RISK AND LIQUIDITY IN FINANCIAL MARKETS

ECON 4544

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ESCUELA DE VERANO 2016

Salón: ML 514
Fechas: 11 de julio al 23 de julio (incluyendo sábado 23 de julio)
Horario: 07:00 a 10:00 AM*
Idioma: Ingles
*La clase del día miércoles 13 de julio será de 5:00 pm a 8:00 pm

Programa sujeto a cambios

Part I: OTC markets

Traditional Walrasian modeling of financial markets takes the view that fragmentation does not matter: it analyzes trading "as if" it were happening in a centralized marketplace in which a fictitious auctioneer provides all transaction services, instantly and at not cost. The search-and-matching approach runs counter to this view. It builds on the premise that trading occurs more slowly than commonly assumed, within many subgroups of investors exchanging subsets of tradable assets, and who make decisions based on partial information about aggregate conditions.

Perhaps the clearest example of a fragmented financial market is an over-the-counter (OTC) market such as the corporate bond market or markets for financial derivatives such as Credit Default Swaps, where investors have to contact each other by phone to bargain over the terms of trades. But even relatively centralized markets (e.g. electronic trading platforms such as Island) are fragmented because they do not simultaneously involve all potential asset holders. Finally, a commonly held view is that during financial disruptions, asset markets become more fragmented: because intermediaries have a harder time accessing the capital that would allow them to participate actively, outside investors find it more difficult to buy and sell assets.
In this class, we will cover recent advances in modeling fragmented financial market using search-and-matching techniques.

• Class 1: Foundations.
Poisson processes continuous time dynamic programming. Nash and Rubinstein [1982] bargaining.

• Class 2: Centralized and semi-centralized OTC markets: Duffie, Gˆarleanu, and Pedersen [2005], Lagos and Rocheteau [2009], Gˆarleanu [2009].

• Class 3: Partially centralized markets with divisible assets.

• Class 4: Directed search and efficiency in OTC markets: Burdett et al. [2001], Lester et al. [2015], Hosios [1990].

• Class 5: Liquidity Provision in OTC markets: Weill [2007], Lagos, Rocheteau, and Weill [2011], and Biais, Hombert, and Weill [2010].

• Equilibrium in fully decentralized markets: Hugonnier, Lester, and Weill [2015].

Part II: Asset Pricing

This class focuses on the economic foundations of asset pricing. After developing and studying the details of investor decision-making under uncertainty, it uses that general framework as a basis for understanding both equilibrium and no-arbitrage theories of securities pricing, including the capital asset pricing model (CAPM), Arrow-Debreu theories, and the arbitrage pricing theory (APT), and the consumption capital asset pricing model (CCAPM).

1. Introduction (Overview of Asset Pricing Theory)
2. Investor decision making under uncertainty (Expected Utility, Risk Aversion)
3. Portfolio Theory (Markowitz)
4. Classic Asset Pricing Theory (CAPM, Arbitrage Pricing)
5. Arrow Debreu Pricing
6. Extensions (to specify: CCAPM, information asymmetry, illiquidity,)

EVALUACIÓN:

Por determinar

CALIFICACIÓN:

Por determinar

FECHA DE RETIRO:

El estudiante podrá retirar el curso, sin devolución, hasta un día hábil antes de la fecha del examen final estipulado por el Profesor. La Universidad no devolverá el dinero cancelado por concepto de matrículas de estos cursos de la Escuela de Verano.

References

Bruno Biais, Johan Hombert, and Pierre-Olivier Weill. Trading and liquidity with imperfect cognition. Working paper, TSE, HEC, UCLA, 2010. 1

Kenneth Burdett, Shouyong Shi, and Randall Wright. Pricing and matching with frictions. Journal of Political Economy, 109:1060–1085, 2001. 1

Darrell Duffie, Nicolae Gˆarleanu, and Lasse H. Pedersen. Over-the-counter markets. Econometrica, 73: 1815–1847, 2005. 1

Nicolae Gˆarleanu. Portfolio choice and pricing in illiquid markets. Journal of Economic Theory, 144:532–564, 2009. 1

Arthur J. Hosios. On the efficiency of matching and related models of search and unemployment. The Review of Economic Studies, 57(1):279–298, 1990. 1

Julien Hugonnier, Benjamin Lester, and Pierre-Olivier Weill. Heterogeneity in decentralized asset markets. Working Paper, SFI, FRB Philadelphia, UCLA, 2015. 1

Ricardo Lagos and Guillaume Rocheteau. Liquidity in asset markets with search frictions. Econometrica, 77:403–426, 2009. 1

Ricardo Lagos, Guillaume Rocheteau, and Pierre-Olivier Weill. Crises and liquidity in otc markets. Journal of Economic Theory, 146:2169–2205, 2011. 1

Benjamin Lester, Guillaume Rocheteau, and Pierre-Olivier Weill. Competing for order flow in otc markets. Journal of Money, Credit and Banking, 47:77–126, 2015. 1

Ariel Rubinstein. Perfect equilibrium in a bargaining model. Econometrica, 50:97–109, 1982. 1
Pierre-Olivier Weill. Leaning against the wind. Review of Economic Studies, 74:1329–1354, 2007. 1