This course is an introduction to securities markets and the pricing of capital assets. Topics covered include efficient markets theory, models for portfolio selection, and asset pricing theory. Emphasis will be on the empirical evidence available on these topics. The required text for the course is:

Zvi Bodie, Alex Kane, and Alan J. Marcus, *Investments (3rd ed.)*, Irwin, 1996 (hereafter "BKM").

The following book is currently back ordered. If it comes in to the bookstore, you should buy it:


Cliff Smith and other instructors usually use Chew in FIN 413. In addition, I have provided references to appropriate sections of the book *Principles of Corporate Finance*, (5th ed.), by R. Brealey and S. Myers that was used in the Capital Budgeting course (FIN 402).

**THE COURSE**

The reading assignments will be announced in class and will more or less follow the sequence given below. The readings marked with an asterisk "*" are required. Since you are already familiar with the Brealey & Myers book, you might want to read the appropriate material in those books. In most cases, it should not be necessary for you to read more than one discussion of a particular topic. You will be provided with copies of required readings not contained in the textbooks. Most of my lectures will use Freelance™ slide shows and you will receive copies of the slides for each lecture.
Expectations of Student Performance

My expectations are that students will come to class prepared by having read the necessary material. The lectures will not rehash the readings. Rather, we will discuss different perspectives on the arguments presented in the readings. Active, high quality class participation will enhance the grades of students who are near margins in the final grade distribution.

I will hand out notes to accompany many of the lectures. I will also hand out sets of stories reproduced from the popular business press (e.g., the Wall Street Journal). Class attendance is very important to successful completion of this course. If you know that you will be unable to attend more than a couple of the classes, you should probably not register for this course (see the description of the grading policies below). If you know that you have to be late for class, or leave early, please show courtesy to me and the rest of the class by entering and leaving the room as discretely as possible. If you miss a class, or are late in arriving, it is your responsibility to obtain copies of any handouts that were distributed in class [do not rummage around on the teaching desk looking for handouts if you arrive late!] I suggest that you form study teams and help each other out -- get extra copies of handouts for missing team-mates. I will not provide a long-term inventory of class hand-outs for people who miss class, but most of the handouts will be available on the class web page (see below).

Grading

There will be a short 10 point quiz at the beginning of class about once a week (which should provide incentive to arrive at class on time). The first quiz will be in the week of April 7 and the last quiz will be on June 4 (the last day of class). They will include one to three questions that are related to the most recent lectures, and/or the reading that was required for that day, and/or current events that relate to the material that is being discussed in class. Some weeks I may substitute a take-home assignment that will be due the next week. Every student will be able to “throw away” their two worst quiz grades, so the maximum score available from quizzes is 60 points.

There will be four case problems that will be done in groups of between 3 and 5 people. The case problems will involve an analysis of: (1) security return data, including an assessment of risk and return, and a very simple event study; (2) bond yields, forward rates, and returns; (3) options and futures prices; and (4) the performance of managed mutual funds. The total group score for the cases equals the average case score times the number of students in the group. On the last day of class (June 4), each group will turn in their grade-allocation sheet containing:
(a) the percentage (summing to 100%) of the total group score that each member by name is to receive towards his/her final grade, and

(b) the signature of each group member.

If one group member’s signature is missing, the grade allocation sheet is valid and binding on all members. If two or more signatures are missing, the allocation sheet is invalid and the group’s score will be allocated equally among the members. I will not arbitrate disputes among group members. Each case will be worth 10 points, so the maximum average score available from cases is **40 points**.

Ph.D. students *must* write a paper (worth 40 points) and will not participate in the case problems.

**Course Information on the Wide World Web (WWW)**

Most of the materials for this course will be posted on the home page for this course [http://www.ssb.rochester.edu/fac/schwert/f411.htm]. For example, I plan to post copies of the slides used in the classroom presentations as Adobe Acrobat files (so they can be viewed and printed from a microcomputer attached to the WWW). In addition, I have collected lists of sites that students can use to collect information on security prices (if you want to do an event study), on financial news, on securities filings with the S.E.C., and so forth. I want to encourage all students to use this resource throughout the course.

**Topics and Readings**

Additional journal articles, *which are not required*, are included for students who want more information on particular topics. These are not on reserve in the library, although copies of the *Journal of Financial Economics* and the *Journal of Finance* are available in the Management Library.

I. **INTRODUCTION: THE STATISTICAL PROPERTIES OF STOCK RETURNS**

*1. BKM, Chapters 2-4, and 26.*


I. INTRODUCTION: THE STATISTICAL PROPERTIES OF STOCK RETURNS


II. EFFICIENT CAPITAL MARKETS

*1. BKM, Chapter 12.

*2. Brealey & Myers, Chapter 13.


II. EFFICIENT CAPITAL MARKETS


III. **BOND MARKETS & INTEREST RATES**


IV. **THE PRICING OF OPTIONS**

IV. THE PRICING OF OPTIONS


V. THE PRICING OF FUTURES

*1. BKM, Chapters 21-22.

*2. Brealey & Myers, Chapter 25.
V. THE PRICING OF FUTURES


VI. PORTFOLIO SELECTION - DIVERSIFICATION AND EFFICIENT PORTFOLIOS

1. BKM, Chapters 5-7.


3. Brealey and Myers, Chapter 7.


VII. **THE CAPITAL ASSET PRICING MODEL: THEORY, TESTS AND EXTENSIONS**

1. *BKM*, Chapters 8 and 9 and Chapter 11.


VII. THE CAPITAL ASSET PRICING MODEL: THEORY, TESTS AND EXTENSIONS


VII. THE CAPITAL ASSET PRICING MODEL: THEORY, TESTS AND EXTENSIONS


VIII. PORTFOLIO EVALUATION AND MANAGEMENT

*1. BKM, Chapter 24.


