

Faculty of Commerce and Economics
School of Banking and Finance

MFIN6214
FINANCIAL THEORY AND POLICY

COURSE OUTLINE
2007, SESSION 1

MFIN6214 – Financial Theory and Policy Page- 2

1 COURSE STAFF 3

1.1 Communication with Staff 3

2 INFORMATION ABOUT THE COURSE 3

2.1 Teaching times and Locations 3

2.2 Units of Credit 3

2.3 Parallel teaching in the course 3

2.4 Relationship of this course to other course offerings 3

2.5 Approach to learning and teaching 3

3 COURSE AIMS AND OUTCOMES 4

3.1 Course Aims 4

3.2 Student Learning Outcomes 4

3.3 Teaching Strategies 4

4 STUDENT RESPONSIBILITIES AND CONDUCT 5

4.1 Workload 5

4.2 Attendance 5

4.3 General Conduct and Behaviour 5

4.4 Keeping informed 5

5 LEARNING ASSESSMENT 5

5.2 Assessment Details 5

5.3 Assignment Submission Procedure 6

5.4 Late Submission 6

5.5 Special Consideration and Supplementary examinations 7

5.6 Assignment Format 7

6 ACADEMIC HONESTY AND PLAGIARISM 7

7 STUDENT RESOURCES 9

7.1 Course Resources 9

7.2 Other Resources, Support and Information 10

8 CONTINUAL COURSE IMPROVEMENT 11

9 COURSE SCHEDULE 11

MFIN6214 – Financial Theory and Policy Page- 3

1 COURSE STAFF

Office Phone Consultation Email

David Feldman

Weeks 1-7

Quad3074 9385-5748 Tues 5–6 & by
appointment d.feldman@unsw.edu.au

Toan Pham

Weeks 8-14

Quad3053 9385-5869

Wed 5–6 & by

appointment t.pham@unsw.edu.au

Lecturer in charge: David Feldman

1.1 Communication with Staff

In class, before and after class, during consultation hours, by sending email notes, by phone calls, by scheduling special appointments, WebCT Vista.

Students should check WebCT Vista regularly.

2 INFORMATION ABOUT THE COURSE

2.1 Teaching times and Locations

Wednesdays, 6-9PM, Webst ThB

2.2 Units of Credit

This is a 6 units of credit course (6 UOC)

2.3 Parallel teaching in the course

None

2.4 Relationship of this course to other course offerings

This is a “core” course within the Master of Finance program (see the handbook for specific details of MFIN courses). It provides essential foundation to financial decision making in general and to other program courses in particular.

2.5 Approach to learning and teaching

In order to obtain the potential benefit from the course, fulfil the course requirements, and succeed in the exams, assignments, and projects, students are required to follow the points below.

1. Read the respective textbook chapters and other related readings *before* class lectures. This will make the class material easier to follow and comprehend.
2. Attend class lectures (arrive on time).
3. Actively participate in class: answer the instructors’ questions, and ask your own questions.

MFIN6214 – Financial Theory and Policy Page- 4

4. After class lectures, study the lecture material, preferably in groups, and solve the homework problems.
5. If issues from last lectures are still not clear, ask your questions or email them to the tutors or instructor.

The course provides the theoretical underpinnings of modern finance and its applications, and is related to capital markets, corporate and individual financial policies and decisions. The approach to teaching and learning will emphasize the link (or lack of) between theory and practice. We might use case studies, financial events, and reports in the financial media to achieve this objective.

3 COURSE AIMS AND OUTCOMES

3.1 Course Aims

The goal of the course is to establish perspectives, approaches, tools and methods of independent thinking, analysis, and problem solving. We will apply these to essential finance theory and applications, most of them conceived by Nobel Laureates. Topics will include capital structure, dividend policy, mergers and acquisitions, corporate governance, utility theory, portfolio theory, arbitrage pricing, equilibrium pricing, security prices’ informational efficiency, and performance measurement.

In addition, the course has two broad and inter-related aims: (i) to explain the essence of finance theory and how various financial aspects fit together; and (ii) to provide an intermediate treatment of some issues in corporate financial policy. These help practising finance executives and scholars to keep up to date with current developments.

3.2 Student Learning Outcomes

At the completion of the course students should have improved their ability to

- L1. Independently think, define, analyze, and solve problems.
- L2. Combine analytical skills, quantitative skills, economic knowledge, and intuition to identify, define, learn, analyze, and implement financial decisions.

L3. Independently work with and learn new material from resources, such as textbooks, articles, and working papers.

Upon completion of this course students will have an intermediate knowledge of the fundamentals of finance theory and practical corporate financial policies.

3.3 Teaching Strategies

Readings will introduce students to issues and subject matters. Class lectures will define, analyze and resolve issues and raise subsequent ones. Tutorials will perform exercises, solve examples reinforcing the lectures. Case studies will extend problems' real life factors and complexities, and will enhance group work and group presentations. Students will study the book and other readings, attend lectures, participate in class lectures, solve problems from the book, perform other assignments, do projects individually and in groups, and make presentations individually and in groups. Students will study book sections and articles that will not be covered in class lectures.

MFIN6214 – Financial Theory and Policy Page- 5

4 STUDENT RESPONSIBILITIES AND CONDUCT

4.1 Workload

It is expected that you will spend at least **ten hours** per week studying this course. This time should be made up of reading, research, working on exercises and problems, and attending classes. In periods where you need to complete assignments or prepare for examinations, the workload may be greater.

Over-commitment has been a cause of failure for many students. You should take the required workload into account when planning how to balance study with employment and other activities.

4.2 Attendance

Punctual attendance at **all** lectures and seminars is required and essential in this course. In addition, university regulations indicate that if students attend less than eighty per cent of scheduled classes they may be refused final assessment.

4.3 General Conduct and Behaviour

You are expected to conduct yourself with consideration and respect for the needs of your fellow students and teaching staff. Conduct which unduly disrupts or interferes with a class, such as ringing or talking on mobile phones, is not acceptable and students may be asked to leave the class. More information on student conduct is available at:

www.my.unsw.edu.au

4.4 Keeping informed

You should take note of all announcements made in lectures, email notes, and the course web sites. From time to time, the University will send important announcements to your university e-mail address without providing you with a paper copy. You will be deemed to have received this information.

5 LEARNING ASSESSMENT

5.1 Formal Requirements

In order to pass this course, you must:

- Achieve a composite mark of at least 50% of the maximum grade **at each** of the two parts of the course; and
- Successfully satisfy all assessment tasks and requirements (see below)

5.2 Assessment Details

Grades are awarded in the following categories: HD, DN, CR, PS, FL. Further information is available at:

<https://my.unsw.edu.au/student/academiclife/assessment/assessmentmainpage.html>

First Half Requirements Weight

MFIN6214 – Financial Theory and Policy Page- 6

Attendance [A_t] 3%

Assignments [A_s] 4%

Projects,* oral presentations,* papers,* quizzes, class participation [P] 0- W %

Exam [F], $0 \leq W \leq 18$ (43- W)%

Maximum first half grade 50%

*Projects, oral presentations, and papers, need to be approved by the instructor. The instructor will consequently select W for each student on individual basis.

Exams will be comprehensive with respect to the corresponding half of the course.

Each of the above requirements is associated with all of the learning outcomes listed in Section 3.2.

The grade of the second half of the course, G , will be the following function of the individual requirement grades A_t , A_s , P , and F , where $A_t, A_s, F, P \in [0,1]$,

$$G = 3 \times A_t + 4 \times A_s + (43-W) \times F + W \times \text{Max} [P, F]$$

or,

$$G = 3 \times A_t + 4 \times A_s + 43 \times F + W \times \text{Max} [P-F, 0]$$

Note that a student involvement in projects, oral presentations, papers, quizzes, quantified in the weight W is an insurance (option) that can only increase the grade.

Second Half Requirements Weight

Two case studies (syndicated – 3 to 4 students) 30%

Exam 20%

Maximum second half grade 50%

On case studies

Students are required to form groups of 3 to 4 students and submit the names of group members in the second class. Those who are not members of any such groups will be allocated to remaining groups. As presentations are to be given in Weeks 11 and 13, early grouping is necessary so that groups can start work immediately.

5.3 Assignment Submission Procedure

Assignment submission procedures will be indicated in class. However, all student submissions should include, in block letters, the student full name, last name first, ID number, and the course code.

Dates of submission are according to the UNSW assessment policy –

<https://my.unsw.edu.au/student/academiclife/assessment/AssessmentPolicyIndex.html>.

5.4 Late Submission

Late submissions will not be accepted.

MFIN6214 – Financial Theory and Policy Page- 7

Special consideration is only granted in exceptional circumstances on medical or compassionate grounds. Medical certificates or other evidence of extreme misfortune must be attached.

As case studies involve group work, this has to be presented as a whole group at the scheduled times and dates. No extension can be given. Exemptions to the **attendance** requirement of a syndicate member may be considered on medical or compassionate grounds. Medical certificates or other evidence must be submitted.

Work and/or other commitments are **not** considered.

5.5 Special Consideration and Supplementary examinations

Information and policy about special consideration and supplementary examinations are available on the School of Banking and Finance website. UNSW policy and process for Special Consideration applies (see

<https://my.unsw.edu.au/student/atoz/SpecialConsideration.html>). Specifically:

- Applications for special consideration (including supplementary examinations) must go through UNSW Central administration (within 3 working days of the assessment to which it refers) – applications will **not** be accepted by teaching staff;
- Applying for special consideration does not automatically mean that you will be granted additional assessment or that you will be awarded an amended result;
- If you are making an application for special consideration (through UNSW Central Administration) please notify your Lecturer in Charge;
- Please note: a register of applications for Special Consideration is maintained. History of previous applications for Special Consideration is taken into account when considering each case.

5.6 Assignment Format

Projects, assignments, and papers formats will be explained in class. However, all students' submissions should include, in block letters, the student full name, last name first, ID numbers, and the course code.

6 ACADEMIC HONESTY AND PLAGIARISM

The University regards plagiarism as a form of academic misconduct, and has very strict rules regarding plagiarism. For full information regarding policies, penalties and information to help you avoid plagiarism see:

<http://www.lc.unsw.edu.au/plagiarism/index.html>

Plagiarism is the presentation of the thoughts or work of another as one's own.*

Examples include:

- direct duplication of the thoughts or work of another, including by copying work, or knowingly permitting it to be copied. This includes copying material, ideas or concepts from a book, article, report or other written document (whether published or unpublished), composition, artwork, design, drawing, circuitry, computer program or software, web site, Internet, other electronic resource, or another person's assignment without appropriate acknowledgement;
- paraphrasing another person's work with very minor changes keeping the meaning, form and/or progression of ideas of the original;
- piecing together sections of the work of others into a new whole;
- presenting an assessment item as independent work when it has been produced in whole or part in collusion with other people, for example, another student or a tutor; and,
- claiming credit for a proportion a work contributed to a group assessment item that is greater than that actually contributed.†

Submitting an assessment item that has already been submitted for academic credit elsewhere may also be considered plagiarism.

The inclusion of the thoughts or work of another with attribution appropriate to the academic discipline does *not* amount to plagiarism.

Students are reminded of their Rights and Responsibilities in respect of plagiarism, as set out in the University Undergraduate and Postgraduate Handbooks, and are encouraged to seek advice from academic staff whenever necessary to ensure they avoid

plagiarism in all its forms.

The Learning Centre website is the central University online resource for staff and student information on plagiarism and academic honesty. It can be located at:

www.lc.unsw.edu.au/plagiarism

The Learning Centre also provides substantial educational written materials, workshops, and tutorials to aid students, for example, in:

- correct referencing practices;
- paraphrasing, summarising, essay writing, and time management;
- appropriate use of, and attribution for, a range of materials including text, images, formulae and concepts.

Individual assistance is available on request from The Learning Centre.

Students are also reminded that careful time management is an important part of study and one of the identified causes of plagiarism is poor time management. Students should allow sufficient time for research, drafting, and the proper referencing of sources in preparing all assessment items.

* Based on that proposed to the University of Newcastle by the St James Ethics Centre.

Used with kind permission from the University of Newcastle

† Adapted with kind permission from the University of Melbourne.

MFIN6214 – Financial Theory and Policy Page- 9

7 STUDENT RESOURCES

7.1 Course Resources

REQUIRED TEXTBOOK AND READINGS

Copeland, T. E., J. F. Weston, and K. Shastri, 2005, *Financial Theory and Corporate Policy*, 4th edition, Pearson Addison Wesley. (CWS)

Copeland, T. E., J. F. Weston, and K. Shastri, 2005, *Financial Theory and Corporate Policy*, 4th edition, *Student Solutions Manual*, Pearson Addison Wesley.

Additional readings will be assigned in class lectures.

ADDITIONAL BOOKS

Bodie, Z., Kane, A. and A. Marcus, 2005, *Investments*, 6th Edition, McGraw-Hill, New York.

Brealey, R., Myers, S. and F. Allen, 2008, *Principles of Corporate Finance*, 8th Edition, McGraw-Hill, New York, New York.

Elton, E. J., Gruber, M. J., Brown, S. J. and W. N. Goetzmann, 2003, *Modern Portfolio Theory and Investment Analysis*, 6th Edition, John Wiley & Sons, New York.

Huang, C-F. and R. Litzenberger, 1988, *Foundations for Financial Economics*, North-Holland, New York. (HL)

Hull, J., 2003, *Options, futures and other derivatives*, Pearson Addison Wesley.

Ingersoll, J. E., 1987, *Theory of Financial Decision Making*, Rowman & Littlefield, Maryland.

Mas-Colell, A., Whinston, M. D. and J. R. Green, 1995, *Microeconomic Theory*, Oxford University Press.

Ross, S., Westerfield, R. and J. Jaffe, 2005, *Corporate Finance*, 7th Edition, McGraw-Hill, New York.

Varian, H., 1993, *Microeconomic Analysis*, 3rd Edition, W. W. Norton and Company.

SELECTED ARTICLES

Black, F., 1972, "Capital Market Equilibrium with Restricted Borrowing," *Journal of Business*, 45, 444-455.

- Black, F., Jensen, M. C. and Scholes, M., 1972, "The Capital Asset Pricing Model: Some Empirical Tests," in *Studies in the Theory of Capital Markets*, Jensen, M. C., editor, Praeger Publishers.
- MFIN6214 – Financial Theory and Policy Page- 10
- Diacogiannis, G. and Feldman, D., 2007, "The CAPM Relation for Inefficient Portfolios," with G. Diacogiannis <http://ssrn.com/abstract=893702>
- Fama, E. F. and Macbeth, J. D., 1973, "Risk, Return, and Equilibrium - Empirical Tests," *Journal of Political Economy*, 81, 607-636.
- Fama, E. F. and French, K. R., 1992, "The Cross-Section of Expected Stock Returns," *The Journal of Finance*, 67, 427-465.
- Feldman, D. and Reisman, H., 2003, "Simple Construction of the Efficient Frontier," *European Financial Management*, 9, 251-259. <http://ssrn.com/abstract=291654>
- Jagannathan, R. and Wang, Z., 1996, "The Conditional CAPM and the Cross-section of Expected Returns," *Journal of Finance*, 51, 3-53
- Kandel, S. and Stambaugh, R. F., 1995, "Portfolio Inefficiency and the Cross-section of Expected Returns," *The Journal of Finance*, 50, 157-184.
- Lintner, J., 1965, "The Valuation of Risk Assets and the Selection of Risky Investments in Stock Portfolios and Capital Budgets," *Review of Economics and Statistics*, 47, 13-37.
- Markowitz, H., 1952, "Portfolio Selection," *Journal of Finance*, 7, 77-91.
- Merton, R., 1972, "An Analytical Derivation of the Efficient Portfolio Frontier," *Journal of Financial and Quantitative Analysis*, 7, 1851-1872.
- Mossin, J., 1966, "Equilibrium in a Capital Asset Market," *Econometrica*, 34, 768-783.
- Roll, R., 1977, "A Critique of the Asset Pricing Theory's Tests," *Journal of Financial Economics*, 4, 129-176.
- Roll, R., 1980, "Orthogonal Portfolios," *Journal of Financial and Quantitative Analysis* 15, 1005-1023.
- Roll, R. and Ross, S. A., 1994, "On the Cross-sectional Relation between Expected Returns and Betas," *The Journal of Finance*, 49, 101-121.
- Sharpe, W., 1963, "A Simplified Model for Portfolio Analysis," *Management Science*, 9, 277-293.
- Sharpe, W. F., 1964, "Capital Asset Prices: A Theory of Market Equilibrium Under Conditions of Risk," *Journal of Finance*, 19, 425-442.

7.2 Other Resources, Support and Information

Information about other services available for students. This can be detailed either on a School website and referred to in the course outline or provided as in the example below.

The University and the Faculty provide a wide range of support services for students, including:

- **Learning and study support**

- FCE Education Development Unit (<http://education.fce.unsw.edu.au>)
- UNSW Learning Centre (<http://www.lc.unsw.edu.au>)
- EdTec – WebCT information (<http://www.edtec.unsw.edu.au>)

- **Counselling support** - <http://www.counselling.unsw.edu.au>

MFIN6214 – Financial Theory and Policy Page- 11

- **Library training and support services** - <http://info.library.unsw.edu.au>

- **Disability Support Services** – Those students who have a disability that

requires some adjustment in their teaching or learning environment are encouraged to discuss their study needs with the Course Coordinator or the Equity Officer (<http://www.equity.unsw.edu.au/disabil.html>). Early notification is essential to enable any necessary adjustments to be made.

In addition, it is important that all students are familiar with University policies and procedures in relation to such issues as:

- **Examination procedures** and advice concerning illness or misadventure
<https://my.unsw.edu.au/student/academiclife/assessment/examinations/examinationrules.html>

- **Occupational Health and Safety** policies and student responsibilities;
<http://www.riskman.unsw.edu.au/ohs/Policies%20&%20Procedures/UNSW%20OHS%20Accountability.pdf>

8 CONTINUAL COURSE IMPROVEMENT

Each year feedback is sought from students and other stakeholders about the courses offered in the School and continual improvements are made based on this feedback. UNSW's Course and Teaching Evaluation and Improvement (CATEI) Process (http://www.ltu.unsw.edu.au/ref4-5-1_catei_process.cfm) is one of the ways in which student evaluative feedback is gathered. Significant changes to courses and programs within the School are communicated to subsequent cohorts of students.

Students are encouraged to provide feedback at each class both anonymously or non-anonymously.

9 COURSE SCHEDULE

MFIN6214 – Financial Theory and Policy Page- 12

Wk Topic Readings

1

Asset Pricing Intelligence; What is Finance?

Introduction to Capital Markets; The Two

period Model: Consumption, Production,

Capital Markets, Investments; Separation

CWS1

2 Utility Theory; Historical Returns; Security

Indices CWS3; HL1

3 Portfolio Theory CWS5; HL3

4 CAPM; APT CWS6; HL4

5

Simple Construction of the Efficient Frontier

The CAPM Relation for Inefficient Portfolios

The Term Structure of Interest Rates

Roll (77); Roll & Ross (94); Kandel

Stambaugh (95); Jagannathan & Wang

(1996); Feldman & Reisman (03);

Diacogiannis & Feldman (07); CWS8

6

Derivatives, Real Options; Informational

Efficiency; Portfolio performance;

Asymmetric Information

CWS7; CWS12; CWS10; CWS9

7 First Half Exam

8 Anzac Day (25 April 2007)

9

Finance in practice: case study of dividend policy – Copies of this case will be distributed in Week 7

The instructor will introduce and lead the discussion. Students will participate and contribute.

10 Lecture on capital structure and dividend policy CWS15, 16

11 Case (I) presentation by student syndicates

12 Lecture on Mergers and Acquisitions CWS18

13 Case (II) presentation by student syndicates

14 Exam (to be held in regular class time)

6 June 2007

Tutorial problems, homework assignments, projects, and further readings will be assigned in class and future communications.