Duke University
Fuqua School of Business

Professors A. Rampini and S. Viswanathan — Corporate Finance Theory
Finance 553 — Fall 2008

Syllabus

This second year Ph.D. course in the theory of corporate finance provides a rigorous introduction and prepares students for theoretical research in corporate finance.

Topics. The topics include financing with various sources of agency problems such as moral hazard, asymmetric information, limited observability, and limited commitment. The last part of the course considers the macroeconomic implications of corporate finance.

The course is based on journal articles, but you may want to use Tirole, J., 2006, *The Theory of Corporate Finance*, Princeton University Press, Princeton, as a reference book. You may also want to refer to Salanié, B., 2005, *The Economics of Contracts*, MIT Press, Cambridge, or Bolton, P., and M. Dewatripont, 2005, *Introduction to the Theory of Contracts*, MIT Press, Cambridge.

Prerequisites, Requirements, and Miscellanea. No background beyond first year graduate microeconomics is required, although familiarity with contract theory and information economics is useful. Course requirements include problem sets, a paper critique/paper, and a final exam. The course meets on Wednesdays from 8:45am to 11:45am in Seminar Room A (except for the first class). The first class meets on Wednesday, August 27, in Conference Room 5. You can contact us by email at rampini@duke.edu or viswanat@duke.edu or by phone at 919 660-7797 (Rampini) or 919 660-7784 (Viswanathan). There is a course web page with a schedule and additional course information (url http://faculty.fuqua.duke.edu/~rampini/finance553.htm).

1. Moral Hazard

Holmström, B., 1982, Moral hazard in teams, *Bell Journal of Economics* 13, 324-340.

Holmström, B., and P. Milgrom, 1991, Multi-task principal agent analyses: linear contracts, asset ownership, job design, *Journal of Law, Economics, & Organization* 7, 24-52.

Prendergast, C., 2002, The tenuous trade-off between risk and incentives, *Journal of Political Economy* 110, 1071-1102.

2. Auctions and Applications to Corporate Finance

Myerson, R., 1981, Optimal auction design, *Mathematics of Operations Research* 6, 58-73.

Beveniste, L., and P. Spindt, 1989, How investment bankers determine the offer price and allocation of new issues, *Journal of Financial Economics* 24, 343-361.

3. Financing with Incomplete Contracts

Aghion, P., and P. Bolton, 1992, An incomplete contracts approach to financial contracting, *Review of Economic Studies* 59, 473-494.

Hart, O., 1995, *Firms, Contracts and Financial Structure*, Oxford University Press, Oxford.

Kaplan, S., and P. Strömberg, 2003, Financial contracting theory meets the real world: an empirical analysis of venture capital contracts, *Review of Economic Studies* 70, 281-315.

4. Bank Runs and Coordination Problems

Diamond, D., and P. Dybvig, 1983, Bank runs, deposit insurance, and liquidity, *Journal of Political Economy* 91, 401-19.

Morris, S., and H. Shin, 1998, Unique equilibrium in a model of self-fulfilling currency attacks, *American Economic Review* 88, 587-597.

Goldstein, I., and A. Pauzner, 2005, Demand deposit contracts and the probability of bank runs, *Journal of Finance* 60, 1293-1327.

5. Takeovers

Grossman, S., and O. Hart, 1980, Takeover bids, the free-rider problem, and the theory of the corporation, *Bell Journal of Economics* 11, 42-64.

Grossman, S., and O. Hart, 1988, One share/one vote and the market for corporate control, *Journal of Financial Economics* 20, 175-202.

6. Bubbles and Corporate Finance

Rubinstein, A., 1989, The electronic mail game: strategic behavior under almost "common knowledge," *American Economic Review* 79, 385-391.

Abreu, D., and M. Brunnermeier, 2003, Bubbles and crashes, *Econometrica* 71, 173-204.

7. Financing with Costly State Verification

Townsend, R., 1979, Optimal contracts and competitive markets with costly state verification, *Journal of Economic Theory* 21, 417-425.

Gale, D., and M. Hellwig, 1985, Incentive-compatible debt contracts: the one-period problem, *Review of Economic Studies* 52, 647-663.

Diamond, D., 1984, Financial intermediation and delegated monitoring, *Review of Economic Studies* 51, 393-414.

8. Financial Distress

Myers, S., 1977, The determinants of corporate borrowing, *Journal of Financial Economics* 5, 147-175.

Gertner, R., and D. Scharfstein, 1991, A theory of workouts and the effects of reorganization law, *Journal of Finance* 46, 1189-1222.

Bulow, J., and J. Shoven, 1978, The bankruptcy decision, *Bell Journal of Economics* 9, 437-471.

Shleifer, A., and R. Vishny, 1992, Liquidation values and debt capacity: a market equilibrium approach, *Journal of Finance* 47, 1343-66.

9. Multiple Financiers

Bolton, P., and D. Scharfstein, 1996, Optimal debt structure and the number of creditors, *Journal of Political Economy* 104, 1-25.

Berglöf, E., and E.-L. von Thadden, 1994, Short-term versus long-term interests: capital structure with multiple investors, *Quarterly Journal of Economics* 109, 1056-1084.

Berglöf, E., G. Roland, and E.-L. von Thadden, 2007, The design of corporate debt structure and bankruptcy, working paper.

Stulz, R., and H. Johnson, 1985, An analysis of secured debt, *Journal of Financial Economics* 14, 501-521.

10. Dynamics of Financing Constraints

DeMarzo, P., and Y. Sannikov, 2006, Optimal security design and dynamic capital structure in a continuous-time agency model, *Journal of Finance* 61, 2681-2724.

DeMarzo, P., M. Fishman, Z. He, and N. Wang, 2008, Dynamic agency and the q theory of investment, working paper.

Albuquerque, R., and H. Hopenhayn, 2004, Optimal dynamic lending contracts with imperfect enforceability, *Review of Economic Studies* 71, 285-315.

Cooley, T., R. Marimon, and V. Quadrini, 2004, Aggregate consequences of limited contract enforceability, *Journal of Political Economy* 112, 817-847.

Clementi, G. L., and H. Hopenhayn, 2006, A theory of financing constraints and firm dynamics, *Quarterly Journal of Economics* 121, 229-265.

DeMarzo, P. and M. Fishman, 2007a, Agency and optimal investment dynamics, *Review of Financial Studies* 20, 151-188.

DeMarzo, P. and M. Fishman, 2007b, Optimal long-term financial contracting, *Review of Financial Studies* 20, 2079-2128.

Hopenhayn, H., and I. Werning, 2008, Equilibrium default, working paper.

11. Financing Constraints and Business Cycles

Bernanke, B., and M. Gertler, 1989, Agency costs, net worth, and business fluctuations, *American Economic Review* 79, 14-31.

Scheinkman, J., and L. Weiss, 1986, Borrowing constraints and aggregate economic activity, *Econometrica* 54, 23-45.

Carlstrom, C., and T. Fuerst, 1997, Agency costs, net worth, and business fluctuations: a computable general equilibrium analysis, *American Economic Review* 87, 893-910.

12. Collateral and Asset Prices

Kiyotaki, N., and J. Moore, 1997, Credit cycles, *Journal of Political Economy* 105, 211-48.

Kiyotaki, N., 1998, Credit and business cycles, *Japanese Economic Review* 49, 18-35.

Kehoe, T., and D. Levine, 1993, Debt-constrained asset markets, *Review of Economic Studies* 60, 865-888.

Rampini, A., and S. Viswanathan, 2008, Collateral, financial intermediation, and the distribution of debt capacity, working paper.

13. Liquidity and Economic Activity

Holmström, B., and J. Tirole, 1997, Financial intermediation, loanable funds, and the real sector, *Quarterly Journal of Economics* 112, 663-91.

Holmström, B., and J. Tirole, 1998, Private and public supply of liquidity, *Journal of Political Economy* 106, 1-40.