



B.E. International Program

Faculty of Economics, Thammasat University



Course Outline

EE 431 Economics of financial markets and financial institutions

Semester 1/2017 (August 15 – December 9, 2017)

1. Logistic information

Instructor's Name: Kittichai Saelee
Date and Time : Tuesday and Thursday, 8.00 – 9.30 AM.
Class venue: **Room 304** , Economics Faculty Building
Office hours: Room 516, TUE: 2 pm – 4 pm, or by appointment
Email: [kittichai_lee\[at\]econ.tu.ac.th](mailto:kittichai_lee[at]econ.tu.ac.th)

2. Course description and Prerequisite:

Course description:

Money and capital markets at the micro level; Financial assets; financial risks and financial risks bearing; Theory of equilibrium pricing of financial assets; the CAPM and APT models; Interest rate structure; bond and equity instruments; Financial derivatives; Asymmetric information in financial market; The study of financial institutions with the emphases on theories regarding the roles and functions of commercial banks; Risk management of financial institutions; Monitoring and controlling of financial institutions; The deposit insurance system and financial institution business from the perspective of industrial economics.

Prerequisite: *EE311*

3. Course Objectives:

- 3.1) To provide students with understanding of financial asset characteristics; risk, return and liquidity
- 3.2) To provide students with understanding of decision process for investment in financial assets at microeconomic level, where investors seek to maximize

their expected utility under constraint (combination of risk and returns available in the financial market

- 3.3) To provide students with understanding of debt market and interest rate at microeconomic level.
- 3.4) To provide students with understanding of diversification, degree of risk aversion, risk premium, which are important determinants of the equilibrium price of financial assets in the financial market.
- 3.5) To provide students with understanding of asymmetric information problem in the financial market and the role of financial intermediaries
- 3.6) To provide students with understanding of risk management of financial institutions
- 3.7) To provide students of understanding of banking industry from the aspect of industrial organization, and the role played by regulation
- 3.8) To understand the cause and consequence of financial crisis

4. Teaching Materials and Resources

Required Text:

1. (DD) Jean-Pierre Danthine (Author), John B. Donaldson (Author) *Intermediate Financial Theory, Third Edition (Academic Press Advanced Finance) 3rd Edition*
2. (MF) Mishkin Frederic "The economics of money, banking and financial institutions" Person series
3. (PS) Peter D Spencer, *The Structure and Regulation of Financial Market (Oxford University Press, 2000)*
4. (CW) Copeland, Thomas E. and J. Fred Weston, *Financial Theory and Corporate Policy, 4th edition, (Addison-Wesley, 2005)*
5. (KM) Kent Matthews and John Thompson, *The Economics of Banking, John Wiley & Sons, LTD, 2005.*

Supplement readings:

1. Diamond Douglas (2007), *Bank and Liquidity Creation: A Simple Exposition of the Diamond-Dybvig Model, Federal Reserve Bank of Richmond Economic Quarterly.*
2. Diamond Douglas (1996), "Financial Intermediation and Delegated Monitoring: A Simple Example, Federal Reserve Bank of Richmond Economic Quarterly.
3. Jean Tirole "Corporate finance" Princeton university press
4. Frexias and Rochet "microeconomics of banking"

Handouts or related materials (if any) will be uploaded on *BE moodle* at least two days before each lecture.

Warning: This is an advanced level course in the field of monetary economics. It requires you deep analytical thinking skill. ***In some parts, your previous training in mathematics and statistics are also required.*** Be prepared! While class attendance is not required in this course, I find it is incredible that you would follow all the materials without attending.

5. Course evaluations:

- Homework: 10%
- Midterm exam: 40% (October, 3rd 2017; 8.00 am – 10.00 am)
- Final exam: 50% (December, 15th 2017; 9.00am – 12.00pm)

Note: No make-up exam will be given to both midterm and final exam.

6. Important dates:

- **Midterm exam:** Oct, 3rd 2017
- **Drop period:** Oct, 18th – 24th, 2017
- **Final exam:** Dec, 15th 2017; no make-up given

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7. Topics:

0. Logistic information and Overview of financial system (2 lectures; Mishkin Ch. 1-Ch.3)

- a. Logistic information + What do we study in this course? (Aug, 15)
- b. Overview on the structure of financial system (Aug,17)

=== Assignment 0 given on Aug 17th due on Aug 24th at the BE office (before 3 pm.) ===

- *Getting familiar with database / CEIC / Thomson Reuter / FRED (grade will not be counted)*

I. Theory of portfolio selection (4 lectures, DD Ch.3 – Ch.5)

- a. Understanding risk and return on asset (Aug, 22)
- b. Decision under uncertainty (Aug, 24)
- c. Traditional portfolio theory (Aug 29, Aug 31)

=== Assignment 1 given on Aug, 31st due on Sept, 7th at the BE office (before 3 pm.) ===

II. Principle of asset valuation (2 lectures)

- a. Principle of valuation: (Sept, 5 and 7)
- b. Valuation of riskless / risky cash flow
- c. Subjective Discount rate v.s. Subjective price
- d. Market discount rate v.s. Market price
- e. Equivalent assets and pricing of exotic assets

=== Assignment 2 given on Sept,7 due on Sept, 14th at the BE office (before 3 pm) ===

III. Bond market (6 lectures)

- a. Bond yield and Bond price (Sept, 12/14; Mishkin Ch.4)
- b. Bond yield, rate of return and interest rate risk (Sept, 19/21; Mishkin Ch.4)

=== Assignment 3 given on Sept, 21 due on Sept 28 at the BE office (before 3 pm) ===

- c. Loanable-fund framework model (Sept 26/28; Mishkin Ch.5)

==== midterm exam 40 points (Oct, 3rd, 08.00 am - 10.00 am) =====

IV. Bond market (4 lectures)

- a. Risk structure of interest rate (Oct, 10; Mishkin Ch.6)
- b. Term structure of interest rate (Oct, 12/17; Mishkin Ch.6)
- c. Information content in financial data (Oct, 19; Mishkin Ch.6)

=== Assignment 4 given on Oct 19 and due on Oct 31 at the BE office (before 3 pm.) ===

V. Capital market (4 lectures)

- a. Stock valuation (Oct 31 / Nov 2; Mishkin Ch.7)
- b. Efficient market hypothesis (Nov 7; Mishkin Ch.7)
- c. Anomalies in the stock market (Nov 9; Mishkin Ch.7)

=== Assignment 5 given on Nov 9 and due on Nov. 16 at the BE office (before 3 pm.) ===

VI. Theory of financial contract (3 lectures)

- a. Stylized-facts on financial/Capital structure around the world: where we are headed (Nov. 14; Mishkin Ch. 8)
- b. Corporate finance approach to the stylized facts (Nov. 16)
- c. Asymmetric information to the stylized facts (Nov 21)

=== Assignment 6 given on Nov 21 and due on Nov. 28 at the BE office (before 3 pm.) ===

VII. Theory of financial intermediation (4 lectures)

- a. Banks and financial intermediation: (KM: ch. 1 - ch. 5) (Nov. 23)
- b. Structure of banking system and Bank management (Nov. 28; Mishkin Ch.9)
- c. Financial stability *and* regulation (Nov. 30 and Dec. 7; Mishkin Ch. 10)

=== No assignment ===

=== Final exam 50 points (Dec 15th; 9.00 am - 12.00 pm) ===

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