

Public Policy 741

Principles of Finance and Global Financial Markets

Josh Hausman

Course Information and Procedures

Location and time

Class meets Monday and Wednesday 2:30-4:00 in 1220 Weill.

Description

Finance is fundamental to many public policy questions. When the financial sector works well, it transfers resources from savers to borrowers, allowing individuals to save and businesses to invest. When the financial sector works badly, resources are misallocated and financial crises threaten the entire economy. This course provides an overview of financial markets and institutions, and then considers the causes, consequences, and possibly policy responses to financial crises.

Course requirements

There will be 2 problem sets, a short (5 page) paper, a midterm on 1/31, a second midterm on 3/7 and a final on April 23rd, 1:30pm-3:30pm. **NOTE: THE FINAL WILL NOT BE RESCHEDULED** (except for medical reasons). **IF YOU CANNOT MAKE THE FINAL EXAM DATE, YOU SHOULD NOT TAKE THIS CLASS.**

Grades will be weighted as follows:

- Problem sets and class participation: 10%
- Short paper: 30%
- Midterms: 30%
- Final: 30%

Contact information and office hours

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Office hours: Mondays, 12:30-2:30pm in Weill 3309.

How to do well in this course

This course's combination of economics and real-world applications makes it both challenging and rewarding. To do well in the course, you will need to master some basic economic theory underlying the operation of financial markets and institutions. The problem sets are designed to help you do this. You will also need to learn a substantial amount about the (mostly recent)

history of financial crises. Much of class time will be spent on this, but it will also be essential that you devote significant time to the readings. In number of pages, the reading list is light. Rarely are more than 60 pages assigned in a week. But I expect that you will come to class having read every page carefully. When parts of readings were not critical, I deliberately assigned only excerpts.

Ford School Inclusivity Statement

Members of the Ford School community represent a rich variety of backgrounds and perspectives. We are committed to providing an atmosphere for learning that respects diversity. While working together to build this community we ask all members to:

- share their unique experiences, values and beliefs
- be open to the views of others
- honor the uniqueness of their colleagues
- appreciate the opportunity that we have to learn from each other in this community
- value one another's opinions and communicate in a respectful manner
- keep confidential discussions that the community has of a personal (or professional) nature
- use this opportunity together to discuss ways in which we can create an inclusive environment in Ford classes and across the UM community

Students with Disabilities

If you believe you need an accommodation for a disability, please let me know at your earliest convenience. Some aspects of this course may be modified to facilitate your participation and progress. As soon as you make me aware of your needs, I can work with the Office of Services for Students with Disabilities to help determine appropriate accommodations. I will treat any information you provide as private and confidential.

Student Mental Health and Wellbeing

The University of Michigan is committed to advancing the mental health and wellbeing of its students. We acknowledge that a variety of issues, such as strained relationships, increased anxiety, alcohol/drug problems, and depression, directly impacts students' academic performance. If you or someone you know is feeling overwhelmed, depressed, and/or in need of support, services are available. For help, contact Counseling and Psychological Services (CAPS) and/or University Health Service (UHS). For a listing of other mental health resources available on and off campus, visit: <http://umich.edu/~mhealth/>.

Ford School Academic Expectations: I expect all students to review and abide by the Ford School academic expectations given here, <http://fordschool.umich.edu/academics/expectations>. I am happy to discuss any questions you may have.

Reading List

Required books:

Mishkin, Frederic S. and Stanley G. Eakins. *Financial Markets and Institutions*, Eighth Edition. (Prentice Hall, 2015). Feel free to purchase the prior (7th) edition instead.

Mian, Atif and Amir Sufi. *House of Debt: How They (and You) Caused the Great Recession, and How We Can Prevent It from Happening Again*. (University of Chicago, 2014).

Note: Other than these required books, all readings will be available online (if a link is provided in the syllabus) or posted on Canvas. In addition to the required readings listed below, I will often post optional readings for those who wish to pursue a topic further.

News: One reason to study finance is to better understand current events and policy discussions. Thus I will frequently reference financial news in class, and while not required, I urge students to follow the financial news. Three standard sources are the *Wall Street Journal*, the *Financial Times*, and the *Economist*. Each offers discounted subscriptions for students (<https://education.wsj.com/students/>, https://sub.ft.com/spa_stu/, <https://www.economist.com/subscribe>).

I. Financial markets and institutions

1/3: Introductory meeting

- Mishkin and Eakins, chapter 1.

1/8: Overview of the financial system

- Mishkin and Eakins, chapter 2.

1/10: Introduction to interest rates

- Mishkin and Eakins, chapter 3.

1/17: Why do interest rates change? 1st PROBLEM SET HANDED OUT.

- Mishkin and Eakins, chapter 4.

1/22: Interest rates, risk, and the term structure

- Mishkin and Eakins, chapter 5.

1/24: The foreign exchange market. 1st PROBLEM SET DUE.

- Mishkin and Eakins, chapter 15 (including the appendix on the interest parity condition).

1/29: Special guest lecture by Professor Kathryn Dominguez

- Readings to be announced

1/31: First Midterm

2/5: Financial institutions.

- Mishkin and Eakins, chapter 7.

2/7: Central banks and the Fed

- Mishkin and Eakins, chapter 9.

2/12: Monetary policy

- Mishkin and Eakins, chapter 10.

2/14: Financial market efficiency, expectations, and the stock market. 2nd PROBLEM SET HANDED OUT.

- Mishkin and Eakins, chapter 6.
- Keynes, John Maynard. *The General Theory of Employment, Interest, and Money*. (Harcourt, Brace, and World, 1936). Chapter 12, pp. 147-164.

2/19: Consumer finance and consumer financial protection.

- John Y. Campbell, Howell E. Jackson, Brigitte C. Madrian, and Peter Tufano. “Consumer Financial Protection,” *Journal of Economic Perspectives*, 25 (Winter 2011): pp. 91-113.

2/21: The mortgage market and mortgage debt. 2nd PROBLEM SET DUE.

- Mishkin and Eakins, chapter 14.
- Mian and Sufi, chapters 1 and 2 (pp. 1-30).

3/5: Banks

- Mishkin and Eakins, chapter 17.

3/7: Second Midterm

II. Causes and consequences of financial crises

3/12: Introduction to financial crises. PAPER TOPICS HANDED OUT.

- Mishkin and Eakins, chapter 8.

3/14: The 2008 crisis

- *Economic Report of the President*, 2010, Chapter 2, pp. 39-62 only (Washington, DC: Government Printing Office, 2010).

3/19: Contagion

- *Economic Report of the President*, 2010, Chapter 6, pp. 159-180 (Washington, DC: Government Printing Office, 2010).

3/21: The role of debt

- Mian and Sufi, chapters 3-5 (pp. 31-71).

3/26: Credit, debt, and bubbles

- Mian and Sufi, chapters 6-8 (pp. 75-116).

3/28: Short and long-run effects of financial crises

- Christina D. Romer and David H. Romer. "New Evidence on the Aftermath of Financial Crises in Advanced Countries." *American Economic Review*, 107:10 (October 2017), pp. 3072-3118.

III. Policy responses to financial crises and regulation of the financial sector

4/2: Rescuing the financial sector

- Mian and Sufi, chapter 9 (pp. 119-134).
- Charles W. Calomiris and Urooj Khan, "An Assessment of TARP Assistance to Financial Institutions," *Journal of Economic Perspectives*, 29 (Spring 2015): pp. 53-80.

4/4: Debt relief and macroeconomic policy

- Mian and Sufi, chapters 10 and 11 (pp. 135-166).

4/9: Financial regulation I

- Mishkin and Eakins, chapter 18.

4/11: Financial regulation II

- Samuel G. Hanson, Anil K. Kashyap, and Jeremy C. Stein, "A Macroprudential Approach to Financial Regulation." *Journal of Economic Perspectives*, 25 (Winter 2011): pp. 3-28.

4/16: Review. PAPER DUE.

4/23: 1:30pm-3:30pm: FINAL EXAM.