

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

Finance 367: Investment Management

Spring 2008

Monday & Wednesday 08:00-09:30, UTC 1.104, unique #02945

Monday & Wednesday 09:30-11:00, UTC 1.104, unique #02960

Monday & Wednesday 11:00-12:30, UTC 1.104, unique #02965

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Course Description

Finance 367 is an introductory investment course. It is intended for those students who want to become investment professionals (portfolio managers, professional investment advisors, or analysts) or knowledgeable individual investors. There are two major themes in the course: 1) valuation of various securities such as bonds, stocks, and major derivatives, and 2) combination of securities into portfolios with desired characteristics (optimally balanced risk and return). Students will study various opportunities arising from investing in financial instruments and the related risks. Special attention will be given to the ways of managing these risks. Also, several topics related to applied portfolio management will be covered, including evaluation of portfolio performance, functions and strategies of major institutional investors, and basics of personal finance.

Prerequisite

The prerequisite is Finance 357: students are expected to be familiar with basic concepts of finance covered in this class. Also, it will be assumed that students have some knowledge of probability and statistics (understand the concepts of expectation, standard deviation, and correlation). Although the coverage of purely quantitative methods will be limited, students will need to be able to do basic algebraic manipulations.

Course Materials

The major material of the course will be covered in lecture notes, which will become available before each class. The required text book for the course is

Investments, by Z. Bodie, A. Kane, and A. Marcus, 7th ed., 2006, McGraw-Hill.

For those students who want to get additional practice in solving problems the following solution manual is recommended (but not required):

Student Solutions Manual to accompany Investments, by Z. Bodie, A. Kane, and A. Marcus, 2006.

There are several books that are recommended for those who want to get deeper understanding of financial markets and the investment process:

A Random Walk Down Wall Street, by Burton G. Malkiel, W. W. Norton & Company;
When Genius Failed: The Rise and Fall of Long-Term Capital Management, by Roger Lowenstein, 2001, Random House.

The material from these books is not necessary for successful completion of course requirements. In addition, students are encouraged to read investment articles in *The Wall Street Journal*. Also, from time to time, recommended articles will be posted on the web. The course web site available through the UT Blackboard system (<https://courses.utexas.edu/webapps/login>) will serve as the official mechanism for distributing course materials, including online articles, problem sets, and lecture notes.

Students will need a calculator on both midterm and final exams. There will be no computationally intensive problems in the exams and students are free to use any type of calculator (the use of financial calculators will not give any advantage). However, the problem sets will require computation of present values, yields, and internal rates of returns. To perform these computations students will need financial calculators, Excel, or other tools. The recommended financial calculators are: *Texas Instruments BA II Plus* (easier to use) and *Hewlett Packard 12C* (harder to use). These calculators are the only ones permitted on the CFA Exam.

Course Requirements and Grading

Grades will be based on the student's performance on a midterm exam, a final exam, three problem sets, and two projects (analyst report and portfolio project). The overall score in the course will be determined *mechanically* as the weighted average of the component scores. The weights of each component and the due dates are as follows:

Midterm Exam	Wednesday, March 5	20%
Three Problem Sets	See course schedule	30%
Analyst Report	Monday, March 31	10%
Portfolio Project	Wednesday, April 30	10%
Final Exam	TBA	30%

The overall grade of each student will be determined by where the 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 "B." **The exact curve cut-offs will depend on the level and shape of the overall score distribution.**

There is only one opportunity in this course to do "extra-credit" work. Those students who attend most of the lectures and actively participate in the class discussions can get extra credit up to 5% at my own discretion. I expect that only few students will be rewarded in this way and the grade of majority will be determined solely by the components listed above.

Exams

There will be two exams, a midterm and a final. The final exam will be comprehensive. Both exams will have a closed book format. Students will be allowed to use one two-sided cheat sheet with the font not less than 10pt. Also, students are expected to bring their own calculators to the exams. Programmable calculators must be cleared before each test. Using laptops and sharing of calculators during the exams is strictly prohibited.

There will be no make-up versions of the mid-term exam. If student has to miss the midterm exam because of an excusable and verifiable reason, he/she must let me know this in advance. If student fails to show up for the mid-term without telling me beforehand, then a doctor's note must be presented stating that the student was too sick to take the test. Other personal reasons may be considered valid at my discretion. Missing the midterm without a valid reason will result in a grade of zero for the exam. If student misses the mid-term for a pre-approved or medical reason, then the percentage weight of the mid-term will be added to the weight of your final exam, which will be 50% (20% + 30%). Do not miss the final exam!

Problem Sets

Three challenging problem sets will be excellent preparation for the exams. Students are allowed and encouraged to form teams of up to three people to complete the problem sets. Although the assignment can be split among team members, each student should fully understand how to solve all problems. All team members will get the same score based on

the provided solutions for all problems. Although it is permissible to change the group or start working individually, students are encouraged to stay within the same group over the whole semester.

All problem sets must be turned in before the class on the due date. Late assignments turned in on the due date after the class will be penalized by subtracting 20% from the grade. Solutions turned in after the due date will automatically earn 0%. Do not forget to indicate all team members on the front page. Although hand written home assignments will be accepted, the submission of type written solutions will be preferred.

Analyst report

There will be a list of 6 stocks out of which students will have to pick up one and write an analyst report. It is expected to be a 5-6 page document providing general overview of the company, discussing prospects, potential, and related risks. Also, students should demonstrate knowledge of valuation techniques and estimate the fair value of the company. The report must contain a recommendation whether to buy the stock, hold it, or sell it. Students will have approximately a month and a half to complete this project. Similar to problem sets, students are encouraged to work in groups of up to 3 members. Further instructions will be provided later.

Individual Portfolio Project

Each student will be asked to invest fictitious \$500,000 in various stocks, bonds, and derivatives using a StockTrak account (www.stocktrak.com) and manage the portfolio during the semester. The purpose of the project is to familiarize students with mechanics of investing and give a chance to apply the obtained knowledge in practice. The only deliverable for the project is a portfolio analysis paper of 2-3 pages due on Wednesday, April 30th. In the paper, students have to explain their investment strategy, attribute the performance of the portfolio to various factors, and evaluate the overall outcome. The performance of the portfolio will not affect the grade. Instead, students will have to demonstrate their knowledge of portfolio theory and allocate their wealth in a judicious way. Note: this is an *individual* project and the work in groups is not allowed.

Academic Integrity

Each student is expected to abide by the University Code of Academic Integrity. 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, the work on your examinations must be entirely your own. Talking is not permitted during the exams. You are not allowed to compare your work with others, copy from others, or collaborate in any way. All examinations will be closed-book and any use of books, lecture notes, personal notes, and other materials

(except the allowed cheat sheet) will be considered as cheating. **Any inappropriate behavior during the examinations will result in failure of the exam, and may lead to failure of the course and other University disciplinary actions.**

Except the exams, students are allowed and encouraged to study together and discuss the material and concepts covered in the lectures with other students. It is permissible to give “consulting” help or receive “consulting” help from other students. However, this permissible cooperation should never involve one student having possession of a copy of all or part of work done by someone else, in any form including an e-mail, an e-mail attachment, or a hard copy. The only exception from this rule is the work of other team members when teams are allowed. Should copying occur, both the student (or the team) who copied work from another student (or the team) and the student (or the team) who gave material to be copied automatically receive a zero for the assignment. Penalty for copying or using the work of others can also be extended to include failure of the course and University disciplinary actions.

The University of Texas Honor Code

“The core values of The University of Texas at Austin are *learning, discovery, freedom, leadership, individual opportunity, and responsibility*. Each member of the university is expected to uphold these values through *integrity, honesty, trust, fairness, and respect toward peers and community*.”

Accommodations for Students with Disabilities

The University of Texas at Austin provides upon request appropriate academic accommodations for qualified students with disabilities. Students who require special accommodations need to get a letter that documents the disability from the Services for Students with Disabilities of the Office of the Dean of Students (471-6259-voice or 471-4641 – TTY for users who are deaf or hard of hearing). This letter has to be presented to me at the beginning of the semester and appropriate accommodations will be discussed at that time. Also, if you need any specific accommodations on the midterm or final exams you should remind me about them five business days before the exam.

Class Web Sites and Student Privacy

Password-protected class sites will be available for all accredited courses taught at The University. Syllabi, handouts, assignments and other resources are types of information that may be available within these sites. Site activities could include exchanging e-mail, engaging in class discussions and chats, and exchanging files. In addition, class e-mail rosters will be a component of the sites. Students who do not want their names included in these electronic class rosters must restrict their directory information in the Office of the

Registrar, Main Building, Room 1. For information on restricting directory information see <http://www.utexas.edu/student/registrar/catalogs/gi02-03/app/appc09.html>.

Feedback

Feedback is an important part of any learning. During this course I will be asking to give me feedback in an informal way mainly using the Ongoing Course Assessment tool (web.austin.utexas.edu/diia/oca/) and/or paper questionnaires. Please let me know when something we discuss is not clear. It will enable me to provide additional information when needed or to explain a concept in different terms.

In addition, I will be asking for feedback about my teaching strategies, which I want to be as efficient as possible. This kind of feedback is very important to me. From time to time, I will ask you to complete short anonymous questionnaires and I encourage you to respond to them. Also, you have an opportunity to attract my attention or express your opinion on any class related issue in anonymous or personal way. Although I keep the right to ignore this sort of feedback, in many cases I will make appropriate steps to ensure that together we create an effective learning environment.

Miscellaneous Policies

- Please send all course-related e-mails—*i.e.*, questions, clarifications, *etc.*—to me *and* Amit Marwaha (the TA). This policy minimizes our response time.
- Although attendance will not be taken, you are responsible for everything covered or assigned in class. The composition of lectures will sometimes depart significantly from the textbook.
- Mobile phones and Blackberries must be switched off in class at all times. In general, the use of laptops is not permitted. However, if you are accustomed to put notes electronically, you can get my individual permission for an open laptop. In this case be prepared to show me your notes after the class. Also, I can revoke the permission if I learn that you use laptop for class unrelated purposes. Laptops are not allowed on the midterm and final exams.

Course Schedule*

	DAY	DATE	TOPIC	CHAPTER
			INTRODUCTION	
1	Mon	14-Jan	Course Overview, Introduction in Financial Markets	1, 2
2	Wed	16-Jan	Valuation of Securities: Basic Concepts	1, 2
3	Mon	21-Jan	<i>Martin Luther King Jr. Day holiday – No Class</i>	
			FIXED INCOME SECURITIES	
4	Wed	23-Jan	Introduction in Fixed Income	14
5	Mon	28-Jan	Term Structure and Bond Pricing	15
6	Wed	30-Jan	Default Risk and Credit Spreads	14
7	Mon	4-Feb	Interest Rate Risk and Duration	16
8	Wed	6-Feb	Managing Bond Portfolios	16
			STOCKS	
9	Mon	11-Feb	Definitions, Indexes, Historical Performance Problem Set #1 DUE	2, 5
10	Wed	13-Feb	Trading and Exchanges	3
11	Mon	18-Feb	Financial Statements and Analyst Reports	17, 19
12	Wed	20-Feb	Valuation Ratios	18, 19
			PORTFOLIO THEORY	
13	Mon	25-Feb	Statistics of Portfolio Returns	6
14	Wed	27-Feb	Optimal Risky Portfolios and Portfolio Frontier	7
15	Mon	3-Mar	Diversification: Systematic vs. Idiosyncratic Risk	7
16	Wed	5-Mar	Mid-term Exam: Fixed Income, Stocks, Portfolio Theory Problem Set #2 DUE	
	Mon	10-Mar	<i>Spring Break – No Class</i>	
	Wed	12-Mar	<i>Spring Break – No Class</i>	

MTG	DAY	DATE	TOPIC	CHAPTER
			EQUILIBRIUM IN CAPITAL MARKETS	
16	Mon	17-Mar	Regression, Alpha, and Beta	8
17	Wed	19-Mar	CAPM: Theory and Evidence	9
18	Mon	24-Mar	Valuation of Stocks: Discounted Dividend Model	18
19	Wed	26-Mar	Efficient Markets Hypothesis	11
			DERIVATIVES	
20	Mon	31-Mar	Introduction to Derivatives Analyst Report DUE	2.5, 20
21	Wed	2-Apr	Options: Definitions, Markets, and Strategies	20
22	Mon	7-Apr	Valuation of Options: Binomial Model and Black-Scholes formula	21
23	Wed	9-Apr	Futures: Markets and Instruments	22
24	Mon	14-Apr	Hedging: Risk Management and Arbitrage	23
			APPLIED PORTFOLIO MANAGEMENT	
25	Wed	16-Apr	Portfolio Performance Evaluation Problem Set #3 DUE	24
26	Mon	21-Apr	Institutional Investors: Mutual Funds	4
27	Wed	23-Apr	Institutional Investors: Hedge Funds and Other Investment Companies	23.4
28	Mon	28-Apr	Wealth Management and Household Finance	26
29	Wed	30-Apr	Course Review Portfolio Analysis Paper DUE	
30	TBA	TBA	FINAL EXAM Date, Time, and Room Will Be Announced	All of the Above

*Course schedule is tentative and subject to changes.