Course description

The topic of this half of the course is asset market frictions. It is an introduction to costly asset trade with applications to monetary economics and finance. We will cover equilibrium asset pricing with heterogeneous agents, segmented markets and endogenous time-varying risk premia.

This syllabus covers the second half of the course only. Laura Veldkamp has a separate syllabus for the first half.

Prerequisites

You are expected to have already taken the first year PhD sequences in micro and macroeconomics.

Course material

There is no required text, but two books that you might find useful are:

   A standard graduate text on theoretical and empirical asset pricing.

   More of a macro perspective, now a bit dated. But contains a hard-to-find overview of material on nominal asset pricing omitted in most texts.

This syllabus contains links to required and supplementary readings. In order to get the most out of the class, you should at least skim the papers listed as “key readings” before class. The other papers listed give background or extensions or further empirical evidence. Many of these would be good candidates for referee reports or presentation (as discussed below).

Lecture notes and slides will be on my personal webpage as we go along.
Deliverables and grades

The grade in this class will be based on:

1. Problem sets 30%
   There will be two problem sets handed out over the course that extend and/or review papers we have discussed in class.

2. Referee report 30%
   Choose in consultation with me an appropriate paper on which to write a professional 2-3 page referee report.

3. Conference presentation 30% and discussion 10%
   We will run a mock conference session with papers and discussants. In consultation with me, you choose an appropriate paper on which to make a 20 minute presentation suitable for a conference. Acting as if you were the paper’s author, your presentation should state the paper’s question clearly, outline the methodology and the paper’s results. There will also be a discussant for each presentation who will provide a more critical perspective.

Outline and Calendar [Draft]

Session 1 (March 24)


Read before class:

1. Friedman (1968): The role of monetary policy. AER.

Cash-in-advance models:


Evidence:

6. Cochrane (1989): The return of the liquidity effect. JBES.
Session 2 (March 31)

*Endogenous asset market segmentation: closed economies.* Fixed costs and asset market participation. Why segmentation gives a liquidity effect. Implications for the term structure of interest rates. High vs. low inflation.

Key reading:


Supplementary reading and more background:


Session 3 (April 7)


Key readings:

2. Alvarez, Atkeson and Kehoe (2007): *If exchange rates are random walks, then almost everything we say about monetary policy is wrong.* AER.

Background on forward premium anomaly:


Time permitting we may also discuss:

5. Lustig and Verdelhan (2006): *Investing in foreign currency is like betting on your intertemporal marginal rate of substitution.* JEEA.
Session 4 (April 14)


Key readings:


Background reading:

4. Dotsey, King and Wolman (1999): *State-dependent pricing and the general equilibrium dynamics of money and output.* QJE.

Due at the start of the class: problem set #1.

Session 5 (April 21)


Key readings:


Textbook version:


Extensions and microfoundations. We probably won’t have time to say much about these, but they too would be good choices for a referee report or presentation:


Session 6 (April 28)


Key reading:

1. Constantinides and Duffie (1996): Asset pricing with heterogeneous consumers. JPE.

Textbook version:


Antecedents:

3. Mankiw (1986): The equity premium and the concentration of aggregate shocks. JFE.


Evidence:


Related ideas. Almost certainly we won’t have enough time to discuss these, but they too would be good choices for a referee report or presentation:


10. Storesletten, Telmer and Yaron (2004): *Cyclical dynamics in idiosyncratic labor market risk*. JPE.

*Limits-of-arbitrage in general equilibrium* (time permitting).


**Background reading:**


**Evidence:**


**Session 7 (May 5)**

*Conference presentations*: 20-minute conference presentation and 5-minute discussion.

*Due Monday May 12*: problem set #2 and referee report.