

Professor Houthakker
Littauer M-8
Office Hours Mon/Wed 11-12

Teaching Fellows: Niko Canner
Ed Sprokholt
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Harvard University

ECONOMICS 1440
SECURITIES, OPTIONS AND FUTURES
Monday/Wednesday/Friday 12:00-1:00 Science Center A
Fall 1992

Course Outline and Reading List

Items marked * are required reading and (if published) will be on reserve in Lamont and Hilles. Additional readings may be assigned in class. Weeks are approximate and subject to change. Some readings are intended for subsequent weeks.

There will be five problem sets, all of which are required and should be done individually. Each counts for 20 points. The midterm counts for 100 points and the final for 200 points. A paper (worth 100 points) is optional; the subject must be approved beforehand. Students choosing this option will have a total of 500 points instead of the usual 400 points. The course grade is based entirely on the points obtained; any letter grades at midterm are irrelevant to the final grade.

The paper is due on the last day of reading period, and cannot be taken in lieu of other requirements. This course cannot be taken "pass-fail."

Prerequisites: Economics 1125; also Economics 1010a and 1010b (the last two may be taken concurrently).

- WEEK 1 Introduction: Some basic concepts of finance and accounting.
- READ *Houthakker & Williamson, Economics of Financial Markets, (preliminary draft, availability to be announced in class) Ch. 1.
- WEEK 2 Macroeconomics: capital formation and its financing; interest rates; inflation. Intersectoral claims and the Flow of Funds.
- READ Federal Reserve, Flow of Funds (any recent issue).
*Houthakker & Williamson, Economics of Financial Markets, Ch. 2.
- WEEK 3 Types of Securities: equities, preferred shares, bonds, convertible securities; security analysis; investment funds.
- READ Miller & Modigliani, "Dividend Policy, Growth and the Valuation of

Shares," in We & Zakon (eds.) Elements of Investments, (Holt, Rinehart and Winston, 1965), originally in Journal of Business, Oct. 1961.

*Malkiel, A Random Walk Down Wall Street (2nd ed.)
*Houthakker & Williamson, Ch. 3.

WEEK 4-5

Microeconomics: decision-making under uncertainty; expectations and information; efficient markets.

READ

*Sharpe, Ch. 4-6.
*T. Copeland & J. F. Weston, Financial Analysis & Corporate Policy (Addison-Wesley) Ch. *2, *4-6, 8.
*Houthakker & Williamson, Ch. 4.

WEEK 6

Stock Exchanges: specialist and brokers; investors and speculator computerization; price indexes; international aspects.

READ

Stone, One Way for Wall Street, Ch. 1-3, 4.
(no author) Marketplace. A Brief History of the New York Stock Exchange (on reserve in Lamont).
*Houthakker & Williamson, Ch. 5.
Richard R. West & Seha M. Tinic, The Economics of the Stock Market, Ch. 1-4.

WEEK 7-8

Determinants of Equity Prices: profits, asset values, effects of inflation and of interest rates, Tobin's q-theory, new issues, security analysis.

READ

*Sharpe, Ch. 7.
J. H. Lorie, P. Dodd & M. H. Kimpton, The Stock Market: Theories & Evidence, 2nd ed. (Irwin, 1984).
*Houthakker & Williamson, Ch. 6. (Chapter 7 is optional.)
M. Jensen, "Tests of Capital Markets Theory..." in J. C. Bicksler (ed.) Handbook of Financial Economics.

MIDTERM EXAM (tentatively scheduled for November 13)

WEEK 9

Options: puts, calls & warrants; valuation of options; options on physicals vs. options on futures.

READ

*Sharpe, Ch. 16.
F. Black, "Fact and Fancy in the Use of Options," Financial Analysts Journal, July-Aug. 1975.

*Houthakker & Williamson, Ch. 8.
S. C. Blank, C. A. Carter & B. H. Schmiesing, Futures & Options Markets, (Prentice Hall 1991) Parts I & V.

- WEEK 10 Futures Markets: commodity inventories; hedging, speculation and arbitrage; straddles; financial futures; organization of futures exchanges.
- READ Houthakker, "The Scope and Limits of Futures Trading," in Abramowitz (ed.) The Allocation of Economics Resources, (Stanford, 1959).
Z. Bodie & V. J. Rozansky, "Risk & Returns in Commodity Futures," Financial Analysts Journal, May-June 1980.
*Houthakker & Williamson, Ch. 9.
Alan L. Tucker, Financial Futures, Options and Swaps, (West Publishing Company Part II).
- WEEK 11 Determination of Futures Prices: gains and losses of various groups of traders; the theory of normal backwardation and its critics.
- READ *Papers by Houthakker, Rockwell, Rutledge, Samuelson, Cootner & Telser, in A. E. Peck (ed.) Selected Writings on Futures Markets, Vol II, Chicago Board of Trade.
Houthakker, "Normal Backwardation," in Wolfe (ed.) Value Capital and Growth.
Gerald D. Gay & Robert W. Kolb, Interest Rate Futures: Concepts & Issues (Richmond, VA: Robert F. Dame, Inc.)
*Houthakker & Williamson, Ch. 10.
Blank, Carter & Schmiesing, Parts II-IV.
- WEEK 12 Regulation of Security and Commodity Markets: The Securities and Exchange Commission: The Commodity Futures Trading Commission Self-regulation of Exchanges. Discussion of a case study.
- READ *J. Friend, "Economic Foundations of Stock Market Regulation" in J. L. Bicksler (ed.) Handbook of Financial Economics.
Houthakker, "Regulation of Financial and Other Futures Markets," Journal of Finance, May 1982.
Blank, Carter & Schmiesing, Ch. 15.
*Houthakker & Williamson, Ch. 11.
*Stephen Fay, Beyond Greed (on reserve in Lamont & Hilles).