Empirical Finance

Module 3, 2014-2015

Peking University HSBC Business School

1. Teaching Faculty

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2. Aims of the Course

The objective of this course to read and understand scientific papers in empirical asset pricing. This course will focus on selected empirical papers regarding various asset pricing issues as well as basic research methodologies used in empirical asset pricing. Any empirical research should be based on theoretical foundations, so this course will explore selected theoretical models upon which empirical applications are based. The goal of this course is to combine econometrics, micro- and macro-economics, with a view to understanding, interpreting, and predicting movements in asset prices.

3. Assessment

Type	Weighting	Date
Presentation	20%	Week 2-Week 9
Group Assignment 1	15%	Distributed on 11th March 2015 Due on 24th March 2015
Group Assignment 2	15%	Distributed on 25th March 2015 Due on 7th April 2015
Individual Assignment 1	25%	Distributed on 8th April 2015 Due on 24th April 2015
Individual Assignment 2 (Take-Home Final Examination)	25%	Distributed on 29th April 2015 Due on 5th May 2015
Total	100%	

4. Class participation

I expect you to have read the assigned chapters/papers for each session thoroughly before each class. I will evaluate your participation based on the quality of your contribution to class discussions. If the presenter makes a mistake, you should be familiar enough with the papers to identify and help correct the mistake. Thorough preparation and participation in every class is mandatory. ***If you miss more than TWO classes, you will fail in this course (If you are absent once, your final grade will be 90% of your marks, twice 80% and three times 70%).***

5. Course Texts

My recommended text books are as follows. You must buy these two books.

(1) John H. Cochrane, "***Asset Pricing***," Princeton University Press, 2001

(2) John Y. Campbell, Andrew Lo, and A. Craig Mackinlay, "***The Econometrics of Financial Markets***," Princeton University Press, 1997

6. Topics and Reading Lists

(1) In addition to the textbooks, I recommend a number of academic papers including the following survey articles.

- Summers, Lawrence H., "On Economics and Finance," *Journal of Finance* 40: 633-635, July 1985.
- Cochrane, John, 1999, "New Facts in Finance," *Economic Perspectives* XXIII (3) Third quarter (Federal Reserve Bank of Chicago).
- Campbell, John Y., "Asset Pricing at the Millennium," *Journal of Finance* 55: 1515-1567, August 2000.
- Hirshleifer, David, 2001, "Investor Psychology and Asset Pricing," *Journal of Finance*, 56: 1533-1598.

(2) The following shows the list of chapters and papers for each topic to be covered in this course.

1) The Capital Asset Pricing Model

- *Cochrane Ch.12,15
- *Campbell, Lo and MacKinlay, Ch.5
- Fama, Eugene F. and James D. MacBeth, 1973, "Risk, Return, and Equilibrium: Empirical Tests", *Journal of Political Economy*, 81(3), 607-636.
- Gibbons, Michael, Stephen Ross, and Jay Shanken, 1989, "A Test of the Efficiency of a Given Portfolio," *Econometrica* 57: 1121-1152.

- Shanken, Jay, 1992, "On the Estimation of Beta-pricing Models," *Review of Financial Studies*, 5, 1-33.

2) The Cross-Section of Expected Returns and Multifactor Models

- *Cochrane Ch.20.2
- *Jegadeesh, Narasimhan and Sheridan Titman, 2001, "Profitability of Momentum Strategies: An Evaluation of Alternative Explanations," *Journal of Finance*, 56:2, 699-720.
- Fama, Eugene and Kenneth R. French, 1996, "Multifactor Explanations of Asset Pricing Anomalies," *Journal of Finance* 51:55-84.
- *Daniel, Kent, Sheridan Titman and K.C. John Wei, 2001, "Explaining the Cross-Section of Stock Returns in Japan: Factors or Characteristic?" *Journal of Finance*, 56(2), p.743-766.
- Jagannathan, R., Wang, Z., 1996, "The Conditional CAPM and the Cross-Section of Expected Returns," *Journal of Finance*, 51, 3-53.

3) Stock Return Predictability

- *Campbell, Lo and MacKinlay, Chapter2.
- Lewellen, Jonathan, 2004, "Predicting Returns With Financial Ratios," *Journal of Financial Economics,* 74, 209-235.
- Stambaugh, R. F., 1999, "Predictive Regressions," *Journal of Financial Economics,* 54, 375-421.
- *Goyal, Amit and Ivo Welch, 2008, "A Comprehensive Look at the Empirical Performance of Equity Premium Prediction," *Review of Financial Studies,* 21, 1455-1508.
- *Campbell, John Y. and Samuel Thompson, 2008, "Predicting the Equity Premium Out of Sample: Can Anything Beat the Historical Average?" *Review of Financial Studies,* 21, 1509-1531.

4) Asset Prices and the Macroeconomy

- *Cochrane Ch.2 and 8
- *Campbell, Lo and MacKinlay, Chapter 8
- Mehra, Rajnish and Edward C. Prescott, "Equity Premium Puzzle in Retrospect," *Handbook of the Economics of Finance* ed. by G. M. Constantinides, M. Harris and R. Stulz, North Holland, Amsterdam, 2003.
- *Hansen, Lars Peter and Kenneth J. Singleton, 1983, "Stochastic Consumption, Risk Aversion, and the Temporal Behavior of Asset Returns," *The Journal of Political Economy*, 91(2), pp.249-65.
- *Lettau, Martin, and Sydney Ludvigson, 2001, "Resurrecting the (C)CAPM: A Cross-Sectional Test when Risk Premia are Time Varying," *Journal of Political Economy,* 109, 1238-1286.

5) Present Value Relations and Return Decomposition

- *Cochrane, Ch.20.1

- *Campbell, Lo and MacKinlay, Chapter 7
- *Vuolteenaho, Tuomo, 2002, "What Drives Firm-Level Stock Returns?" *Journal of Finance* 57:233-264
- Campbell, John Y. and Tuomo Vuolteenaho, 2004, "Bad Beta, Good Beta," *American Economic Review* 94:1249-1275.

6) Trading and Liquidity

- *Campbell, Lo and MacKinlay, Ch.3
- *Hasbrouck, Joel, 1991, "Measuring the Information Content of Stock Trades," *Journal of Finance,* 66:179-207.
- Gallant, A., P. Rossi, and G. Tauchen, 1992, "Stock Prices and Volume," *Review of Financial Studies,* 5, 199-242.
- Campbell, J. Y., Tarun Ramadorai and Tuomo O. Vuolteenaho, 2005, "Caught on Tape: Institutional Order Flow and Stock Returns," NBER Working Paper #11439.