

IB9RDO Macro Finance

A good understanding of the topics covered and the tools introduced in this module is an important complement to the current offering in our MSc, in particular the asset pricing and portfolio management modules. Most importantly, the topics covered and skills developed with this module are in good demand for those students that aim at a career in asset management, risk management and banking.

Overview:

This module looks at the link between the real economy and financial valuations, known as macro-finance. Students will learn to understand macroeconomic fluctuations and the implications for different asset prices with particular emphasis given to the role of monetary and fiscal policy in determining the macroeconomic environment and asset prices. The course offers an integrated framework to understand the effects of macroeconomic shocks and policies, including their consequences to financial markets. The topics covered will be of particular interest to students pursuing careers in asset management, hedge funds and risk management.

Module Aims:

This module aims to:

- i) Understand real world macroeconomic question using modern macroeconomic tools and frameworks.
- ii) Develop student understanding of how the macroeconomy affects asset prices (including stocks, bonds, currencies), focussing on both short term and long term determinant of asset returns.
- iii) Help students appropriately use the main techniques and methodologies employed in macroeconomic theory. Develop students' ability to exposit and critically appraise modern theoretical models of the determination of the major macroeconomic variables in light of empirical evidence.
- iv) Develop student understanding of the impact of macroeconomic shocks and monetary and fiscal policy on asset prices
- v) Develop student understanding of how portfolio allocations are affected by the evolving macroeconomic environment.

The module will aim to cover the following topics:

1. Facts and methodology. Microfoundations. Two-period model of intertemporal consumption choices. Households intertemporal optimization problem.
2. Present value decomposition, intertemporal Portfolio Choice and Asset Pricing.
3. Consumption-based capital asset pricing model, the equity premium puzzle and possible solutions (habits, long-run risk, heterogeneity in risk preferences)

4. Capital accumulation and macroeconomic fluctuations. The Real business cycle model. Production based asset pricing model, supply factors and their effect on the equity premium
5. Evolving macroeconomic escape and equity returns. Aging population, productivity and other long run determinant of asset returns.
6. Introduction to nominal frictions, inflation and aggregate demand: the New-Keynesian model
7. Monetary policy: objective and transmission. Credibility in monetary policy. Monetary policy institutions. Understanding the drivers of bond returns and their relation to the macroeconomy and monetary policy
8. Consumption and capital accumulation in a small open economy. Current account dynamics and net foreign assets, real exchange rate dynamics in a two-sector open economy
9. The real exchange rate and inflation in a small open economy.
10. Implications for monetary policy. Introduction to household finance, understanding portfolio allocation over the life cycle. Long-run investors, strategic asset allocations and the influence of the macroeconomy

Assessment:

This module will be assessed by a 2 hour exam worth 80%, and an individual assignment for the remaining 20%.