"Inspiration, Creativity, Service"

UNIVERSITY AT ALBANY ♦ SCHOOL OF BUSINESS
Finance 333 Investment Management --- Fall 2004

Professor: **Dr. Christophe Faugère** (pronounce Christoff Fo-jair)
Office: BA 309C, Phone: 442-4973
Office Hours: T, Th: 1 - 3 pm
E-mail: c.faugere@albany.edu

COURSE DESCRIPTION

This course focuses on the pricing and valuation of individual securities and investment portfolios. The coverage in this course can be broken into three major sections. The *first part* examines the structure and operations of the securities markets and the valuation of equity securities. In the *second portion* of the course, we shall develop the fundamental aspects of portfolio theory and management with some discussion of some of the current market anomalies. The *last portion* of this course will deal primarily with derivative securities. Our emphasis in this section will be more on the use and the real life applications of these complex securities as a risk management tool than on their valuation. An integral part of this course is hands on experience in trading various securities and managing a portfolio using a portfolio simulation game. Training in the use of Excel, Research Insight (Standard and Poors' Compustat) and the Internet are essential to achieve our learning objectives.

Prerequisites

FIN 300 and FIN 301

Required Material:

Textbook: Bodie, Kane and Marcus, Essentials of Investments, (2004) McGraw-Hill. Fifth Edition
PowerPoint Lecture Slides: and other materials will be made available on WebCT at http://webct.albany.edu:8900/. The material for a given week will be posted on *Friday* by 5:00pm, unless notified. **Always** check WebCT for *special messages* on *Friday* evenings.
Group subscription to STOCK-TRAK which costs $19.95 per account. STOCK-TRAK is an on-line service that allows us to play a portfolio simulation game.

Strongly Recommended Readings: The Wall Street Journal/Business Week

Grading Policy:

Final Exam	25 points
Midterm Examination	25
1 Spreadsheet Assignment	15
Stock Trak Project Portfolio Simulation part I	15
Stock Trak Project Portfolio Simulation part II	10
Oral presentations, quizzes, and class participation	10

Philosophy:

As a *teacher* I have the following responsibilities:

1. Come prepared to every class.
2. Plan my class so you can accomplish the cognitive objectives listed in the syllabus.
3. Treat you as responsible adults.
4. Realize that it is not necessarily your fault if you don't understand the material.
5. Create a mutually engaging and respectful class environment.

6. Encourage you to **be involved** in class: that is, to be engaged in expressing your viewpoint.

As a *student* you have the following responsibilities:

1. Come prepared to every class.
2. Complete all work on time with proper thought.
3. Behave as responsible adults.
4. Consider that it is not always my fault if you don't understand the material.
5. Be respectful of other people's opinions.
6. Approach the course with a *willingness* to be engaged in dialogs (with the teacher and classmates).

Recommendations on how to study:

For your success in this course (and in your life as an executive), I recommend that you practice the following:

1. Take notes in class on the left hand side of my PowerPoint lecture handouts. Especially when I say or when you feel that I am placing a *special* emphasis on a particular problem or concept. I cannot emphasize enough that part of learning is to *read signals* from the teacher!!! (Everything is *not* on equal footing).
2. After class, spend about 5 minutes to create queue cards summarizing the lecture slides. This will ease the pain of studying for the exams, and help you connect material in your own mind.
3. Spend at least one ½ hour per week, going over the lectures with someone else in the class, and make a point of going over the concepts and translating them into your own words. Within that ½ hours, pick a couple of problems similar to those I will have covered in class and attempt to do them. I will be more than happy to help you with those if you need consultation.

The two minutes paper:

At the end of each **lecture**, and for each member of **a constituted group of 5 people** I require that you spend a couple of minutes answering (**anonymously**) the following questions on a small piece of paper:

1. What concepts or ideas did you find the clearest?
2. What concepts or ideas did you find the least clear for yourself?

The group captain (selected within the group) will be responsible to gather the answers within the group and e-mail me a summary of the responses using the WebCT **e-mail function** by **next day 12:00 noon**. (For Friday's lectures the deadline is **Midnight on Friday**). The group captain will receive **5 extra** points on the spreadsheet assignment for doing that. If the group captain does his/her job well (on time and consistent), he/she'll get 5 additional points for a total of **10 points** for rendering this service all semester long**.**
On the other hand, captain rotation is possible after mid-semester that is, **starting October 18**. New captains will be chosen by the group and must take over during that week! In that case **each** captain will receives **5 extra points** if the job is well attended.

SCHEDULE

We shall proceed according to the following schedule, although it may be necessary from time-to-time to change or skip topics. *There will be no incompletes (grades of "I") given, so it is important that all students remain continuously up-to-date with their work*. Class will be cancelled on the following days: September 6th, 15th and 17th (break), October 8th (out of town conference), November 24th and 26th (break).

WEEK	TOPIC	BOOK READINGS

30-Aug	Course Introduction and Overview	1, 2
6-Sep	Organization of Securities Markets	3
13-Sep	Organization of Securities Markets (cont'd)	3
20-Sep	Valuation of Equity	12
27-Sep	Valuation of Equity (cont'd)	12
4-Oct	Technical Analysis	19, pp. 659 on
Monday 10/4	*DUE: Spreadsheet Application Project #1*	
11-Oct	Financial Statement Analysis	13
18-Oct	Risk and Return part 1	5, 6
Wednesday 10/20	*Midterm Examination*	
25-Oct	Risk and Return part 2	6 cont'd, 7
1-Nov	Market Anomalies	8 and 19
8-Nov	Portfolio Management Strategies part 1	4, 20
Wednesday, 11/10	*DUE: StockTrak Portfolio Simulation Report (Part 1)*	
15-Nov	Portfolio Management Strategies part 2	20 cont'd
22-Nov	Fundamentals of Options	14, 15
29-Nov	Option Strategies	TBA
6-Dec	Review Finals	
Wednesday, 12/8	*DUE: StockTrak Portfolio Simulation Report (Part 2)*	
Finals Week (day TBA)	*Final Examination*	

STOCK TRAK PORTFOLIO SIMULATION GROUP PROJECT

The Stock Trak portfolio simulation game is a very important aspect of this course. It is one assignment that you will undertake within a group. As such, your individual performances as well as the group dynamics are critical to the overall success of your group. Under normal circumstances, all members of a group will receive the same grade.

Important Note. If an individual is identified by the all the other members of the group as non-contributing (hard to get a hold of…hard to get along with…etc.) this person will receive no credit or a zero grade for this segment of the course.

You are requested to register with STOCK-TRAK in order to complete this assignment. The following is the procedure: You will be assigned a group account number through a sign-up sheet in class. Once you have obtained your account number go to the STOCK-TRAK web page at http://www.stocktrak.com/traderules2004.pdf and print out the registration materials/trading rules from the web page. (Following the "Read Rules" link in the left hand column of the home page directs you to the same link.) After having printed out the trading rules, register your assigned account number at the "Open Account" link in the left hand side of the home page. Your accounts will be active on a date TBA with $200,000. The details of the assignment will be communicated to you in due time.

Policies and Procedures:

Missing Exams/Quizzes

No makeup exams or quizzes will be given. It is impossible to make an equivalent exam or quiz without placing the student at either an advantage or disadvantage. If a student misses one exam/quiz **without a legitimate excuse**, s(he) will receive a grade of zero for that exam/quiz. If a student misses one quiz **with a legitimate excuse**, s(he) can apply the best grade on one of the following quizzes (if applicable) to the missed one.

Legitimate reasons	**Due to illness**	**Note from doctor**
	Due to business	**Note from supervisor**
	Unfortunate death in the family	**Note from family member**
	Other	**on a case by case basis**

Please read carefully: I must be informed at least before the exam starts to count as an excused absence. If you cannot reach me, leave a message on my answering machine (indicate the time). Notifying me after this deadline will result in a grade of zero for that exam. Your excuse should be submitted before the semester's end, and must contain a phone number so that your absence can be verified**. Failure to follow the guidelines will mean that you forfeit the excused absence option**.

Professional Ethics

Although I will entrust you to behave ethically, plagiarism or any forms of cheating are prohibited. Individual assignments should be done individually without outside help (which includes past students or solutions). Whenever a group project is assigned, the group alone should do the project. The penalty for such behaviors is an F for the course and referral to the judiciary board.

Professional Behavior

Tardiness: Please arrive on time. If you arrive later than the start of the class, please quietly take a seat nearest the entrance. Please try not to walk in front of the classroom, as this disturbs the flow of the lecture. My **5 minutes policy**: I understand that you may be late for reasons outside your control. On the other hand, students arriving more than 5 minutes late creates great disruption. The 5 minutes policy stipulates that the classroom door will be shut and no students will be allowed in the classroom if *more than* 5 minutes late.

Inattention: Please do not read other books or newspaper or study for other courses during my class. It is not polite. The Buddhists have a saying: "Be here now!" Please join in the individual and group discussions, we're glad you are with us! This will help your mastery of the material.

Projects, Take Home Exams and other Homework Assignments

Each problem or each homework assignment should have the team (or individual) members' names clearly displayed in the *header* of the page. Projects, homework or exams handed in late will be penalized **20% off** per additional day, starting the minute after the stated due time. Assignments due for class are due during the class period. Unless otherwise stated, assignments should be handed in **both** electronic form (diskette) and printed hard copy.

Students are responsible for behaving professionally toward their teams. If problems develop that cannot be resolved even after consultation with the professor, teams may "fire" a member. The dismissed student will receive a grade of 0 on all team assignments.

Course Cognitive/Learning Objectives

(Although unlikely, I may modify these objectives during the semester. Depending on how much time we have left we may also skip some of these objectives. You will be notified in that case.)

Course Introduction and Overview

1. Explain the role of Ethics in personal conduct
2. Explain why Ethics is a necessary component of Financial decisions
3. Describe the different classes of assets
4. Describe the recent history of returns
5. Be able to read stock quotations from the Wall Street Journal

Organization of Securities Markets

1. Describe how stock securities are issued.
2. Identify and describe the function of the various types of markets.
3. Describe the various types of orders and their functions.
4. Be able to compute and use excel to determine margins (calls) needed for buying on margin.
5. Be able to compute and use excel to determine margins (calls) needed for a short sell.

Valuation of Equity

1. Explain why equity is valued using the PV of future dividends and not earnings.
2. Explain the difference between a savings account and a stock.
3. Compute price of stocks using the dividend discount model and Excel.
4. Relate a stocks expected return to its dividend yield and capital gains.
5. Explain the factors that determine the equity premium and compute it.
6. Compute price of stocks that do not pay dividends.
7. Explain the fundamental determinants of the Price/Earnings ratio.
8. Utilize the savings account model to determine the market Price/Earnings ratio
9. Explain how the FED model works and apply it.
10. Understand investment strategies based on other relative valuation ratios (price to book, etc..).
11. Be able to value a Technology stock with no earnings.

Technical Analysis

1. Explain in plain English what technical analysis is.
2. Describe the various techniques: Moving Averages and Stochastic.
3. Utilize MACD and Stochastic using actual stock charts to infer trading strategies.

Financial Statement Analysis

1. Be able to work with cash flow statements, and compute operating cash flows
2. Compute Free Cash Flows to Equity and describe when best used.
3. Know and compute the key ratios that come into play into the Dupont (ROE) decomposition formula and explain their importance and meaning.
4. Know the Dupont (ROE decomposition formula) and be able to use it numerically.
5. Describe and analyze accounting manipulations that are possible and their ethical impact.
6. Use ratio analysis to analyze various industries.
7. Use MS-Excel to do ratio analyses.

Risk and Return parts I and II

4. Explain in plain English what the return on an asset is.

5. Explain in plain English what risk is.
6. Compute risk and return for various investment horizons.
7. Explain what expected return means.
8. Explain the difference between arithmetic and geometric average returns.
9. Explain why holding period return may be misguiding and why compounded return is a better measure.
10. Explain why the dividend reinvestment hypothesis used to compute historical returns can mislead investors.
11. Explain why there is an inverse relationship between risk and expected returns.
12. Explain the role of covariance in reducing the risk of a portfolio.
13. Explain and describe the frontier of efficient portfolios.
14. Differentiate between systematic and un-systematic risk.
15. Explain in plain English what the beta of a stock is.
16. Explain in plain English what the CAPM is.
17. Know the CAPM formula. And compute an expected return based on the formula.
18. Compute the risk premium and explain what the factors are that determine it.
19. Use MS-Excel to generate the CAPM and efficient frontiers.

Efficient Markets and Anomalies

1. Explain what the conditions for an efficient market are.
2. Explain the current theories of why value stocks outperform growth stocks, or the so-called value premium.
3. Describe the small firm effect and January effects.
4. Describe the findings by Jagdeesh and Titman (1993) on reversal of winners and losers.

Portfolio Management Strategies I and II

1. Compute and utilize the various measures of portfolio performance Sharpe, Treynor ratios and Jensen's alpha.
2. Use these measures with Excel.
3. Explain how Sharpe benchmarks are used.
4. Explain what sell-discipline is, and describe the kind of sell-discpline that seem the perform best over time.

Fundamentals of Options and Option Strategies

1. Explain what an option is.
2. Explain what call and put options are.
3. Graph a payoff or profit loss diagram for calls and puts.
4. Explain what factors affect call option prices and how.
5. Apply options to the issue of portfolio insurance
6. Compute payoff tables of combinations of strategies: protective put, covered calls.
7. Use the Black-Sholes formula to price an option.