This course examines a variety of econometric methods for addressing substantively important questions in financial research. It builds on material presented by Jay Shanken in FIN 532. We will have one class meeting per week. Grading will be flexible – students will have input to determine what type of evaluation procedure will be used. There will be several homework problems assigned throughout the quarter. One of the homework assignments will involve replicating and extending some empirical results that are reported in some of the papers we are going to be discussing in class (or in another paper that we mutually agree on).

Jay discussed material on CAPM tests, Bayesian methods, Mean Reversion, Macroeconomic Variables and Stock Returns, and APT tests. This course will cover related material on interest rates, inflation, time-varying conditional expected returns and volatility, and applications of econometric methods to financial problems (e.g., sample selection bias, GMM estimation, or GARCH models). Emphasis will be on the application of empirical methods to financial data.

The reading assignments will be announced in class and will more or less follow the sequence given below. You will be provided with copies of required readings (shown with an asterisk “*” below). I have included additional references, which are not required, for students who want more information on particular topics. These are not on reserve, but copies of these journals are available in the Management Library. The required text for the course is:


In addition, the following book is recommended for this course:


I will put these books on reserve in the library (if they are available).
There will be several guest lecturers (other faculty members and Ph.D. students). In addition, I will ask each student who is registered for the course to be responsible for leading the discussion of one or more related papers during some part of the course. Of course, I will be available to help you plan your lecture, and I will supplement what you say in class. You should find a topic that interests you and volunteer early.

This course is intended to help you overcome fear of using new methods to analyze problems that interest you. If you have a specific topic or area of interest that is not currently on the outline, I would be glad to consider adding/substituting that material into the course.

**Course Information on the Wide World Web (WWW)**

Most of the materials for this course will be posted on the home page for this course [http://www.ssb.rochester.edu/fac/schwert/f533.htm](http://www.ssb.rochester.edu/fac/schwert/f533.htm). For example, I plan to post copies of the assignments as HTML and/or as Adobe Acrobat PDF files (so they can be viewed and printed from a microcomputer attached to the WWW). In addition, I will use the home page for posting information about future class meetings, etc., so you should check regularly to see if new information is available.

**READINGS**

I. **Time-Varying Expected Returns**

A. **Interest Rates, Inflation, Real Activity and Stock Returns**

*JH*, Chap. 4 (read earlier chapters if you have not taken APS 420).


*JH*, Chap. 14 (very good exposition on GMM).

*Kang, Jangkoo, “Bond Mutual Fund Performance Evaluation: The Numeraire Portfolio Approach,”* working paper, University of Rochester, 1996 (we are going to focus on the GMM estimation).


*CLM*, Chaps. 8, 10, and 11.
I. Time-Varying Expected Returns (cont.)

B. Mean Reversion in Prices and Other Predictable Components of Returns

*CLM, Chaps. 2 and 7.

*JH, Chaps. 15 and 17.


II. Time-Varying Volatility

A. ARCH & GARCH models (and their relatives)

*CLM, Chap. 12.2.

*JH, Chap. 21.


II. Time-Varying Volatility (cont.)

B. Nonparametric and regime-switching models

*CLM, Chap. 12.3.

*JH, Chap. 22.


III. Limited Dependent Variable Models & Sample Selection Bias


III. Limited Dependent Variable Models & Sample Selection Bias (cont.)


IV. Speed of Adjustment to Macroeconomic Information
