BOSTON COLLEGE
Department of Economics

Ec. 380.01
Harold Petersen
Capital Markets
21 Campanella Way, Room 480-O
Fall, 2011
Office Hrs. M 2-3, W 1-2, Th 3-4
Campion 303, T, Th., 9:00
petersen@bc.edu, phone 617-552-4550


Prerequisites: Statistics (Ec. 151 or 155) and Micro Theory (Ec. 201 or 203)

Course Requirements and Grading:
Two midterm exams (20% apiece), October 6 and November 10
An investment research report (20%), Part I due October 27 and the complete report on December 6
A final exam (40%), on Friday, December 16, at 12:30 p.m.
Problem Sets in the first part of the course (optional but strongly encouraged)

Course Organization and Expectations:
The course works best if pursued as a joint enterprise where the student contributes as much as the instructor. I expect to work hard at the course and I expect as much from you. This means coming to class, reading the assigned materials, working through the problem sets, and raising questions on material you find difficult or confusing. You will find me available outside of class, with sign-up times for appointments posted on my door, and you will find me more than willing to help if you are doing your share as well. I also expect you to read the financial pages of the newspaper and to generate discussion on current topics as they develop.

You are encouraged to work together on the problem sets if you like, to discuss your investment briefs with each other, and to study together. Your work on exams is to be entirely your own, and on your investment report anything drawn from others or worked out in conjunction with others should be carefully cited. Be sure you are familiar with the section on "Academic Integrity" in the Boston College Catalog (pp. 32-33), or online at BCInfo (A-Z index, Academic Integrity), and be aware that I take this most seriously.

There will be no make-up exams. If you miss an exam for good reason, let me know immediately by email or phone and you will be graded on the other exam and the final. If you do poorly on one mid-term but consistently well on the other one and the final, the one poor exam will be discounted but not completely ignored. (One poor midterm will reduce your grade by at most one notch, from B+ to B for example).

The problem sets and your record of attendance will be used for additional evidence up to one notch on your grade. If your problem sets are much better than your exam grades and if your class attendance is excellent, then your grade will be raised one notch. If they are good but about the same as exam grades, then if you are on the borderline, they will pull you up. In no case will I grade you below what I see on the exams and the investment project.

I want you to follow current press reports on developments in financial markets. Raise questions in class and/or approach me after class. The course will be much more meaningful if we follow current policy issues and then look at them in terms of the analytical apparatus developed throughout the course.

For the investment report, you are to select a firm whose stock is publicly traded, find out as much as you can about the firm, and then arrive at a buy, hold, or sell recommendation. There is a good deal of economic analysis involved in this, but if you pick a firm that really interests you it will be fun and will be a great learning experience. I will give you more information on this as we go along.

Good luck. It should be fun.
# Syllabus

## Topics

### I. Introduction

| A. Capital theory and tradeoffs over time. | Notes, Introduction |
| B. Financial markets and economic efficiency. | Notes, Chs. 1-2 |
| C. Discounting, present value, and compound interest arithmetic. | Notes, Ch. 3 |
| D. Present value and internal rate of return | Notes, Chs. 4-5 |
| E. An introduction to speculative booms and busts | Malkiel, Chs. 1-4 |

### II. Investment Criteria and Pricing of Assets.

| A. Rate of return: an application to yield to maturity on a bond. | Notes, Chs. 6-7 |
| B. Valuation: an introduction to common stock pricing models. | Malkiel, Ch. 5, Notes, Chs. 8-11 |
| C. Leverage, risk, and asset bubbles | |

**First Exam (October 6)** Covers Sections I and II

### III. Accounting Problems: Measurement of Earnings and Rate of Return.

| A. Financial statements. | Notes, Ch. 12 |
| B. The importance and use of earnings data. | Notes, Ch. 13 |
| C. Depreciation, intangibles, and earnings bias. | Notes, Chs. 14-15 |
| D. Current issues in measurement and reporting. | Notes, Ch. 16 |

### IV. Financial Markets.

| A. Investment banking, securities exchanges, the declining role of the specialist | Notes, Ch. 17-18 |
| B. Investment strategies: fundamentalists, technicians, and random walk. | Malkiel, Chs. 6-7, Notes, Ch. 19 |
| C. The efficient market hypothesis, and some apparent inconsistencies | Malkiel, Ch. 11, Notes, Chs. 20-21 |
| D. Tobin's "Q" and investment. | |

**Second Exam (November 10)** Covers Sections III and IV

### V. Portfolio Selection.

| A. Diversification and risk reduction. | Malkiel, Chs. 8-10, Notes, Ch. 22-23 |
| B. The Sharpe-Lintner model. | Notes, Ch. 24 |
| C. The Capital Asset Pricing Model. | Notes, Ch. 25 |
| D. Beta as a Measure of Risk | Notes, Ch. 26 |
| E. The Pursuit of Alpha | Notes, Ch. 27 |
| F. Market Equilibrium and Asset Bubbles | Notes, Chs. 28-31 |

**Final Exam (December 16 at 12:30 p.m.)** Covers the Course
Periodicals and T.V.

The Wall Street Journal, daily, Monday through Friday. Excellent coverage of financial and economic news.

Forbes, biweekly. Perhaps the best of the magazines specializing in finance.

CNBC most of the day for up-to-date market information and for excellent coverage of business and financial news. MSNBC and Fox Business News are also excellent.

Data Sources

The Value Line Investment Survey. Financial data for the past 15 years for a large number of widely traded firms, updated quarterly. (available online)

Barrons. Good source of current information re. earnings, dividends, recent developments on a large number of firms (periodicals room, newspaper rack).

Standard and Poor’s Industry Surveys, fundamental analysis, plus additional data, on a large number of firms (reference section, O'Neil, HC106.6.S742).

Mergent’s Manuals. Detailed background and financial information on most publicly traded firms (reference section, O'Neil, HG4961.M75).

Internet. A huge and growing number of sources for market quotes, company reports, and financial news. Google.Finance, Yahoo Finance, CNN Money, and Bloomberg are all good. Let’s share information on other good sources that we might have found.