Speculative Markets  
FNCE 206/717  
Summer 2004

Time: M-Th 4:20-5:55  
Location: JMHH F50  
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Course Description: This course is an introduction to the world of derivative securities, and in particular explores the interaction between an elegant mathematical theory and real-world application. Although the theory may appear fairly mathematical and abstract, it has proved to be one of the success stories of modern economics, providing surprisingly accurate predictions. We will develop a clear understanding of, and appreciation for, this theory, while at the same time demonstrating how it is applied in practice. Applications will be through cases, and we will also discuss how to use Bloomberg Machines to value derivatives.

Prerequisites: A first course in Finance (e.g. FNCE 100/601). Statistics and a course providing a reasonable background in calculus.

Readings: The main text for the course is Options, Futures and Other Derivatives, by Hull (5th edition); this is the book favored by Wall Street practitioners. You should purchase this book, which comes together with the solutions manual. There are two bulk packs available from Wharton Reprographics – one has my notes (you should make sure to get this one before the first day of class) and the other has cases and readings. In addition, I highly recommend Infectious Greed by Frank Partnoy, which is a lively account of derivatives in the 1990s.

Grading: Grading will be based on cases (30%), an in-class midterm on July 15 (20%) and a final on August 5 (50%).
Speculative Markets – Topic List

H: refers to Options, Futures and Other Derivatives by Hull (5th Edition)

Session 1 Introduction, Financial Innovation, Form Groups (Bernstein & Miller readings; Sill reading is optional).
Session 2 Futures & Options – Introduction (H Ch 1, §2.1-2.2, 2.4-2.5, 2.7, 2.9-2.10, 7.1-7.9)
Session 4 Qualitative Properties of Option Prices (H 8.1-8.2, 8.4-8.7)
Session 5 Options Trading Strategies (H Ch 9)
Session 6 Binomial Option Pricing (H 10.1-10.4)
Session 7 Continued (H 10.5-10.7, §18.2, pp. 269-70, 402 (skim 403-5), 407-9)
Session 8 Foundations of Binomial Option Pricing (Fed Fund Futures Articles)
Session 9 A Mathematical Model for Security Prices (H 11.1-11.5)
Session 10 Midterm Review
Midterm Exam: July 15 (in class) – covers through session 8
Session 11 Continued (H 11.6-11.7, 12.1-12.4, skim 12.12)
Session 12 The Black-Scholes Model (H 12.5-12.6, 12.8-12.9, 12.11)
Session 15 Value at Risk (H 16.1-16.8, Simons VaR article)
Session 16 Interest Rate Duration, Floaters & Inverse Floaters (H 5.13, pp. 116-117)
Session 17 Swaps, Warrants (6.1, 6.3, pp. 136-7, 12.10)
Session 18 Chrysler Warrants (discussed in class), Options in Corporate Securities (H 26.5)
Session 19 Additional Material (TBA)
Session 20 Exam Review and Conclusion
Final Exam: August 5 (in class) - comprehensive