam.
- **March 10:** No classes, spring break.
- **March 17.** Mid-term overview and Compustat.
  - Overview of mid-term exam solution.
  - Practice class: An introduction to Compustat (by Marcos)
  - Problem set #6 (Compustat).
- **March 24.** CAPM model and bank runs.
  - References: Diamond and Dybvig (1983), Kurlat's notes.
- **March 31.** Credit market frictions.
  - Modigliani-Miller
  - Costly state verification, Townsend (1979)

  - Supply of liquidity, Holmström and Tirole (1998)
  - Problem set #7 (credit market frictions).
  - References: Townsend (1979); Holmström and Tirole (1998) and Kurlat's notes.

- **April 7.** Information in Macroeconomics and Finance.
  - The market for lemons, Akerlof (1970)
  - Bayesian updating
  - Learning from prices, Grossman and Stiglitz (1980)
  - Problem set #8 (information in macroeconomics and finance).
  - References: Veldkamp (2011) and Kurlat's notes.

- **April 14.** Search in financial markets, and liquidity in macroeconomics and finance. Mid-term review.
  - References: Duffie, Gârleanu, and Pedersen (2005); Kozlowski (2021); Ebsim, Faria-e Castro, and Kozlowski (2022); Caramp, Kozlowski, and Teeple (2022).

- **April 21.** Second mid-term exam.

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