

DEPARTMENT OF FINANCE  
MCCOMBS SCHOOL OF BUSINESS  
UNIVERSITY OF TEXAS AT AUSTIN

**Finance 367: Investment Management**

*Summer 2008*

*Subject to change*

Unique #: 71505  
Classroom: GSB 2.122  
Meeting time: MTWThF, 1:00pm – 2:30pm

Instructor: Jeremy Page  
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Office Hours: MTWThF 2:30pm-3:30pm and by appointment

Course Description

Finance 367 is a course in investment analysis. It is intended for students who want to become investment professionals, knowledgeable individual investors, or both. The course covers the primary financial securities—bonds, stocks, and derivatives—and methods for combining these underlying assets into a portfolio.

First, we will cover the overall layout of U.S. financial markets and the financial instruments available in these markets. Then we will learn how these financial securities are traded in real markets. After this brief overview, we will review the statistical tools used in finance to think about risk and return, and examine how investors hold securities in portfolios in order to achieve a desired trade-off between return and risk. We will then study the leading asset pricing theories that try to explain the returns on financial securities based on their characteristics and the portfolio decisions of investors. We will conclude the first segment of the course with the topic of market efficiency.

Following our discussion of portfolio and asset pricing theories, we will proceed with the valuation of specific classes of securities, starting with fixed income securities (bonds). Because bonds pay a fixed amount of interest on a set schedule to investors, the valuation and pricing of bonds is primarily an application of the time value of money concept. This concept should be familiar to students satisfying the central prerequisite to this course (FIN 357).

Following our work on fixed income securities, we will study equity securities (stocks). Because stocks represent a residual ownership stake in a company, the cash flows to

stockholders are generally more variable than the cash flows to bondholders. The course will cover various valuation methods for stocks, focusing on dividend growth models but also discussing other valuation techniques.

We will then discuss derivative securities (options and futures). We will analyze the uses of options to construct various payoff schemes and the valuation of options with the Black-Scholes model. Finally, we will learn how to judge investment performance and discuss some of the insights from psychology for investment decision-making. The final exam will be cumulative, testing students' knowledge on all of the material covered in the course.

### Course Requirements and Grading

Grades will be based on the student's performance on two in-class tests and one final exam. Your overall score in the course will be determined *mechanically* as the weighted average of the three component scores. The weights on each component of the overall course grade are (TENTATIVELY) as follows:

First Test	Friday, July 25 <sup>rd</sup>	20%
Second Test	Wednesday, August 6 <sup>nd</sup>	20%
Final Exam	TBA ( <i>To Be Announced</i> )	40%
Assignments (4)	Various dates	20%

Exams will be comprised of multiple choices and short or long answer questions. Your overall grade will be determined by where your overall score lies in the distribution of all students' overall scores. The cut-offs in the distribution will be such that roughly 40% of students receive "A"s, 40% receive "B"s, and 20% receive grades below a "B." *However, if the average performance is rather excellent, then the scheme will be adjusted.* The exact curve cut-offs will depend on the level and shape of the overall score distribution. The course letter grade cannot be determined until all exams have been taken.

There will also be 4 assignments, which are mini-projects that ask you to apply the knowledge and tools we will study in the class to practical problems. More details and instructions on these assignments will be given out in class.

Class participation is also important. Be prepared to answer questions. At the instructor's discretion, students who participate actively in class will get the higher grade if she/he is at a cut-off point along the grade curve.

Make-up exams are generally not possible. There will certainly not be make-up versions of either the first or second test. If you miss either the first test or the second test for a *pre-approved* reason, then the percentage of the missed test will be added to your final. For example, if you miss the first test for a *pre-approved* reason, your final exam will

count 65% (40% + 25%). Likewise, if you miss the second test for a *pre*-approved reason, your final exam will count 75% (40% + 35%). Do not miss the final.

**What is a valid pre-approved reason for missing a test?**

Any conflicts must be documented in writing and submitted to me for my approval. The request must include the student's name and the conflict. Check your schedules now! If you develop a schedule conflict with the first test, then I must approve your reason for missing the first test no later than Friday, July 18<sup>th</sup>. If you develop a schedule conflict with the second test, then I must approve your reason for missing the second test no later than Wednesday, July 30<sup>th</sup>.

If you fail to show up for either test without telling me beforehand, then you must present a doctor's note stating that you were too sick to take the test. Other personal reasons may be considered valid at my discretion. If you miss either test without a valid reason, then you will receive a zero on the missed test. Again, do not miss the final.

There is no opportunity in this course to do "extra-credit" work. Your grade will be determined solely by the components listed above.

At the end of each lecture, I will suggest optional problems from the text that may be useful as study guides for the examinations. A solutions manual accompanying the text, containing solutions to the problems in the text, is available for purchase at the Co-op bookstore. If you suspect there is an error in the solutions manual, please bring it to my attention. I will try to alert you to the errors as I find them.

Course Materials

Both course textbooks are available at the Co-op. The required text for the course is:

**Investments**, Bodie, Kane, and Marcus, 7<sup>th</sup> ed., 2006, McGraw-Hill.

- ◆ Supplemental student resources including quizzing and review material are available from:

[http://highered.mcgraw-hill.com/sites/0073530611/student\\_view0/index.html](http://highered.mcgraw-hill.com/sites/0073530611/student_view0/index.html)

- ◆ PowerPoint:

[http://highered.mcgraw-hill.com/sites/0073530611/student\\_view0/powerpoint\\_presentations.html](http://highered.mcgraw-hill.com/sites/0073530611/student_view0/powerpoint_presentations.html)

A recommended, but not required, book for the course is the solutions manual entitled:

**Solutions Manual for Use with Investments**, Bodie, Kane, Marcus.

All required readings should be completed *prior* to the class meeting for which they are assigned. The course web site, available through the UT Blackboard system, will serve as the official mechanism for distributing course materials.

Finally, students will need a financial calculator capable of calculating present values, solving for yields, and performing other basic time value calculations. Time value tables will not be distributed with the tests in this class. Students bear the responsibility for learning to operate their calculators proficiently. Programmable calculators must be cleared before each test; and there is no sharing of calculators during the test.

### General and Miscellaneous Policies

- During lectures, you should always be prepared to answer questions. I will address questions to individuals and to the class as a whole at my discretion. These questions will assume that you have completed the assigned readings *prior* to the class session.
- Although attendance will not be taken, you are responsible for everything covered or assigned in class. The lectures will sometimes depart significantly from the reading material assigned.
- The use of laptop computers is permitted during lectures solely for the purposes of taking notes and obtaining course materials. E-mail and the Internet may not be accessed during lectures except to visit the course web sites listed in the syllabus.
- Academic dishonesty will not be tolerated. Your responsibilities with regard to scholastic dishonesty are described in detail in the Policy Statement on Scholastic Dishonesty for the McCombs School of Business. In particular, it is expected that the work on your examinations will be entirely your own. Failure to do so may result in failure on the examination, or course.
- The University of Texas at Austin provides upon request appropriate academic accommodations for qualified students with disabilities. For more information, contact the Office of the Dean of Students at 471-6259.
- Examinations will not be returned. The method of review will be announced in class but will occur only **during the week directly following the examination**. If you feel your posted examination grade is incorrect, you must notify me in writing during this same one-week period. After one week, the examination papers will be stored and the problem will not be researched.
- You cannot assume that all information needed for the examinations will be presented in class. It is imperative that the textbook be read and studied.

### Study Guide

My teaching will be mainly based on my lecture notes, which will be posted on the Blackboard website before each class. You need to print out your own copy and preview it before come to class. In each class, I will explain the concepts and solve some example problems. You are responsible for everything I teach in class. Moreover, you need to read the assigned readings carefully. The textbook is a very useful resource and I suggest you read every chapter at least twice. I also expect your active participation in class discussion. You can expect to be called on to answer questions in class if you do not participate on your own initiative. If you want to do well, come prepared, speak up when you have questions, and apply your best efforts.

You need to understand what you are studying, whether it is conceptual or analytical. When you study, ask yourself such question as:

What is the purpose of this concept or formula?  
Why is it important?  
How does the author demonstrate its importance?  
How does it “fit” with what you have studied so far?

I suggest that you read each chapter once before it is discussed in class and then read it again after the topic is covered in class. Reading the material beforehand will greatly assist in having meaningful class discussions. If you are having trouble with a concept or problem, see me during regular office hours as soon as possible.

The assigned homework problems are not to be handed in; however, it is important that you work and understand them. The examination problems will appear simpler for those who work the problem sets. Reviewing the solutions will also be useful in mastering the material and preparing for the examinations.

A sample class schedule is shown below. This schedule may be modified somewhat as the semester progresses as some topics take more or less time than anticipated. The availability of new material and practice questions may be announced in class, but check Blackboard for new material. The student is responsible for checking Blackboard for new materials.

Course Schedule (subject to change)

MTG	DAY	DATE	TOPIC	CHAPTER
1	Monday	14-July	INTRODUCTION and OVERVIEW - Schedule, Grading, Assignments, Class Policies	1, 2
2	Tuesday	15-July	OVERVIEW - Financial Instruments and Markets	3, 4
<b>PORTFOLIO THEORY AND ASSET PRICING</b>				
3	Wednesday	16-July	MODELING UNCERTAINTY – Statistical tools	Notes
4	Thursday	17-July	RISK AND RETURN - Expected Return and Variance; $E(R_p)$ , Asset Allocation	5
5	Friday	18-July	DIVERSIFICATION - Portfolio E(R) and Variance; Allocations Under Uncertainty	6
6	Monday	21-July	DIVERSIFICATION – Optimal Risky Portfolios	7
7	Tuesday	22-July	CAPM - Theory and Evidence	9
8	Wednesday	23-July	APT - Theory and Evidence	10
9	Thursday	24-July	EMH - Efficient Markets Hypothesis: Theory and Evidence	11
10	Friday	25-July	<b>TEST 1 : PORTFOLIO THEORY + Overview material</b>	
<b>BOND VALUATION</b>				
11	Monday	28-July	BONDS – Bond Markets, Yields, and Pricing	14, 15
12	Tuesday	29-July	BONDS - Yield Curve and Credit Spreads	16
13	Wednesday	30-July	BONDS - Interest Rate Risk: Duration and Immunization	16
<b>STOCK VALUATION</b>				
14	Thursday	31-July	STOCKS - Definitions and Valuation Models	18
15	Friday	1-Aug	STOCKS - Valuation Models (DDM)	18
16	Monday	4-Aug	STOCKS – Other Valuation Issues	17, 19
<b>DERIVATIVE VALUATION</b>				
17	Tuesday	5-Aug	OPTIONS - Instruments, Markets, Definitions, and Payoffs	20

*Syllabus, FIN 367, Summer 2008, Jeremy Page*

18	Wednesday	6-Aug	<b>TEST 2 : BOND and STOCK VALUATION</b>	
19	Thursday	7-Aug	OPTIONS – Valuation: Black-Scholes	21
20	Friday	8-Aug	FUTURES - Markets and Instruments	22
21	Monday	11-Aug	HEDGING - Risk Management and Arbitrage	23
			<b>OTHER TOPICS</b>	
22	Tuesday	12-Aug	PERFORMANCE - Investment Manager Performance Evaluation	4, 24
23	Wednesday	13-Aug	Guest Presentation: Steve Yacktman of Yacktman Funds	
24	Thursday	14-Aug	BEHAVIORAL FINANCE	12
25	Friday	15-Aug	COURSE WRAP-UP	
26	TBA	TBA	<b>FINAL EXAM : EVERYTHING Date, Time, and Room Will Be Announced</b>	<b>All of the Above</b>