Tentative Syllabus for Fall 2010

MGT/MGP/MGB 261: Investment Analysis

Daytime MBA:  Tu 12:00p.m. - 3:00 p.m.  Location: 2310 Gallagher  (CRN: 70844)
Sacramento MBA: Tu  6:00p.m. - 9:00 p.m.  Location: 1204 Sac Ed Ctr (CRN: 70807)
Bay Area MBA:  Fr  2:00p.m. - 5:00 p.m.  Location: 1503 Bishop Rch(CRN: 70793)
Sa  9:00a.m - 12:00 p.m.

Contact Information
Instructor: Joe Chen
Office: 3216 Gallagher Hall
Office Hours: to be determined (or by appointment)
e-mail: chenjs@ucdavis.edu
Course Website: on SmartSite (http://smartsite.ucdavis.edu)

Course Objectives
The objective of this course is to study theory and empirical evidence relevant for portfolio management. The perspective taken is that of portfolio allocation rather than individual stock selection. In particular, an emphasis is placed on understanding how an investment professional would allocate funds in a hypothetical portfolio, across stocks, bonds, and other asset classes. Major topics include estimation of capital market parameters, trade-off between risk and return, optimal portfolio selection, equilibrium asset pricing models, delegated portfolio management and additional topics as time allows. Emphasis will be put on development of techniques that should be part of the tool kit of those interested in becoming professional investors and/or researchers in finance. This course is designed to primarily address the needs of advanced students in an MBA program.

Prerequisites

- I will assume a good understanding of basic notions in finance: the time-value of money; return, risk and portfolio diversification; net present value; etc.  These are materials covered in MGT/P/B 205 (core finance class). I will discuss some of these topics in class, but I expect you to refresh your memory on them at the very beginning of the quarter. Spending time in class to review topics that are covered by more basic courses would be inefficient and, most important, would take time away from new and more exciting topics. I assume that you are in this class to learn new material and get ready for the job market and I will teach the course accordingly.

- Uncertainty is what makes the study of financial markets fascinating. If there were no uncertainty there would be very few job opportunities in finance. Unfortunately, uncertainty also makes our task more difficult. The good news is that you will finally understand why you had to study statistics. No serious study of portfolio and risk management can be undertaken without solid knowledge of statistics. You should have covered these materials in MGT/P/B 203 (core statistics class). For this reason, I expect you to make a serious effort to refresh your memory on some essential concepts such as descriptive statistics, inference techniques and basic regression analysis. Any introductory book in statistics should help you to get up to speed.

- A mathematical approach is necessary to avoid superficiality for many of the topics covered by this course. We will assume a good knowledge of mathematics, such as linear algebra and calculus. I am not a fan of technicalities per se, but I hope that by the end of the semester you will appreciate how the use of technical tools is important to make this a useful course.

- I will assign problem sets that require a proficiency of computing skills, such as the use of Microsoft Excel. If you are planning to work in the area of investment management, it is essential that you develop your computer skills. I will assume that you know how to use spreadsheets to perform some basic analysis.
Exams, Assignments and Course Policy

Grading Criteria
The course grade is based on the following criteria:

<table>
<thead>
<tr>
<th>Assignments (5)</th>
<th>40%*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bi-weekly Quizzes (4)</td>
<td>30%*</td>
</tr>
<tr>
<td>Final Exam</td>
<td>20%</td>
</tr>
<tr>
<td>Participation</td>
<td>10%</td>
</tr>
</tbody>
</table>

* For the purpose of grading, you are allowed to drop your lowest scoring assignment and replace it with your highest scoring assignment. However, an incomplete assignment may only be replaced with the average of remaining assignment scores. Similarly, you are allowed to drop your lowest quiz score and replace it with your highest quiz score. An incomplete (absent) quiz may also be dropped, but will be replaced with the average of the remaining quiz scores.

Course Groups
- Teamwork is a critical skill to be developed in investment management. Each class participants are to form into groups of 3-5 students. If you have problems creating groups or finding enough members, one will be assigned for you.
- Name your group with business name appropriate for an investment company. Eg. “Aggie Inv’t Co.”
- All assignments and the course project must be done in groups.

Course Policy
- Assignments: I will assign homework problems on a regular basis, which are to be done in groups. There will be a total of 5 assignments – (for Bay Area MBA: with the first assignment due on the first meeting). Submit one write-up for the entire group, being careful to note all the names of group members and the section number. Hard copies are preferred, but properly formatted electronic copies in PDF may also be submitted via the course website. Any documents submitted electronically must be properly formatted for printing – supporting documents should be provided as separate non-printing pages. Unformatted MS Words or MS Excel files will not be accepted. Late assignments are NOT acceptable.

- Quizzes and Final Exam: The quizzes and final exam are closed book and closed notes. You are not allowed to use any notes or “cheat sheets”. We will allow the use of non-programmable calculators during the exam. The final exam will be held during the last meeting sessions, rather than during the final exam period.

- Makeup Quizzes and Final Exam: There will be no makeup quizzes or exams. Any missed quizzes, exams or assignment not turned in will receive a credit of zero and included in the computation of the final grade. By registering for this class you are committing, among other things, to take quizzes and exams on the scheduled dates.

- Breaks: There are no scheduled breaks in the course schedule. However, there will be ample opportunities during our meetings to take necessarily excursions to restrooms or coffee rooms.

- Office Hours: If you have any questions about the material covered in class please do not hesitate to see me. Please send me an e-mail to schedule an appointment (but please do not ask for an appointment for a time within 24 hours) or during office hours. Dropping in without an appointment outside of office hours is highly discouraged (except in emergencies). If you have problems keeping up with the material, do not wait hoping that things will get better. They will probably get much worse. Remember that the reason why you enrolled in this course is to learn some finance, not to survive through the course.
• **E-mail and Course Forums:** Open discussion of course materials is an integral component of the learning process – both in the classroom and outside. To facilitate ongoing discussion, we will be using the discussion forum on the course website extensively (on SmartSite). Make use of the forum to address any questions concerning the class – whether they are administrative questions or those regarding content. Do not use e-mail except for inquiries of personal or private nature. Questions submitted by e-mail regarding course materials will only be addressed via the course forums.

• **Return of Graded Paperwork:** Returned paperwork, unclaimed by a student, will be discarded after 4 weeks and, hence, will not be available should a grade appeal be pursued by a student following the receipt of his/her course grade.

• **Additional Course Materials:** Homework assignments, solutions, additional readings, and all other additional course materials will be posted on the course web page. **You are responsible for timely downloads of the materials from the course web page.** I will also provide copies of my lecture notes on the course web page by the evening before the lecture.

• **Research Travel:** UC Davis is a world-renowned research institution. The advantage of studying under our faculty is that you will be exposed to up-to-date leading research in finance (materials not found in any textbook). The disadvantage is that the faculty is sometimes required to share the ideas developed here with other research institutions and will periodically be unavailable on campus.

• **Calculators and Computers:** The nature of the subject matter requires significant amount of numerical computations. Students are expected to bring a calculator to every class session and to all examinations. Moreover, use of laptop computers in the classroom may be necessary.

• **Tent Cards:** Classroom participation and interaction is an integral part of the learning experience. To facilitate this, students are expected to bring a tent card to every class session and place it visibly.

## Textbooks and Additional Readings

**Textbooks**

- **Required:**
  
  *Investment Analysis, 8th Edition* (referred to as *BKM* hereafter)

  Authors: Zvi Bodie, Alex Kane, and Alan Marcus

  Publisher: McGraw-Hill/Irwin

  (ISBN: 978-0073382371)

**Additional Readings**

- **Required:**
  
  A course reader (textpak) with copies of HBS cases will be assigned.

  Additional required readings may be assigned and provided electronically.

- **Highly Recommended:**
  
  1. Daily reading of the *Wall Street Journal* or the *Financial Times*.
  2. Weekly reading of the *Economist* and *Barron’s*.

- **Recommended:**
  
  Articles from: *Journal of Portfolio Management* and *Financial Analysts Journal*. 
Tentative Course Outline and Assigned Readings

This is a tentative course outline and assigned readings: topics and assigned readings are subject to change.

1a. Overview of Portfolio Management
We classify the main types of financial markets, and introduce the basic securities traded on them. We then discuss the different exchanges in which securities are traded, the typical positions taken and the costs associated with trading. We discuss some of the practical aspects of investment decision-making and introduce the process of portfolio management. We also study the industry of active portfolio management, such as mutual funds, pension funds and hedge funds. This section summarizes the basic institutional details we need to know when discussing the main themes of the investment process for equities.

- Required Reading: BKM, Chapters 1 (all), 3.6, 3.7, 28.1-28.3
- Optional Reading: BKM, Chapters 2.3, 2.4, rest of 3, 4 (all), 28.4, 28.5.

1b. Quantitative Review, Historical Return Analysis and Portfolio Mathematics
We review some basic concepts of statistics and probability theory: namely, means, standard deviations, variances, covariances and correlations. We discuss estimating these statistical moments using historical samples, as well as running and interpreting regression analysis. We also consider how to mathematically represent returns and portfolio holdings as to account for cash deposits and loans, margin accounts and short-selling.

- Required Reading: BKM, Chapters 5 (all), 17.2 and 17.5.
- Optional Reading: BKM, Chapters rest of 17

2. Optimal Portfolio Choice
We first introduce the notions of risk and portfolio diversification and discuss how to compute important descriptive statistics for portfolios of assets. We use Markowitz’s approach to portfolio formation to show how investors can take advantage of the correlation structure among assets to generate an investment opportunity set that dominates (in a reward-to-risk sense) any of the individual assets taken in isolation. We show how to construct the best set of attainable portfolios and provide precise measures for the benefits of portfolio diversification. We also discuss how different attitudes towards risk affect the composition of the portfolio held by each investor.

- Required Reading: BKM, Chapters 6 (all), 7 (all), 25.1, 25.2 and 25.3.
- Optional Reading: BKM, Chapters 25.4 and 25.5.

3. Equilibrium Asset Pricing Models
We assume that the investors are rational and, therefore, optimize their portfolio holdings according to their preferences, subject to their budget (and possibly some institutional) constraints. Using this approach we derive the Capital Asset Pricing Model (CAPM) and discuss its implications for asset pricing and investment-decision making. We then assume that assets returns are generated by a finite number of factors and all arbitrage opportunities are exploited, which lead to the Arbitrage Pricing Theory (APT).

- Required Reading: BKM, Chapters 8 (all), 9.1-9.4 and 10 (all).
- Optional Reading: BKM, Chapters 9.5 and 9.6

We discuss some of the main tests carried out to investigate the empirical merits of the asset pricing models discussed so far. We then go on to approach the problem of market efficiency; we discuss the different levels of efficiency (weak, semi-strong and strong) and analyze the basic empirical evidence that supports, or rejects, this notion. Anomalies to the asset pricing models and revised models are analyzed.

We will also discuss how to evaluate past performance of portfolio management by investment advisors in the context of the asset pricing models. Specific topics include measures of past performance, survivorship bias, benchmarks and style drifts.

- Optional Reading: BKM, Chapters 11.3, 12 (all), 24.2-24.4, 26.4-26.6, 27 (all).
MGT/MGP/MGB 461: Investment Analysis

Daytime MBA: Tu 12:00p.m. - 3:00 p.m. Location: 2310 Gallagher (CRN: 70844)
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Sa 9:00a.m - 12:00 p.m.

Contact Information
Instructor: Joe Chen
Office: 3216 Gallagher Hall
Office Hours: to be determined (or by appointment)
e-mail: chenjs@ucdavis.edu
Course website: on SmartSite (http://smartsite.ucdavis.edu)

Course Objectives
The objective of this practicum course is to apply theory and knowledge of portfolio management to a realistic asset allocation problem. The course centers on a major project based on a realistic investment management exercise by a financial advisor for a client with a hypothetical portfolio. Students are expected to make informed capital market assumptions, perform portfolio optimization with necessary investment constraints, and make stock selection decisions in the context of a benchmarked portfolio. In addition, students are expected to incorporate tools learned in other classes in order to understand how to run a money management business. Emphasis will be put on addressing real problems faced by investment professionals responsible for welfare of their clients. This course is designed primarily to address the needs of advanced students in an MBA program interested in managing portfolios professionally or personally.

Co-requisite
- This course is a practicum designed to accompany Investment Analysis. It is expected that you are concurrently enrolled in MGT/P/B 261. You are not required to enroll in this course to complete MGT/P/B 261. However, this course will provide additional practical exercise designed to further your understanding of materials learned in investment analysis, as well as materials in other courses you have taken.
Grading Criteria and Course Policy

Grading Criteria
The course grade is based on the following criteria:

<table>
<thead>
<tr>
<th>Course Project</th>
<th>70%</th>
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<tbody>
<tr>
<td>Participation</td>
<td>30%</td>
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</table>

Course Groups
- Teamwork is a critical skill to be developed in investment management. Each class participants are to form into groups of 3-5 students. If you have problems creating groups or finding enough members, one will be assigned for you.
- Name your group with business name appropriate for an investment company. Eg. “Aggie Inv’t Co.”
- The course project must be done in groups. It is recommended that the group be the same as the one for the co-requisite class, MGT/P/B 261, Investment Analysis.

Course Policy and Office Hours
- **Course Project:** There will be one major project dealing with asset allocation. We will be working on this project throughout the term, with small sections due intermittently. We will apply the portfolio choice and diversification theory from class to some actual real-life scenarios. Extensive use will be made of Excel (or any other mathematical package). The project must be done in your groups.

  A final printed version of the project write-up must be delivered on December xxx, during the designated final exam period.

  Furthermore, the project will involve presentation components. Each group must also prepare two Powerpoint presentations. The first is a shorter (five minute) presentation on a small portion of the project, which will be due as the course progresses (see course schedule). The second presentation is the final presentation due during the final exam period. You may sign up for presentation slots as soon as groups are formed.

- **Mandatory Office Hours:** There is a mandatory (at least 20 minutes) office meeting, which can be conducted in person or over web-conferencing. This meeting is designed to ensure your group is making good progress towards presentation of your work. The ideal time is to meet prior to your group’s shorter presentation during the quarter. Additional meetings can be scheduled as needed.

- **Other Policies:** All course policies listed under MGT/MGP/MGB 261 also apply for this course.
## Tentative Course Schedule for MGT/P/B 261 and MGT/P/B 461

Subject to change and approval.

<table>
<thead>
<tr>
<th>Day</th>
<th>Section</th>
<th>Sacramento Section</th>
<th>Bay Area Section</th>
<th>Length</th>
<th>Deliverable</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Sep 28</td>
<td>12:00pm-3:00pm</td>
<td>Sep 24</td>
<td>180min</td>
<td>Due: Assignment #1</td>
</tr>
<tr>
<td>2</td>
<td>Oct 5</td>
<td>12:00pm-2:30pm</td>
<td>Oct 5</td>
<td>150min</td>
<td>Quiz #1</td>
</tr>
<tr>
<td>P1</td>
<td>Oct 5</td>
<td>2:30pm-3:00pm</td>
<td>Oct 5</td>
<td>30min</td>
<td></td>
</tr>
<tr>
<td>3</td>
<td>Oct 12</td>
<td>12:00pm-3:00pm</td>
<td>Oct 8</td>
<td>180min</td>
<td>Due: Assignment #2</td>
</tr>
<tr>
<td>4</td>
<td>Oct 19</td>
<td>12:00pm-2:00pm</td>
<td>Oct 9</td>
<td>120min</td>
<td>Quiz #2</td>
</tr>
<tr>
<td>P2</td>
<td>Oct 19</td>
<td>2:00pm-3:00pm</td>
<td>Oct 9</td>
<td>60min</td>
<td>Project part 1</td>
</tr>
<tr>
<td>5</td>
<td>Nov 2</td>
<td>12:00pm-2:00pm</td>
<td>Oct 22</td>
<td>180min</td>
<td>Due: Assignment #3</td>
</tr>
<tr>
<td>P3</td>
<td>Nov 2</td>
<td>2:00pm-3:00pm</td>
<td>Oct 23</td>
<td>120min</td>
<td>Quiz #3</td>
</tr>
<tr>
<td>7</td>
<td>Nov 9</td>
<td>12:00pm-3:00pm</td>
<td>Nov 5</td>
<td>180min</td>
<td>Due: Assignment #4</td>
</tr>
<tr>
<td>8</td>
<td>Nov 16</td>
<td>12:00pm-2:00pm</td>
<td>Nov 6</td>
<td>120min</td>
<td>Quiz #4</td>
</tr>
<tr>
<td>P4</td>
<td>Nov 16</td>
<td>2:00pm-3:00pm</td>
<td>Nov 6</td>
<td>60min</td>
<td>Project part 3</td>
</tr>
<tr>
<td>9</td>
<td>Nov 23</td>
<td>12:00pm-3:00pm</td>
<td>Nov 19</td>
<td>180min</td>
<td>Due: Assignment #5</td>
</tr>
<tr>
<td>Fin</td>
<td>Nov 30</td>
<td>12:00pm-1:30pm</td>
<td>Nov 20</td>
<td>90min</td>
<td>Final Exam</td>
</tr>
<tr>
<td>P5</td>
<td>Nov 30</td>
<td>1:30pm-3:00pm</td>
<td>Nov 20</td>
<td>90min</td>
<td>Project Rough Draft</td>
</tr>
<tr>
<td>PF</td>
<td>xxx</td>
<td>12:00pm-3:00pm</td>
<td>xxx</td>
<td>180min</td>
<td>Project Presentation</td>
</tr>
</tbody>
</table>

Meetings 1-9 are regular meeting times for MGT/P/B 261
Meeting ‘Fin’ is the final exam period for MGT/P/B 261
Meetings P1-P5 are meeting times for the practicum (MGT/P/B 461)
Meeting ‘PF’ is the practicum project presentation period for the practicum (MGT/P/B 461)

Note: total scheduled meeting time for MGT/P/B 261 is 1500 minutes (equals 3 quarter units). Total schedule meeting times for MGT/P/B 461 is 480 minutes, plus additional 20 minutes of mandatory office hours (equals 1 quarter unit).

Note: scheduled final exam period for MGT 261/461 is December 10-11. Scheduled final exam period for MGP 261/461 is December 6-10. Scheduled final exam period for MBG 261/461 is December 10-11. The exam date and time is still to be determined.