

Econ 134A—Introduction to Finance

Fall 2008

General Information

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

When e-mailing me, please put 134A in the subject line.

Please check the class website regularly; announcements 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—TR 5:00-6:15, Buchanan 1940

	Monday	5:00-5:50	Dandan	Phelps 1425
Sections:	Monday	6:00-6:50	Dandan	Phelps 1425
	Friday	9:00-9:50	João	Girvitz 1115
	Friday	11:00-11:50	João	Girvitz 2123

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 (40%) and two midterms (30% each). There will be two midterms during the quarter. If your final score is higher than your lowest midterm score, the final score will replace it. Only one midterm can be replaced. **No makeup tests allowed**, for any reasons—if you miss one, that will be the midterm that the final replaces. The midterm dates are:

1. Tuesday of Week 5: Oct. 28
2. Tuesday of Week 8: Nov. 18

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.

Grades will be distributed as follows:

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

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.