

BOSTON COLLEGE

Department of Economics

EC 362
Financial Markets
Fall 1997
Prof. Christopher Baum

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Office Hours: F 2-4
& by appt.
Syllabus available on the Web:
<http://fmwww.bc.edu/EC/>

Required texts:

- (1) Dubofsky, *Options and Financial Futures: Valuation and Uses*.
- (2) Daily issues, *Wall Street Journal*; a semester's subscription is highly recommended.

Recommended:

StataQuest statistical software for Macintosh or Windows (in bookstore under EC151; also available in OCF)

Requirements:

grades will be based on:
20% Midterm examination
30% Final examination
20% Assignments
30% Empirical research project

Goals and purposes:

This course is designed to familiarize economics majors with the major instruments and institutions of U.S. financial markets, focusing particularly on "derivatives" (futures and options) markets and the underlying "cash" markets for Treasury securities, equities, and foreign exchange. There is no specific assumption of background beyond microeconomic and macroeconomic theory, statistics, and an understanding of the algebra of present value.

The course will require significant individual research of an empirical nature into an aspect of those markets. EC362 should be viewed as complementary (but not a substitute) to EC361 (Monetary Theory and Policy), EC380 (Capital Theory and Finance) and EC395 (Real Estate Finance). Prerequisites include completion of intermediate theory (EC201,202, or 401,402), and statistics (EC151). As empirical research is a sizable element of the course, econometrics (EC228, EC328 or EC428) would be helpful but is not required. Many high-quality research papers have been written with elementary statistical techniques.

Policy statement:

Absolutely no makeup examinations. Assignments – especially the term project – will not be accepted after their announced due dates. It is your responsibility to be familiar with the College’s policy on academic integrity and intellectual honesty, especially as it applies to the preparation of research papers.

Empirical Research Project

The term paper will be an empirical research paper, in which you research a topic of interest using data from the financial markets which you gather and manipulate. I will try to provide some suggested topics, and will expect you to discuss your topics with me prior to doing the major work on the paper. This is to be an analytical paper, rather than purely library research, which must make use of appropriate empirical techniques to study some relevant data on the topic. I cannot stress strongly enough that papers which do not contain some first-hand analysis of data are not acceptable, and will not lead to an acceptable grade in the course. A good model for such a paper can be found in any of the economics or finance journals which publish applied work.

You may use any set of research tools you choose for the paper; many students have used a spreadsheet such as Excel to produce tables, compute statistical results, and produce graphs. This year, we are instituting use of a very intuitive, easy-to-use statistical package, *StataQuest*, in economics statistics courses, and you may find that this package is more appropriate than Excel, StatView, or DataDesk. Copies are available at relatively low cost in the bookstore, and it also should be available (with some level of support) in the OCF. If you have familiarity with other computer programs, feel free to use them.

Warning: most of the data you might need for a project in this area will have to be collected and input “by hand” from the *Wall Street Journal* or industry yearbooks. This will involve a considerable amount of time and effort; budget your time accordingly. Please note that if you do not have a clear and acceptable proposal for this research project by the date noted below, it is very unlikely that you will meet the deadline for paper completion. That deadline is firm, and papers handed in after that deadline are will be graded subject to a sizable discount for tardiness. Take the proposal deadline seriously! In the past, those students who have not had a well-formed concept at the time of the proposal have had considerable difficulty completing a quality project.

The class will meet for 25 lectures and one midterm examination. The final examination will be comprehensive. Tentative topics are given below. You are expected to have prepared for each lecture prior to the class meeting.

TENTATIVE OUTLINE

| <i>lectures</i> | <i>dates</i> | <i>Chapter</i> | <i>Topics</i> |
|-----------------|----------------|----------------|---|
| 1 | 3 Sep | 1 | Introduction |
| 2-3 | 8, 10 Sep | 11 | Introduction to Futures |
| 4-6 | 15-22 Sep | 12 | Pricing Theory |
| 7-8 | 24, 29 Sep, | 13 | Hedging |
| 9-10 | 1, 6 Oct | 14 | Stock Index Futures |
| 11-12 | 8, 15 Oct | 15 | Debt Instruments |
| | 20 Oct | | <i>MIDTERM EXAMINATION</i> (ch. 1, 11-15) |
| 13-14 | 22, 27 Oct | 16 | Short-term Interest rate futures |
| | 27 Oct | | <i>RESEARCH PROJECT PROPOSAL</i> due |
| 15-16 | 29 Oct, 3 Nov | 17 | Treasury bond/note futures |
| 17-18 | 5, 10 Nov | 18 | Foreign exchange futures |
| 19-20 | 12, 17 Nov | 2 | Introduction to Options |
| 21-22 | 19, 24 Nov | 3-5 | Strategies, Arbitrage, Put-call parity |
| 23-25 | 1, 3, 8 Dec | 6-7 | Option pricing: binomial, Black-Scholes |
| | 15 Dec 9:00 AM | | <i>FINAL EXAMINATION</i> |
| | 15 Dec 5:00 PM | | RESEARCH PROJECTS DUE, C-136 |