

# Econ 134A—Introduction to Finance

## Fall 2006

### General Information

Shane Parendo: 2051 North Hall  
Office hours: Monday 1-2, Wednesday 3-4, and by appointment  
E-mail: sparendo@econ.ucsb.edu

Class Web site: <http://www.econ.ucsb.edu/~sparendo/econ134a.html>

When e-mailing me, please use a descriptive subject line (or put 134A in the subject line) and do not send HTML e-mail. HTML e-mail with ambiguous subject lines is subject to deletion as spam/virus.

Please check the class website regularly; announcements, homework and other important information will be posted to the web site, as well as solutions and other useful items for your study in finance.

Meeting Times:

Lecture—MWF 2:00-2:50, Life Science 1001

	Friday	10:00-10:50	Alok	<b>NH 1110</b>
	Friday	11:00-11:50	Alok	<b>NH 1110</b>
Sections:	Tuesday	4:00-4:50	Bryan	NH 1111
	Tuesday	5:00-5:50	Bryan	SH 1430

### Objectives

This is a first class in Corporate Finance. At the end of this course, students should be able to think analytically about portfolio selection, corporate decision making and asset pricing. These skills can also be used for personal financial decisions.

### Texts and Notes

Required Text: Ross, Westerfield and Jaffe, *Corporate Finance*, 7th Edition  
Supplemental Reading: Malkiel, *A Random Walk Down Wall Street*

RWJ looks mainly at Corporate Financial decisions, while the Malkiel text uses some of the ideas learned in the course to individual investment decisions in the stock market.

Other interesting reading:

- Liar's Poker, Michael Lewis. Inside look at Wall Street firms in the late '80s. He also wrote Moneyball, focusing on the small-market Oakland A's and their valuation of baseball players.
- Smartest Men in the Room: The Amazing Rise and Scandalous Fall of Enron. What it sounds like.
- Beating the Street, Peter Lynch and John Rothchild. Investment ideas from Peter Lynch, who ran the Magellan funds at Fidelity, one of the few mutual funds to consistently perform well.
- Buffettology, Mary Buffett and David Clark. Written by Warren's daughter-in-law (Buffett never wrote a book himself) this gives insight into Buffett's investing style and decision making process.

There will be several copies of RWJ on reserve in the library, but everyone should try to secure access to a copy (your own or a friend's); there will be many students in this class, and the books may be unavailable from the reserve at critical times. Also on reserve will be solution manuals that should be very useful in your study of finance.

The lecture notes used in class will be available on the class web site. I will usually post the notes at least a day in advance of lecture, so that they can be printed out. This will allow you (if you so choose) to be able to follow along with lecture instead of writing notes. The last time I taught this class there were two class meetings a week, so the lectures might not line up exactly with days, but I will try to indicate our progress.

You should obtain a calculator, preferably not a financial calculator. We will be solving many problems that involve arithmetic for which you should show your work (intermediate steps). On the exams to receive full credit you will need to show your intermediate steps. Microsoft Excel (or another spreadsheet program) is not necessary for the class but it might be useful to answer some problems, and it is a good skill to know how to use Excel.

## Topics

1. Introduction to Corporate Financial Decision Making  
RWJ, Ch.1
2. Interest Rate Mathematics and NPV  
RWJ, Ch. 4
3. Equity Valuation and Investment Decisions Under Certainty

- (a) Present Value of Stocks and Bonds  
RWJ, Ch. 5
  - (b) Alternative Investment Criteria  
RWJ, Ch. 6
  - (c) Net Present Value and Capital Budgeting  
RWJ, Ch. 7 and 8
4. Risk and Return
- (a) Diversification and Portfolio Selection  
RWJ, Ch. 9
  - (b) Risk, Reward and the Capital Asset Pricing Model  
RWJ, Ch. 10 and 12
  - (c) Efficient Capital Markets  
RWJ, Ch. 13
5. Capital Structure
- (a) Cost of Capital  
RWJ, Ch. 12
  - (b) The M&M Propositions  
RWJ, Ch. 15
6. Options  
RWJ, Ch. 22

## Grading

The grading will be based on the final (50%) and two midterms (25% each). There will be three midterms during the quarter. Everyone's **lowest** midterm will be dropped in the calculation of your final grade. **No makeup tests allowed**, for any reasons—if you miss one, that will be the midterm you drop. The midterm dates and the material likely to be covered on the exams are:

1. October 18, Chapters 1, 4, 5.
2. November 3, Chapters 6, 7, 8, 9, and
3. November 20, Chapters 10 and 12

The final is cumulative (with equal weights to all the material) and will be given at the time scheduled by the registrar.

The exams will be closed book, however a sheet of formulae will be included in the test sheets. Thus, you will not have to memorize any formula, but you will be expected to know what all the terms mean, and be able to apply them

to the exam problems. Calculators and writing instruments are allowed, but no other resources (books, notes, other people) are allowed on the exams. You will have plenty of room on the test itself for scratch work and your answer.

The TAs will grade the the exams. All exam questions should be directed to your TA. To appeal a grade, submit a *written* argument explaining why you feel your grade should be changed. All appeals of grades must be made within one week of the return of the exams in class. If a satisfactory conclusion cannot be reached between the TA and yourself, then I will get involved.

In a class with 100-200 students, grades are distributed as follows:

A	10%
A-	10%
B+	13%
B	13%
B-	13%
C+	8%
C	8%
C-	8%
D, F	17%

However, with the small number of students in this class, deviations from this distribution may occur.

If you are a student with a disability and would like to discuss special academic accommodations, please see me or send me an e-mail.

**How to do well in the class.** This will likely be one of the toughest Economics classes you'll have. The lectures are designed to compliment the text. The text will usually have the same material (though presented differently) as the lectures. Reading the chapters is a good idea, and should go quickly if you understood the material in lectures. However, the main learning tool should be working problems. The homework will have some problems, but practicing the problems from the end of the chapters is extremely valuable for learning. Answers to the end of chapter problems will be posted on the website to compare with your work. There is no substitute for working on these problems.