Academic Integrity

All students are expected to know, understand and live up to the standards of academic integrity explained at http://academicintegrity.rutgers.edu/integrity.shtml.

Course Description

This course is the first of the two-course sequence in financial theory for Ph.D. students. The course surveys the fundamental assumptions and the analytical techniques of the modern finance theory. It builds a foundation for the study of higher-level courses in investment theory and corporate finance. Topics covered include capital market equilibrium models, risk analysis using utility theory, state preference theory, portfolio selection, market efficiency, empirical tests of asset pricing models, and introduction to continuous-time finance.

Useful References

Grading Policy

1. Exam I, Monday, March 8, 2010, 27.5%.
2. Exam II, Monday, May 3, 2010, 27.5%.
3. Problem sets, 10%.
4. Term paper with presentation, 25%. Each student will have to submit a term paper by May 3, 2010. The term paper can be a short literature survey of a topic that is of interest to you but is not covered in class, an application of some techniques discussed in the course to a specific area, or an empirical study using current data. After choosing a paper topic, each student should see me to discuss the feasibility of the project. Each student will present his/her research paper in class.
5. Active class participation, 10%.

Topics Covered (tentative, subject to change)

I. Expected Utility Theory and Portfolio Decision Problem

Huang-Litzemberger Chapter 1
Copeland-Weston Chapter 3


II. Generalized Risk and Asset Pricing

Huang-Litzemberger Chapter 2
Copeland-Weston Chapter 3


III. The Mean-Variance Frontier

Huang-Litzemberger Chapter 3
Copeland-Weston Chapter 5
Cochrane Chapter 5


IV. Market Equilibrium and the CAPM

Huang-Litzemberger Chapter 4
Copeland-Weston Chapter 6

V. **Linear Valuation and Factor Models**

Huang-Litzernberger Chapter 4
Copeland-Weston Chapter 6
Cochrane Chapter 9


VI. **State Preference Theory and Equilibrium under Complete Markets**

Huang-Litzernberger Chapter 5
Copeland-Weston Chapter 4


VII. **Empirical Tests of Asset Pricing Models**

Campbell, Lo and MacKinlay, Chapters 5, 6
Huang-Litzernberger Chapter 10
Cochrane Chapters 12, 15
Copeland-Weston Chapter 6


Additional readings

**VIII. Consumption-Based Asset Pricing**

Cochrane Chapter 1
Campbell, Lo and MacKinlay, Chapter 8


Additional readings
Constantinides George M., Habit formation: a resolution of the equity premium puzzle, *Journal of Political Economy* 98, 519-543


IX. **Introduction to Continuous-time Finance and Intertemporal Asset Pricing**


X. **Other Asset Pricing Models**


XI. **Market Efficiency and Market Anomalies**


Additional readings


